

Key 1998 Highlights

\$495M Free Cash Flow
+5% Sales Growth
+23% EPS Growth
\$165M Economic Value Added

Table of Contents

- 1 Letter to Shareowners
- 4 Honeywell's Focus
- 20 Management's Discussion and Analysis (MD&A) Segments
- 26 Selected Financial Data
- 30 MD&A Operations
- 33 MD&A Financial Position
- 40 Financial Statements and Notes
- 58 Management and Facilities
- 59 Board of Directors and Corporate Officers
- 60 Honeywell at a Glance
- 63 Shareowner Information

Honeywell is the world's leading provider of control technologies for buildings, homes, industry, space and aviation. The company employs 57,000 people in 95 countries.

Financial Highlights

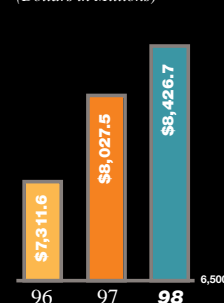
(Dollars and Shares in Millions Except Per Share Amounts)

	1998	1997	1996
Sales	\$8,426.7	\$8,027.5	\$7,311.6
Sales Growth Rate	5.0%	9.8%	8.6%
Income before Income Taxes	\$ 829.3	\$ 703.2	\$ 610.2
Net Income ¹	\$ 572.0	\$ 471.0	\$ 402.7
Net Income Growth Rate	21.4%	17.0%	20.7%
Diluted Earnings Per Common Share ¹	\$ 4.48	\$ 3.65	\$ 3.11
EPS Growth Rate	22.7%	17.4%	20.5%
Cash Dividends Per Common Share	\$ 1.13	\$ 1.09	\$ 1.06
Dividend Growth Rate	3.7%	2.8%	5.0%
Shareowners' Equity Per Average Common Share	\$ 22.09	\$ 18.80	\$ 17.44
Common Shares Outstanding	126.1	127.1	126.6
Common Shareowners	30,533	30,821	31,734
Total Assets	\$7,170.4	\$6,411.4	\$5,493.3
Employees at Year-end	57,000	57,500	53,000

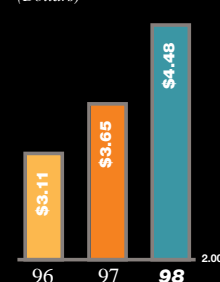
¹Includes \$53.7 (\$0.27 per share) and \$90.7 (\$0.48 per share) in 1998 and 1997, respectively, from special charges for costs associated with work force reductions and worldwide facilities consolidation. In 1998, Honeywell benefited from a settlement with U.S. tax authorities on previously questioned items, this tax-effected benefit was \$16.7 (\$0.13 per share). Additionally, the company benefited from litigation settlements of \$23.6 (\$0.11 per share) in 1998 and other one time gains of \$77.1 (\$0.41 per share) in 1997.

Statements contained in this report concerning the company's goals, strategies and expectations for business and financial results are "forward-looking statements" based on current expectations. No assurances can be given that the results in any forward-looking statements will be achieved and actual results could differ materially. Please review the section of this report captioned "Management's Discussion and Analysis" as well as reports the company files periodically with the Securities and Exchange Commission for information concerning factors which could affect the company's businesses.

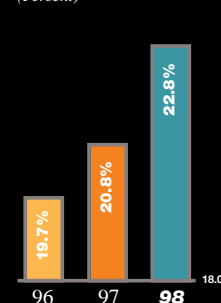
Total Sales
(Dollars in Millions)



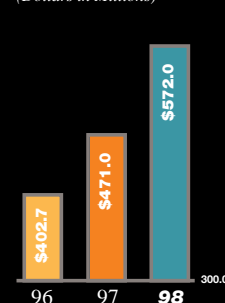
Diluted Earnings Per Share
(Dollars)



Return on Equity
(Percent)



Net Income
(Dollars in Millions)



To Our Shareowners:



Michael R. Bonsignore (left)
Chairman of the Board and
Chief Executive Officer

Giannantonio Ferrari (right)
President and Chief Operating Officer

I am pleased to report that Honeywell delivered strong bottom line results in 1998 while creating increased value for our shareowners. We finished the year with our 16th consecutive quarter of double-digit earnings growth. We surpassed \$1 billion of operating earnings for the first time in the company's history. Net income rose 21 percent to \$572 million, or \$4.48 per diluted share, including 6 percent from an accounting change. Revenue increased 5 percent to \$8.43 billion. Operating margins continued to expand in all three of our business segments, while total company margins increased to 12.2 percent. We generated \$495 million of free cash flow, well in excess of our \$400 million target, largely the result of a company-wide focus on cash generation.

Our bottom line results for the year were impressive. But we were not satisfied with the top line, since our objective has been to grow about 10 percent per year compounded. Orders and sales growth rates were negatively affected by a number of macroeconomic factors, including the crises in Asia and Latin America, depressed oil and commodity prices, unseasonably warm weather across North America and reduced capital spending.

Fortunately, we anticipated many of these market circumstances. Margin improvements in each of our lines of business resulted from improved product mix and the benefits of operational excellence initiatives across the corporation. At the same time, we took swift and aggressive action in late 1997 and throughout 1998 to continue reducing costs and streamlining our worldwide operations, so that our earnings and cash flow delivery goals for the year could be accomplished. In 1998, Honeywell proved that we can perform even when economic and market conditions deteriorate.

As we move into 1999, we are fully aware that some of the macroeconomic conditions that softened our orders and sales growth may prevail for at least the first half of the year. Investor confidence will strengthen even more when we demonstrate continuing double-digit earnings and cash flow growth, despite cyclical pressures in some of our market segments.

We will deal with the prospects of slower market growth in 1999 in two ways.

First, we will continue to deploy our discretionary investments toward the best candidates for greater top line growth. The pipeline is full of exciting new products, service offerings and software solutions that we will bring to the market throughout 1999. One of our primary goals is to have at least 30 percent of Honeywell's revenues generated by products introduced within the last three years, up from the current 26 percent.

Second, we will continue to manage our operations with a rigorous, demanding and disciplined approach to eliminate unproductive effort, quicken our responsiveness to customer needs and improve product and service quality. We have successfully lowered the company's sales and general overhead costs from 18.8 percent to 15.6 percent during the past four years. We will continue to rely on our Honeywell Quality Value Operational Excellence process to further reduce cost, improve efficiency, share best practices and capitalize on our unique strengths. I am confident that we can make significant additional progress with Honeywell's overall productivity.

We are convinced that our strategic position and our value proposition for customers are solid. Around the world, we are witnessing a growing need to manage complexity. We provide a unique capability to combine sensors, control devices, software, networks and human factors to help our customers succeed in this environment. Our technology enables us to simplify complex tasks that enhance human comfort and safety, that save energy and protect the environment, and that help our customers be more productive, efficient and competitive. As a result, our long-term sustainability and opportunity is undisputed.

Our 1999 growth priorities will be concentrated on new opportunities for our portfolio, through internal investment and acquisition. In addition, we will dampen, to the extent possible, the cyclical characteristics of our core businesses.

Our Mission

To create value for shareowners through our leadership in advanced control solutions that help customers worldwide achieve their goals.

Our Space and Aviation Control business has performed extremely well during the past few years. Our objective during this period of prosperity has been to accelerate revenue growth from a number of new market initiatives that will mitigate the cyclicity of our traditional commercial aviation business. Airport Systems, Aviation Services, commercial space programs and precision tactical guidance are four examples of real opportunities for revenue growth in the short term. The acquisition during 1998 of Hughey and Phillips airport lighting products and the Daimler-Benz airport systems business helped us generate a revenue stream of more than \$100 million in airport infrastructure improvements.

In September, we achieved an aviation industry milestone with the first landing of a commercial aircraft using the Honeywell/Pelorus Satellite Landing System. Our system is the world's first differential global positioning system ground station to receive type acceptance certification and operational approval from the FAA. It opens up a leading position in aircraft landing efficiency and safety. This accomplishment gives us first-in-market position in this important element of our Airport Systems business, a segment with tremendous growth potential over the next decade.

Our Industrial Control business top line softened in the second half of 1998, due largely to depressed oil, chemical, and pulp and paper prices. Despite the market conditions, the business delivered record earnings and margin rates, and made excellent progress in negotiating strategic alliances and partnerships with a number of our major customers, including Mobil, Phillips and CITGO. These alliances help us expand our competitive leadership position in the industry. They also provide us with an excellent platform for growth in software and advanced services that include the PlantScape™ hybrid automation system. In 1998, PlantScape™ became Honeywell's most successful new product introduction ever, with more than \$50 million of sales in the first year. And our Hi-Spec advanced control solutions, another exciting area in Industrial Control, presents our greatest opportunity for creating value in the process and hybrid control markets, with growth of more than 50 percent in 1998.

We continue to benefit from our 1997 Measurex acquisition, not only for paper production control, but also for color printing and control of other industrial flat sheet processes for rubber, plastic and aluminum. During 1999, Honeywell-Measurex will introduce a family of exciting new products to the market, reinforcing our leadership.

Our Sensing and Control business also contributed breakthrough technology, with the introduction of our vertical cavity surface emitting laser (VCSEL) — a business that grew strongly during 1998.

Overall, we are extremely well-positioned in Industrial Control when the markets turn up. In the meantime, we will manage the business aggressively and invest for growth.

Home and Building Control made excellent progress with the strategic positioning of the Solutions and Services unit in 1998. Margins improved 150 basis points in Solutions and Services, in part because our service revenues grew 8 percent over 1997. Building security and access control is a fast-growing segment and our Excel Security Manager offering resulted in a number of large orders including Nortel, Dow Chemical and Exxon. To bolster growth, we acquired VVE Security and ESD Electronics to round out our security offering. The acquisition of Phoenix Controls has provided us with controls and solutions for critical environment management among our laboratory, research center and pharmaceutical customers.

We anticipate good progress in federal government energy-saving performance contracting. Honeywell was selected as a supplier for all of the government's contracting regions across the United States. Specific work orders from these contracts have been awarded and are expected to grow appreciably in 1999.

Home and Building Control also delivered solid profit growth in its core Control Products segments in 1998, despite adverse weather challenges. Warm weather in both the spring and fall affected the heating, ventilation, air conditioning and Home Control replacement business. The Perfect Climate business completed its line of residential thermostats, air cleaners and humidifiers, and drove strong growth in 1998.

During the year, we successfully launched a number of LonMark®-compliant products, including the Excel 10 family of open system applications for the commercial market. The acquisition of Westinghouse Security Electronics, an access control company, broadens our comprehensive commercial portfolio for building automation.

We also expanded into the cooling and refrigeration market with the acquisition of two companies: Flica, a German-based producer of valve components for refrigeration equipment; and Elm, headquartered in Scotland, a leader in electronic controllers for refrigerator cases in supermarkets, which are LonMark®-compliant.

Our Vision

To grow profitably by delighting customers and achieving undisputed leadership in control.

A special focus in our business was placed on marketing our indoor air quality and security solutions to the strong new residential construction market, with many builders exclusively featuring Honeywell solutions.

Home and Building Control Products' operational excellence focus on total supply chain management and the implementation of our Six Sigma quality initiative in 1998 helped our customers decrease their inventory levels and dramatically improved our delivery performance. Our supply chain focus will further solidify a best-in-class position and will have a strong positive impact on working capital in 1999.

Overall, my 57,000 Honeywell associates across the corporation are proud of what we have accomplished. At the same time, we are determined to continue our progress until our full potential has been realized. Honeywell is a good, solid company with the potential to be a great one. We will not rest until our ambitions have been realized. 1999 will be challenging, but we are prepared with four imperatives for delivering maximum shareowner value.

PERFORMANCE. We compare ourselves to 19 of the best companies in our peer electrical equipment group. We measure our progress against this peer group for all key financial indicators: revenue growth, earnings growth, cash flow, return on equity and total shareholder return. We compensate management relative to how we perform against this group. After four years of consistent quarter-to-quarter earnings growth, we certainly do not intend to compromise the credibility we have earned. We are determined to go on delivering strong earnings growth and return to double-digit revenue growth as soon as possible.

GROWTH. Since I became CEO in 1993, we have positioned Honeywell on a revenue growth trajectory that would reach or exceed \$10 billion by the year 2000. As I have already mentioned, we were disappointed with 1998 sales growth of 5 percent and all of our energies are focused on improving revenue as soon as possible. I believe that our growth opportunities are extraordinary and our cash flow performance in 1998 gives us ample financial flexibility to augment organic growth with acquisitions. Our investments will emphasize service and applications software as well as market segments already mentioned that are less cyclical in nature.

COMMITMENT. We understand that our success as a company is tied closely to the dedication and commitment of our employees around the world. We have worked hard to help as many employees as possible become shareowners. Currently, employees hold close to 7 percent of the company's outstanding shares — nearly double their holdings

five years ago. Virtually all of our U.S. employees own stock, and we are introducing stock ownership plans around the world to reach our international employees.

Seventy-eight percent of our U.S. employees are covered by variable pay programs that link a portion of their compensation to the company's results. 1999 goals for operating profit and cash flow improvement link all of us together in a common focus on performance and commitment.

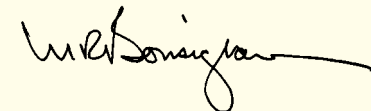
REPUTATION. We believe strongly that Honeywell has the potential to be one of the most successful and admired companies in the world. That ambition took a big step forward with our inclusion in Fortune magazine's 1998 list of the World's Most Admired Companies. Our reputation is of vital importance in developing partnerships with our customers, our employees, our suppliers and the communities where we live and work. Our reputation and our track record are critical to achieving our lofty ambitions.

LOOKING FORWARD. I am very bullish about Honeywell's future. The world demands what we have to offer. We are performance driven with a record of delivering on our promises. We have prepared ourselves well for the future, and we have redoubled our efforts to continue delivering double-digit earnings and cash flow growth.

For 1999, we will continue to strive for improvement in all of our value drivers, to aggressively control our costs, and to move decisively to strengthen our leading market shares. We are blessed with a world-class workforce and we will demonstrate further progress in making more of our employees owners in the company.

We are also aware that a new millennium waits just around the corner, filled with opportunities for Honeywell. Energy efficiency, human comfort and safety, productivity and environmental quality are global requirements, irrespective of geography or politics. Honeywell is there, in 95 countries, to work and partner with our customers to profitably manage ever more complex operating environments and to create value for them and for our shareowners. Honeywell's best days, many of them, lie ahead of us.

In closing, let me extend a warm welcome again to two new members of our Board of Directors — Katherine M. Hudson, President and CEO, Brady Corporation, and Jaime Chico Pardo, CEO, Teléfonos de México S.A. de C.V.



Michael R. Bonsignore
Chairman of the Board and Chief Executive Officer
February 10, 1999

The world isn't getting any simpler.

In fact, it's getting more complex.

W

E CAN SENSE THE CONTRADICTIONS ALL AROUND US... The worker heads home, tethered to the office with cell phone and computer. Companies trying to become more agile as they grow ever larger. Ecotourism and mega-cities. Reduce, reuse, recycle. More, faster, better.

The world isn't getting any simpler. Civilization is evolving toward greater complexity because we don't want to go backwards. Nor do we want to lose touch with the things that make us human. The basic need for simplicity in our lives is as constant as our pulse.

We want to have it both ways—to experience change and stay secure, to do more and pay less, to let machines into our lives without becoming machines ourselves. Is it possible to be the butterfly *and* live in the cocoon?

Honeywell's business has been at the core of this paradox ever since the first thermostat saved a homeowner a trip to the basement. Honeywell technology senses the world around us, makes routine decisions for us and provides information so we can make the big ones. Control technologies make our lives more comfortable and secure, businesses more productive and profitable, the air cleaner and travel safer.

If you're at all aware of the Honeywell technology in your life, you may think of us as a thermostat prompting a furnace, switches clicking away in factories or black boxes emitting signals only an airplane can understand. But there's much more to control technology—and much more opportunity to provide greater value to our customers as their world grows more complex. It's no longer optional to have energy efficiency, comfort, safety, productivity and environmental protection. They're essential—simultaneously. And Honeywell is uniquely able to provide solutions for this complex world, while keeping things simple for everyone in it.

**Technology is helping
create that complexity.**

**"We compete on a global basis.
There's no cover—no safe local markets.
No choice but to be best in class."**

**— Markos Tambakeras, President,
Industrial Control**



But technology is also helping to manage it.

"We don't view our products as just pieces of hardware. Even something as basic as an appliance gas valve can be delivered as a solution that enhances simplicity for the manufacturer, the installer and the user."

— Albrecht Weiss, President,
Products Business, Home and Building Control

With: **SENSORS**

EMBEDDED SYSTEMS

APPLICATION SOFTWARE

SYSTEM ARCHITECTURE

USER INTERFACES

and **ADVANCED SERVICES.**

CONTROL BASICS. Control is a method for achieving a specific outcome under changing conditions. The more often or radically the environment changes—or the more critical it is to maintain precise conditions—the greater the benefits of Honeywell's control technology.

Control loops are the building blocks of control solutions. Our bodies contain many examples of control loops in action. When climbing stairs, our breathing and heart rate increase and then return to normal based on the oxygen demanded by our muscles. We never have to turn the system on or off. It's entirely self-regulating.

A control loop contains a sensor, which measures a condition and sends an input to a control device. The device compares the input to a setpoint. If the input falls outside the setpoint's range, the device initiates a corrective action, such as adjusting a furnace damper. It also gives feedback that the desired response has occurred. Control loops may respond to one variable such as temperature. Or they may be extended to regulate many interacting variables, such as those found in a moving combat vehicle or a power plant running at full steam.

A simple thermostat works efficiently because it contains a sensor which measures temperature continuously and makes adjustments to stay within the comfort range. Stoke the fire manually and you'll likely fall below or overshoot the desired temperature. You're less sensitive than a thermostat to temperature changes—and besides, you have better things to do.

Honeywell is the [world leader in technologies](#) that make automated control possible. Exploiting the communication revolution, digital information systems and these technologies, we have exciting growth opportunities ahead of us.

SENSORS. The process of control begins with sensors, the electronic eyes, ears and nerve cells that convert physical conditions into data. Honeywell's advanced sensors make appliances, automobiles, assembly lines, computer networks, satellites and security systems perform more precisely than ever.

EMBEDDED SYSTEMS. Electronic microchips that process sensor data can be placed in a device, allowing it to perform functions independently. Embedded systems are found in everything from gas



valves to microwave ovens to automobile engines. Not only do they make devices smarter, embedded systems make products simpler. Simpler to assemble, install and operate—and, therefore, less costly.

APPLICATION SOFTWARE. To manage most complex and specialized functions—as well as most mundane tasks—application software provides the instructions that assume control. Businesses now spend more for software than for hardware. Indeed, 90 percent of Honeywell's products contain software, and more than one-third of our R&D engineering workforce is involved in software development. We're a leader in developing advanced software solutions that integrate information from multiple sources. So a customer's ability to act is not limited by the data's form or point of origin—whether it came from a real-time production process, a product's history, human experts, the buildings they work in or the other information systems they use.

SYSTEM ARCHITECTURE. In most cases, control has moved away from proprietary hardware solutions to open systems that integrate hardware and software from many vendors. System architecture defines the parts of a system and the rules for how they work together. Because open system architecture is one of the primary technologies needed for today's complex systems, Honeywell's expertise makes us a valued partner. Honeywell open system architecture is widely used for all types of aircraft, in refineries and paper mills, and in building control applications.

USER INTERFACES. With so much more going on in our homes and appliances, automobiles and aircraft or plants and buildings, it's essential for people to interact simply and effectively with those complex systems. Honeywell is a leader in the software, display technologies and human ergonomics that make it easy to visualize and manipulate data—so you stay in control.

ADVANCED SERVICES. Another way to make technology more manageable is to have someone else manage it. Honeywell's advanced services allow customers to focus on their core businesses while we ensure systems deliver the desired outcomes. Traditional services are reactive and task-based. A customer reports a problem, and a technician goes out to fix it. Advanced services employ monitoring, on-line diagnostics and specialized knowledge to deliver quality, productivity or comfort—and the customer may not even have to be in the loop.



Keeping critical research safe from fire, intruders, airborne contamination and temperature swings.

Landing an airport's worth of passengers in a storm.



www.honeywell.com

"We are controlling the environment, safety, security and productivity in areas most vital to our customers. If a bank's data center gets too hot or lab specimens get too cold, millions of dollars can go down the drain."

— Kevin Gilligan, President, Solutions and Services Business, Home and Building Control

IT'S A TOUGH JOB, BUT.... Compare a glider to an airliner, a calculator to a computer, an individual to a team. Complexity can be a sign of value added—and the opportunity to increase value. Honeywell solutions help customers extract even greater value from complex situations.

In hydrocarbon processing industries, one challenge is controlling increasingly complex chemistries. In a pharmaceutical plant, it's efficiently switching from one product batch to another while maintaining purity and traceability. For airlines, it's delivering passengers safely, comfortably and on time. For homes, it's accommodating new lifestyles or expanded uses. For large buildings, it's keeping a variety of occupants safe and comfortable without driving energy costs through the roof.

For nearly every Honeywell customer, pressures are rising to deliver better quality and increased profits. Meanwhile, downtime, energy use and environmental impact must be reduced. Competing is not a matter of choosing either/or. It's all of the above.

These are problems that have Honeywell solutions.

Plant shutdowns are a major cost driver in many industries. Idled production can occur for a wide variety of reasons: planned maintenance and product changeovers, material shortages, operator errors, equipment breakdowns or accidents. Preventing unplanned downtime alone can add 5 percentage points to a typical petrochemical plant's bottom line.

Although plant and building automation systems can generate alerts of potentially dangerous conditions, the exact cause of an alarm is often not apparent. Without guidance about the incident, an operator may needlessly shut down the plant or take action that worsens the situation.

In 1998 Honeywell **Hi-Spec Solutions** business introduced **@sset.MAX™** advanced control solutions to protect industrial assets and lessen the impact of **abnormal situations**. The suite of solutions includes an Equipment Health Management application to reduce equipment failures through preventive maintenance, and tools to train and assist operators dealing with abnormal situations. We also introduced a suite of new machine safety products to protect operators.

Although these may seem like very different challenges, they have one thing in common:

All can be made more manageable with applied control technology.

"The number of airports hasn't grown nearly as fast as the world's air traffic. Airspace is finite. The air traffic control system needs to find new solutions—in the air and on the ground."

— Don Schwanz, President, Space and Aviation Control

QUICK, SAFE DECISION MAKING. Around the world, our building fire and security solutions are helping industrial plants—as well as schools, hospitals, museums, office buildings, government facilities and shopping malls—protect lives and reduce the cost of security. In some cases, improved monitoring can help avert expensive business interruptions. For example, a 13-acre Canadian manufacturing plant is now monitored using less than half the security staff required with its old fire alarm system. And there's a substantially lowered risk of costly downtime caused by a false alarm that leads to a general plant evacuation.

More companies will seek to integrate formerly separate systems and critical plant infrastructure—once they discover how Honeywell integrated solutions and services can lower operating costs, improve consistency from processes and deliver better information for decision making.

And there's no place where quick and accurate decision making is more critical than on the digital battlefield. Honeywell navigation controls, processors and displays help combat crews maneuver their vehicles with precision regardless of conditions.

OPENING UP THE SKIES. In this decade, world air passenger traffic has doubled. With a fixed amount of airspace and limits upon building new airports and runways, the air traffic system must find new ways to increase its capacity.

The air traffic management system of the future will place more of the control on pilots of aircraft, requiring new integrated systems of hardware, software and services. Our traditional stronghold has been avionics systems for new aircraft. Since existing aircraft will have to be retrofitted with the new systems, we see an additional multi-billion-dollar growth opportunity emerging.

Our new and evolving end-to-end solution for "free flight" is called **WorldNav™**. It links onboard communications, navigation and surveillance technologies with air traffic management systems. No other supplier has as many of the technologies for free flight available today. And when you combine WorldNav's approach with our extensive ground-based solutions, no other supplier can offer as complete a solution, either.

And no one in the world does control better than...

Honeywell

"Control was our original business, but we're not in it today for sentimental reasons. There's tremendous potential yet to be tapped."

— Giannantonio Ferrari, President and Chief Operating Officer

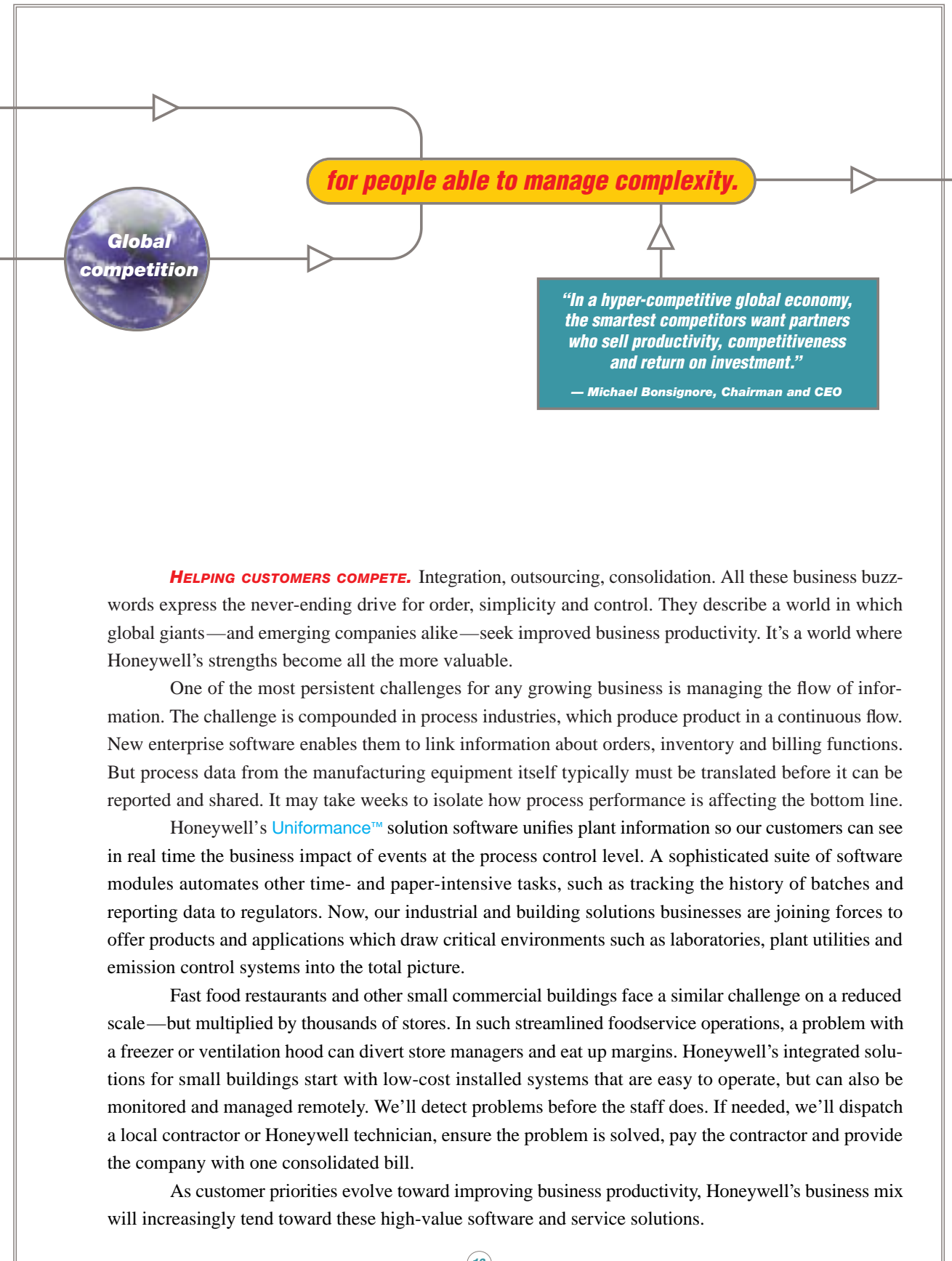
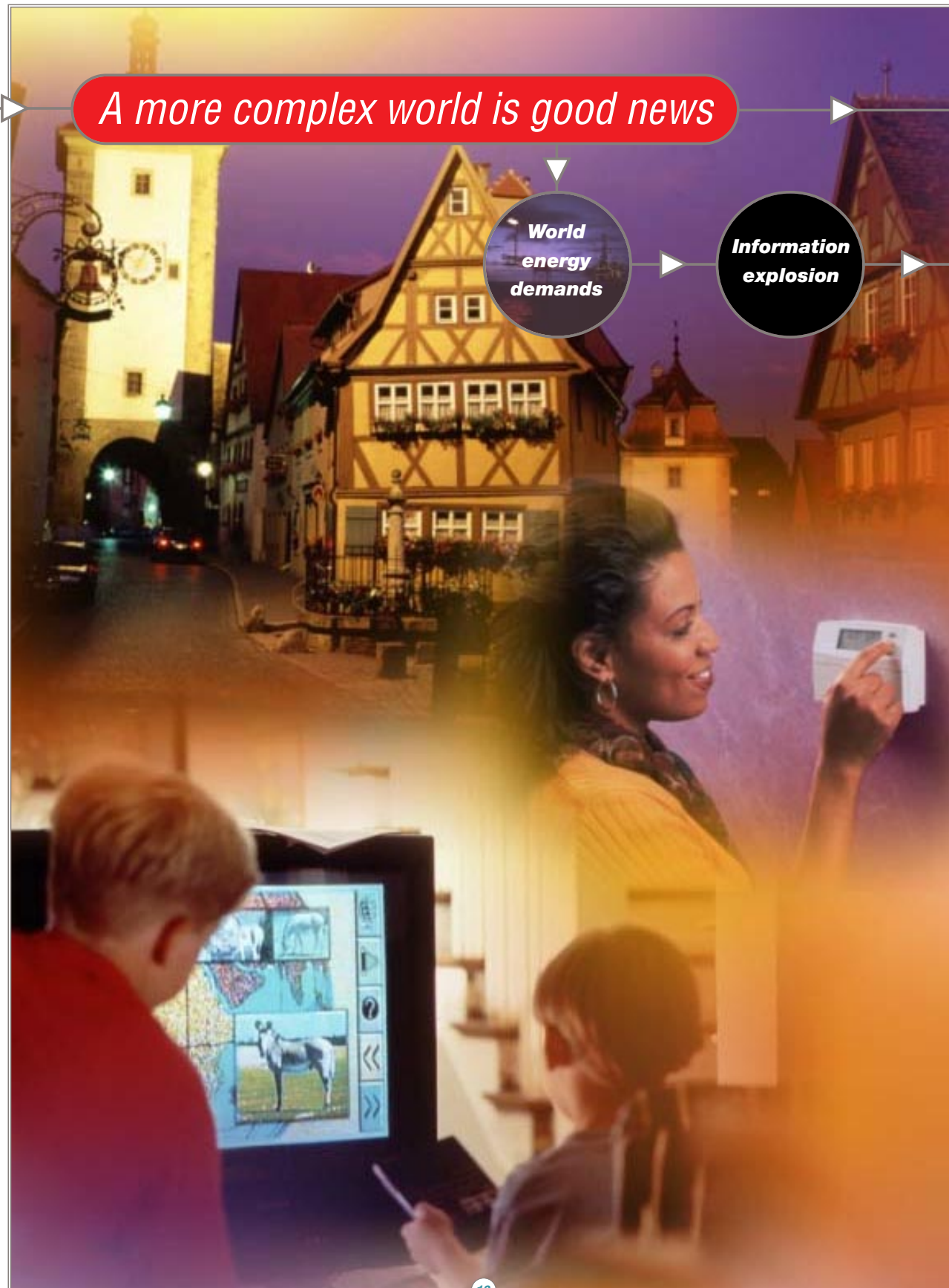
AIR-TO-GROUND AND END-TO-END SOLUTIONS. One component of this solution, the Honeywell/Pelorus Satellite Landing System (SLS), assists properly equipped aircraft to land more quietly, safely and precisely. Eventually, it will allow airports with the system to use runways in any weather and for less cost than airports with traditional navigation aids.

We're applying global positioning system technology and digital two-way communication to provide airports with a taxiway navigation system. TracLink™ controls all types of vehicles driving on the airport surface—from catering trucks and baggage tugs to fuel tankers and emergency equipment. For Cologne/Bonn Airport, and new airports in Korea, Hong Kong and Kuala Lumpur, Honeywell is providing building automation. Our systems control gate information, life safety, security, people movers, lighting, ventilation and temperature control—as well as integrate with weather, air traffic, baggage and other systems.

In 1998, our acquisition of airport systems and lighting companies increased our ability to provide end-to-end airport solutions. And we will add new features to Honeywell's aviation services through alliances. For example, we'll deliver Matsushita Avionics Systems in-flight entertainment products to airline passengers and develop other information services for the cabin, such as e-mail and Internet access. We're also leading a consortium of companies developing long-distance weather displays for airline cockpits. This next-generation "weather channel" will allow pilots to reroute around storms, saving fuel and potential delays.

Integrating all these facets of the air transportation system—and keeping travelers comfortable and safe in the process—presents a most complex challenge. Before long, the commercial space industry will face similar challenges as it moves from launching satellites for TV broadcast and mobile telephone communication to putting the Internet in the sky. And Honeywell will make it all possible.

THE WORRY STOPS HERE. Our own homes should be a haven from a complex world—but some days, they may feel more like busy airports or factories. And no wonder. It's where utilities, room comfort, lighting, security, cleaning and food preparation, entertainment and communication systems all converge to serve us. While some systems are automated, most homes are far from integrated. But stay tuned. Honeywell is actively developing new products and applications that will simplify operation, increase performance, reduce cost and increase your enjoyment of a worry-free home.



HELPING CUSTOMERS COMPETE. Integration, outsourcing, consolidation. All these business buzz-words express the never-ending drive for order, simplicity and control. They describe a world in which global giants—and emerging companies alike—seek improved business productivity. It's a world where Honeywell's strengths become all the more valuable.

One of the most persistent challenges for any growing business is managing the flow of information. The challenge is compounded in process industries, which produce product in a continuous flow. New enterprise software enables them to link information about orders, inventory and billing functions. But process data from the manufacturing equipment itself typically must be translated before it can be reported and shared. It may take weeks to isolate how process performance is affecting the bottom line.

Honeywell's **Uniformance™** solution software unifies plant information so our customers can see in real time the business impact of events at the process control level. A sophisticated suite of software modules automates other time- and paper-intensive tasks, such as tracking the history of batches and reporting data to regulators. Now, our industrial and building solutions businesses are joining forces to offer products and applications which draw critical environments such as laboratories, plant utilities and emission control systems into the total picture.

Fast food restaurants and other small commercial buildings face a similar challenge on a reduced scale—but multiplied by thousands of stores. In such streamlined foodservice operations, a problem with a freezer or ventilation hood can divert store managers and eat up margins. Honeywell's integrated solutions for small buildings start with low-cost installed systems that are easy to operate, but can also be monitored and managed remotely. We'll detect problems before the staff does. If needed, we'll dispatch a local contractor or Honeywell technician, ensure the problem is solved, pay the contractor and provide the company with one consolidated bill.

As customer priorities evolve toward improving business productivity, Honeywell's business mix will increasingly tend toward these high-value software and service solutions.

So how are we going to manage?

Simple.

"The objective of HQV Operational Excellence is to build a value-creating organization that consistently delights customers and delivers first quartile financial performance."

— Arnie Weimerskirch, Vice President, Corporate Quality

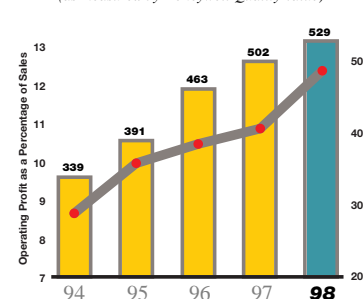
It's clear the world is full of opportunities for Honeywell to grow by supplying solutions that help customers gain control of their operations. But especially in today's demanding environment, top-line growth by itself can't lift us to the highest level of financial performance. Every aspect of our operating disciplines must be world-class and aligned to support our business strategies.

FIT FOR THE FUTURE. Our framework for assessing the fitness of our business is called the **Honeywell Quality Value (HQV)**. "HQV Operational Excellence" is the company-wide name for everything we do to improve the execution of our strategies and improve customer responsiveness by streamlining processes.

Each business unit is evaluated annually and is scored on a 1,000-point scale. Because the HQV is based on the Malcolm Baldrige National Quality Award Criteria, these evaluations also provide us with a benchmark against world-class practices in all aspects of our business. Our goal for the year 2000 is to have every business unit score above 500. Currently, 65 percent have reached the goal.

Collectively, the HQV reports create a comprehensive global snapshot. This helps us discover opportunities to reduce costs, improve responsiveness and share knowledge across the company. For instance, Honeywell units starting to adopt Six Sigma continuous improvement techniques can identify and learn from others more advanced in applying these quality methods.

Operating Profit vs. Business Management Practices
(as measured by Honeywell Quality Value)



The average HQV score for all Honeywell business units increased to 529 in 1998. By comparison, the most recent National Quality Award finalists ranged between 550 and 690. Ten Honeywell units scored within that range.

By setting ambitious goals

- Double-digit earnings growth
- Top quartile financial performance
- Increased employee ownership
- World-class reputation

and aligning our people, business structure and incentives to achieve them.

Each business unit applies HQV Operational Excellence principles in ways that best fit its business strategies, core competencies and customer requirements. Improvement efforts focus on realigning the organization with our strategies or aligning and refining processes to create more value.

LINING UP WITH CUSTOMER VALUE. It's necessary to continually refocus on what customers truly value, because one-time innovations can eventually become commodities. For example, we've traditionally installed the building systems sold in North America, but now these contracts have become increasingly price-driven. So we've shifted from installation contracting to supplying world-class building systems with the lowest total installed cost, using a network of third-party contractors. We supply the higher value project management and advanced applications and services. This approach still grows our installed base for ongoing services and upgrades.

The change enabled us to restructure our North American sales branch offices and centralize more services. With a streamlined cost structure and focus on higher margin opportunities, the business is now generating higher total earnings on a lower revenue base. At the same time, we're introducing new offerings that will grow the top line profitably.

In our home consumer products business, we've simplified the complexity of our product portfolio. By eliminating slow moving parts, kits and product variations from inventory, we've cut in half the number of items we're tracking. Now ordering is more streamlined. Factories can build and ship faster. All of which reduces cost while making us more responsive to our customers.

Honeywell's space systems business has a stellar history, with 26 consecutive years of successful mission launches. But we also recognize that our expertise with government space programs won't completely translate to the fast-moving and fast-growing commercial space market. So we've established a new organization built around commercial processes and market experience. It positions us to be the preferred partner for the unprecedented number of commercial launch vehicles and communication satellites scheduled in the decade ahead.

By focusing our strategies on delighting customers

"As the playing field in Europe is leveled, businesses will no longer be able to use currency differences to mask their performance. Capital will flow to the best innovators, to the low-cost providers and the most attentive and speedy suppliers."

— Bill Hjerpe, President, Honeywell Europe

with technology leadership

streamlined, agile processes

world-class execution

value-based cost structure

LEAPING BOUNDARIES. In recognition of the globalizing economy, we are reducing the emphasis on geography as a basis for structuring our businesses. This transition from country-based management is most advanced in [Honeywell Europe](#). The unfolding European Unification and introduction of a single currency will minimize the impact of foreign exchange rates and individual country's policies on Honeywell and our customers. Organizing by strategic lines of business will make it easier for us to reduce duplication, determine where best to invest, and purchase materials and services based on lowest cost. It will also mean we're better prepared to compete based on innovation, speed and fundamental performance.

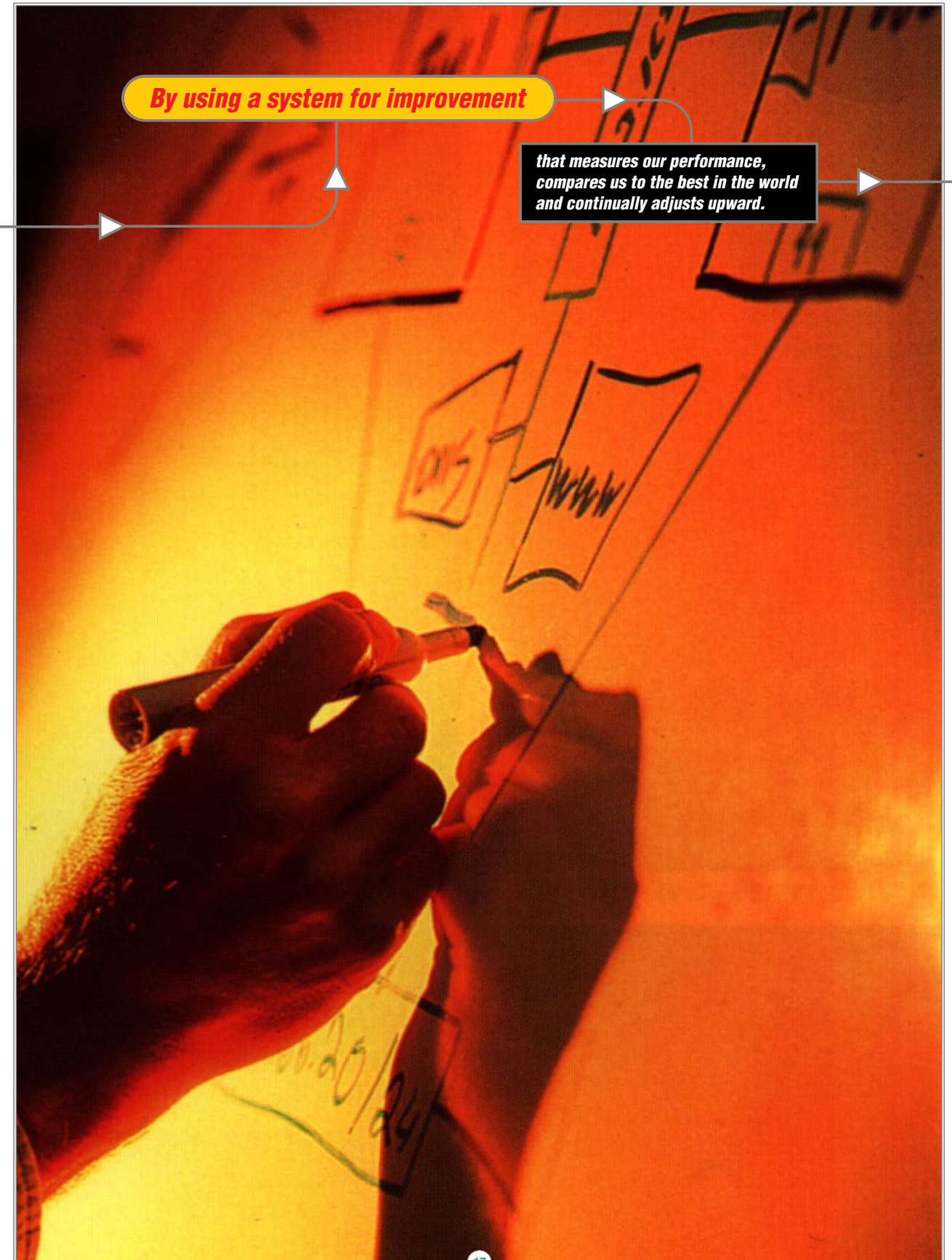
As we streamline our global management structure, internal borders become less significant, too. We are increasingly sharing services and applying communication tools across business units. A new common global telecommunications network will eliminate 21 different voice messaging systems. We're in the process of consolidating 154 independent financial software applications being used around the world into one integrated system. And we've dramatically simplified the number of medical plans.

In areas where multiple business units are located, we're finding ways to share support functions such as finance and human resources. For example, a single training center serves Honeywell's industrial, space and aviation businesses in the western U.S. They also coordinate staffing plans to better handle production peaks and retain workers during downturns.

The sharing extends to technology, too. Our industrial business developed the [PlantScape™](#) system to put the powerful features of distributed process control within reach of hybrid process manufacturers who need flexible, cost-effective control. Our building solutions business recently adopted the same system platform. Using a common system eliminates the need for a separate R&D effort, lowers costs and speeds development of our next-generation building control. A new software center focused on building control applications has been located in Phoenix to promote sharing with the industrial R&D center there.

By using a system for improvement

that measures our performance, compares us to the best in the world and continually adjusts upward.



Sure, it looks complicated.

"Although we work at the edge of uncertainties, R&D is a process that can be measured and improved like any other. Like any critical investment, our research dollar has become more tightly linked to delivering superior financial benefits."

—Ron Peterson, Vice President, Corporate Technology

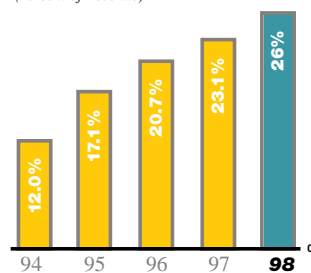
Through our alliance partnerships with leading companies like Mobil, Sinopec, Petróleos de Venezuela, Boeing and Anheuser-Busch, we ensure our technology development is clearly aligned with real needs. Pursuing research in areas critical to our partners makes our R&D extremely efficient. It attracts customer funding that nearly doubles the research budget—and 85 percent of these externally funded projects also result in new products for Honeywell. Alliance relationships with industrial customers alone will account for more than \$500 million in annual revenues by 2000.

PROCESS ALIGNMENT AND REFINEMENT. HQV Operational Excellence applies to every process, from new product development to our support of customers in the field.

We're determined to reduce the cycle time of product introductions and increase to 30 percent the annual revenue generated by new products released in the previous three years. Speed to market is more critical than ever. But strategically targeted research can also pay off for decades. For example, our technology investment in gyros, cockpit displays and navigation processing has benefited surface vehicle programs such as the Crusader combat vehicle—plus dozens of others and more still on the drawing board. The **Primus Epic™** integrated avionics system derived from our Boeing 777 work has won more than 50 percent of the business and regional jet contracts awarded in recent years. In 1998, the new Fairchild Dornier 728 became the latest to sign on. Opportunities stemming from the 777 development effort have a potential to generate \$5 billion in top-line growth by 2010.

In keeping with the HQV Operational Excellence emphasis on streamlining, our industrial business opened a new Solution Support Center in 1998. The center enabled us to consolidate 13 customer support facilities into two locations working as one virtual center. Around the clock, customers from anywhere in North America now can make a single call for service dispatch, order tracking or technical questions. As a result, customer satisfaction has increased to the best-in-class level of 92 percent. A focus on skills, consistent processes and new technologies continues to reduce overhead, streamline call-handling and improve response time, with a net yield of \$1 million in annual savings.

Revenue from Products Introduced in Last Three Years
(Percent of Revenue)



Our goal is to produce 30 percent of revenue from new or significantly improved products introduced in the last three years.

But we can master complexity.

"Our focus on operational excellence—combined with our growing reputation for strategic leadership—will lead to strong shareowner value creation."

—Larry Stranghoener, Vice President and Chief Financial Officer

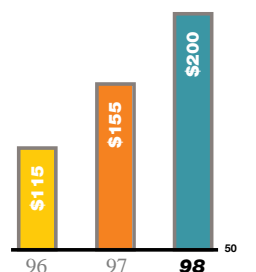
ASSETS WORKING OVERTIME. We continue to benefit from our ongoing initiative to improve the predictability of software development processes throughout the company. On the Software Engineering Institute's industry-standard scale of software process maturity, Honeywell's India Software Operation (HISO) ranks among the very best in the world. By drawing upon HISO engineers, the Arizona-based air transport systems business reduced development costs by \$3 million in 1998. Exploiting the time zone difference, software development engineers in Bangalore, Phoenix and Maintal, Germany, log onto global workstations that make software development a 24-hour-a-day operation.

Education is an important element of HQV Operational Excellence. Once people understand the business significance of goals, they can start to affect outcomes by rethinking processes. For example, space and aviation employees trying to reduce working capital looked for reasons why certain customers paid slower. They discovered government purchasing agents typically processed invoices on certain days. Billings that arrived a day later could sit for weeks until the next cycle. In contrast, commercial customers responded to incentives for faster payment. Aligning our billing processes to how customers paid has helped cut receivables and contributed to the unit's 2.1 percentage points of controlled working capital improvement in 1998.

VISIT www.Honeywell.com. After reading this, you can view an enhanced version of the annual report and [investor information](#) on our Web site. It's just one example of how we're further extending our reach to customers through electronic commerce, while lowering the cost of individual transactions. Customers can visit a [virtual trade show](#) and access [Web-based catalogs](#) to learn about Honeywell solutions. Product selection tools, technical documents and order status are available to our home and building channel partners in real time so contractors can respond to their customers immediately. Consumers can download a do-it-yourself [home security system](#) demo and order products from Honeywell's Web site.

CFO Magazine, *Computerworld* and *PCWeek* are among the publications ranking Honeywell's use of information technology as world-class. And in 1999, we will substantially increase the flow of new selling tools, user manuals and consumer information available on the Web.

Supply Management Cost Savings 1996-98: \$470 million
(Dollars in Millions)



Supply Management strategies, including more cost-effective purchases, global sourcing and increased use of electronic commerce contributed to savings of \$470 million over the last three years.

SEGMENT: Home and Building Control



J. Kevin Gilligan
President, Solutions and
Services Business



Albrecht Weiss
President, Products Business

Home and Building Control is a global leader in providing comfortable, healthy, safe and energy-efficient indoor environments. Customer loyalty to our brand is based on more than 3,500 products, a broad range of systems and services, a large installed base and an unmatched distribution network that supports our customer solutions worldwide.

Three-Year Sales Overview

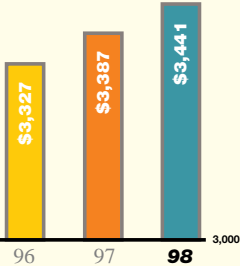
Sales in 1998 were \$3.441 billion compared with \$3.387 billion in 1997 and \$3.327 billion in 1996. Sales were driven by continued solid growth in the Services business, with strong contributions from both North American and European markets. This growth was moderated by a planned reduction in the lower margin Solutions business, reduced volume in Consumer Products and unusually warm winters in North America and Europe.

In 1997, Home and Building Control Products business experienced strong sales growth from the international market, driven by demand in our water products and combustion control businesses. Sales improvement **in 1996** resulted from growth in the retail business, new product introductions in Europe and the introduction of small to mid-sized building management systems.

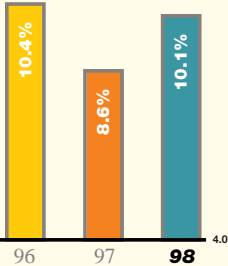
Three-Year Operating Profit Overview

Home and Building Control's **1998 operating profit** was \$349 million including \$26 million in special charges compared with \$290 million last year, which includes \$47 million in 1997 special charges. Excluding the planned impact of software capitalization of \$18 million, special charges and gains (see Note 19 to the Financial Statements on page 52), operating profits increased 6 percent. The key drivers of the margin improvement were the strategic repositioning of the Solutions and Services business, which

Home and Building
Control Sales
(Dollars in Millions)



Home and Building Control
Operating Margin Rate



Honeywell Home and Building Control's mechanical building management system controls the fire alarm system, as well as security and access at the Hong Kong International Airport.
(Photo courtesy of Hong Kong Airport Authority)

Home and Building Control is focused on revenue, margin and working capital improvements through operational excellence and innovative customer solutions.

included improving the quality and margins of the Solutions business and growing the higher margin Services business, and the emphasis placed on HQV Operational Excellence programs. Despite the challenges posed by weather, the Products business also saw solid profit growth in 1998, with strong growth from our residential products area.

In 1997, operating profit was \$290 million, including special charges of \$47 million and a gain of \$6 million on the sale of a small international security monitoring business. Excluding the impact of the gain and special charges, operating profit declined from 1996 due to the mix of lower margin Products business and lower than expected volume in Solutions and Services. **In 1996**, profits from Home and Building Control Products improved through volume increases and cost reductions while profits in Solutions and Services declined due to a competitive energy retrofit business and investment in programs to enhance productivity.

Business Strategies

Our Home and Building Control business began a strategic repositioning at the beginning of 1998, and the initiatives showed strong results throughout 1998. Growth initiatives in building security continued with key contract wins around the globe and several strategic acquisitions, including VVE Security, Inc., and ESD Electronics. Further acquisitions, including Flica, a German-based company, and Elm, headquartered in Scotland, expanded our cooling and refrigeration business, while Westinghouse Security Electronics, Inc., enhanced our commercial component line.

We also showed strong success from the government vertical market. As part of the U.S. government's policy to reduce energy use 30 percent by 2005, Honeywell was selected to participate in contracts worth up to \$1 billion to upgrade federal facilities in the 11-state central region and U.S. Air Force bases in nine western states.

Operational improvements made in 1998 will enable our customers to decrease their inventory levels. Working capital is also expected to improve in 1999, with our build-to-order/build-to-stock program.



In 1998, we completed the launch of our full line of electronic programmable thermostats.



Honeywell fire and security and ventilation control systems are installed in most McDonald's restaurants in St. Petersburg and Moscow.



Honeywell's Building Supervisor system maintained ideal ice conditions at recent curling competitions in Canada.

SEGMENT: Industrial Control



Markos Tambakeras
President, Industrial Control

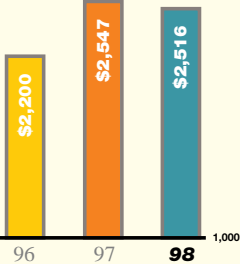
Industrial Control is a global leader in automation solutions from sensors to integrated solutions, and provides systems, products and services for process industries such as hydrocarbon processing, chemicals and pulp and paper. Additionally, Industrial Control manufactures switches and sensors for use in vehicles, consumer products, data communication and industrial applications, as well as smart position-sensing devices and systems used in factories and package distribution systems.

Three-Year Sales Overview

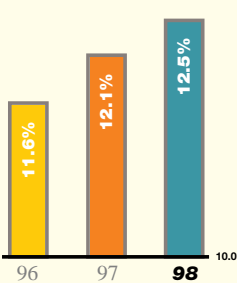
Industrial Control sales in 1998 were \$2.516 billion, compared with \$2.547 billion in 1997 and \$2.200 billion in 1996. Sales in 1998 were down slightly; however, after adjusting for divestitures and negative currency fluctuations due to the strong dollar, Industrial Control increased sales by 4 percent in a tough external environment. Despite significant weakness in the pulp and paper, refining and industrial components markets, Industrial Control remains well positioned in the industry through the introduction of superior technologies, leveraging of our installed base and increases in the number of our market-leading strategic alliances.

In 1997, sales reflected strong demand for the TotalPlant Solution (TPS) system, the introduction of over 80 new products and the successful acquisition of Measurex Corporation. In 1996, sales benefited from the successful introduction of new measurement, sensing and control products; the acquisition of Leeds & Northrup; the excellent market reception of our TotalPlant Solution (TPS) system; and continued strong demand for upgrades and services that increase the value of our installed control systems.

Industrial Control Sales
(Dollars in Millions)



Industrial Control Operating Margin Rate



Honeywell-Measurex provides Web inspection systems for Roibox in Aylesford, England.

Industrial Control's leading position in industries from automotive onboard sensors to process automation is supported by internal emphasis on operational excellence in all functions and, at the same time, a sense of urgency to achieve top-line growth.

Three-Year Operating Profit Overview

Industrial Control operating profit in 1998 was \$314 million including special charges of \$26 million compared to \$309 million in 1997, which included special charges of \$41 million. In 1998, excluding the planned impact of software capitalization of \$13 million, special charges and gains (see Note 19 to the Financial Statements on page 52), operating profits increased by 15 percent. The increase in profit was driven by substantial earnings improvement from Honeywell Measurex, the contribution of higher margin services and software growth and ongoing HQV Operational Excellence programs focused on reducing overhead and product costs.

In 1997, operating profits were driven by higher volume and improvement in ongoing productivity initiatives, which offset the negative impact of expenses associated with the Measurex acquisition. Operating profits increased in 1996 as a result of continuing strategic actions to reduce overhead, streamline business operations, improve the mix of higher-margin field instruments and automate component manufacturing.

Business Strategies

Superior technologies and a focus on HQV Operational Excellence, coupled with a balanced business model of sensors, systems solutions and services, are enhancing Industrial Control's strong industry position. Superior technologies like Industrial Control's Hi-Spec™ Software Solutions continue to demonstrate its competitive position in the marketplace with many strategic contract wins. In the fourth quarter, China's largest refiner, Sinopec, placed an order for 75 Profit Controller™ and Uniformance™ system licenses. Since the acquisition of Measurex, Honeywell is the undisputed leader in the pulp and paper automation market, and Sensing and Control's growth prospects were enhanced with the acquisition of Data Instruments Inc., a \$50 million per year manufacturer of precision sensing devices.

Alliances and strategic partnerships are providing advanced control technology, solutions, optimization software and training to industries around the world. Honeywell was chosen by a number of industrial customers for strategic alliances in 1998, including Mobil, CITGO, Exxon, Phillips and Petrofina.



Numerous pharmaceutical companies rely on Honeywell's system software to automate manufacturing processes.



At Subaru-Isuzu Automotive in Lafayette, Indiana, Honeywell's light curtains protect factory workers from hazardous motion in robotic and welding cells.



One of the largest refineries in Eastern Europe, the Gdansk Refinery has been a Honeywell customer for 20 years.

SEGMENT: Space and Aviation Control



Don Schwanz
President, Space and Aviation Control

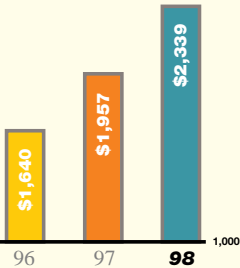
As a leading supplier of avionics systems and products for the commercial, military and space markets, our Space and Aviation Control business serves customers that range from aircraft manufacturers and business aircraft operators to prime space contractors and the U.S. government. Our systems are on board virtually every commercial aircraft produced in the Western world, and we have also been aboard every manned space flight launched in the United States.

Three-Year Sales Overview

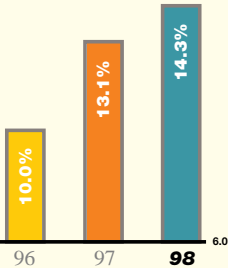
In 1998, Space and Aviation Control sales were \$2.339 billion, compared with \$1.957 billion in 1997 and \$1.640 billion in 1996. The 20 percent increase in sales was driven by strong growth in commercial avionics and solid performance from the military business. The growth in commercial avionics is the result of a continued increase in air transport deliveries, collision avoidance systems, satellite landing systems and business and commuter avionics shipments.

In 1997, strong commercial avionics and business and commuter jet markets drove 19 percent sales growth from the prior year. **Sales in 1996** increased 7 percent from the prior year led by increased commercial aviation OEM business and our strategies to expand our GPS-based guidance products and systems, pursue retrofit opportunities and extend our Boeing 777 technology to additional markets of interest.

Space and Aviation Control Sales
(Dollars in Millions)



Space and Aviation Control Operating Margin Rate



Honeywell's performance resulted in its being named the Crusader Program Supplier of the Year by United Defense, L.P. in July 1998.

Space and Aviation Control is well positioned for growth.

Three-Year Operating Profit Overview

Space and Aviation Control's **1998 operating profit** was \$334 million compared to \$256 million in 1997 and \$163 million in 1996. Excluding the planned impact of software capitalization of \$12 million, special charges and gains (see Note 19 to the Financial Statements on page 52), operating profit increased 26 percent, driven by the mix of higher margin commercial aviation business and leverage from higher sales volumes.

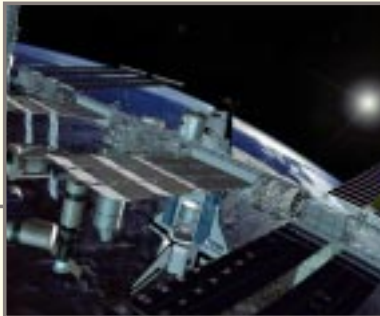
Operating profit in 1997 and 1996 increased due to improved margins in commercial aviation systems, lower development expenses and productivity improvements.

Business Strategies

Space and Aviation Control continued to make progress on its growth initiatives: communication, navigation, surveillance (CNS)/air traffic management (ATM); aviation services; airport systems; commercial space; tactical guidance; surface vehicles electronics; and railway electronics. These initiatives are expected to mitigate many of the cyclical characteristics of the OEM aerospace business and provide new avenues for business growth. These growth initiatives leverage Space and Aviation Control's core technologies in navigation, control displays, flight management and communications. Already, we are seeing the benefits of our key acquisitions—Hughey and Phillips and DASA Airports Systems—with our first contracts integrating Honeywell's Satellite Landing System and airfield lighting products. Our aviation services offerings for business jets have been expanded with the introduction of OneLink™ worldwide satellite communications services, and the OneView™ airborne information system, which provides live video and Internet service.



Our versatile integrated avionics system is used on the Boeing 737.



Our multiplexer/demultiplexer functioned perfectly during the first two launches of the International Space Station.



Key acquisitions enhanced our offerings in the area of airport infrastructure improvements, which include airfield lighting.

Selected Financial Data

Honeywell Inc. and Subsidiaries

(Dollars and Shares in Millions Except Per Share Amounts)	1998	1997	1996	1995	1994	1993	1992	1991	1990	1989	1988
Results of Operations											
Sales	\$8,426.7	\$8,027.5	\$7,311.6	\$6,731.3	\$6,057.0	\$5,963.0	\$6,222.6	\$6,192.9	\$6,309.1	\$6,058.6	\$5,857.0
Sales growth rate	5.0%	9.8%	8.6%	11.1%	1.6%	(4.2%)	0.5%	(1.8%)	4.1%	3.4%	4.8%
Cost of sales	5,677.0	5,425.1	4,975.4	4,584.2	4,082.1	4,019.6	4,195.3	4,185.1	4,308.7	4,172.5	4,258.8
Research and development	481.9	446.6	353.3	323.2	319.0	337.4	312.6	300.7	279.6	283.5	288.9
Selling, general and administrative	1,317.9	1,359.4	1,313.1	1,263.1	1,173.8	1,075.7	1,196.8	1,150.9	1,170.0	1,127.9	1,151.9
Litigation settlements ¹	(23.6)					(32.6)	(287.9)				
Discontinuance of product lines											150.8
Special charges	53.7	90.7			62.7	51.2	128.4			81.6	101.9
Interest—net	102.2	92.5	72.9	68.9	60.2	51.0	58.5	61.4	67.6	90.3	217.1
Gain on sale of businesses		(77.1)							(21.7)	(340.1)	(33.7)
Equity income	(11.7)	(12.9)	(13.3)	(13.6)	(10.5)	(17.8)	(15.8)	(14.6)	(11.5)	(33.0)	(9.8)
	7,597.4	7,324.3	6,701.4	6,225.8	5,687.3	5,484.5	5,587.9	5,683.5	5,792.7	5,382.7	6,125.9
Income from continuing operations before income taxes	829.3	703.2	610.2	505.5	369.7	478.5	634.7	509.4	516.4	675.9	(268.9)
Provision for income taxes ²	257.3	232.2	207.5	171.9	90.8	156.3	234.8	178.3	144.6	125.6	212.6
Income from continuing operations	572.0	471.0	402.7	333.6	278.9	322.2	399.9	331.1	371.8	550.3	(481.5)
Income from discontinued operations									10.1	53.8	46.6
Extraordinary item ³							(8.6)				
Cumulative effect of accounting changes ⁴							(144.5)				
Net income	\$ 572.0	\$ 471.0	\$ 402.7	\$ 333.6	\$ 278.9	\$ 322.2	\$ 246.8	\$ 331.1	\$ 381.9	\$ 604.1	\$ (434.9)
Net income growth rate	21.4%	17.0%	20.7%	19.6%	(13.4%)	30.6%	(25.5%)	(13.3%)	(36.8%)	N/A	N/A
Basic Earnings Per Common Share											
Continuing operations	\$ 4.54	\$ 3.71	\$ 3.18	\$ 2.62	\$ 2.15	\$ 2.40	\$ 2.88	\$ 2.35	\$ 2.45	\$ 3.23	\$ (2.83)
Discontinued operations									0.07	0.32	0.27
Extraordinary item ³							(0.06)				
Cumulative effect of accounting changes ⁴							(1.04)				
Net income	\$ 4.54	\$ 3.71	\$ 3.18	\$ 2.62	\$ 2.15	\$ 2.40	\$ 1.78	\$ 2.35	\$ 2.52	\$ 3.55	\$ (2.56)
Basic earnings per share growth rate	22.4%	16.7%	21.4%	21.9%	(10.4%)	34.8%	(24.3%)	(6.7%)	(29.0%)	N/A	N/A
Diluted Earnings Per Common Share	\$ 4.48	\$ 3.65	\$ 3.11	\$ 2.58	\$ 2.15	\$ 2.38	\$ 1.76	\$ 2.32	\$ 2.49	\$ 3.50	\$ (2.56)
Diluted earnings per share growth rate	22.7%	17.4%	20.5%	20.0%	(9.7%)	35.2%	(24.1%)	(6.8%)	(28.9%)	N/A	N/A
Cash Dividends Per Common Share	\$ 1.13	\$ 1.09	\$ 1.06	\$ 1.01	\$ 0.97	\$ 0.91	\$ 0.84	\$ 0.77	\$ 0.70	\$ 0.57	\$ 0.53
Dividend growth rate	3.7%	2.8%	5.0%	4.1%	6.6%	8.3%	9.1%	10.0%	22.8%	7.5%	3.9%
Financial Position											
Current assets	\$3,621.8	\$3,258.2	\$2,981.2	\$2,766.9	\$2,649.4	\$2,550.2	\$2,707.8	\$2,698.9	\$2,582.2	\$2,800.7	\$2,576.3
Current liabilities	\$2,452.7	\$2,318.9	\$2,066.9	\$2,022.5	\$2,071.8	\$1,856.1	\$1,969.2	\$2,095.0	\$2,175.1	\$2,415.8	\$2,286.9
Working capital	\$1,169.1	\$ 939.3	\$ 914.3	\$ 744.4	\$ 577.6	\$ 694.1	\$ 738.6	\$ 603.9	\$ 407.1	\$ 384.9	\$ 289.4
Current ratio	1.5	1.4	1.4	1.4	1.3	1.4	1.4	1.3	1.2	1.2	1.1
Short-term debt	\$ 178.9	\$ 146.4	\$ 252.4	\$ 312.4	\$ 360.6	\$ 187.9	\$ 188.4	\$ 168.4	\$ 109.0	\$ 145.6	\$ 314.8
Long-term debt	\$1,299.3	\$1,176.8	\$ 715.3	\$ 481.0	\$ 501.5	\$ 504.0	\$ 512.1	\$ 639.8	\$ 616.3	\$ 692.5	\$ 800.7
Total debt	\$1,478.2	\$1,323.2	\$ 967.7	\$ 793.4	\$ 862.1	\$ 691.9	\$ 700.5	\$ 808.2	\$ 725.3	\$ 838.1	\$1,115.5
Shareowners' equity	\$2,785.5	\$2,389.2	\$2,204.9	\$2,040.1	\$1,854.7	\$1,773.0	\$1,790.4	\$1,850.8	\$1,696.9	\$1,918.2	\$1,731.3
Capitalization	\$4,263.7	\$3,712.4	\$3,172.6	\$2,833.5	\$2,716.8	\$2,464.9	\$2,490.9	\$2,659.0	\$2,422.2	\$2,756.3	\$2,846.8

¹In 1998, the settlement of long-standing legal claims resulted in a gain of \$23.6. In 1993, the settlement of the lawsuits against Unisys Corporation and other parties in connection with Honeywell's 1986 purchase of the Sperry Aerospace Group resulted in a gain of \$22.4. Litigation settlements in 1993 and 1992 in the amounts of \$10.2 and \$287.9, respectively, are one time settlements, after associated expenses, reached with various camera manufacturers for their use of Honeywell's patented automatic focus camera technology.

²Financial Accounting Standard No. 96, "Accounting for Income Taxes," was adopted in 1988 and had the effect of increasing the Provision for Taxes and the net loss by approximately \$20.0 (\$0.12 per share).

³Extraordinary item resulting from the loss on early redemption of debt.

⁴The cumulative effect of accounting changes is the result of adopting Statement of Financial Accounting Standards (SFAS) No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions," which reduced net income by \$151.3 (\$1.09 per share); SFAS No. 109, "Accounting for Income Taxes," which increased net income by \$31.4 (\$0.23 per share); and SFAS No. 112, "Employers' Accounting for Postemployment Benefits," which reduced net income by \$24.6 (\$0.18 per share).

Selected Financial Data

Honeywell Inc. and Subsidiaries

(Dollars and Shares in Millions Except Per Share Amounts)	1998	1997	1996	1995	1994	1993	1992	1991	1990	1989	1988
Sales											
Home and Building Control	\$3,440.5	\$3,386.6	\$3,327.1	\$3,034.7	\$2,664.5	\$2,424.3	\$2,393.6	\$2,249.1	\$2,196.7	\$2,076.8	\$2,036.2
Industrial Control	2,516.3	2,547.1	2,199.6	2,035.9	1,835.3	1,691.5	1,743.9	1,626.8	1,653.5	1,491.4	1,400.2
Space and Aviation Control	2,339.1	1,956.9	1,640.0	1,527.4	1,432.0	1,674.9	1,933.1	2,132.3	2,071.3	2,004.1	1,839.6
Other	130.8	136.9	144.9	133.3	125.2	172.3	152.0	184.7	387.6	486.3	581.0
Total sales	\$8,426.7	\$8,027.5	\$7,311.6	\$6,731.3	\$6,057.0	\$5,963.0	\$6,222.6	\$6,192.9	\$6,309.1	\$6,058.6	\$5,857.0
Operating Profit^{1,2,3}											
Home and Building Control	\$ 348.9	\$ 290.2	\$ 345.8	\$ 308.6	\$ 236.5	\$ 232.7	\$ 193.4	\$ 229.1	\$ 237.0	\$ 225.1	\$ 216.1
Industrial Control	314.2	309.2	254.9	233.8	206.6	189.7	156.9	224.0	219.5	136.8	119.4
Space and Aviation Control	334.0	255.7	163.3	127.6	80.9	148.1	175.8	226.1	200.4	111.5	(141.9)
Other	31.2	18.8	6.2	2.8		(1.8)	(9.5)	(3.1)	18.8	20.8	(51.6)
Discontinuance of product lines ⁴											(150.8)
Total operating profit	1,028.3	873.9	770.2	672.8	524.0	568.7	516.6	676.1	675.7	494.2	(8.8)
Operating profit as a percent of sales	12.2%	10.9%	10.5%	10.0%	8.7%	9.5%	8.3%	10.9%	10.7%	8.2%	(0.2%)
Interest expense	(113.0)	(101.9)	(81.4)	(83.3)	(75.5)	(68.0)	(89.9)	(89.4)	(106.0)	(135.2)	(254.1)
Litigation settlements						32.6	287.9				
Gain on sale of assets									21.7	340.1	33.7
Equity income	11.7	12.9	13.3	13.6	10.5	17.8	15.8	14.6	11.5	33.0	9.8
General corporate expense	(97.7)	(81.7)	(91.9)	(97.6)	(89.3)	(72.6)	(95.7)	(91.9)	(86.5)	(56.2)	(49.5)
Income before income taxes	\$ 829.3	\$ 703.2	\$ 610.2	\$ 505.5	\$ 369.7	\$ 478.5	\$ 634.7	\$ 509.4	\$ 516.4	\$ 675.9	\$ (268.9)
External sales by region											
United States	\$5,201.6	\$4,843.5	\$4,477.9	\$4,087.5	\$3,824.7	\$3,895.1	\$4,014.9	\$4,100.2	\$4,302.4	\$4,347.0	\$4,216.5
Europe	2,246.0	2,136.1	1,981.7	1,858.9	1,528.5	1,441.2	1,556.3	1,428.4	1,392.1	1,144.8	1,153.6
Other areas	979.1	1,047.9	852.0	784.9	703.8	626.7	651.4	664.3	614.6	566.8	486.9
Total sales	\$8,426.7	\$8,027.5	\$7,311.6	\$6,731.3	\$6,057.0	\$5,963.0	\$6,222.6	\$6,192.9	\$6,309.1	\$6,058.6	\$5,857.0
Additional information											
Average number of common shares outstanding	126.1	127.1	126.6	127.1	129.4	134.2	138.5	140.9	151.8	170.4	170.3
Return on average shareowners' equity	22.8%	20.8%	19.7%	17.1%	15.6%	18.4%	13.8%	19.2%	20.6%	33.5%	Loss
Shareowners' equity per average common share	\$ 22.09	\$ 18.80	\$ 17.44	\$ 16.09	\$ 14.57	\$ 13.48	\$ 13.10	\$ 13.25	\$ 11.99	\$ 11.99	\$ 10.04
Price/Earnings ratio ⁵	16.6	18.5	20.7	18.6	14.7	14.3	11.5	13.9	9.1	6.5	Loss
Percent of debt to total capitalization	35%	36%	31%	28%	32%	28%	28%	30%	30%	30%	39%
Research and development											
Honeywell-funded	\$ 481.9	\$ 446.6	\$ 353.3	\$ 323.2	\$ 319.0	\$ 337.4	\$ 312.6	\$ 300.7	\$ 279.6	\$ 283.5	\$ 288.9
Customer-funded	\$ 300.3	\$ 322.5	\$ 341.4	\$ 336.6	\$ 340.5	\$ 404.8	\$ 390.5	\$ 373.5	\$ 417.5	\$ 460.9	\$ 388.9
Capital expenditures	\$ 353.0	\$ 298.3	\$ 296.5	\$ 238.1	\$ 262.4	\$ 232.1	\$ 244.1	\$ 240.2	\$ 251.5	\$ 268.0	\$ 292.4
Depreciation and amortization	\$ 327.9	\$ 319.6	\$ 287.5	\$ 292.9	\$ 287.4	\$ 284.9	\$ 292.7	\$ 286.0	\$ 283.0	\$ 294.8	\$ 306.9
Employees at year-end	57,000	57,500	53,000	50,100	50,800	52,300	55,400	58,200	60,300	65,300	70,900

¹Operating profit in 1998 includes \$23.6 gain on litigation settlements as follows: Home and Building Control, \$4.6; Industrial Control, \$5.3; Space and Aviation Control, \$1.8; Other, \$11.5; and General Corporate Expense, \$0.4. Operating profit in 1997 includes \$77.1 gain on sale of businesses as follows: Home and Building Control, \$5.7 and Industrial Control, \$71.4.

²Operating profit is net of special charges amounting to \$53.7, \$90.7, \$62.7, \$51.2, \$128.4, \$81.6, and \$101.9 in 1998, 1997, 1994, 1993, 1992, 1989, and 1988, respectively, as follows: Home and Building Control, \$25.8, \$46.9, \$28.7, \$9.9, \$42.7, \$28.4, and \$22.5; Industrial Control, \$25.8, \$40.8, \$14.4, \$9.0, \$38.6, \$32.7, and \$9.3; Space and Aviation Control, \$1.4, \$0.0, \$19.6, \$7.4, \$34.9, \$12.1, and \$27.6; Other, \$0.0, \$3.0, \$0.0, \$16.4, \$2.6, \$3.1, and \$27.2; and General Corporate Expense, \$0.7, \$0.0, \$0.0, \$8.5, \$9.6, \$5.3, and \$15.3.

³Operating profit is net of the additional operating expense impact of adopting SFAS 106 and SFAS 112 amounting to \$16.4 and \$3.8, respectively, in 1992 as follows: Home and Building Control, \$4.3 and \$1.0; Industrial Control, \$4.0 and \$0.9; Space and Aviation Control, \$7.0 and \$1.6; Other, \$0.5 and \$0.1; and General Corporate Expense, \$0.6 and \$0.2.

⁴Operating profit includes provision for discontinuance of product lines amounting to \$150.8 in 1988 as follows: Home and Building Control, (\$31.1); Industrial Control, \$4.8; Space and Aviation Control, \$23.8; and Other, \$153.3.

⁵Price/Earnings ratio calculated using basic earnings per common share from continuing operations.

OPERATIONS

Sales Honeywell's sales increased 5 percent to \$8.427 billion in 1998, compared with \$8.028 billion in 1997 and \$7.312 billion in 1996. The 1998 increase in sales was driven by strong growth in Space and Aviation Control offset by declines in Industrial Control and Home and Building Control's consumer products business. Sales in the United States of \$5.202 billion were up 7 percent, primarily as a result of increased volume in Space and Aviation Control. International sales of \$3.225 billion increased 4 percent in local currency terms, and 1 percent after consideration of the stronger U.S. dollar. U.S. export sales, including exports to foreign affiliates, were \$1.211 billion in 1998 compared with \$1.165 billion in 1997 and \$973 million in 1996.

In 1997, sales benefited from strong demand in Space and Aviation Control's commercial aviation and commuter jet businesses and the acquisition of Measurex Corporation. Sales growth in 1996 was the result of increased commercial OEM business and the introduction of new products in all three businesses.

Cost of Sales Cost of sales was \$5.677 billion in 1998, or 67.4 percent of sales, compared with \$5.425 billion (67.6 percent) in 1997 and \$4.975 billion (68.0 percent) in 1996. The decrease in cost as a percent of sales in 1998 was due to improvements in Industrial Control, offset by deterioration in Home and Building Control's consumer products business driven by lower sales. In 1997, cost as a percentage of sales decreased due to a mix of higher margin products, primarily in the Space and Aviation Control business. Cost as a percentage of sales decreased slightly in 1996 due to improved gross-margins in the commercial Space and Aviation Control business.

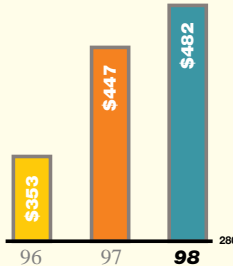
Research and Development Honeywell spent \$482 million, or 5.7 percent of sales, on research and development in 1998, compared with \$447 million (5.6 percent) in 1997 and \$353 million (4.8 percent) in 1996. The additional spending in 1998 was a result of increased investment in Space and Aviation Control as it continues to invest in market leading technology platforms. Honeywell expects to maintain or slightly decrease its current rate of R&D spending in 1999 as a result of a strong technology position in many core markets. Honeywell also received, primarily from the U.S. government, \$300 million in funds for customer-funded research and development in 1998, compared with \$323 million in 1997 and \$341 million in 1996.

Other Expenses and Income Selling, general and administrative expenses were \$1.318 billion, or 15.6 percent of sales in 1998, compared with \$1.359 billion (16.9 percent) in 1997 and \$1.313 billion (18.0 percent) in 1996. Selling, general and administrative expenses have declined almost 320 basis points since 1995 as a result of the continued emphasis on improving processes, investment in information systems, productivity and continued consolidation of our selling, general and administrative functions. Net interest expense was \$102 million in 1998, \$93 million in 1997 and \$73 million in 1996. Interest expense was 7.8 percent of average debt in 1998, compared with 7.8 and 8.3 percent in 1997 and 1996, respectively. Information concerning Honeywell's exposure to, and management of, interest rate risk through the use of derivative financial instruments is provided on Page 35 and in Notes 6, 14 and 15 to the Financial Statements on pages 47, 48 and 49, respectively.

Earnings of companies owned 20 percent to 50 percent (primarily Yamatake Corporation), which are accounted for using the equity method, were \$12 million in 1998, \$13 million in 1997 and \$13 million in 1996.

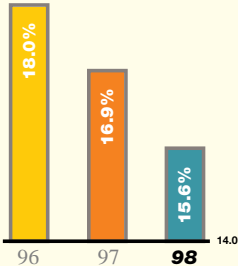
Special Charges In 1998, Honeywell's management, with the approval of the Board of Directors, committed itself to a plan of action and recorded special charges of \$53.7 million intended to reduce operating costs and improve margins. The special charges by segment are as follows: \$25.8 million in Home and Building Control; \$25.8 million in Industrial Control; \$1.4 million in Space and Aviation Control; and \$0.7 million at the corporate level. Special charges include costs for work force reductions, worldwide

Research and Development Expenses
(Dollars in Millions)



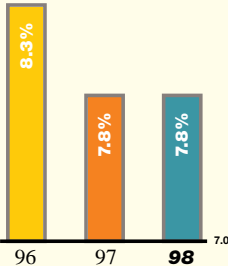
Investments in R&D allow Honeywell to maintain its leadership in technology.

Selling, General and Administrative Expenses
(Percent of Sales)



With focused efforts on Honeywell Quality Value Operational Excellence programs, SG&A continues to drop as a percent of sales.

Interest Expense
(Percent of Average Debt)



Honeywell manages its exposure to interest rate risk with a portfolio of swaps.

facilities consolidations, reorganizations and other cost reductions. The work force reduction costs of \$45.5 million primarily include severance costs related to involuntary termination programs instituted to improve efficiency and reduce costs. Approximately 1,200 employees have been or will be terminated. Facility consolidation costs amounting to \$6.0 million are primarily associated with combining field office locations, and other cost reductions total \$2.2 million. For more information on the special charges, see Note 3 to the Financial Statements on page 45.

In the second half of 1997, Honeywell recorded special charges of \$90.7 million. The actions taken included productivity initiatives and the rationalization of the Honeywell and Measurex product lines. Special charges were recorded by Home and Building Control (\$46.9 million) and Industrial Control (\$40.8 million) with an additional \$3.0 million of special charges recorded by an operation included in the Other operating segment.

Litigation Settlements In December 1998, Honeywell was awarded a favorable settlement on long-standing litigation claims. Proceeds, after expenses, resulted in a gain of \$23.6 million.

Sales of Businesses On July 5, 1998, Honeywell sold Honeywell-Measurex Data Measurement Corporation located in Gaithersburg, MD, to Metrika Systems Corporation for \$29.0 million in cash. The gain on the sale of this business and the impact on the financial statements and results of operations were immaterial. In 1997, Honeywell sold the net assets of Industrial Control's solenoid valve business for approximately \$102 million, resulting in a gain of \$64.3 million. Additionally in 1997, Honeywell sold the control valve business of the Industrial Control business segment and a small security monitoring business related to Home and Building Control for approximately \$24 million in cash and receivables for a gain of \$12.8 million.

Income Taxes The provision for income taxes was \$257 million in 1998 or 31 percent, compared with \$232 million in 1997 (33 percent) and \$208 million in 1996 (34 percent). The 1998 effective income tax rate was reduced as a result of a settlement with U.S. tax authorities on previously questioned items. Further information about income taxes is provided in Note 5 to the Financial Statements on page 46.

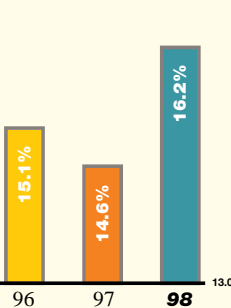
Net Income Honeywell's net income increased 21 percent in 1998, primarily due to the benefits of Honeywell Quality Value (HQV) Operational Excellence, focused on reducing costs. Net income was \$572 million in 1998, compared with \$471 million in 1997 and \$403 million in 1996. Honeywell achieved a 22 percent increase in its Basic Earnings Per Share in 1998 despite an after-tax provision for special charges of \$34.9 million (\$0.28 per share). These special charges were mostly offset by the after-tax gain on a litigation settlement of \$14.2 million (\$0.11 per share) and the favorable impact of a settlement with U.S. tax authorities on previously questioned items of \$16.7 million (\$0.13 per share). Basic and Diluted Earnings Per Share were \$4.54 and \$4.48, respectively, in 1998, compared with \$3.71 and \$3.65 in 1997 and \$3.18 and \$3.11 in 1996.

Return Measurements Return on Equity (ROE) was 22.8 percent in 1998, 20.8 percent in 1997 and 19.7 percent in 1996. Return on Investment (ROI) was 16.2 percent in 1998, 14.6 percent in 1997 and 15.1 percent in 1996. Return on Investment increased significantly in 1998 due to increased operating margin and more efficient use of assets.

Economic Value Added (EVA), calculated by subtracting the cost of capital from operating profits net of tax, continued to improve to \$165 million in 1998, compared to \$95 million in 1997, and \$92 million in 1996.

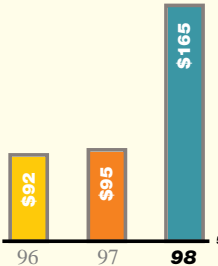
Other Operating Segments The "other" category, which generated revenues of \$131 million, \$137 million and \$145 million in 1998, 1997 and 1996, respectively, is primarily the result of Honeywell's research operations. Operating profit for the Other operations totaled \$31 million in 1998, compared to \$19 million in 1997 and \$6 million in 1996. The 1998 increase was primarily the result of the applicable portion of the favorable litigation settlement. The operating profit increase in 1997 was driven primarily from improved performance in the research centers and lower environmental remediation costs associated with discontinued businesses.

Return on Investment



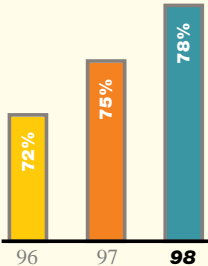
ROI improved in 1998 due to increased profitability and efficient asset utilization.

Economic Value Added
(Dollars in Millions)



EVA increased significantly in 1998 as Honeywell continues to focus on value creating activities.

U.S. Employees on Performance Pay
(Percent of total U.S. employees)



By having employees' pay based on Honeywell performance, employees' interests are aligned with the shareowners'.

Management's Discussion and Analysis

Currency The U.S. dollar strengthened 3 percent in 1998 compared with 1997 based on the weighted average of profits denominated in the principal foreign currencies in countries where Honeywell products and services were sold. A stronger dollar has a negative effect on international results because foreign exchange denominated transactions translate into fewer U.S. dollars. Information about Honeywell's exposure to, and management of, currency risk through the use of derivative financial instruments is provided on page 35 and in Notes 6, 14 and 15 to the Financial Statements on pages 47, 48 and 49, respectively.

Inflation Highly competitive market conditions have minimized inflation's impact on the selling prices of Honeywell's products and the cost of its purchased materials. Productivity improvements and cost-reduction programs have largely offset the effects of inflation on other costs and expenses.

Employment Honeywell employed 57,000 people worldwide at year-end 1998, compared with 57,500 employees in 1997 and 53,000 employees in 1996. Approximately 30,750 employees work in the United States, with 26,750 employed in other regions, primarily in Europe. Total compensation and benefits in 1998 were \$3.2 billion, or 43 percent of total costs and expenses. Sales per employee were \$147,800 in 1998, compared with \$139,600 in 1997 and \$138,500 in 1996.

Environmental Matters Honeywell is committed to protecting the environment, both through its products and in its manufacturing operations. A number of its products are designed to reduce energy consumption and eliminate hazardous materials from the environment. The company has also established effective internal programs to foster compliance with environmental laws and regulations worldwide, and increase environmental awareness, health and safety.

Honeywell's use and release of chemicals to the environment continues to decline steadily, and releases of toxic and ozone-depleting chemicals are being phased out well ahead of regulatory requirements. Honeywell has increased its commitment to pollution prevention; establishing company-wide environmental health and safety goals targeting reductions in air emissions, hazardous waste and energy consumption, and the recycling of solid wastes generated, while decreasing the costs of managing wastes. For more information on these environmental matters, see Note 20 to the Financial Statements on page 55.

New Accounting Standards In June 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 130, "Reporting Comprehensive Income," which was adopted by Honeywell beginning January 1, 1998. SFAS 130 requires the reporting of comprehensive income and its components in the general-purpose financial statements. This Statement also requires that an entity classify items of other comprehensive income by their nature in an annual financial statement. Honeywell has disclosed this information through a Statement of Shareowners' Equity on page 43.

In June 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 131, "Disclosures about Segments of an Enterprise and Related Information," which was adopted by Honeywell beginning January 1, 1998. SFAS 131 redefines how operating segments are determined and requires disclosure of certain financial and descriptive information about a company's operating segments. Honeywell has concluded that the current reportable segments are consistent with the "management approach" methodology outlined in SFAS 131. The additional disclosures can be found in Note 19 to the Financial Statements on page 52.

In February 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits," which is effective for fiscal years beginning after December 15, 1997. SFAS 132 revises and standardizes disclosures required by SFAS 87, SFAS 88 and SFAS 106. Honeywell has adopted this standard for its 1998 fiscal year and the required disclosures can be found in Note 21 to the Financial Statements on page 56.

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities" which is effective for Honeywell on January 1, 2000. SFAS 133 requires companies to record derivatives on the balance sheet as assets or liabilities, measured at fair value. Gains or losses resulting from changes in the values of those derivatives would be accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. Honeywell is currently reviewing the standard and its effect on the financial statements.

In 1998, the American Institute of Certified Public Accountants issued Statement of Position (SOP) 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use," which is effective for fiscal years beginning after December 15, 1998. Honeywell has elected to adopt this SOP effective January 1, 1998. The accounting change has a positive impact on Income before Income Taxes and Net Income. The planned impact of the change to Income before Income Taxes and Net Income for 1998 was \$44.1 million and \$29.5 million, respectively. Basic and Diluted Earnings per share were planned to increase \$0.23 as a result of the change. Since the effect of the accounting change is to account for software in a manner similar to other capital items such as property, plant, and equipment, management chose to divert other capital expenditures to software related expenditures in 1998. This accelerated the amount spent on capitalized software from the planned level of \$44.1 million to \$52.2 million in 1998.

In October 1997, the American Institute of Certified Public Accountants issued Statement of Position (SOP) 97-2, "Software Revenue Recognition." This SOP provides guidance on specific accounting issues that are present in the recognition and measurement of software revenue. Honeywell has adopted this SOP effective January 1, 1998, and the impact on results of operations and financial position is immaterial.

In 1998, the American Institute of Certified Public Accountants issued Statement of Position (SOP) 98-5, "Reporting on the Costs of Start-Up Activities," which is effective for fiscal years beginning after December 15, 1998. This SOP requires that companies expense start-up costs and organizational costs as they are incurred. Honeywell has adopted this SOP effective January 1, 1999, and the impact on results of operations and financial position is expected to be immaterial.

Safe Harbor Cautionary Statement Any statements in this report regarding Honeywell's outlook for its businesses and their respective markets, such as projections of future performance, statements of management's plans and objectives, forecasts of market trends and other matters, are forward-looking statements, some of which may be identified by such words or phrases as "will likely result," "are expected to," "will continue," "outlook," "is anticipated," "estimate," "project" or similar expressions. No assurance can be given that the results in any forward-looking statement will be achieved and actual results could be affected by one or more factors which could cause them to differ materially. For these statements, Honeywell claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

The following is a summary of certain factors, the results of which, if markedly different from Honeywell's planning assumptions, could cause Honeywell's future results to differ materially from those expressed in any forward-looking statements contained in this report:

- foreign currency translations of sales denominated in other currencies, which may fluctuate adversely based on local currency valuations;
- changes in macroeconomic conditions in those regions throughout the world in which Honeywell does business, such as those which have recently occurred in Asia, Latin America and Eastern Europe, or changes in trade or monetary policies, any of which may affect customer demand for the company's products and services;
- risks pertaining to performance and energy retrofit contracts, including dependence on the performance of third parties;
- various competitive pressures, such as new technologies, industry consolidation and deregulation of certain industries;
- the ability of material suppliers or key customers of the company to reduce or eliminate risks to their businesses or operations arising from the year 2000 issue;
- availability of intellectual property rights for newly developed products or key technologies; and
- significant acquisitions or divestitures.

Please refer to Honeywell's annual report on Form 10-K for the fiscal year ended December 31, 1998, and subsequent quarterly reports on Form 10-Q, as filed with the Securities and Exchange Commission, for a more detailed discussion of these and other factors that could cause Honeywell's actual results in future periods to differ materially from those projected in any forward-looking statements.

FINANCIAL POSITION

Financial Condition At year-end 1998, Honeywell's capital structure was comprised of \$179 million of short-term debt, \$1.299 billion of long-term debt and \$2.786 billion of shareowners' equity. The ratio of debt-to-total capital was 35 percent, compared with 36 percent in 1997 and 31 percent at year-end 1996. Total debt increased \$155 million during 1998, to fund general operations.

Shareowners' equity increased \$396 million in 1998 driven by net income of \$572 million, stock option exercises and employee stock plan issuances of \$122 million and accumulated foreign currency translation of \$15 million. The gross increase of \$709 million was offset by \$143 million of dividends, \$160 million of treasury stock purchases, and a \$10 million change in the pension liability adjustment.

Cash Generation and Deployment In 1998, \$779 million of cash was generated from operating activities, compared with \$645 million in 1997, and \$494 million in 1996. The increase in 1998 was largely due to additional net income. In 1998, cash generated from investing and financing activities included \$252 million from the issuance of debt, \$29 million of proceeds from the sale of a business, \$68 million of proceeds from the sale of other assets and \$60 million of proceeds from the exercise of stock options. In 1998, Free Cash Flow, which is cash generated from operating and investing activities excluding acquisitions and the proceeds from the sales of businesses, improved to \$495 million. In 1998, these funds were used to support \$258 million of acquisitions, net of cash acquired and escrowed, \$143 million of dividend payments and \$160 million of payments for share repurchases. Cash balances increased \$172 million in 1998.

Controlled Working Capital Controlled working capital, which consists of trade and long-term receivables and inventories, offset by accounts payable and customer advances, consumed \$6 million of cash in 1998, compared with a usage of \$45 million in 1997. Average working capital as a percentage of sales improved 70 basis points to 24.0 percent in 1998 compared with 24.7 percent in 1997 and 24.6 percent in 1996. The decrease in controlled working capital as a percent of sales in 1998 was primarily driven by additional customer advances and a decrease in receivables.

Management's Discussion and Analysis

Investment Honeywell continues to invest in its businesses at levels it believes to be necessary to enhance its technological leadership position. Capital expenditures for property, plant, equipment and software were \$353 million in 1998, compared with \$298 million in 1997 and \$296 million in 1996, while depreciation charges were \$250 million in 1998. The increase in 1998 capital expenditures was primarily driven by the adoption of SOP 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use," which resulted in \$52 million of capitalized software costs as described on page 32. During 1998, Honeywell invested an additional \$281 million in complementary business acquisitions (see Note 2 to the Financial Statements on page 45). In addition, Honeywell invested \$482 million in research and development activities in 1998, compared with \$447 million in 1997 and \$353 million in 1996.

Share Repurchase Programs In October 1997, the Board of Directors authorized a program to repurchase \$350 million of Honeywell shares of which \$160 million was used during 1998 and \$116 million in 1997. In October of 1998, the Board of Directors authorized a new program to repurchase \$400 million of Honeywell shares, of which none has been used. The purpose of the repurchase program is to acquire shares to be issued as part of Honeywell's Stock and Incentive Plans and other issuances as described in Note 17 to the Financial Statements on page 50. Honeywell repurchased a total of \$160 million of shares in 1998, \$154 million in 1997 and \$163 million in 1996.

At year-end 1998, Honeywell had issued 188 million shares, of which 126 million were outstanding. On December 31, 1998, there were 30,533 shareowners of record. At year-end 1997, Honeywell had 188 million shares issued, 126 million shares outstanding and 30,821 shareowners of record.

Dividends Honeywell has paid a quarterly dividend since 1932 and has increased the annual payout per share in each of the last 23 years. In October 1997, the Board of Directors approved an additional 4 percent increase in the dividend to \$1.12 per share effective in the fourth quarter 1997. In October of 1998, the Board of Directors approved an additional 4 percent increase in the dividend to \$1.16 per share effective in the fourth quarter of 1998. Honeywell paid \$1.13 per share in dividends in 1998, compared with \$1.09 per share in 1997 and \$1.06 in 1996.

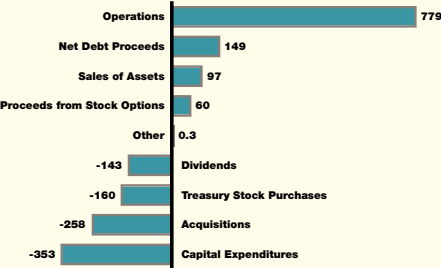
Employee Stock Programs In 1998, Honeywell contributed 555,746 shares of Honeywell common stock to U.S. employees under the Honeywell Savings and Stock Ownership Plan. The number of shares contributed under this program is based on employee savings levels and company performance. Additionally in 1998, new stock purchase programs were initiated in the U.S., Canada and several European countries to increase employee ownership of Honeywell stock. Under these programs, employees who are participants in the program can buy stock at a discount from market prices. Employees purchased 290,959 shares of stock pursuant to the U.S. and International Employee Stock Purchase Plans established in 1998. For more information on these plans, see Note 17 to the Financial Statements on page 50.

Stock Performance The market price of Honeywell stock ranged from \$58 3/4 to \$96 3/4 in 1998, and was \$75 3/4 at year-end. Book value per common share at year-end was \$22.09 in 1998, \$18.80 in 1997 and \$17.44 in 1996.

Pension Contributions Cash contributions to Honeywell's pension and retirement plans were \$155 million in 1998, \$215 million in 1997 and \$201 million in 1996.

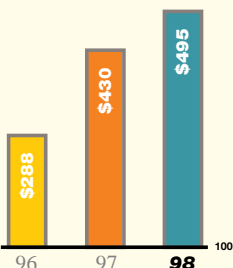
Taxes In 1998, Honeywell paid \$277 million in taxes compared to \$204 million in 1997. The amount Honeywell accrued for income taxes and related interest decreased \$10 million from 1997.

Cash Generation and Deployment



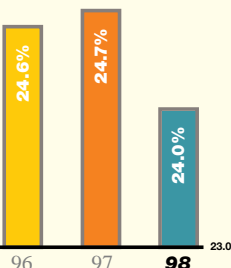
With strong cash generated by operations, Honeywell is able to reinvest in its business with capital expenditures and acquisitions and add value for shareowners through dividend payments and share repurchases.

Free Cash Flow



Expanding free cash flows affords more opportunities to accelerate growth.

Controlled Working Capital



The decrease in 1998 Controlled Working Capital was driven by improvements in Space and Aviation Control and Europe.

Liquidity Short-term debt at year-end 1998 was \$179 million, consisting of no commercial paper, \$53 million of notes payable and \$126 million of current maturities of long-term debt. Short-term debt at year-end 1997 totaled \$146 million, consisting of \$43 million of commercial paper, \$39 million of notes payable and \$64 million of current maturities of long-term debt.

Through its banks, Honeywell has access to various credit facilities, including committed credit lines for which Honeywell pays commitment fees and uncommitted lines provided by banks on a best-efforts basis. The interest rates for Honeywell's material lines of credit are indexed to a rate, such as Prime, LIBOR or Commercial Paper. Available general-purpose lines of credit at year-end 1998 were \$1.771 billion. This consisted of \$1.325 billion of committed credit lines to meet Honeywell's financing requirements, including support of commercial paper and bank note borrowings, and \$446 million of uncommitted credit lines available to certain foreign subsidiaries. This compared with \$1.683 billion of available credit lines at year-end 1997, consisting of \$1.325 billion of committed credit lines and \$358 million of uncommitted credit lines. In August 1997, Honeywell and its wholly-owned subsidiaries, Honeywell Canada Limited and Honeywell Finance B.V., filed a shelf registration statement which provides for the issuance of up to \$500 million, in the aggregate, of debt securities by Honeywell or such subsidiaries, with the guarantee of Honeywell. On June 15, 1998, Honeywell issued \$250 million in debentures with a coupon rate of 6 3/4 percent maturing on June 15, 2028. At December 31, 1998, \$250 million remained available for issuance under the shelf registration. Long-term debt maturities consist of \$126 million in 1999, \$78 million in 2000 and \$117 million in 2001. In addition, Honeywell has an agreement with a major financial institution whereby it may convert designated pools of trade accounts receivable up to \$50 million Canadian dollars on an ongoing basis for cash (see Note 8 to the Financial Statements on page 47).

Cash and short-term investments totaled \$313 million at year-end 1998 and \$159 million at year-end 1997. Honeywell believes its available cash, committed credit lines, receivables program and access to the public debt markets, through its debt securities and commercial paper programs, provide adequate short-term and long-term liquidity.

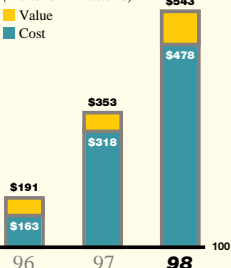
Credit Ratings As of December 31, 1998, Honeywell's credit ratings for long-term and short-term debt, respectively, were A/A-1 by Standard and Poor's Corporation, A2/P1 by Moody's Investors Service, Inc. and A/D-1 by Duff and Phelps Corporation.

Risk Management Honeywell is exposed to market risk from changes in interest rates and foreign currency exchange rates. To mitigate the risk from these exposures, Honeywell enters into various hedging transactions through derivative financial instruments that have been authorized pursuant to its corporate policy. Honeywell policy prohibits the use of derivative financial instruments for trading or other speculative purposes, and Honeywell is not a party to leveraged financial instruments.

Foreign Exchange Honeywell primarily uses foreign exchange forwards and purchased options to hedge exposures to adverse changes in foreign exchange rates (see Notes 6 and 15 to the Financial Statements on pages 47 and 49, respectively). Such exposures have resulted from cross-border transactions principally in Belgian francs, Deutsche marks and Great Britain pounds. Foreign exchange contracts reduce Honeywell's overall exposure to exchange rate movements, since gains and losses on these contracts offset losses and gains on the underlying exposures. Transactions that are hedged include foreign currency net asset and net liability exposures on the balance sheet, anticipated transactions, firm purchase orders and firm sales commitments. At year-end 1998, the notional amount of outstanding foreign exchange contracts were \$1.072 billion.

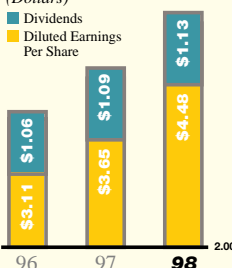
Interest Rates Honeywell manages its exposure to interest rate movements and the cost of borrowing through the use of interest rate swaps by maintaining a proportionate relationship of fixed rate debt to total debt between a minimum and maximum percentage as set by management. To manage this mix in a cost efficient manner, Honeywell enters into interest rate swap agreements, in which it agrees to exchange, at specified intervals, the difference between fixed and variable interest amounts calculated by reference to an agreed upon notional principle amount (see Notes 14 and 15 to the Financial Statements on pages 48 and 49, respectively). At year-end 1998, the notional amount of outstanding interest rate swaps was \$1.000 billion.

Share Repurchase Program



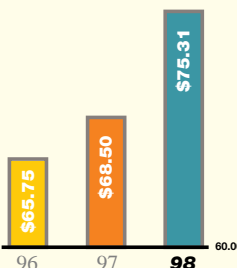
Creating shareowner value is a priority for Honeywell. The share repurchase program is one of the mechanisms for expanding value for Honeywell shareowners.

Diluted Earnings Per Share and Dividends



Honeywell has increased its dividend payout for the 23rd consecutive year.

Stock Performance



The Honeywell strategies of growth and margin expansion create shareowner value as reflected by the increasing stock price.

Management's Discussion and Analysis

Value at Risk To estimate the maximum potential loss in the fair market value of financial instruments that may arise from adverse market movements in foreign exchange rates and interest rates, Honeywell uses a "value at risk" statistical model. The value at risk estimation utilizes weighted historical foreign exchange rates and interest rates to estimate the volatility and correlation of these rates in the future. The calculated volatility is used to estimate the potential loss in the fair market value of financial instruments at a specified probability level. The value at risk methodology used by Honeywell uses variance-covariance statistical modeling and includes debt, interest rate swaps and foreign exchange hedges. The estimated value at risk amounts represent the maximum potential loss in the fair market value of Honeywell's financial instruments from adverse changes in foreign exchange rates and interest rates based on a five-day time horizon and a 95 percent confidence level on December 31, 1998.

The value at risk for the combined portfolio was \$11.8 million at December 31, 1998. This amount includes the diversification benefit of analyzing the value at risk, including the interest rates and foreign exchange on a combined basis as compared to individually, as changes in market conditions affect interest rates and foreign exchange differently. The average value at risk represents the simple average of the quarterly amounts for the past year. The value at risk for the combined portfolio and the individual components are as follows:

Value at Risk (In Millions)	Average	December 31	
	1998	1998	1997
Combined Portfolio	\$9.5	\$11.8	\$6.8
Foreign Exchange	\$4.4	\$ 3.6	\$6.1
Interest Rates	\$6.8	\$10.4	\$2.3

The increase in the value at risk associated with interest rates is primarily due to the extended duration of Honeywell's debt portfolio from the issuance of a 30-year bond in 1998. Value at risk measures the potential decrease in the fair market value of financial instruments given estimated changes in foreign exchange rates and interest rates. Long-term financial instruments, which are price sensitive to interest rates, will result in a higher calculation of value at risk. However, changes in value of debt instruments used for financing operations do not affect the cash flows of Honeywell. Consequently, the increase in the value at risk associated with interest rates is not considered to be a material risk to the company.

The value at risk amounts presented above for foreign exchange and interest rates do not consider the potential effect of favorable movements in market factors nor does the value at risk model include all of the underlying exposures that the hedges are designed to cover. Anticipated transactions, firm commitments and accounts receivable and accounts payable denominated in foreign currencies, which certain of these instruments are intended to hedge, were excluded from the model due to model limitations. Since Honeywell utilized foreign exchange contracts to hedge foreign currency transactions, a loss in fair value for these instruments is generally offset by increases in the value of the underlying transaction. The quantitative information generated by the value at risk model is limited by the parameters built into the model that rely on historical results, which may not be representative of future events. Consequently, Honeywell relies on the experience and expertise of management's regular review of its financial instruments and the current market environment to manage its exposure to foreign exchange rates and interest rates.

Year 2000 Readiness Disclosures

Background Computer programs which were written using two digits (rather than four) to define the applicable year may recognize a date using "00" as the year 1900 rather than the year 2000. This is generally referred to as the "year 2000 issue," which may affect the performance of computer programs, hardware, software and other products with embedded computer technology that is date sensitive. Unless corrective action is taken to ensure that such items are "year 2000 ready," which means that they will be able to process dates and times in such a manner that their technical and functional requirements will continue to be met without interruption for the year 2000, they may generate erroneous data or cause systems, equipment or other products to fail.

Honeywell's Year 2000 Program In the fourth quarter of 1995, Honeywell initiated a program to determine whether or not its business systems, operations and products are year 2000 ready. This program addresses the company's information technology systems and other systems with embedded computer technology; products provided to customers; products purchased from suppliers; and most recently, the year 2000 readiness of its significant customers.

Product Readiness Substantially all of Honeywell's current products have been tested internally to ascertain if they are year 2000 ready. Approximately 99 percent of these products are year 2000 ready and the remainder are expected to be so by the end of first quarter 1999. The company expects to complete its tests by the end of first quarter 1999. In some areas of its businesses, Honeywell is conducting external integration tests of year 2000 ready products in existing customer systems to verify that they are compatible with such systems.

Certain older products that are still in use by Honeywell customers and subject to warranties or service contracts, may not be year 2000 ready. Honeywell is formally communicating with distributors and direct customers to make them aware of any potential problems that may result from the use of such products and encouraging them to modify or replace same, or providing warranty or contract service as appropriate. The process is complete except for some of the security products, and communication related to these products is expected to be completed during first quarter 1999. For older products which are not year 2000 ready, and were sold through distributors or are no longer under warranty or service contracts, various means are being employed to raise the awareness of any potential year 2000 problems, including advertising and contracting with external service providers to help identify current owners.

Honeywell realizes that new year 2000 issues may arise, and if so, will notify customers as appropriate.

Supplier Readiness Honeywell has sent questionnaires to substantially all suppliers who furnish products or services to the company, to ascertain whether products or services supplied are year 2000 ready, as well as the effect the year 2000 issue may have on their ability to continue supplying same. At least 300 suppliers have been identified by the company as critical to its business and the various business units are investigating a greater number to verify that critical supplier products or services will be year 2000 ready. Various methods are being used to validate supplier readiness, including symposiums, site visits and telephone interviews. The verification process is expected to be completed during the third quarter of 1999 and contingency plans will be implemented for critical suppliers identified to be at risk.

Internal System Readiness In 1993, prior to the commencement of the Honeywell year 2000 program, the company implemented a program to upgrade most of its key information technology (IT) systems to common applications software packages, with completion scheduled prior to the year 2000. Recent revisions of these packages are marketed as year 2000 ready; however, Honeywell has decided it is necessary to validate this is true in our environment. While Honeywell expects its critical internal business systems to be year 2000 ready by third quarter of 1999, integration testing of the software packages may extend beyond that date. Critical business systems of Honeywell Measurex Corporation, a company acquired in March 1997, are planned to be year 2000 ready by the end of the third quarter of 1999. The remainder of Honeywell's business systems which are considered to have a financial or operational impact on its businesses, are expected to be year 2000 ready by the end of 1999.

The company is still assessing the status of its non-IT systems and making repairs or upgrades to such systems as necessary. It expects to conclude this effort during the third quarter of 1999 for critical non-IT systems, and by the end of 1999 for other non-IT systems which are considered to have a financial or operational impact on its businesses. Honeywell does not expect the costs associated with the remediation of non-IT systems to be material, and such costs are included in the amounts forecasted for contingencies in 1999 as discussed below under the caption "Costs."

Customer Readiness Honeywell recently expanded its year 2000 program to evaluate the readiness of its significant customers to deal with the year 2000 issue and the effect, if any, that it may have on their requirements for Honeywell's products and services. Though Honeywell does not foresee any significant problems in this area, the information collected to date as part of this effort is not sufficient to form a basis for any conclusions regarding customer readiness and its effect, if any, on customer demand for the company's products and services. Honeywell expects to complete its assessment of the readiness of significant customers by July 1999, though no assurance can be given that all customers will respond to its inquiries or that all responses will be accurate.

Risks/Contingency Plans Honeywell's products are used in a wide variety of control applications including, but not limited to, industrial processing control systems, home and building products and automation control systems, and space and aviation control systems. In a most likely worst case scenario, if Honeywell's products are not year 2000 ready, a control application could be disrupted, which could affect the ability of the system in which it is installed to function properly, depending on other safeguards. Similarly, if customers are unable to conduct adequate integration testing of Honeywell's year 2000 ready products within their equipment or systems, they could experience temporary equipment or systems failure if compatibility problems arise. While the company does not expect any worst case scenario to occur, it is working closely with customers of critical systems to advise them of potential problems and the need to complete systems integration testing.

If a critical supplier cannot supply products or services to Honeywell that are year 2000 ready, or if the supplier is adversely affected by the year 2000 issue, that source of supply could be interrupted. This could affect the ability of Honeywell to supply other products or services, or disrupt a business operation which is dependent thereon. Furthermore, if a year 2000 issue affecting a component is not detected by a supplier, it could affect the performance of the product or system of which it becomes a part and possibly cause one or more of the scenarios discussed above to occur. To reduce the risk of such occurrences, Honeywell is taking steps to verify the year 2000 readiness of all critical suppliers as discussed above under the caption "Supplier Readiness." In addition, each of Honeywell's business units is developing contingency plans to identify substitute materials and services, and alternate suppliers.

Honeywell expects that all of its internal applications systems will be year 2000 ready by the end of 1999. However, if its strategy to replace its order management systems in some European countries is not completely executed prior to the year 2000, there may be difficulty in processing customer orders in such countries. Contingency plans have been developed to mitigate such risks and will be implemented if necessary.

Honeywell acquires other companies from time to time as part of its business development strategy, and it anticipates that acquisitions will continue through the year 2000. In the course of conducting due diligence investigations of acquisition candidates, Honeywell endeavors to ascertain whether or not their products or services, or those of their critical suppliers, are year 2000 ready, and whether or not such suppliers and key customers, if any, will be adversely affected by the year 2000 issue. While acquisition candidates may provide certain information or make representations and warranties regarding year 2000 readiness, in some cases, Honeywell may be unable to verify same until the acquisition is completed and the steps outlined herein as part of Honeywell's year 2000 program are undertaken.

Costs Honeywell estimates that historical and future costs associated with its year 2000 program will not exceed \$60 million for fiscal years 1995 through 1999. Approximately \$20 million in costs have been incurred in fiscal year 1998, and \$30 million has been forecasted for the 1999 fiscal year to cover additional costs and contingencies. Funding for the 1998 and 1999 costs was previously forecasted as part of Honeywell's operating expenditures and included in the company's budgets. Management believes that such costs will not have a material impact on the operations, cash flows or financial condition of Honeywell and its subsidiaries, taken as a whole, in future periods.

Management's Discussion and Analysis

The preceding "Year 2000 Readiness Disclosures" contain forward-looking statements of Honeywell's expectations regarding the ability of its products and systems to be year 2000 ready, as well as its ability to assess the readiness of its suppliers and customers, and related risks. These statements relate to future events, the outcome of which is uncertain, and should be read in conjunction with the cautionary factors listed in Exhibit 99(i) to Honeywell's annual report on form 10-K for the fiscal year ended December 31, 1998.

Euro Currency In January 1999, the European Monetary Union (EMU) entered into a three-year transition phase during which a common currency called the Euro was introduced in participating countries. Initially, this new currency is being used for financial transactions, and progressively, it will replace the old national currencies that will be withdrawn by July 2002. The transition to the Euro currency will involve changing budgetary, accounting and fiscal systems in companies and public administrations, as well as the simultaneous handling of parallel currencies and conversion of legacy data.

Uncertainties related to the Euro conversion In 1996, Honeywell began studying the ongoing process of European integration, focussing on issues and opportunities created by the EMU. Task teams were established to develop Honeywell's Euro strategies and policies. The findings of these teams have been integrated into our strategic and operational plans. At this time, there are no significant remaining uncertainties related to the Euro conversion and no material impact has been identified.

Competitive implications Making a broader European market requires product lines to become more international and less local. In 1993, Honeywell restructured and its market focus was changed from a country basis to a European line-of-business approach. Today, our pricing strategies are largely European, except in those instances where technical or cultural market characteristics warrant price differentiation. The expectations of our customers, with respect to the currency to be used in the transition period have been reflected in our changeover strategies, resulting in a pro-active dual currency capability since January 1, 1999. The same approach with our suppliers will allow us to benefit from the increased price transparency on the cost side. Plans are in place, including shared service centers and consolidation of operations, to pursue the economies of scale offered by the single European market. We believe converting to the Euro has no material impact on Honeywell's competitive position.

Information Technology and Other Systems Compliance with European Commission regulations concerning conversion, triangulation and rounding rules related to the Euro introduction, have been addressed in detailed action plans involving all information systems in all Honeywell units, both for in-house and purchased systems. The cost of modification is insignificant, as the action plan builds on new systems implementation required for shared services and Year 2000 readiness. Timelines for implementation have been established, adequate resources are available and contingency plans are in place. We believe converting the information technology and other systems to the Euro has no material impact on Honeywell.

Currency Risk With the convergence of short-term interest rates in the EMU countries, observed during the last two years, the foreign exchange exposure between the currencies of these countries has diminished considerably. Our foreign exchange exposure management has systematically been adapted to this evolution, thereby benefiting from reduced hedging cost. The definitive fixing of the exchange rates will only make this benefit permanent without creating any other issue or opportunity other than eliminating the spread on the spot exchange. All balance sheet exposures between EMU currencies and non-EMU currencies are systematically hedged from month to month. The functional currency will not change to Euro in 1999 in any of the Honeywell units concerned. Current plans call for functional currency conversion by year-end 2001. We do not anticipate this change will have a material impact on Honeywell. We believe converting to the Euro has no material impact on Honeywell's currency exchange cost and/or risk exposure.

Derivatives and Other Financial Instruments, Continuity of Contracts and Taxation We believe converting to the Euro has no material impact on outstanding derivatives, other financial instruments, continuity of contracts or taxation.

Litigation On March 13, 1990, Litton Systems, Inc. filed a legal action against Honeywell in U.S. District Court, Central District of California, Los Angeles, with claims that were subsequently split into two separate cases. One alleges patent infringement under federal law for using an ion-beam process to coat mirrors incorporated in Honeywell's ring laser gyroscopes, and tortious interference under state law for interfering with Litton's prospective advantage with customers and contractual relationships with an inventor and his company, Ojai Research, Inc. The other case alleges monopolization and attempted monopolization under federal antitrust laws by Honeywell in the sale of inertial reference systems containing ring laser gyroscopes into the commercial aircraft market. Honeywell generally denied Litton's allegations in both cases. In the patent/tort case, Honeywell also contested the validity as well as the infringement of the patent, alleging, among other things, that the patent had been obtained by Litton's inequitable conduct before the United States Patent and Trademark Office.

In 1993 and 1995, trials were held in each case and juries initially awarded Litton significant monetary damages. However, those verdicts were set aside by the trial court judge who ordered, at a minimum, new trials on the issue of damages in each case.

Following cross-appeals by the parties of various issues to the Federal Circuit and the U.S. Supreme Court in the patent/tort case, it has been remanded to the trial court for further legal and perhaps factual review with respect to both liability and damages. This review was held in abeyance during a retrial of the anti-trust damages in 1998 and its procedures remain to be defined and scheduled by the trial court.

The retrial of damages in the antitrust case commenced October 29, 1998, and on December 9, 1998, a jury returned a verdict against Honeywell for actual damages in the amount of \$250 million. On January 27, 1999, the trial court entered a treble damages judgment in the total amount of \$750 million for actual and attempted monopolization. Honeywell believes that there is no factual or legal basis for the magnitude of the jury's award and believes that it should be overturned. Honeywell intends to file appropriate post-judgment motions with the trial court and Litton will move to add substantial attorneys fees and costs to the judgment. Honeywell also believes it has very strong arguments that the liability portion of the jury verdict in the first antitrust trial was erroneous. Once the trial court rules on those motions, the parties will have the right to appeal the eventual judgment, as to both liability and damages, to the U.S. Court of Appeals for the Ninth Circuit.

For a detailed discussion of this litigation, see Note 20 to the Financial Statements on page 53.

Report of Management

To the Shareowners of Honeywell Inc.:

The financial statements of Honeywell published in this report were prepared by company management, who is responsible for their integrity and objectivity. The statements have been prepared in accordance with generally accepted accounting principles, applying certain estimates and judgments as required. The financial information elsewhere in this report is consistent with the statements.

Honeywell maintains a system of internal control adequate to provide reasonable assurance that its transactions are appropriately recorded and reported, its assets are protected and its established policies are followed. This system is enforced by written policies and procedures, effective internal audit and a qualified financial staff.

Our independent auditors, Deloitte & Touche LLP, provide an objective independent review by audit of Honeywell's financial statements and issuance of a report thereon. Their audit is conducted in accordance with generally accepted auditing standards.

The audit committee of the board of directors, comprised solely of outside directors, meets periodically and privately with the independent auditors, internal auditors and representatives from management to appraise the adequacy and effectiveness of the audit functions, control systems and quality of our financial accounting and reporting.



Philip M. Palazzari

Vice President and Controller
February 10, 1999



Lawrence W. Stranghoener

Vice President and Chief Financial Officer
February 10, 1999

Independent Auditor's Report

Deloitte & Touche

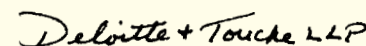


To the Shareowners of Honeywell Inc.:

We have audited the statement of financial position of Honeywell Inc. and subsidiaries as of December 31, 1998 and 1997, and the related statements of income, shareowners' equity, and cash flows for each of the three years in the period ended December 31, 1998. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of Honeywell Inc. and subsidiaries as of December 31, 1998 and 1997, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles.



Deloitte & Touche LLP

Minneapolis, Minnesota
February 10, 1999

Income Statement

Honeywell Inc. and Subsidiaries

Years Ended December 31

(Dollars and Shares in Millions Except Per Share Amounts)

	1998	1997	1996
Sales	\$8,426.7	\$8,027.5	\$7,311.6
Costs and Expenses			
Cost of sales	5,677.0	5,425.1	4,975.4
Research and development	481.9	446.6	353.3
Selling, general and administrative	1,317.9	1,359.4	1,313.1
Gain on sale of businesses		(77.1)	
Litigation settlements	(23.6)		
Special charges	53.7	90.7	
Total Costs and Expenses	7,506.9	7,244.7	6,641.8
Interest			
Interest expense	113.0	101.9	81.4
Interest income	10.8	9.4	8.5
Net Interest	102.2	92.5	72.9
Equity Income	11.7	12.9	13.3
Income before Income Taxes	829.3	703.2	610.2
Provision for Income Taxes	257.3	232.2	207.5
Net Income	\$ 572.0	\$ 471.0	\$ 402.7
Basic Earnings Per Common Share	\$ 4.54	\$ 3.71	\$ 3.18
Average Number of Basic Common Shares Outstanding	126.1	127.1	126.6
Diluted Earnings Per Common Share	\$ 4.48	\$ 3.65	\$ 3.11
Average Number of Diluted Common Shares Outstanding	127.8	129.2	129.5

See accompanying Notes to Financial Statements.

Statement of Financial Position

Honeywell Inc. and Subsidiaries

December 31

(Dollars in Millions)

	1998	1997
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 306.0	\$ 134.3
Short-term investments	7.2	24.9
Receivables	1,906.7	1,837.8
Inventories	1,116.0	1,028.0
Deferred income taxes	285.9	233.2
Total Current Assets	3,621.8	3,258.2
Investments and Advances	269.9	243.8
Property, Plant and Equipment		
Property, plant and equipment	3,355.8	3,045.0
Less accumulated depreciation	(2,097.4)	1,916.3
Net Property, Plant and Equipment	1,258.4	1,128.7
Other Assets		
Long-term receivables	34.0	39.2
Goodwill	952.2	786.0
Intangibles	343.0	376.0
Deferred income taxes	18.9	41.7
Other	672.2	537.8
Total Assets	\$7,170.4	\$6,411.4
LIABILITIES AND SHAREOWNERS' EQUITY		
Current Liabilities		
Short-term debt	\$ 178.9	\$ 146.4
Accounts payable	676.6	634.2
Customer advances	340.2	269.7
Accrued compensation and benefit costs	280.0	271.2
Accrued income taxes	334.4	344.2
Deferred income taxes	18.0	11.3
Other accrued liabilities	624.6	641.9
Total Current Liabilities	2,452.7	2,318.9
Long-Term Debt	1,299.3	1,176.8
Other Liabilities		
Accrued benefit costs	457.3	435.9
Deferred income taxes	66.2	51.4
Other	109.4	39.2
Total Liabilities	4,384.9	4,022.2
Shareowners' Equity		
Common stock—\$1.50 par value		
Authorized—250,000,000 shares		
Issued—1998—187,536,597 shares	281.3	
1997—187,633,023 shares		281.5
Additional paid-in capital	697.6	608.4
Retained earnings	3,835.9	3,407.0
Treasury stock—1998—61,206,715 shares	(2,005.5)	
1997—61,433,075 shares		(1,879.3)
Other comprehensive income	(23.8)	(28.4)
Total Shareowners' Equity	2,785.5	2,389.2
Total Liabilities and Shareowners' Equity	\$7,170.4	\$6,411.4

See accompanying Notes to Financial Statements.

Statement of Cash Flows

Honeywell Inc. and Subsidiaries

Years Ended December 31

(Dollars in Millions)

Cash Flows from Operating Activities

	1998	1997	1996
Net income	\$572.0	\$471.0	\$402.7
Adjustments to reconcile net income to net cash flows from operating activities:			
Depreciation	249.6	246.0	236.1
Amortization of intangibles	78.3	73.6	51.4
Deferred income taxes	(2.6)	(19.5)	38.5
Equity income, net of dividends received	(9.6)	(10.3)	(10.8)
Gain on sale of businesses		(77.1)	
Gain on sale of assets	(9.1)	(7.3)	(12.0)
Contributions to employee stock plans	59.9	48.9	38.2
Increase in receivables	(10.8)	(60.7)	(203.0)
Increase in inventories	(38.5)	(67.1)	(89.9)
Increase (decrease) in accounts payable	(1.6)	38.3	51.8
Increase in customer advances	45.1	45.0	45.9
Increase in accrued income taxes and interest	3.9	49.7	57.4
Increase (decrease) in accrued liabilities	(72.0)	113.2	35.5
Other noncurrent items—net	(85.3)	(199.1)	(148.0)
Net cash flows from operating activities	779.3	644.6	493.8

Cash Flows from Investing Activities

Proceeds from sale of assets	68.0	77.2	90.3
Proceeds from sale of business	29.0	100.6	
Capital expenditures	(353.0)	(298.3)	(296.5)
Investment in acquisitions	(258.2)	(598.4)	(376.2)
(Increase) decrease in short-term investments	1.0	0.4	(0.2)
Other—net	(0.7)	5.6	0.4
Net cash flows from investing activities	(513.9)	(712.9)	(582.2)

Cash Flows from Financing Activities

Net increase (decrease) in short-term debt	(32.1)	(73.4)	18.8
Proceeds from issuance of long-term debt	252.2	597.7	340.4
Repayment of long-term debt	(70.7)	(182.3)	(188.8)
Purchase of treasury stock	(159.6)	(154.3)	(163.2)
Proceeds from exercise of stock options	60.2	44.7	57.3
Dividends paid	(143.2)	(140.1)	(133.5)
Net cash flows from financing activities	(93.2)	92.3	(69.0)

Effect of exchange rate changes on cash

	(0.5)	(16.8)	(7.1)
Increase (decrease) in cash and cash equivalents	171.7	7.2	(164.5)
Cash and cash equivalents at beginning of year	134.3	127.1	291.6
Cash and cash equivalents at end of year	\$306.0	\$134.3	\$127.1

See accompanying Notes to Financial Statements.

Statement of Shareowners' Equity

Honeywell Inc. and Subsidiaries

(Dollars in Millions)

	Total	Retained Earnings ²	Accumulated Other Comprehensive Income ³	Common Stock	Treasury Stock	Paid-in Capital
Beginning balance 1/1/96	\$2,040.1	\$2,805.8	\$121.0	\$282.2	\$(1,650.2)	\$481.3
Comprehensive income						
Net income	402.7	402.7				
Other comprehensive income ¹						
Currency translation adjustments	(52.7)		(52.7)			
Pension liability adjustment ¹	14.9		14.9			
Other comprehensive income	(37.8)		(37.8)			
Comprehensive income	364.9					
Common stock issued	96.9			(0.5)	49.9	47.5
Treasury stock acquired	(163.2)				(163.2)	
Dividends declared on common stock	(133.8)	(133.8)				
Ending balance 12/31/96	\$2,204.9	\$3,074.7	\$ 83.2	\$281.7	\$(1,763.5)	\$528.8
Comprehensive income						
Net income	471.0	471.0				
Other comprehensive income ¹						
Currency translation adjustments	(109.6)		(109.6)			
Pension liability adjustment ¹	(2.0)		(2.0)			
Other comprehensive income	(111.6)		(111.6)			
Comprehensive income	359.4					
Common stock issued	117.9			(0.2)	38.5	79.6
Treasury stock acquired	(154.3)				(154.3)	
Dividends declared on common stock	(138.7)	(138.7)				
Ending balance 12/31/97	\$2,389.2	\$3,407.0	\$ (28.4)	\$281.5	\$(1,879.3)	\$608.4
Comprehensive income						
Net income	572.0	572.0				
Other comprehensive income ¹						
Currency translation adjustments	14.5		14.5			
Pension liability adjustment ¹	(9.9)		(9.9)			
Other comprehensive income	4.6		4.6			
Comprehensive income	576.6					
Common stock issued	122.4			(0.2)	33.4	89.2
Treasury stock acquired	(159.6)				(159.6)	
Dividends declared on common stock	(143.1)	(143.1)				
Ending balance 12/31/98	\$2,785.5	\$3,835.9	\$ (23.8)	\$281.3	\$(2,005.5)	\$697.6

¹All items included in other comprehensive income are shown net of income taxes. The tax effect for the pension liability adjustment was \$(6.2), \$(1.3) and \$9.4 for 1998, 1997 and 1996, respectively.

²Included in retained earnings are undistributed earnings of companies 20 to 50 percent owned, amounting to \$175.1, \$165.5, and \$155.2 at December 31, 1998, 1997 and 1996, respectively.

³Accumulated other comprehensive income is comprised of accumulated currency translation of \$(6.9), \$(21.4) and \$88.2; and pension liability adjustment of \$(16.9), \$(7.0) and \$(5.0) at December 31, 1998, 1997 and 1996, respectively.

See accompanying Notes to Financial Statements.

Notes to Financial Statements

Honeywell Inc. and Subsidiaries (Dollars in Millions Except Per Share Amounts)

NOTE 1 ACCOUNTING POLICIES

Consolidation The consolidated financial statements and accompanying data comprise Honeywell Inc. and subsidiaries. All material intercompany transactions are eliminated.

Estimates The preparation of financial statements in conformity with generally accepted accounting principles requires Honeywell to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates.

Sales Product sales are recorded when title is passed to the customer, which usually occurs at the time of delivery or acceptance. Sales under long-term contracts are recorded on the percentage-of-completion method measured on the cost-to-cost basis for engineering-type contracts and the units-of-delivery basis for production-type contracts. Provisions for anticipated losses on long-term contracts are recorded in full when such losses become evident.

Earnings Per Common Share Basic Earnings Per Share (EPS) is calculated using income available to common shareowners divided by the weighted average of common shares outstanding during the year. Diluted EPS is similar to Basic EPS except that the weighted average of common shares outstanding is increased to include the number of additional common shares that would have been outstanding if the dilutive potential common shares, such as options, had been issued. The treasury stock method is used to calculate dilutive shares, which reduces the gross number of dilutive shares by the number of shares purchasable from the proceeds of the options assumed to be exercised. See Note 4 on page 46 for more information regarding the earnings per share calculations.

Statement of Cash Flows Cash equivalents are all highly liquid, temporary cash investments with an original maturity of three months or less. Cash flows from purchases and maturities of held-to-maturity securities that are not considered cash equivalents are classified as cash flows from investing activities.

Inventories Inventories are valued at the lower of cost or market. Cost is determined using the weighted average method. Market is based on net realizable value. Payments received from customers relating to the uncompleted portion of contracts are deducted from applicable inventories.

Investments Investments in companies owned 20 to 50 percent are accounted for using the equity method.

Property Property is carried at cost and depreciated primarily using the straight-line method over estimated useful lives of 10 to 40 years for buildings and improvements, up to 5 years for software and 3 to 15 years for machinery and equipment.

In 1998, Honeywell adopted Statement of Position (SOP) 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use," and began to capitalize the costs of developing software for internal use. Honeywell previously only capitalized purchased software when costs exceeded \$250 thousand. The amount of software capitalized in 1998 was \$52.2.

Intangibles Intangibles are carried at cost and amortized using the straight-line method over their estimated useful lives of 15 to 40 years for goodwill, 4 to 17 years for patents, licenses and trademarks and 3 to 24 years for other intangibles. Intangibles also include the asset resulting from recognition of the defined benefit pension plan minimum liability, which is amortized as part of net periodic pension cost.

Derivatives Derivative financial instruments are used by Honeywell to manage interest rate and foreign exchange risks. These financial exposures are managed in accordance with Corporate policies and procedures. Honeywell does not hold or issue derivative financial instruments for trading purposes. Derivatives used for hedging purposes must be designated as, and effective as, a hedge of an identified risk exposure at the inception of the contract. Accordingly, changes in the fair market value of the derivative contract must be highly correlated with the changes in the fair market value of the underlying hedged item both at the inception of the hedge and over the life of the hedge contract.

Foreign exchange contracts are accounted for as hedges to the extent they are designated as, and are effective as, hedges of firm or anticipated foreign currency commitments. Any foreign exchange contracts designated but no longer effective as a hedge are marked to market and the related gains and losses are recognized in earnings.

Interest rate contracts designated and effective as a hedge of underlying debt obligations are not marked-to-market, but cash flow from such contracts results in adjustments to interest expense recognized over the life of the underlying debt agreement. Gains and losses from terminated contracts are deferred and amortized over the remaining period of the original contract. Cash flows from such terminations are classified according to the underlying financial instrument the contract was designated to hedge. Open interest rate contracts are reviewed regularly to ensure that they remain effective as hedges of interest rate exposure.

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities" which is effective for Honeywell on January 1, 2000. SFAS 133 requires companies to record derivatives on the balance sheet as assets or liabilities, measured at fair value. Gains or losses resulting from changes in the values of those derivatives would be accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. Honeywell is currently reviewing the standard and its effect on the financial statements.

Foreign Currency Foreign currency assets and liabilities are translated into U.S. dollars using the exchange rates in effect at the statement of financial position date. Results of operations are translated generally using the average exchange rates throughout the period. The effects of exchange rate fluctuations on translation of assets, liabilities and hedges of cash dividend payments from subsidiaries are reported as accumulated foreign currency translation and increased/(decreased) shareowners' equity: \$14.5 in 1998, \$(109.6) in 1997 and \$(52.7) in 1996.

Long-Lived Assets Honeywell evaluates the recoverability of long-lived assets using discounted cash flows when events and circumstances warrant such a review.

Stock-Based Compensation Honeywell uses the recognition and measurement principles of Accounting Principles Board (APB) No. 25 to record its stock options and other stock-based employee compensation awards. The disclosure of the pro forma net income and pro forma earnings per share as if the fair value method of recording stock-based awards had been applied can be found in Note 17 to the Financial Statements on page 50.

Basis of Presentation Certain prior year amounts have been reclassified to conform with the current year presentation.

NOTE 2 ACQUISITIONS AND SALE OF ASSETS

Honeywell acquired 14 companies in 1998, 7 companies in 1997 and 17 companies in 1996 for \$281.4, \$650.2 and \$411.2, respectively. These acquisitions were accounted for as purchases, and accordingly, the assets and liabilities of the acquired entities have been recorded at their estimated fair values at the dates of acquisition. Cash acquired through acquisitions was \$7.0, \$51.7 and \$35.0 in 1998, 1997 and 1996, respectively. The excess of purchase price over the estimated fair values of the net assets acquired, in the amount of \$213.3 in 1998, \$323.7 in 1997 and \$294.7 in 1996, has been recorded as goodwill and is amortized over estimated useful lives.

The largest acquisition in 1997, consisting of approximately \$600 in cash, was Measurex Corporation. The allocation of the purchase price for Measurex resulted in goodwill of \$305.9 and intangibles, including patents/developed technology, work force value and customer lists, of \$202.5 which will be amortized over an average of approximately 26 years.

The pro forma results for 1998, 1997 and 1996, assuming these acquisitions had been made at the beginning of the year, would not be materially different from reported results.

On July 5, 1998, Honeywell sold Honeywell-Measurex Data Measurement Corporation located in Gaithersburg, MD, to Metrika Systems Corporation for \$29.0 in cash. The gain on the sale of this business and the impact on the financial statements and results of operations are immaterial. In 1997, Honeywell sold the net assets of Industrial Control's solenoid valve business for approximately \$102 in cash, resulting in a gain of \$64.3. Additionally in 1997, Honeywell sold the control valve business of the Industrial Control business segment and a small security monitoring business related to Home and Building Control for approximately \$24 in cash and receivables for a gain of \$12.8.

Proceeds from the sale of other assets amounted to \$68.0 in 1998, \$77.2 in 1997 and \$90.3 in 1996. In June 1998, Honeywell entered into a sale/leaseback agreement on a facility in Cupertino, CA, which generated cash proceeds of \$50.4. A gain of \$5.6 was recognized in the second quarter of 1998. The remaining gain was deferred and is recognized over the term of the lease. The annual impact of the deferred gain on the results of operations will be immaterial. Gains and losses from other asset sales were not material in any year and are included in selling, general and administrative expenses on the income statement.

NOTE 3 SPECIAL CHARGES

In 1998, Honeywell's management, with the approval of the board of directors, committed itself to a plan of action and recorded special charges of \$53.7. Honeywell remains committed to efforts to reduce operating costs and improve margins. Special charges include costs for work force reductions, worldwide facilities consolidations, organizational changes, and other cost reductions. The Home and Building Control business segment recorded special charges of \$25.8 as a result of a rapidly changing marketplace by consolidating field office locations. Industrial Control recorded \$25.8 to rationalize product lines, restructure the organization, and complete other activities associated with the integration of Measurex. Space and Aviation Control recorded special charges of \$1.4 to strengthen the competitive position of its cost structure through workforce reductions and field office consolidations. A total of \$0.7 was recorded at the corporate level, which is related to work force reductions in administration. As of December 31, 1998, Honeywell had a total of \$48.2 of remaining reserves related to the 1998 special charges.

Work force reduction costs primarily include severance costs related to involuntary termination programs instituted to improve efficiency and reduce costs. These costs amounted to \$45.5 in 1998, and approximately 1,200 employees, consisting largely of sales, marketing, factory and other administrative personnel who have been or will be terminated. Facility consolidation costs are primarily associated with combining field office locations and rationalizing product lines to streamline Honeywell's operations, and amounted to \$6.0 in 1998. Other cost accruals totaling \$2.2 in 1998 include costs associated with the integration of product lines. The charges are included as special charges on the income statement. The remaining expenditures, to be paid in cash, for special charges in 1999 will be \$40.1 for workforce reductions, \$5.1 for facilities and \$1.1 for other expenses.

In 1997, Honeywell's management committed itself to a cost reduction plan and recorded special charges of \$90.7. Costs amounted to \$74.2 for work force reductions, \$8.3 for facility consolidations and \$8.2 for other cost reductions. As of December 31, 1998, Honeywell had a total of \$18.6 of reserves remaining related to the 1997 special charges. The balances of the 1997 special charges are primarily related to terminated employees who continue to receive pay.

Adjustments to the estimated plan's costs have not been material and the remaining reserves will be funded with cash generated from operations.

Notes to Financial Statements

Honeywell Inc. and Subsidiaries (Dollars in Millions Except Per Share Amounts)

NOTE 4 EARNINGS PER SHARE

	1998	1997	1996
Basic Earnings Per Share:			
Income:			
Income available to common shareowners	\$572.0	\$471.0	\$402.7
Shares:			
Weighted average shares outstanding	126,086,121	127,051,613	126,632,082
Basic Earnings Per Share	\$ 4.54	\$ 3.71	\$ 3.18
Diluted Earnings Per Share:			
Income:			
Income available to common shareowners	\$572.0	\$471.0	\$402.7
Shares:			
Weighted average shares outstanding	126,086,121	127,051,613	126,632,082
Dilutive shares issuable in connection with stock plans	4,828,865	4,767,393	6,286,392
Less: Shares purchaseable with proceeds	(3,116,255)	(2,626,784)	(3,437,695)
Total Shares	127,798,731	129,192,222	129,480,779
Diluted Earnings Per Share	\$ 4.48	\$ 3.65	\$ 3.11

Options to purchase 1.2 million shares of common stock ranging from \$67.13 to \$94.47 were outstanding during 1998 but were not included in the computation of the Diluted Earnings Per Share (EPS) because the options' exercise prices were greater than the average market price of the common shares. Options to purchase 1.4 million shares ranging from \$69.43 to \$78.91 were outstanding during 1997 but were not included in the computation of 1997 Diluted EPS. In 1996, an immaterial amount of options was excluded from the Diluted EPS calculation since most of the option prices were less than the average market price for the period.

NOTE 5 INCOME TAXES

The components of income before income taxes consist of the following:

	1998	1997	1996
Domestic	\$485.1	\$377.3	\$349.4
Foreign	344.2	325.9	260.8
	\$829.3	\$703.2	\$610.2

The provision for income taxes on that income is as follows:

	1998	1997	1996
Current tax expense			
United States	\$125.5	\$124.9	\$ 60.8
Foreign	110.5	101.6	84.7
State and local	33.3	27.1	27.2
Total current	269.3	253.6	172.7
Deferred tax expense			
United States	(18.8)	(13.9)	27.4
Foreign	8.9	(5.6)	4.0
State and local	(2.1)	(1.9)	3.4
Total deferred	(12.0)	(21.4)	34.8
Provision for income taxes	\$257.3	\$232.2	\$207.5

A reconciliation of the provision for income taxes to the amount computed using U.S. federal statutory rates is as follows:

	1998	1997	1996
Taxes on income at U.S. federal statutory rates	\$290.3	\$246.1	\$213.6
Tax effects of foreign income	(1.3)	(17.6)	(15.9)
State taxes	19.4	15.7	21.1
Goodwill	11.3	10.6	4.3
Tax effect of settlements	(26.5)	(6.8)	0.0
Other	(35.9)	(15.8)	(15.6)
Provision for income taxes	\$257.3	\$232.2	\$207.5

Interest costs related to prior years' tax issues are included in the provision for income taxes. Taxes paid were \$258.9 in 1998, \$203.7 in 1997 and \$113.1 in 1996.

Deferred income taxes are provided for the temporary differences between the financial reporting basis and the tax basis of Honeywell's assets and liabilities. Temporary differences comprising the net deferred taxes shown on the statement of financial position are:

	1998	1997
Employee benefits	\$ 30.8	\$ 54.7
Miscellaneous accruals	132.5	107.0
Asset valuation reserves	52.3	44.0
Long-term contracts	12.3	12.0
State taxes	27.1	24.9
Pension liability adjustment	10.6	4.4
Other	(45.0)	(34.8)
	\$220.6	\$212.2

The components of net deferred taxes shown in the statement of financial position are:

	1998	1997
Deferred tax assets	\$642.3	\$506.8
Deferred tax liabilities	421.7	294.6

Provision has not been made for U.S. or additional foreign taxes on \$882.4 of undistributed earnings of international subsidiaries, as those earnings are considered to be permanently reinvested in the operations of those subsidiaries. It is not practicable to estimate the amount of tax that might be payable on the eventual remittance of such earnings.

At December 31, 1998, foreign subsidiaries had tax operating loss carryforwards of \$29.2.

NOTE 6 FOREIGN CURRENCY

Honeywell has entered into various foreign currency exchange contracts designed to manage its exposure to exchange rate fluctuations on foreign currency transactions. Foreign exchange contracts reduce Honeywell's overall exposure to exchange rate movements, since the gains and losses on these contracts offset losses and gains on the assets, liabilities and transactions being hedged. Honeywell hedges a significant portion of all known foreign exchange exposures, including non-functional currency receivables and payables and foreign currency imports and exports. The notional amount of Honeywell's outstanding foreign currency contracts, consisting of forwards, purchased options and swaps, was approximately \$1,071.6 and \$1,213.7 at December 31, 1998, and 1997, respectively. At December 31, 1998, these contracts generally have a term of less than one year and are primarily denominated in Belgian francs (\$366.8), Deutsche marks (\$253.3), Great Britain pounds (\$129.9) and Canadian dollars (\$89.3).

NOTE 7 INVESTMENTS IN DEBT AND EQUITY SECURITIES

Honeywell's investments in held-to-maturity securities are reported at amortized cost in the statement of financial position as follows:

	1998	1997
Cash equivalents	\$171.1	\$27.7
Short-term investments	7.2	8.0
Investments and advances	3.5	5.7
	\$181.8	\$41.4

Held-to-maturity securities generally mature within one year and include the following:

	1998	1997
Time deposits with financial institutions	\$ 13.8	\$34.8
Commercial paper	157.2	0.1
Other	10.8	6.5
	\$181.8	\$41.4

Honeywell's purchases of held-to-maturity securities, consisting primarily of commercial paper, amounted to \$2,212.0 and \$1,809.0 in 1998 and 1997, respectively. Proceeds from maturities of held-to-maturity securities amounted to \$2,058.4 in 1998 and \$1,812.5 in 1997. The majority of the held-to-maturity securities that were purchased and had matured during the year are considered cash equivalents since the duration was less than three months. Honeywell has no investments in trading securities, and available-for-sale securities are not material. The estimated aggregate fair value of these securities approximates their carrying amounts in the statement of financial position. Gross unrealized holding gains and losses were not material in any year.

NOTE 8 RECEIVABLES

Receivables have been reduced by an allowance for doubtful accounts as follows:

	1998	1997
Receivables, current	\$41.1	\$38.5
Long-term receivables	1.8	2.7

Receivables include approximately \$24.9 in 1998 and \$16.5 in 1997 billed to customers but not paid pursuant to contract retainage provisions. These balances are due upon completion of the contracts, generally within one year.

Unbilled receivables related to long-term contracts amount to \$345.6 and \$331.0 at December 31, 1998, and 1997, respectively, and are generally billable and collectible within one year.

Long-term, interest-bearing notes receivable from the sale of assets have been reduced by valuation reserves of \$1.3 in 1998 and \$1.5 in 1997 to an amount that approximates realizable value.

In 1996, Honeywell entered into an asset securitization program with a large financial institution to sell, with recourse, certain eligible trade receivables up to a maximum of \$50.0 Canadian dollars (approximately \$32.3 and \$34.8 U.S. dollars at December 31, 1998 and 1997, respectively). As receivables transferred to the trust are collected, Honeywell may transfer additional receivables up to the predetermined facility limits. Gross receivables transferred to the trust amounted to \$243.3 in 1998 and \$292.6 in 1997. Honeywell retains the right to repurchase transferred receivables under the program, and therefore, the transaction does not qualify as a sale under the terms of Statement of Financial Accounting Standard No. 125, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." Included on the statement of financial position as receivables are at year-end \$18.0 and \$27.7 in 1998 and 1997, respectively, of uncollected receivables held in trust.

Notes to Financial Statements

Honeywell Inc. and Subsidiaries (Dollars in Millions Except Per Share Amounts)

NOTE 9 INVENTORIES

	1998	1997
Finished goods	\$ 373.2	\$ 379.3
Inventories related to long-term contracts	186.1	151.4
Work in process	224.9	211.3
Raw materials and supplies	331.8	286.0
	\$1,116.0	\$1,028.0

Inventories related to long-term contracts are net of payments received from customers relating to the uncompleted portions of such contracts in the amounts of \$28.7 and \$43.5 at December 31, 1998 and 1997, respectively.

NOTE 10 PROPERTY, PLANT AND EQUIPMENT

	1998	1997
Land	\$ 71.2	\$ 68.7
Buildings and improvements	602.9	557.4
Machinery and equipment	2,525.1	2,336.4
Construction in progress	156.6	82.5
	\$3,355.8	\$3,045.0

NOTE 11 FOREIGN SUBSIDIARIES

The following is a summary of financial data pertaining to foreign subsidiaries:

	1998	1997	1996
Net income	\$ 245.0	\$ 235.6	\$ 172.9
Assets	\$2,662.1	\$2,114.8	\$1,847.8
Liabilities	1,548.6	1,019.0	838.5
Net assets	\$1,113.5	\$1,095.8	\$1,009.3

Insofar as can be reasonably determined, there are no foreign-exchange restrictions that materially affect the financial position or the operating results of Honeywell and its subsidiaries.

NOTE 12 INVESTMENTS IN OTHER COMPANIES

Following is a summary of financial data pertaining to companies 20 to 50 percent owned. The principal company included is Yamatake Corporation, located in Japan, of which Honeywell owned 21.7 percent of the outstanding common stock at December 31, 1998 and 1997. This investment had a market value of \$191.1 and \$216.9 at December 31, 1998 and 1997, respectively.

	1998	1997	1996
Sales	\$1,717.8	\$1,971.5	\$1,949.2
Gross profit	577.9	662.7	688.8
Net income	46.9	58.7	51.8
Equity in net income	11.7	12.9	13.3
Current assets	\$1,454.2	\$1,427.8	\$1,576.9
Noncurrent assets	297.5	332.8	421.1
	1,751.7	1,760.6	1,998.0
Current liabilities	647.7	706.7	853.5
Noncurrent liabilities	116.7	123.2	181.4
	764.4	829.9	1,034.9
Net assets	\$ 987.3	\$ 930.7	\$ 963.1
Equity in net assets	\$ 259.3	\$ 238.0	\$ 241.0

NOTE 13 INTANGIBLE ASSETS

Intangible assets have been reduced by accumulated amortization as follows:

	1998	1997
Goodwill	\$163.7	\$134.8
Intangibles	337.2	305.3

NOTE 14 DEBT

Short-Term Debt At December 31, 1998, Honeywell had general-purpose lines of credit available totaling \$1,770.6, which management believes is adequate to meet its financing requirements, including support of commercial paper and bank note borrowings. Committed revolving credit lines with 17 banks totaled \$1,325.0. These lines have commitment fee requirements. There were no borrowings on these lines at December 31, 1998. The remaining credit facilities of \$445.6 have been arranged by non-U.S. subsidiaries in accordance with customary lending practices in their respective countries of operation. Borrowings against these lines amounted to \$19.8 at December 31, 1998. The interest rates for Honeywell's material lines of credit are indexed to a rate, such as Prime, LIBOR, or Commercial Paper. The weighted average interest rates on short-term borrowings outstanding at December 31, 1998 and 1997, respectively, were as follows: commercial paper, 0.0 percent and 6.8 percent; and notes payable, 5.0 percent and 5.2 percent.

Short-term debt consists of the following:

	1998	1997
Commercial paper	\$ 0.0	\$ 43.0
Notes payable	52.7	38.9
Current maturities of long-term debt	126.2	64.5
	\$178.9	\$ 146.4

Long-Term Debt

	1998	1997
Honeywell Inc.		
7.15% to 7.71% due 1998	\$ 0.0	\$ 50.0
7.36% to 7.46% due 1999	70.5	70.5
7.35% due 2000	75.0	75.0
6.60% due 2001	100.0	100.0
6.75% due 2002	200.0	200.0
8.63% due 2006	100.0	100.0
7.00% due 2007	350.0	350.0
7.13% due 2008	200.0	200.0
7.45% to 9.50% due 2001 to 2010	27.0	27.0
6.63% due 2028	250.0	0.0
Unamortized premiums and discounts	(6.0)	(2.6)
Subsidiaries		
3.0% to 7.50% due 1999 to 2002, various currencies	59.0	71.4
	1,425.5	1,241.3
Less amount included in short-term debt	126.2	64.5
	\$1,299.3	\$1,176.8

Debt in the amount of \$50.0 with interest rates ranging from 7.15 percent to 7.71 percent matured between March and May 1998. In August 1997, Honeywell filed a shelf registration statement, which provides for the issuance of up to \$500.0 of debt securities. On June 15, 1998, Honeywell issued \$250.0 in debentures, to fund general operations, with a coupon rate of 6 percent maturing on June 15, 2028. At December 31, 1998, \$250.0 remained available for issuance under the shelf registration statement.

Honeywell uses interest rate swaps to manage its interest rate exposures and its mix of fixed and floating interest rates. In 1994, Honeywell entered into interest rate swap agreements effectively converting \$50.0 of the \$70.5 of medium-term notes due in 1999 to floating rate debt based on three-month LIBOR rates. In 1996, Honeywell entered into interest rate swap agreements converting the \$100.0 of bonds due in 2001 and \$200.0 of bonds due in 2008 to floating rate debt based on six-month LIBOR rates. In 1997, Honeywell entered into swap agreements converting \$550.0 of new debt from fixed rate to floating rate debt based on six-month LIBOR. In addition, \$420.0 of debt and previous swaps were

converted to fixed rate debt at an average fixed rate of 6.18 percent. In 1998, \$200.0 of interest rate swaps due in 2008 were terminated. The swap agreements outstanding at December 31, 1998 expire as follows: \$100.0 in 1999, \$250.0 in 2000, \$100.0 in 2001, \$200.0 in 2002 and \$350.0 in 2007.

Annual sinking-fund and maturity requirements for the next five years on long-term debt outstanding at December 31, 1998, are as follows:

1999	\$ 126.2
2000	77.6
2001	116.5
2002	210.3
2003	0.0
2004 and beyond	900.1
Unamortized premiums/discounts	(6.0)
Total long-term debt	\$1,425.5

Interest paid amounted to \$109.2, \$95.0 and \$77.3 in 1998, 1997 and 1996, respectively.

NOTE 15 FAIR VALUE OF FINANCIAL INSTRUMENTS

All financial instruments are held for purposes other than trading. The estimated fair values of all nonderivative financial instruments approximate their carrying amounts in the statement of financial position with the exception of long-term debt. The estimated fair value of long-term debt is based on quoted market prices for the same or similar issues or on current rates available to Honeywell for debt of the same remaining maturities. The carrying amount of long-term debt was \$1,425.5 and \$1,241.3 at December 31, 1998 and 1997, respectively; and the fair value was \$1,510.8 and \$1,291.3 at December 31, 1998 and 1997, respectively.

The estimated fair value of interest rate swaps, foreign currency contracts and option contracts, which is the net unrealized market gain or loss, is based primarily on quotes obtained from various financial institutions that deal in these types of instruments. The following table summarizes the notional value, carrying value and fair value of Honeywell's derivative financial instruments.

	At December 31, 1998			At December 31, 1997		
	Notional Value	Carrying Value	Fair Value	Notional Value	Carrying Value	Fair Value
Interest rate swaps	\$1,000.0	\$0.0	\$6.0	\$1,340.0	\$0.0	\$38.5
Currency contracts	1,071.6	0.0	(4.1)	1,213.7	0.0	6.7
Total	\$2,071.6	\$0.0	\$1.9	\$2,553.7	\$0.0	\$45.2

The counterparties to the foreign currency contracts and the interest rate swaps shown above expose Honeywell to credit risk to the extent of non-performance. However, the credit ratings of the counterparties, which consist of a diversified group of financial institutions, are regularly monitored and risk of default is considered remote.

Notes to Financial Statements

Honeywell Inc. and Subsidiaries (Dollars in Millions Except Per Share Amounts)

NOTE 16 LEASING ARRANGEMENTS

As lessee, Honeywell has minimum annual lease commitments outstanding at December 31, 1998, with the majority of the leases having initial periods ranging from one to 10 years. Following is a summary of operating lease information.

	Operating Leases
1999	\$140.1
2000	109.2
2001	80.8
2002	55.9
2003	41.6
2004 and beyond	\$142.1
	\$569.7

Rent expense for operating leases was \$141.8 in 1998, \$141.6 in 1997 and \$153.7 in 1996.

Substantially all leases are for plant, warehouse, office space, personal computers and automobiles. A number of the leases contain renewal options ranging from one to 10 years.

NOTE 17 CAPITAL STOCK

	Common Stock	Additional Paid-In Capital	Treasury Stock
Balance December 31, 1995	\$282.2	\$481.3	\$(1,650.2)
Purchase of treasury stock—2,904,000 shares			(163.2)
Issued for Honeywell Foundation Pledge—450,000 treasury shares		8.3	9.2
Issued for employee stock plans—2,399,438 shares		55.8	40.7
317,192 shares canceled	(0.5)	(16.6)	
Balance December 31, 1996	\$281.7	\$528.8	\$(1,763.5)
Purchase of treasury stock—2,250,600 shares			(154.3)
Issued for Honeywell Foundation Pledge—285,700 treasury shares		7.9	5.7
Issued for employee stock plans—1,892,638 shares		84.4	32.8
176,489 shares canceled	(0.2)	(12.7)	
Balance December 31, 1997	\$281.5	\$608.4	\$(1,879.3)
Purchase of treasury stock—2,054,500 shares			(159.6)
Issued for Honeywell Foundation Pledge—264,300 treasury shares		7.2	5.3
Issued for employee stock plans—2,016,560 shares		89.8	28.1
96,426 shares canceled	(0.2)	(7.8)	
Balance December 31, 1998	\$281.3	\$697.6	\$(2,005.5)

Stock-Based Compensation Plans for Key Employees

In 1997, the Board of Directors adopted, and the shareowners approved, the 1997 Honeywell Stock and Incentive Plan. The 1997 plan replaced the 1993 Honeywell Stock and Incentive Plan. Awards currently outstanding under the 1993 plan were not affected. The 1997 plan, which terminates on April 15, 2002, provides for the award of up to 7,500,000 shares of common stock. The 1997 plan is intended to facilitate ownership and increase the interest of key employees in the growth and performance of Honeywell and motivate them to contribute to the company's future success.

Also in 1997, the Board of Directors approved the 1997 Honeywell Employee Stock and Incentive Plan. This plan, which provides for the award of up to 2,000,000 shares of common stock, is primarily intended to retain and recognize non-executive employees for their contributions to Honeywell's success.

The 1993 Honeywell Stock and Incentive Plan, which expired with the adoption of the 1997 plan, provided for the award of up to 7,500,000 shares of common stock. Awards made under any of the above plans may be in the form of stock options, restricted stock or other stock-based awards. At December 31, 1998, there were 12,405,731 shares reserved for all employee plans.

In 1996, Honeywell adopted Statement of Financial Accounting Standards (SFAS) No. 123, "Accounting for Stock-Based Compensation." As permitted by SFAS 123, Honeywell has elected to continue following the guidance of APB 25 for measurement and recognition of stock-based transactions with employees (see Note 1 on page 44). The compensation cost that has been charged against income for the restricted stock and other stock-based awards, including directors' stock compensation, was \$16.7, \$11.2 and \$12.2 in 1998, 1997 and 1996, respectively. No compensation cost has been recognized for the awards made in the form of stock options or from the Employee Stock Purchase Plans. If compensation cost for Honeywell's stock-based compensation plans had been determined based on the fair value at the grant dates for awards under those plans, consistent with the method provided in SFAS 123, Honeywell's net income and basic earnings per share would have been reduced to the pro forma amounts indicated below:

		1998	1997	1996
Net Income	As reported	\$572.0	\$471.0	\$402.7
	Pro forma	\$551.3	\$456.2	\$392.6
Basic Earnings Per Share	As reported	\$ 4.54	\$ 3.71	\$ 3.18
	Pro forma	\$ 4.37	\$ 3.59	\$ 3.10

Fixed Stock Options Stock option grants for executive officers are reviewed and approved by the Personnel Committee of the Board of Directors and for non-executive officers by the Chief Executive Officer. Stock options are granted periodically at the fair market value of Honeywell common stock on the date of the grant and are typically exercisable one year from the grant date.

In July 1997, Honeywell introduced an international stock purchase plan in the United Kingdom. This plan allows eligible employees the option to purchase Honeywell shares in July 2000, at an option price of \$54.72. The number of shares estimated to be issued from this program is 148,000 and has been included in the fixed options numbers below.

A summary of the status of the fixed stock options as of December 31, 1998, 1997 and 1996 and changes during the years ending on those dates is presented below:

	1998		1997		1996	
	Weighted Average Shares Exercise (000)	Price	Weighted Average Shares Exercise (000)	Price	Weighted Average Shares Exercise (000)	Price
Fixed Options						
Outstanding at beginning of year	5,483	\$51	4,507	\$39	5,963	\$35
Granted	2,088	\$54	1,784	\$73	423	\$54
Assumed			671	\$52		
Exercised	1,354	\$52	1,287	\$37	1,821	\$31
Forfeited	126	\$64	192	\$67	58	\$42
Outstanding at end of year	6,091	\$60	5,483	\$51	4,507	\$39
Options exercisable at year-end	3,801	\$53	3,820	\$41	4,088	\$37
Weighted average fair value of options granted during the year	\$16.77		\$18.91		\$14.19	

The weighted average fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model and represents the difference between the fair market value on the date of grant and the estimated market value on the exercise date. The following weighted average assumptions are used in the Black-Scholes model for grants in 1998, 1997 and 1996, respectively: dividend yield of 1.4, 1.5 and 1.5 percent; expected volatility of 24, 24 and 27 percent; risk-free interest rates of 4.7, 5.6 and 6.3 percent; and expected life of four years for all options except the international stock purchase plan which has a three year life. The "Assumed" line identifies the options Honeywell assumed in the 1997 acquisition of Measurex and converted to options to purchase Honeywell shares.

The following table summarizes information about fixed stock options outstanding at December 31, 1998. The fixed options outstanding include options issued under the 1997 plans as well as the 1993 Honeywell Stock and Incentive Plan and the previous plans which the 1993 plan replaced.

	Options Outstanding			Options Exercisable		
Range of Exercise Prices	Shares Outstanding at 12/31/98 (000)	Remaining Contractual Life	Weighted Average Exercise Price	Shares Exercisable at 12/31/98 (000)	Weighted Average Exercise Price	
\$16-\$24	55	1.2 yrs	\$22	55	\$22	
\$25-\$36	719	3.7 yrs	\$32	719	\$32	
\$37-\$54	1,766	5.2 yrs	\$45	1,568	\$44	
\$55-\$80	3,448	7.8 yrs	\$74	1,459	\$74	
\$81-\$96	103	8.6 yrs	\$87	0	\$0	

Restricted Stock Awards Restricted shares of common stock are issued to certain key employees as compensation and as incentives, some of which are tied to Honeywell performance. Restricted shares issued as compensation are awarded with a fixed restriction period ranging from three to six years. In 1993, shares were issued and tied to performance goals which restricted the shares until the earlier of: (i) the achievement of performance goals within a specified measurement period, not more than three years, or (ii) nine years. The vesting of performance shares awarded in 1996 to senior executives was established at not more than two years. Owners of restricted shares have the rights of shareowners, including the right to receive cash dividends and the right to vote. Restricted shares forfeited revert to Honeywell at no cost. Restricted shares issued totaled 352,625 in 1998, 237,009 in 1997 and 371,917 in 1996. At December 31, restricted shares outstanding under key employee plans totaled 867,301 in 1998, 913,667 in 1997 and 835,443 in 1996, with a weighted average grant date fair value of \$63, \$55 and \$46 in 1998, 1997 and 1996, respectively.

Employee Stock Purchase Plans In July 1998, Honeywell introduced an Employee Stock Purchase Plan in the U.S. and Canada. Employees may contribute from 1 percent to 10 percent of their eligible pay on an after-tax basis. The plan allows employees to purchase Honeywell stock quarterly at the end of each purchase period at 85 percent of the fair market value on the grant date (the first day of the purchase period) or the exercise date (the last day of the purchase period), whichever is lower. During 1998, 276,812 shares were issued under this plan. Also in 1998, International Employee Stock Purchase Plans were introduced in Austria, Belgium, France, Germany, Italy and Switzerland. These plans allowed for employees to purchase stock at a discount. Belgium, Italy and France have quarterly purchase windows and Austria, Germany and Switzerland have December purchase windows. In 1998, 14,147 shares were issued under the International Employee Stock Purchase Plans.

Employee Stock Match Plans In 1990, Honeywell adopted Stock Match and Performance Stock Match plans under which Honeywell matches, in the form of Honeywell common stock, certain eligible U.S. employee savings plan contributions. Employees are vested in the shares after three years of employment. Shares issued under the stock match plans totaled 555,746 in 1998, 542,406 in 1997 and 394,534 in 1996 at a cost of \$42.4, \$37.9 and \$23.4, respectively.

Stock Pledge In 1993, Honeywell pledged to the Honeywell Foundation a five-year option to purchase 2,000,000 shares of common stock at \$33.00 per share. The Honeywell Foundation exercised all options to purchase the 2,000,000 shares with 264,300 purchased in 1998, 285,700 in 1997, 450,000 in 1996 and 1,000,000 in 1995.

Preference Stock Twenty-five million preference shares with a par value of \$1.00 have been authorized. None have been issued at December 31, 1998.

Notes to Financial Statements

Honeywell Inc. and Subsidiaries (Dollars in Millions Except Per Share Amounts)

NOTE 18 QUARTERLY DATA (UNAUDITED)

1998	1st Qtr.	2nd Qtr.	3rd Qtr.	4th Qtr.
Sales	\$1,923.3	\$2,035.2	\$2,119.5	\$2,348.7
Cost of sales	1,326.8	1,383.0	1,412.0	1,555.2
Special charges	—	—	—	53.7
Litigation settlements	—	—	—	(23.6)
Net income	96.3	125.8	145.4	204.5
Basic earnings per share	0.76	1.00	1.15	1.63
Diluted earnings per share	0.75	0.98	1.14	1.61

1997	1st Qtr.	2nd Qtr.	3rd Qtr.	4th Qtr.
Sales	\$1,685.7	\$1,977.3	\$2,038.7	\$2,325.8
Cost of sales	1,149.7	1,359.1	1,390.3	1,526.0
Special charges	—	—	60.4	30.3
Gain on sale of businesses	—	—	60.3	16.8
Net income	75.6	98.4	118.9	178.1
Basic earnings per share	0.60	0.77	0.93	1.41
Diluted earnings per share	0.59	0.76	0.92	1.38

Shareowners of record on February 1, 1999, totaled 30,571. The fourth quarter of 1998 includes \$53.7 of special charges (\$0.27 per diluted share), \$23.6 gain from the settlement of long-standing litigation claims (\$0.11 per diluted share) and \$16.7 resulting from the favorable resolution of certain prior-year research and development tax claims (\$0.13 per diluted share). The fourth quarter of 1997 includes a \$16.8 gain from the sale of businesses (\$11.5 after-tax) and special charges of \$30.3 (\$20.8 after-tax).

NOTE 19 SEGMENT INFORMATION

Honeywell is a global controls company focused on creating value through control technology. Honeywell serves customers worldwide through operations engaged in the design, development, manufacture, marketing and service of control solutions in three industry segments—Home and Building Control, Industrial Control and Space and Aviation Control. Honeywell’s broad range of control products, systems, and services provide solutions worldwide as our customers look to improve productivity, energy efficiency and environmental protection, increase safety and enhance comfort. Honeywell’s reportable segments are strategic business units that offer different products and services. They are managed separately as each business requires different products, services and marketing strategies.

Honeywell adopted Statement of Financial Accounting Standards (SFAS) No. 131, “Disclosures about Segments of an Enterprise and Related Information,” during 1998. Operating

segments are defined by SFAS 131 as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance (the “management approach”). Honeywell’s chief operating decision making group that determines the allocation of resources and assesses the performance of the operating segments is the Chief Executive Officer and the Board of Directors.

Honeywell’s reportable operating segments include Home and Building Control, Industrial Control and Space and Aviation Control. The Other segment includes two research and development operations that promote technology and products to both external customers and operating units.

The accounting policies of the segments are the same as those described in Note 1. Honeywell evaluates performance based on profit or loss from operations before income taxes excluding interest expense, equity income and other indirect general corporate expenses. Honeywell accounts for intersegment sales and transfers on negotiated transfer prices and all intersegment profit or loss is eliminated in consolidation.

Home and Building Control provides products and services to create efficient, safe, comfortable environments by offering controls for heating, ventilation, humidification and air-conditioning equipment; security and fire alarm systems; home automation systems; energy-efficient lighting controls; building management systems and services; and home comfort consumer products. Customers include building managers and owners; distributors and wholesalers; heating, ventilation and air-conditioning manufacturers; homebuilders; home owners; and original equipment manufacturers.

Industrial Control produces systems for the automation and control of process operations in industries such as oil refining, oil and gas drilling, pulp and paper manufacturing, food processing, chemical manufacturing and power generation; solid-state sensors for position, pressure, air flow, temperature and current; precision electromechanical switches; manual controls; advanced vision-based sensors; and fiber-optic components. Customers include appliance manufacturers; automotive companies; food processing companies; oil and gas producers; refining and petrochemical companies; pharmaceutical companies; paper companies; and utilities.

Space and Aviation Control is a full-line avionics supplier and systems integrator for commercial, military and space applications, providing automatic flight control systems, airport control systems, electronic cockpit displays, flight management systems, navigation, surveillance and warning systems, severe weather avoidance systems and flight reference sensors. Customers include airframe manufacturers; international, national and regional airlines; airports; NASA; prime U.S. defense contractors; and the U.S. Department of Defense.

Following is financial information relating to the industry segments:

	1998	1997	1996
External sales			
Home and Building Control	\$3,440.5	\$3,386.6	\$3,327.1
Industrial Control	2,516.3	2,547.1	2,199.6
Space and Aviation Control	2,339.1	1,956.9	1,640.0
Other	130.8	136.9	144.9
Total external sales	\$8,426.7	\$8,027.5	\$7,311.6
Sales between segments			
Home and Building Control	\$ 24.8	\$ 23.6	\$ 29.8
Industrial Control	38.1	49.3	32.8
Space and Aviation Control	2.6	0.8	3.2
Other	62.4	57.9	41.1
Total sales between segments	\$ 127.9	\$ 131.6	\$ 106.9
Operating profit			
Home and Building Control	\$ 348.9	\$ 290.2	\$ 345.8
Industrial Control	314.2	309.2	254.9
Space and Aviation Control	334.0	255.7	163.3
Other	31.2	18.8	6.2
Total operating profit	\$1,028.3	\$ 873.9	\$ 770.2
Interest expense	(113.0)	(101.9)	(81.4)
Equity income	11.7	12.9	13.3
General corporate expense	(97.7)	(81.7)	(91.9)
Income before income taxes	\$ 829.3	\$ 703.2	\$ 610.2
Special charges			
Home and Building Control	\$ 25.8	\$ 46.9	
Industrial Control	25.8	40.8	
Space and Aviation Control	1.4		
Corporate and Other	0.7	3.0	
Total special charges	\$ 53.7	\$ 90.7	
Gain on sale of businesses and litigation settlement			
Home and Building Control	\$ 4.6	\$ 5.7	
Industrial Control	5.3	71.4	
Space and Aviation Control	1.8		
Corporate and Other	11.9		
Total gains	\$ 23.6	\$ 77.1	
Depreciation and amortization			
Home and Building Control	\$ 116.8	\$ 108.0	\$ 98.4
Industrial Control	94.5	99.4	72.3
Space and Aviation Control	84.0	79.2	84.0
Corporate and Other	32.6	33.0	32.8
Total depreciation and amortization	\$ 327.9	\$ 319.6	\$ 287.5

Honeywell is a global company and as such engages in material operations in countries worldwide. Geographic areas of operation include Europe, Canada, Mexico, Asia, Australia, and South America.

Following is financial information relating to geographic areas:

	1998	1997	1996
External sales			
United States	\$5,201.6	\$4,843.5	\$4,477.9
Other areas	3,225.1	3,184.0	2,833.7
Total sales	\$8,426.7	\$8,027.5	\$7,311.6
Long-lived assets			
United States	\$1,990.4	\$1,830.9	\$1,355.9
Other areas	563.2	459.8	469.3
Total long-lived assets	\$2,553.6	\$2,290.7	\$1,825.2

External sales are attributed to countries based on the location of the affiliate responsible for the sale. Honeywell transfers products from one geographic region for resale in another. These transfers are priced to provide both areas with an equitable share of the overall profit. Long-lived assets are comprised of property, plant and equipment, goodwill and intangible assets. No customers exceeded 10 percent of total Honeywell sales in 1998, 1997 or 1996.

NOTE 20 CONTINGENCIES

Litton Litigation On March 13, 1990, Litton Systems, Inc. filed a legal action against Honeywell in U.S. District Court, Central District of California, Los Angeles (the “trial court”) with claims that were subsequently split into two separate cases. One alleges patent infringement under federal law for using an ion-beam process to coat mirrors incorporated in Honeywell’s ring laser gyroscopes, and tortious interference under state law for interfering with Litton’s prospective advantage with customers and contractual relationships with an inventor and his company, Ojai Research, Inc. The other case alleges monopolization and attempted monopolization under federal antitrust laws by Honeywell in the sale of inertial reference systems containing ring laser gyroscopes into the commercial aircraft market. Honeywell generally denied Litton’s allegations in both cases. In the patent/tort case, Honeywell also contested the validity as well as the infringement of the patent, alleging, among other things, that the patent had been obtained by Litton’s inequitable conduct before the United States Patent and Trademark Office.

Patent/Tort Case U.S. District Court Judge Mariana Pfaelzer presided over a three month patent infringement and tortious interference trial in 1993. On August 31, 1993, a jury returned a verdict in favor of Litton, awarding damages against Honeywell in the amount of \$1.2 billion on three claims. Honeywell filed post-trial motions contesting the verdict and damage award. On January 9, 1995, the trial court set them all aside, ruling, among other things, that the Litton patent was

Notes to Financial Statements

Honeywell Inc. and Subsidiaries (Dollars in Millions Except Per Share Amounts)

invalid due to obviousness, unenforceable because of Litton's inequitable conduct before the Patent and Trademark Office, and in any case, not infringed by Honeywell's current process. It further ruled that Litton's state tort claims were not supported by sufficient evidence. The trial court also held that if its rulings concerning liability were vacated or reversed on appeal, Honeywell should at least be granted a new trial on the issue of damages because the jury's award was inconsistent with the clear weight of the evidence and based upon a speculative damage study.

The trial court's rulings were appealed to the U.S. Court of Appeals for the Federal Circuit (the "Federal Circuit"), and on July 3, 1996, in a two to one split decision, a three judge panel of that court reversed the trial court's rulings of patent invalidity, unenforceability and non-infringement, and also found Honeywell to have violated California law by intentionally interfering with Litton's consultant contracts and customer prospects. However, the panel upheld two trial court rulings favorable to Honeywell, namely that Honeywell was entitled to a new trial for damages on all claims, and also to a grant of intervening patent rights which are to be defined and quantified by the trial court. After unsuccessfully requesting a rehearing of the panel's decision by the full Federal Circuit appellate court, Honeywell filed a petition with the U.S. Supreme Court on November 26, 1996, seeking review of the panel's decision. In the interim, Litton filed a motion and briefs with the trial court seeking injunctive relief against Honeywell's commercial ring laser gyroscope sales. After Honeywell and certain aircraft manufacturers filed briefs and made oral arguments opposing the injunction, the trial court denied Litton's motion on public interest grounds on December 23, 1996, and then scheduled the patent/tort damages retrial for May 6, 1997.

On March 17, 1997, the U.S. Supreme Court granted Honeywell's petition for review and vacated the July 3, 1996, Federal Circuit panel decision. The case was remanded to the Federal Circuit panel for reconsideration in light of a recent decision by the U.S. Supreme Court in the Warner-Jenkinson vs. Hilton Davis case, which refined the law concerning patent infringement under the doctrine of equivalents. On March 21, 1997, Litton filed a notice of appeal to the Federal Circuit of the trial court's December 23, 1996, decision to deny injunctive relief, but the Federal Circuit stayed any briefing or consideration of that matter until such time as it completed its reconsideration of liability issues ordered by the U.S. Supreme Court.

The liability issues were argued before the same three judge Federal Circuit panel on September 30, 1997. On April 7, 1998, the panel issued its decision:

(i) affirming the trial court's ruling that Honeywell's hollow cathode and RF ion-beam processes do not literally infringe the asserted claims of Litton's '849 reissue patent ("Litton's patent");

(ii) vacating the trial court's ruling that Honeywell's RF ion-beam process does not infringe the asserted claims of Litton's patent under the doctrine of equivalents, but also vacating the jury's verdict on that issue, and remanding that issue to the trial court for further proceedings in accordance with the Warner-Jenkinson decision;

(iii) vacating the jury's verdict that Honeywell's hollow cathode process infringes the asserted claims of Litton's patent under the doctrine of equivalents and remanding that issue to the trial court for further proceedings;

(iv) reversing the trial court's ruling with respect to the torts of intentional interference with contractual relations and intentional interference with prospective economic advantage, but also vacating the jury's verdict on that issue and remanding the issue to the trial court for further proceedings in accordance with California state law;

(v) affirming the trial court's grant of a new trial to Honeywell on damages for all claims, if necessary;

(vi) affirming the trial court's order granting intervening rights to Honeywell in the patent claim;

(vii) reversing the trial court's ruling that the asserted claims of Litton's patent were invalid due to obviousness, and reinstating the jury's verdict on that issue; and

(viii) reversing the trial court's determination that Litton had obtained its '849 reissue patent through inequitable conduct.

Litton's request for a rehearing of the panel's decision by the full Federal Circuit court was denied and its appeal of the denial of an injunction was dismissed. The case remanded to the trial court for further legal and perhaps factual review. A status conference was held on August 17, 1998 and the review was held in abeyance during a retrial of damages in the antitrust case in 1998. Honeywell intends to file motions with the trial court to dispose of the remanded issues as matters of law, but the review procedures remain to be defined and scheduled by the trial court. If some of the remanded issues are not disposed of by legal motions, a jury trial of the remaining issues may be necessary.

When preparing for the patent/tort damages retrial that was scheduled for May 1997, Litton had submitted a revised damage study to the trial court, seeking damages as high as \$1.9 billion. Honeywell believes that its ion-beam processes do not infringe Litton's patent, and further, that Litton's damage study remains flawed and speculative for a number of reasons. Based on the U.S. Supreme Court's decision in the Warner-Jenkinson vs. Hilton Davis case which refined the law concerning patent infringement under the doctrine of equivalents, and the Federal Circuit panel's recent decision remanding certain issues in the patent/tort case to the trial court, Honeywell also believes that it is reasonably possible that the trial court will conclude that Honeywell did not infringe Litton's patent or interfere with its contractual relationships, and that no damages will ultimately be awarded to Litton. Although it is not possible at this time to predict the outcome of the issues remanded to the trial court or any further appeals in this case, some potential does remain for adverse judgments which could be material to Honeywell's financial position or results of operations. Honeywell believes however, that any potential award of damages for an adverse judgment of infringement or interference should be based upon a reasonable royalty reflecting the value of the ion-beam coating process, and further that such an award would not be material to Honeywell's financial position or results of operations. As a result of the uncertainty regarding the outcome of this matter, no provision has been made in the financial statements with respect to this contingent liability.

Antitrust Case Preparations for, and conduct of, the trial in the antitrust case have generally followed the completion of comparable proceedings in the patent/tort case. The antitrust trial did not begin until November 20, 1995. Judge Pfaelzer also presided over the trial, but it was held before a different jury. At the close of evidence and before jury deliberations began, the trial court dismissed, for failure of proof, Litton's contentions that Honeywell had illegally monopolized and attempted to monopolize by:

(i) engaging in below-cost predatory pricing;

(ii) tying and bundling product offerings under packaged pricing;

(iii) misrepresenting its products and disparaging Litton products; and

(iv) acquiring the Sperry Avionics business in 1986.

On February 2, 1996, the case was submitted to the jury on the remaining allegations that Honeywell had illegally monopolized and attempted to monopolize by:

(i) entering into certain long-term exclusive dealing and penalty arrangements with aircraft manufacturers and airlines to exclude Litton from the commercial aircraft market, and

(ii) failing to provide Litton with access to proprietary software used in the cockpits of certain business jets.

On February 29, 1996, the jury returned a \$234 million single damages verdict against Honeywell for illegal monopolization which verdict would have been automatically trebled. On March 1, 1996, the jury indicated that it was unable to reach a verdict on damages for the attempt to monopolize claim, and a mistrial was declared as to that claim.

Honeywell subsequently filed a motion for judgment as a matter of law and a motion for a new trial, contending, among other things, that the jury's partial verdict should be overturned because Honeywell was prejudiced at trial, and Litton failed to prove essential elements of liability or submit competent evidence to support its speculative, all-or-nothing \$298.5 million damage claim. Litton filed motions for entry of judgment and injunctive relief. On July 24, 1996, the trial court denied Honeywell's alternative motions for judgment as a matter of law or a complete new trial, but concluded that Litton's damage study was seriously flawed and granted Honeywell a retrial on damages only. The court also denied Litton's two motions. At that time, Judge Pfaelzer was expected to conduct the retrial of antitrust damages sometime following the retrial of patent/tort damages. However, after the U.S. Supreme Court remanded the patent/tort case to the Federal Circuit in March 1997, Litton moved to have the trial court expeditiously schedule the antitrust damages retrial. In September 1997, the trial court rejected that motion, indicating that it wished to know the outcome of the current patent/tort appeal before scheduling retrials of any type.

Following the April 7, 1998, Federal Circuit panel decision in the patent/tort case, Litton again petitioned the trial court to schedule the retrial of antitrust damages. The trial court tentatively scheduled the trial to commence in the fourth quarter of 1998, and reopened limited discovery and other pretrial preparations. Litton then filed another antitrust damage claim of nearly \$300 million.

The damages only retrial began October 29, 1998, before Judge Pfaelzer, but a different jury. On December 9, 1998, the jury returned verdicts against Honeywell totaling \$250 million, \$220 million of which is in favor of Litton Systems Inc. and \$30 million of which is in favor of its sister corporation LSL, Canada.

On January 27, 1999, the court vacated its prior mistrial ruling with respect to the attempt to monopolize claim and entered a treble damages judgment in the total amount of \$750 million for actual and attempted monopolization.

Honeywell believes that there was no factual or legal basis for the magnitude of the jury's award in the damages retrial and that, as was the case in the first trial, the jury's award should be overturned. Honeywell also believes there are serious questions concerning the identity and nature of the business arrangements and conduct which were found by the first antitrust jury in 1996 to be anti-competitive and damaging to Litton, and there are very strong grounds to overturn the verdict of liability as a matter of law. Honeywell is now filing appropriate post-judgment motions with the trial court and Litton will soon file motions seeking to add substantial attorney's fees and costs to the judgment. Once the trial court has ruled on those motions, the parties will have the right to appeal the eventual judgment, as to both liability and damages, to the U.S. Court of Appeals for the Ninth Circuit.

Although it is not possible at this time to predict the outcome of the motions before the trial court or any eventual appeals in this case, some potential remains for adverse judgments which could be material to Honeywell's financial position or results of operations. As a result of the uncertainty regarding the outcome of this matter, no provision has been made in the financial statements with respect to this contingent liability. Honeywell also believes that it would be inappropriate for Litton to obtain recovery of the same damages, e.g. losses it suffered due to Honeywell's sales of ring laser gyroscope-based inertial systems to OEMs and airline customers, under multiple legal theories, claims and cases, and that eventually no duplicative recovery would be eliminated from the antitrust and patent/tort cases.

In the fall of 1996, Litton and Honeywell commenced a court-ordered mediation of the patent, tort and antitrust claims. No claim was resolved or settled, and the mediation is currently in recess.

Environmental Matters Honeywell's manufacturing sites generate both hazardous and nonhazardous wastes, the treatment, storage, transportation and disposal of which are subject to various local, state and federal laws relating to protection of the environment. Honeywell is in varying stages of investigation or remediation of potential, alleged or acknowledged contamination at on-site locations (currently or previously owned or operated sites) and at off-site locations where its wastes were taken for treatment or disposal. In connection with the cleanup of various off-site locations, Honeywell, along with a large number of other entities, has been designated a potentially responsible party (PRP) by the U.S. Environmental Protection Agency under the Comprehensive Environmental Response, Compensation and Liability Act or by state agencies under similar state laws (Superfund), which potentially subject PRPs to joint and several liability for the costs of such cleanup.

Notes to Financial Statements

Honeywell Inc. and Subsidiaries (Dollars in Millions Except Per Share Amounts)

Since Honeywell's first Superfund case in 1980, Honeywell has received notice regarding 119 Superfund sites and on-sites. Of these sites, 67 have been settled or Honeywell expects no further involvement.

At most of the Superfund sites where it is named as a PRP, Honeywell is a de-minimis party or minor player. Honeywell has maintained records of waste taken to or disposed of at many sites, and most sites have records kept by site owners or waste haulers. Honeywell's records and site records indicate that most of its disposals at these sites involve small quantities of materials relative to other PRPs. Based on Honeywell's experience, the amounts contributed by PRPs to the settlement or resolution of Superfund matters has been directly proportionate to the waste attributed to a PRP at a site relative to the waste attributed to other PRPs. Therefore, this information enables Honeywell to fairly accurately assess its exposure as a PRP with respect to each site. In addition, most Superfund site proceedings to which Honeywell is a PRP, are in the advanced stages of investigation or remediation, and in many cases a "Record of Decision" has been made by the Federal Environmental Protection Agency determining the potential aggregate exposure of the PRPs involved.

At on-sites, assessments are conducted by outside environmental consulting firms hired by Honeywell specifically for such purpose, and involve field studies of soil samples, water samples and other testing procedures as appropriate. On-site investigations have proceeded to the point where Honeywell has determined its exposure and in many cases, implemented remediation. Honeywell works closely with applicable local, state or federal regulatory agencies to request or secure approval of its investigatory and remediation efforts.

Honeywell has assessed its potential exposure with respect to all Superfund and on-site matters, including predicted investigation, remediation and associated costs, Honeywell's expected share of those costs, the financial viability of other PRPs with which it is involved at these Superfund sites and the availability of legal defenses, and has determined that there is not a reasonable possibility that a loss materially exceeding amounts already recognized will occur. Based on Honeywell's assessment of the costs associated with its environmental responsibilities, compliance with federal, state and local laws regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, it is the opinion of Honeywell's management, that such costs have not had and will not have a material effect on Honeywell's financial position, net income, capital expenditures or competitive position.

Other Matters Honeywell is a party to a large number of other legal proceedings, some of which are for substantial amounts. It is the opinion of management that any losses in connection with these matters will not have a material effect on Honeywell's net income, financial position or liquidity.

Honeywell has entered into letter of credit agreements with various financial institutions to support certain financing instruments and insurance policies aggregating approximately \$227.9 at December 31, 1998.

NOTE 21 PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS

Honeywell and its subsidiaries sponsor a number of retirement programs covering its employees throughout the world.

Pensions: Noncontributory defined benefit pension plans cover a substantial majority of Honeywell's U.S. employees. The plan covering U.S. non-union employees is based on the employee's highest five years of earnings during their last 10 years of employment. The plans covering U.S. union employees provides pension benefits based on a stated amount for each year of service. Employees in foreign countries, who are not U.S. citizens, are covered by various retirement benefit arrangements, some of which are considered to be defined benefit pension plans for accounting purposes. These foreign programs represent about 20 percent of Honeywell's total benefit obligation.

Other Postretirement Benefits: Substantially all of Honeywell's domestic and Canadian employees are eligible to receive medical benefits upon retirement after age 55. The eligibility requirements are 10 years of service for U.S. employees and 2 years of service for Canadian employees. These medical benefits are identical to those provided to active employees, and continue to age 65. For Canadian employees, the medical benefits are limited and coverage can continue for life as long as the employee shares in the cost. These benefits are funded on a pay-as-you-go basis.

The cost of these programs are as follows:

	Pension Benefits			Other Postretirement Benefits		
	1998	1997	1996	1998	1997	1996
Net periodic cost						
Service cost	\$ 93.9	\$ 87.9	\$ 89.2	\$ 9.0	\$ 8.2	\$13.0
Interest cost	298.7	294.9	284.6	18.4	18.3	22.4
Expected return on assets	(370.6)	(329.9)	(342.0)	0.0	0.0	0.0
Prior service cost amortization	32.7	32.3	31.5	0.8	0.8	0.8
Actuarial (gain)/loss	1.8	(0.7)	28.9	(6.1)	(7.1)	0.1
Transition amount amortization	(9.7)	(10.4)	(10.1)	0.0	0.0	0.0
Curtailment gain	0.7	0.0	0.0	0.0	(0.8)	0.0
Net periodic benefit cost	\$47.5	\$74.1	\$82.1	\$22.1	\$19.4	\$36.3

The plans' funded status is shown below, along with a description of how the status changed during the past two years. Plan assets are held by trust funds devoted to servicing pension benefits and are not available to Honeywell until all covered benefits are satisfied after a plan is terminated. The assets held by the trust funds consist primarily of a diversified portfolio of fixed-income investments and equity securities. For defined benefit pension plans, the benefit obligation is the projected benefit obligation—the actuarial present value as of a date of all benefits attributed

by the pension benefit formula to employee service rendered prior to that date. For defined benefit postretirement plans, the benefit obligation is the accumulated postretirement benefit obligation—the actuarial present value of benefits attributed to employee service rendered to a particular date.

	Pension Benefits		Other Postretirement Benefits	
	1998	1997	1998	1997
Change in benefit obligation				
Benefit obligation, October 1 prior year	\$4,177.4	\$4,010.2	\$ 246.2	\$ 287.4
Service cost	93.9	87.9	9.0	8.2
Interest cost	298.7	294.9	18.4	18.3
Participant contributions	7.5	7.0	3.0	3.0
Plan amendments	73.5	0.0	0.0	0.0
Actuarial loss (gain)	269.1	145.5	34.8	(49.1)
Acquisition	0.0	5.0	0.0	0.0
Divestiture			(0.5)	
Foreign currency translation adjustment	2.2	1.0	0.0	0.0
Benefits paid	(275.8)	(374.1)	(21.3)	(21.0)
Benefit obligation, September 30	\$4,646.5	\$4,177.4	\$ 290.1	\$ 246.3
Change in plan assets				
Fair value of plan assets, October 1 prior year	\$4,643.6	\$3,963.9	\$ 0.0	\$ 0.0
Actual return on plan assets	163.1	848.9	0.0	0.0
Company contributions	136.8	192.9	18.3	18.0
Participant contributions	7.5	7.0	3.0	3.0
Acquisition	0.0	5.0	0.0	0.0
Benefits paid	(275.8)	(374.1)	(21.3)	(21.0)
Fair value of plan assets, September 30	\$4,675.2	\$4,643.6	\$ 0.0	\$ 0.0
Funded status of plan	\$ 28.7	\$ 466.2	\$(290.1)	\$(246.3)
Unrecognized actuarial loss	166.3	(302.3)	(48.4)	(82.4)
Unrecognized prior service cost	257.6	214.8	3.6	4.3
Unrecognized net transition obligation	(14.6)	(28.9)	0.0	0.0
Fourth quarter contributions	1.1	21.0	4.6	0.0
Recognized amount	\$ 439.1	\$ 370.8	\$(330.3)	\$(324.4)

The amount recognized in the statement of financial position consists of the following:

	Pension Benefits		Other Postretirement Benefits	
	1998	1997	1998	1997
Prepaid benefit cost	\$497.1	\$415.9	\$ 0.0	\$ 0.0
Accrued benefit liability	(58.0)	(45.1)	(330.3)	(324.4)
Additional minimum liability	(68.7)	(50.5)	N/A	N/A
Intangible asset	41.4	39.2	N/A	N/A
Accumulated other comprehensive income	27.3	11.3	N/A	N/A
Recognized amount	\$439.1	\$370.8	\$(330.3)	\$(324.4)

The projected benefit obligation, accumulated benefit obligation, and fair value of plan assets for pension plans with accumulated benefit obligations in excess of plan assets were \$294.7, \$258.7 and \$173.4, respectively, as of December 31, 1998 and \$204.3, \$182.6 and \$118.4, respectively, as of December 31, 1997.

Weighted average assumptions as of 9/30

	Pension Benefit Plans			Other Postretirement Benefits		
	1998	1997	1996	1998	1997	1996
Discount rate	6.75%	7.50%	7.75%	6.75%	7.50%	7.50%
Expected return on plan assets	9.50%	9.50%	9.50%	N/A	N/A	N/A
Rate of compensation increase	4.00%	4.40%	4.65%	N/A	N/A	N/A

The company has assumed a health-care cost trend rate of 5 percent for 1999 and beyond. The health-care trend rate assumption has a significant effect on the amounts reported. A 1 percentage point change in the health-care trend rate would have the following effects on 1998 service and interest cost and the accumulated postretirement benefit obligation at December 31, 1998:

	1 Percentage Point	
	Increase	Decrease
Effect on service and interest cost components on net periodic cost	14.3%	(10.9%)
Effect on accumulated postretirement benefit obligation	9.8%	(7.4%)

Management and Facilities

Honeywell Inc. and Subsidiaries

Home and Building Control

Solutions and Services Business

J.K. Gilligan, *President*

Products Business

A. Weiss, *President*

Headquarters:

2701 4th Avenue South
Minneapolis, MN 55408

Manufacturing:

Golden Valley, MN;
San Diego, CA;
Albuquerque, NM;
Newbern, TN;
Annapolis, MD

Honeywell Consumer Products Inc.

J.E. Teela, *President*

Headquarters:

250 Turnpike Road
Southborough, MA 01722

Industrial Control

M.I. Tambakeras, *President*

Industrial Automation and Control

M.I. Tambakeras, *President*

Headquarters:

16404 N Black Canyon Hwy
Phoenix, AZ 85023

Manufacturing and Engineering:

Phoenix, AZ; Ft. Washington
and York, PA

Honeywell-Measurex

R.L. Rowe, *Vice President and General Manager*

Headquarters:

One Results Way
Cupertino, CA 95014

Manufacturing & Engineering:

Cupertino, CA; Vancouver, BC;
Cincinnati, OH; Gaithersburg,
MD; Varkaus and Kuopio,
Finland; Neuweid, Germany;
Waterford, Ireland

Sensing and Control

R.E. Sieck, *Vice President and General Manager*

Headquarters:

11 West Spring Street
Freeport, IL 61032

Manufacturing:

Freeport, Galena and Warren, IL;
Mars Hill, NC;
Richardson, TX;
Juarez, Mexico;
Acton, MA

Space and Aviation Control

D.K. Schwanz, *President*

Headquarters:

21111 North 19th Avenue
Phoenix, AZ 85027

Commercial Aviation Systems

M.A. Smith, *President*

Headquarters:

21111 North 19th Avenue
Phoenix, AZ 85027

Manufacturing:

Glendale and Phoenix, AZ;
Coon Rapids, MN

Space Systems

L.N. Speight, *Vice President and General Manager*

Headquarters:

13350 US Highway 19 North
Clearwater, FL 34624

Manufacturing and Engineering:

Clearwater, FL;
Houston, TX;
Glendale, AZ

Defense Avionics Systems

R.G. Marrah, *Vice President and General Manager*

Headquarters:

9201 San Mateo Blvd NE
Albuquerque, NM 87113

Manufacturing:

Albuquerque, NM;
Phoenix, AZ

Sensor and Guidance Products

G.C. Vandevoort, *Vice President and General Manager*

Headquarters:

2600 Ridgway Parkway
Minneapolis, MN 55413

Manufacturing:

Minneapolis, Golden Valley
and Coon Rapids, MN;
Clearwater, FL;
Phoenix, AZ

International

Asia Pacific

Honeywell Asia Pacific Inc.

E. Castro-Wright, *President*

Headquarters:

Suite 3213-25
Sun Hung Kai Centre
30 Harbour Road
Wanchai, Hong Kong

Affiliates:

Australia, China, Hong Kong,
Indonesia, Japan, Malaysia, New
Zealand, Pakistan, Philippines,
Singapore, Taiwan, Thailand

Joint Ventures:

Beijing Honeywell Energy
Saving Equipment Co., Ltd.
(China); Berkat-Honeywell
Sdn Bhd (Malaysia); Sinopec
Honeywell (Tianjin) Ltd.
(China); Yamatake Corporation
(Japan); Tata Honeywell Ltd.
(India); LG-Honeywell Co.,
Ltd. (Korea)

Manufacturing:

Sydney, Australia; Auckland,
New Zealand; Taipei, Taiwan;
Shenzhen and Tianjin, China

Joint Venture Manufacturing:

Pune, India; Fujisawa, Hadano,
Kamata, Isehara and Shonan,
Japan; Bupyeong, South Korea

Distributors:

Bangladesh; Brunei; Guam;
Sri Lanka

Canada

Honeywell Limited

P.F. Rankine, *President*

Headquarters:

155 Gordon Baker Road
Toronto, Ontario
Canada M2H 3N7

Manufacturing:

Toronto, Ontario;
Brossard, Quebec

Europe, the Middle East and Africa

Honeywell Europe SA

W.M. Hjerpe, *President*

Headquarters:

3, Ave du Bourget, B1140,
Brussels, Belgium

Affiliates:

Austria, Belgium, Botswana,
Bulgaria, Cyprus, Czech
Republic, Denmark, Egypt,
Finland, France, Germany,
Greece, Hungary, Ireland, Italy,
Kazakhstan, Mauritius, The
Netherlands, Norway, Poland,
Portugal, Romania, Russia,
Slovak Republic, South Africa,
Spain, Sweden, Switzerland,
Ukraine, United Arab Emirates,
United Kingdom

Joint Ventures:

Kuwait, Oman, Saudi Arabia,
Turkey, Uzbekistan

Centers of Excellence and Manufacturing:

Brussels, Belgium; Varkaus,
Finland; Amiens and Grenoble,
France; Arnsberg, Maintal,
Mosbach, Neuweid, and
Shonaich, Germany;
Nagykanizsa, Hungary; Milan,
Italy; Waterford, Ireland;
Den Bosch and Emmen,
The Netherlands; Bracknell and
Newhouse, United Kingdom;
Zurich, Switzerland

Latin America

J.J. Conesa, *Vice President and General Manager*

Headquarters:

480 Sawgrass Corporate Parkway
Suite 200
Sunrise, FL 33325

Affiliates:

Argentina, Brazil, Chile, Mexico,
Panama, Puerto Rico, Venezuela,
Colombia, Ecuador and Peru

Centers of Excellence and Manufacturing:

Caracas, Venezuela; Chihuahua,
Ciudad Juarez, Distrito Federal
and Tijuana, Mexico;
Sao Paulo, Brazil

Board of Directors and Corporate Officers

Board of Directors

Michael R. Bonsignore
*Chairman of the Board and
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Honeywell Inc.*

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*Retired Vice Admiral,
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President, The Baciocco
Group Inc., a private
consulting practice*

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*John C. Hower Professor of
Public Policy and Management,
The Wharton School,
The University of Pennsylvania*

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*Chief Executive Officer,
Teléfonos de México, S.A. de C.V.,
a Mexico City-based
telecommunications company*

Giannantonio Ferrari
*President and
Chief Operating Officer,
Honeywell Inc.*

R. Donald Fullerton
*Chairman — Executive
Committee, Canadian Imperial
Bank of Commerce, a financial
services institution*

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*Chairman of the Board,
President and
Chief Executive Officer,
Northern States Power
Company, a Minneapolis-based
energy company*

Katherine M. Hudson
*President and
Chief Executive Officer,
Brady Corporation,
an international manufacturer
of industrial identification,
safety, graphics, and precision
tape products based in Milwaukee*

Bruce Karatz
*Chairman of the Board,
President and
Chief Executive Officer,
Kaufman and Broad Home
Corporation, an international
residential and commercial
builder based in Los Angeles*

A. Barry Rand
*Former Executive Vice President,
Worldwide Operations,
Xerox Corporation,
a document processing office
equipment company*

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*Chairman of the Board and
Chief Executive Officer,
Great Northern Capital,
a private asset management firm*

Michael W. Wright
*Chairman of the Board,
President and
Chief Executive Officer,
SUPERVALU INC., a major
food distributor and retailer*

Corporate Officers

Michael R. Bonsignore
*Chairman and
Chief Executive Officer*

Giannantonio Ferrari
*President and
Chief Operating Officer*

Betty A. Beaty
Vice President and Treasurer

Frances B. Emerson
*Vice President,
Communications*

Kathleen M. Gibson
*Vice President and
Corporate Secretary*

J. Kevin Gilligan
*President, Solutions
and Services Business,
Home and Building Control*

Edward D. Grayson
*Vice President and
General Counsel*

William M. Hjerpe
President, Honeywell Europe

Philip M. Palazzari
Vice President and Controller

Ronald E. Peterson
Vice President, Technology

James T. Porter
*Vice President and
Chief Administrative Officer*

William L. Sanders
*Vice President,
Information Systems*

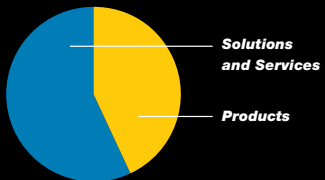
Donald K. Schwanz
*President, Space and
Aviation Control*

Lawrence W. Stranghoener
*Vice President and
Chief Financial Officer*

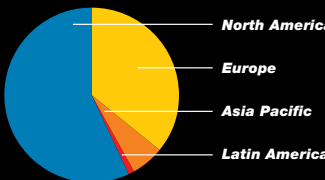
Markos I. Tambakeras
President, Industrial Control

Albrecht Weiss
*President, Products Business,
Home and Building Control*

HOME AND BUILDING CONTROL



1998 Sales Mix



Financial Results

(Dollars in Millions)

	1998	1997	1996
Sales	\$3,440.5	\$3,386.6	\$3,327.1
Operating Profit	\$348.9	\$290.2	\$345.8
Margin	10.1%	8.6%	10.4%



HOME AND BUILDING CONTROL

Consumer Products: Air cleaners, thermostats, heaters; humidifiers; fans; and ceiling fans.

Control Products: Perfect Climate Comfort Center® System; whole-house humidifiers; SysNet™ Facilities Integration System; thermostats; HVAC equipment controls; integrated/electronic furnace and boiler controls; demand-side energy management systems; energy-efficient lighting equipment; utility services; water controls; direct-coupled actuators; zoning systems; media controls; heat recovery and energy recovery ventilators.

Solutions and Services Business: Enterprise building solutions for improved business outcomes, including building controls; facility integration; critical environments; energy and process utilities; integrated security and asset management; and building information services.

REPRESENTATIVE CUSTOMERS

Architects and developers; building managers and owners; consulting engineers; contractors; distributors and wholesalers; hardware and home center stores; heating, ventilation and air conditioning equipment manufacturers; home builders; consumers; airports; healthcare facilities; hotels; manufacturing facilities; office and government buildings; restaurants; retail stores; education facilities; utilities; and security directors.

HIGHLIGHTS

- Introduced New Valve Platform (NVP), bringing superior gas systems technology to new growth areas in decorative gas fireplaces and other gas-powered home and smaller commercial appliances.
- Introduced Integrated Valve Train, with breakthrough technology that allows customers to reduce the size, labor and inventory costs for commercial and industrial gas valves.

- Introduced new family of oil-hydraulics products, moving from labor- and capital-intensive electro-mechanical designs to electronic controls, which offer both manufacturing and product feature benefits to the end user.
- Added consumer product distribution in Target and Wal-Mart, and continued focus on key category partnerships with Sears, Lowe's and Home Depot.
- Introduced the industry's first all-in-one fresh air economizer with demand-controlled ventilation. The system eliminates excessive ventilation in commercial buildings for greater energy savings and improved comfort, and by optimizing ventilation based on input from two to 10 different sensors.
- Introduced Flica, a leading European manufacturer of refrigeration valves, and acquired Elm Controls Ltd., a leading supplier of control systems and products for supermarket and commercial refrigeration applications, with a strong record of developing innovative products and the first "open-systems" Echelon-based control system for supermarket refrigeration.

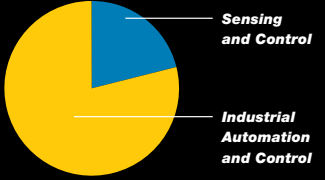
- Acquired Westinghouse Security Electronics, Inc. (WSE). WSE designs, manufactures and sells access control through a worldwide system integrators network, allowing channel expansion for electronic access control products and a complete product portfolio to the growing global market.
- Completed acquisitions of two service companies, M&E Sales in Baltimore, Md., and Thermal Control Inc. in El Paso, Texas, to help grow the business and provide advanced, technology-oriented services.
- Continued to succeed in the building security marketplace as several large orders were received for Excel Security Manager (XSM) systems, including a \$4 million order at the Dubai

- International Airport. Security growth prospects were further enhanced by the following acquisitions and alliances: the acquisition of ESD Electronics, a Dutch supplier of high-end networked access control and security system applications; the acquisition of VVE Security, a commercial security firm serving the New York City metropolitan area; and the strategic alliance with Kronos, Inc., to provide integrated time and labor management and security control solutions.
- Chosen by the U.S. government for energy savings performance contracts to upgrade government facilities (potentially worth \$750 million over the next 25 years), and by the U.S. Air Force for bases in nine western U.S. states under an indefinite delivery, indefinite quantity program with the Air Force (potentially worth up to \$250 million).

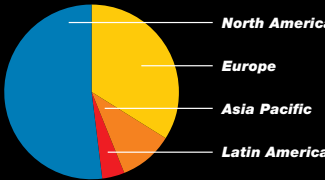
- Chosen to provide the building automation and control systems for the new Cargo Terminal at the new Hong Kong airport, as well as the building automation controls for the new airport in Kuala Lumpur.
- COMPETITIVE ADVANTAGES**
Large installed base, open systems solutions, systems integration expertise, broad range of product offerings, global distribution network, targeted market focus.
- COMPETITORS**
Johnson Controls, Siebe, Emerson, Holmes, Alerton, Siemens, Fireye, Carlin, S.I.T., and Tyco.
- KEY STRATEGIES**
 - Expand overall business through product and application innovation, geographic growth, acquisitions with the Air Force (potentially worth up to \$250 million).

- Develop an end-user application solutions business that delivers improved business outcomes.
- Grow the Services business by creating advanced services offerings and through acquisitions.
- Expand Products business by extending home systems leadership, leveraging home comfort, security and combustion competencies and expanding cooling and refrigeration portfolio.
- Expand geographic areas and retail product categories in Consumer Products business.
- Grow the fire and security business both organically and through acquisitions.

INDUSTRIAL CONTROL



1998 Sales Mix



Financial Results

(Dollars in Millions)

	1998	1997	1996
Sales	\$2,516.3	\$2,547.1	\$2,199.6
Operating Profit	\$314.2	\$309.2	\$254.9
Margin	12.5%	12.1%	11.6%



INDUSTRIAL CONTROL

Industrial Automation and Control Products and Solutions: Advanced control software and industrial automation systems for control and monitoring of continuous, batch and hybrid operations; process control instrumentation; analytical instrumentation; field instrumentation; recorders; controllers; flame safeguard equipment; web inspection; production management software; programmable controllers; communications systems for industrial control equipment and systems; and professional services, including consulting, networking, engineering and installation.

Honeywell-Measurex Products and Solutions: Measurement, control and industrial automation systems that unify business and control information for the pulp and paper industry and other continuous web producers in the paper, plastics, metals, rubber, non-wovens and printing industries worldwide, providing sensor-based quality

control, distributed control and cross-directional control systems, web inspection systems, paper machine actuators and professional services including: consulting, optimization, engineering and installation.

Sensing and Control Products and Solutions: Solid-state sensors for position, pressure, airflow, temperature and current; optical-based sensors; precision electromechanical switches; PC-based control systems; manual controls; smart micro-processor-based sensors; fiber-optic components; and industrial safety products.

REPRESENTATIVE CUSTOMERS

Refining and petrochemical firms; chemical plants; oil and gas producers; food and beverage processors; pharmaceutical companies; pulp and paper mills; newspaper companies; metals and mining; utilities; plastics; film and coated producers; medical equipment manufacturers; textile manufacturers; heat treat processors; flame safeguard

equipment; computer and business equipment manufacturers; data acquisition companies; packaging and material handling operations; appliance manufacturers; automotive companies; aviation companies.

HIGHLIGHTS

- Signed agreements with Exxon, Mobil, Phillips CITGO, Petrofina and MOL making Honeywell a preferred supplier of systems and services.
- Introduced OpenField™, an encompassing fieldbus solution that includes integration with TPS, field instruments, tools, devices, and extensive services.
- Introduced @sset.MAX™, a full suite of software solutions that protect customer assets, including people, plants, and equipment.
- Created and launched the Solution Support Center, a new customer support operation that consolidates multiple service centers into a single point of contact for customers.

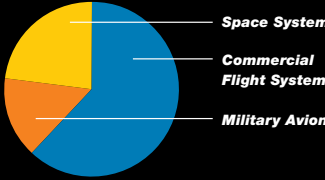
- Introduced PlantScape™SCADA, a hybrid system tailored for industries requiring remote communications and device control.
- Acquired Data Instruments Inc., a Massachusetts-based manufacturer of pressure and position sensors and sensor-based factory automation and safety equipment.
- Introduced PlantScape Vista™, a system for smaller manufacturing and processing environments.
- Introduced MXProLine Measurement and Control system for flat sheet production.
- Introduced SpectraFoil full-sheet measurement sensor—the industry's first scannerless measurement system, and FullWeb Advanced Systems Technology wet-end optimization package.
- Reorganized to improve responsiveness to customers, enhance productivity and flexibility and emphasize cross-functional rotation.

- Announced a full-scale entry into the machine safety business in North America with one of the industry's broadest portfolios of machine safety products.
- Transitioned the temperature and moisture sensor business to Juarez, Mexico.
- Received Product of the Year Award from *Plant Engineering* magazine for diagnostic limit switches.
- Grew VCSEL (Vertical Cavity Surface Emitting Laser) business by over 500%.
- COMPETITIVE ADVANTAGES**
Technology strength and innovation, applications and advanced control expertise, cost-competitive manufacturing, unmatched global services, industry knowledge, large installed base, global reach, systems integration and advanced control software.

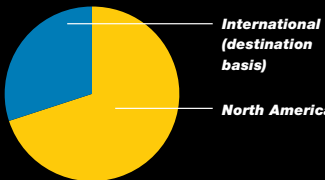
- COMPETITORS**
Asea Brown Boveri, Elsas-Bailey, Fisher-Rosemount, Siebe (Foxboro), Siemens, AspenTech, Yokogawa, Allen-Bradley, Banner, Cherry, Omron, Sprague, Telemecanique, Turck.
- KEY STRATEGIES**
 - Provide the best-value integrated system solutions (TotalPlant Solution system) for defined industries.
 - Provide customers around the world with technology solutions through internal development, alliances and partnerships, and acquisitions.
 - Balance business by pursuing growth in products, systems and service.
 - Capitalize on geographic growth opportunities for systems and solutions; focus on fast-growing global segments including information technology and onboard automotive sensors.

- Grow smart sensor business and integrate factory floor solutions with intelligent sensors.
- Sustained performance through continued solution leadership, superior technology and operational excellence.

SPACE AND AVIATION CONTROL



1998 Sales Mix



Financial Results

(Dollars in Millions)

	1998	1997	1996
Sales	\$2,339.1	\$1,956.9	\$1,640.0
Operating Profit	\$334.0	\$255.7	\$163.3
Margin	14.3%	13.1%	10.0%



SPACE AND AVIATION CONTROL

Major Products: Integrated cockpit avionics, including automatic flight controls, electronic display systems, flight management systems; global positioning system (GPS) based avionics; communications systems; traffic alert and collision avoidance systems (TCAS); automatic test systems; helmet-mounted display and sighting systems; space instruments and sensors; data management and processing systems; inertial reference systems; inertial navigation systems; integrated radio systems; and differential GPS-based landing systems and surface vehicle tracking.

REPRESENTATIVE CUSTOMERS

Airframe manufacturers; international, national and regional airlines; corporate operators; NASA; prime U.S. defense contractors; the U.S. Department of Defense; allied military forces; and airports.

HIGHLIGHTS

- Received U.S. military indefinite delivery/indefinite quantity (ID/IQ) contract awards for commercially developed equipment including traffic collision avoidance systems, weather radar units and the XS950 Mode S/IFF transponder.
- In cooperation with Boeing, developed a commercial-based, advanced multipurpose display core processor and 5x5 color display for the F-15/F-18 with significant reduction in development-to-test-flight cycle time.
- Selected by Lockheed Martin to develop the 4x4 color display system for the U.S. Air Force F-16 Common Configuration Implementation Program (CCIP).
- Selected by United Defense, L.P. to provide four computer software configuration items for Crusader, the U.S. Army's premier ground vehicle development program.

- Selected by Boeing to provide the Inertial Measurement Unit (IMU) for the Joint Direct Attack Munition program.
- Selected by Lockheed Martin to provide an F-16 avionics depot to the Republic of Korea Air Force.
- Selected by General Dynamics Amphibious Systems to provide the Marines' number one development program—the Advanced Amphibious Assault Vehicle—with the Tactical Advanced Land Inertial Navigation (TALIN) system.
- Won United Defense, L.P. "Supplier of the Year" award for work on the Crusader program.
- Introduced, in partnership with Racal, an enhanced satellite communications system for commercial airliners and business jets for 2000 and beyond.
- Chosen by Federal Express to supply collision avoidance systems for their cargo jet fleet.

- Received FAA certification for the "Pegasus" flight management system, ushering in the long-anticipated era of Communication, Navigation, Surveillance/Air Traffic Management (CNS/ATM) with the eventual evolution to "free flight."
- Selected by NASA to lead an 11-member industry team to create a worldwide aviation weather distribution and display system, Aviation Weather Information System (AWIN)—a veritable weather channel in the sky.
- Launched the latest addition to the WorldNav CNS/ATM product line with a Communications Management Unit designed to support future airborne data link applications in the airline, regional and defense markets.
- Earned the world's first airliner certification for "Aero-I" SATCOM on the Boeing 737-800 at launch customers Royal Air Maroc and Hainan Airlines.

- Acquired Hughey & Phillips of Simi Valley, CA, and Daimler-Benz Airport Systems, headquartered in Wedel, Germany, building on Honeywell's Airport Systems business.
- Celebrated the first commercial landing of an aircraft using the Honeywell/Pelorus SLS-2000 GPS Landing System, the only GPS Landing System (GLS) in the world that has received all necessary approvals from the Federal Aviation Administration (FAA).
- Won contracts to provide Primus Epic™ next generation integrated avionics systems in all three of Business and Commuter Aviation Systems' (BCAS) major markets—business, regional and helicopter aircraft.
- Shipped the 1000th TCAS 2000 unit at the end of November, making the enhanced Traffic Alert and Collision Avoidance System one of the most successful new product launches in S&AC history.

- Expanded our commercial space product offerings with new standardized mechanisms and reaction wheels from Hughes Space and Communications and Loral Space in the fourth quarter for commercial spacecraft mechanisms.
- Signed a long term Memorandum of Understanding with Boeing North America to provide avionics upgrades for the Space Shuttle.
- Awarded a Lockheed Martin contract for the development and production of a next generation launch vehicle guidance system for the Evolved Expendable Launch Vehicle and Atlas/Titan launch vehicles.
- Selected by Space Port Florida to provide major elements of a low cost launch Range Safety system.
- COMPETITIVE ADVANTAGES**
Leading industry position, significant product breadth, systems integration expertise, technological strength, worldwide customer support;

- ability to bring affordable, commercially based solutions to 21st century military requirements.
- COMPETITORS**
Allied Signal, Litton, Kaiser, Rockwell, Sextant.
- KEY STRATEGIES**
 - Apply commercial products and technology to government markets.
 - Expand into adjacent product and service markets through internal development, alliances and acquisitions.
 - Use Space and Aviation Control synergies to improve operational performance and competitiveness.
 - Maintain leading position as supplier of avionics systems by capitalizing on advanced systems architectures derived from work on 777 aircraft and Primus Epic.
 - Mitigate future cyclicality in commercial aircraft sector through aggressive growth initiative actions.

Shareowner Information

Honeywell Inc. and Subsidiaries

Stock Exchanges

Honeywell common stock is traded principally on the New York Stock Exchange (ticker symbol: HON). The stock is also listed on exchanges in London, Paris, Amsterdam, Antwerp, Brussels and Zurich.

Shareowner Return

The market value of Honeywell common stock on December 31, 1998, was \$75 $\frac{1}{2}$ per share. Honeywell shareowners have realized a compound annual rate of return (with reinvestment of cash dividends) of approximately 19.5 percent for the five-year period ended December 31, 1998.

Dividends

Quarterly dividends on common stock are normally paid in the months of March, June, September and December.

At its October meeting, the company's board of directors increased the quarterly dividend to 29 cents a share, equivalent to an annual dividend of \$1.16 per share.

Shareowner Inquiries

Questions regarding ownership of Honeywell Inc. stock, dividend checks and direct deposit, address changes, status of an account or stock transfer may be directed to:

ChaseMellon Shareholder Services, L.L.C.
P.O. Box 3315
South Hackensack, NJ 07606
1 (800) 647-7147

For shareowner on-line services and a Honeywell Inc. profile, access: <http://www.chasemellon.com>, or for information about Honeywell Inc. and a copy of the annual report, access: <http://www.honeywell.com>.

Dividend Reinvestment

All shareowners of record are invited to participate in the company's automatic dividend reinvestment plan. The plan gives shareowners a convenient and economical way to reinvest their dividends in Honeywell stock and/or invest additional cash contributions free of brokerage or service charges.

For further information, contact:

The Chase Manhattan Bank
c/o ChaseMellon Shareholder Services, L.L.C.
Dividend Reinvestment Department
P.O. Box 3315
South Hackensack, NJ 07606
1 (800) 647-7147

E-mail address:
shrrelations@chasemellon.com

To obtain a free copy of the annual report, 10-K, 10-Q, proxy or quarterly earnings release, contact:

Customer Assistance Center
Honeywell Inc.
P.O. Box 524
Minneapolis, MN 55440-0524
1 (800) 345-6770

E-mail address:
investor@corp.honeywell.com

To request an annual report or the above material directly, access: <http://www.honeywell.com/investor/printmatreq>

Analysts or Investors may direct their questions to:

Scott M. Clements
Director, Investor Relations
Honeywell Inc.
P.O. Box 524
Minneapolis, MN 55440-0524
(612) 951-2122

E-mail address:
investor@corp.honeywell.com

Honeywell Information and Inquiries

Corporate Offices

Honeywell Inc.
Honeywell Plaza
Minneapolis, MN 55408
(612) 951-1000

Internet Address

For the company's annual report and financial information, company facts, product descriptions, news releases and historical data, access Honeywell on the Internet at:
<http://www.honeywell.com>.

Annual Meeting

The annual meeting of shareowners will be held at the Minneapolis Convention Center, 1301 Second Avenue South, Minneapolis, Minnesota on April 20, 1999, at 2:00 p.m. A meeting notice and proxy materials were mailed to all shareowners of record as of February 19, 1999.

Shareowners are encouraged to vote their shares for the meeting via telephone or the Internet. Instructions will be provided on the proxy card you receive.

Independent Public Accountants

Deloitte & Touche LLP
400 One Financial Plaza
120 South Sixth Street
Minneapolis, MN 55402
(612) 397-4000

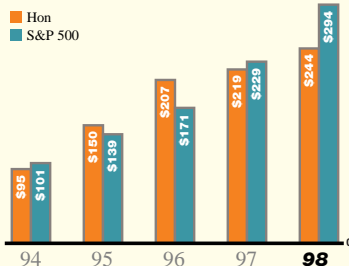
Duplicate Annual Reports

Securities and Exchange Commission rules permit us to send a single copy of this Annual Report to Honeywell shareowners residing in the same household, provided you consent in writing. If this Annual Report is a duplicate copy for your household, you may discontinue receiving the duplicate copy by marking the appropriate box on the proxy card that may accompany this Annual Report. If you mark the box on your proxy card, we will not send future annual reports to the account address on your proxy card unless you contact us to resume mailings.

Forward-Looking Statements

This Annual Report contains forward-looking statements which are based on current expectations, estimates and projections. These statements are not guarantees of future performance and involve risks and uncertainties which are difficult to predict. For a discussion of these risks and uncertainties, please refer to page 33 of this Report and to Forms 10-Q and 10-K which we file with the Securities and Exchange Commission.

Total Shareowner Return



Annual Dividend Performance

