

Oil Field Products and Services LUFKIN IS A LEADING GLOBAL PROVIDER of artificial lift oil field equipment and services, primarily consisting of highly adaptable pumping units, automation technology equipment and a variety of services including on-site installation, technical support and maintenance. Additionally, the Company operates a gray and

ductile iron foundry producing up to 300 tons per day of captive and commercial castings for the heavy equipment, valve and machine tool markets. Lufkin maintains a significant presence in all major oil markets.



Power Transmission Products and Services LUFKIN IS ALSO A LEADING WORLDWIDE PROVIDER of power transmission equipment, primarily precision-made gears in weights of from 300 pounds to 250 tons and in power levels from 20 to 85,000 horsepower. These highly engineered products are used in industrial applications in a variety of industries, such as oil and gas,

petrochemical, steel, plastics, sugar, rubber, marine and power generation. Lufkin's global service organization supports new equipment sales as well as an extensive after-market for installed power transmission equipment.



Trailers LUFKIN DESIGNS AND MANUFACTURES many different sizes and styles of platforms and high capacity, lightweight dump trailers, primarily for sale in its core South Central U.S. market. Lufkin's trailers are known for their quality construction, reliability, innovative design and competitive price. The Company has been in the trailer business for over 65 years.



ANNUAL REPORT

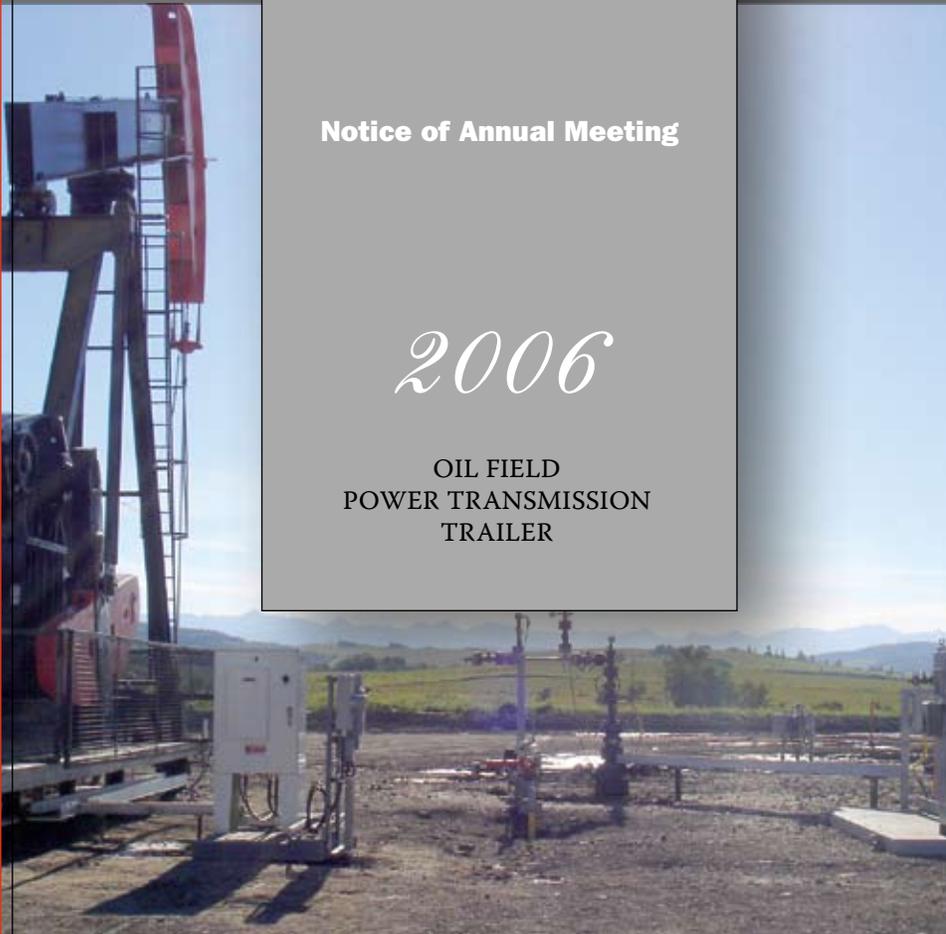


Notice of Annual Meeting

2006

OIL FIELD
POWER TRANSMISSION
TRAILER

The Annual Meeting of Shareholders of Lufkin Industries, Inc. will be held at the Museum of East Texas, 503 North Second Street, Lufkin, Texas on May 2, 2007, at 9:00 a.m. local time.



(Thousands of dollars, except per share amounts)	December 31,				
	2006	2005	2004	2003	2002
Sales	\$605,492	\$492,167	\$356,281	\$262,255	\$228,724
Operating expenses	502,237	422,961	333,568	247,782	215,314
Earnings before income taxes	104,729	69,275	22,704	15,706	13,767
Net earnings	72,994	44,544	14,417	9,738	8,535
Earnings per share:					
Basic*	\$4.92	\$3.10	\$1.06	\$0.74	\$0.65
Diluted*	\$4.83	\$3.03	\$1.04	\$0.73	\$0.63
Dividends per share*	\$0.62	\$0.38	\$0.36	\$ 0.36	\$0.36
Total assets	429,069	359,795	300,269	263,656	248,355
Working capital	181,957	133,628	87,231	70,831	64,421
Long-term notes payable, net of current portion	-	-	-	-	164
Shareholders' equity	328,140	261,078	208,932	188,196	178,949

* Years 2002 - 2004 adjusted for 2-for-1 Stock Split effective on April 19, 2005.



ANNUAL REPORT



Letter to the Shareholders

2006

OIL FIELD
POWER TRANSMISSION
TRAILER



Douglas V. Smith
President and Chief
Executive Officer

Letter to the Shareholders

It is with pleasure that we report Lufkin Industries' strong profitable growth for 2006, our third consecutive year in which earnings per diluted share has increased at a rate in excess of 40%. We are very proud of this performance and of the flexibility and innovation our entire organization has demonstrated in responding to our customers' pressing needs, while continuing to build the foundation of the business for long-term growth. As a result, and despite the operational challenges presented by our more than doubling revenues and expanding earnings per diluted share more than six-fold in the past three years, we are well prepared to meet demand for 2007 in each of our businesses.

For 2006, our growth primarily reflected rising oil prices and worldwide demand for energy, which drove significantly higher sales from both domestic and international customers for all of our primary oil field and power transmission products and services. In addition, in response to evolving market needs in the trailer market, we initiated important steps that we expect will produce more consistent and profit-

able growth. Meeting the increased demand evident in our sales growth required an extensive effort throughout the Company to expand capacity during 2006, as well as the associated effort to increase our workforce and procurement. Despite the operating inefficiencies inherent in such an effort, each of our businesses again produced an increased gross margin for 2006, contributing to the expansion of our overall profitability.

Our total sales for 2006 were a record \$605.5 million, an increase of 23% over sales for 2005. Due to strong bookings, particularly in our power transmission division, our backlog increased 23.8% to \$181.1 million at the end of 2006 from the end of 2005. Because of our effort to expand capacity, we reduced our backlog by the end of 2006 from a high of \$208.3 million at the end of the second quarter of 2006. As a result, we completed the year with a reduced backlog with acceptable product lead-times, supporting our continued ability to differentiate Lufkin through our highly competitive order-to-shipment cycle.

The growth in our sales, as well as continued relative stability in the cost and availability of our raw materials, contributed to greater operating leverage for the year. Gross margin increased to 25.8% of sales for 2006 from 23.0% for 2005, and selling, general and administrative expenses declined to 8.8% of sales from 9.0%. Reflecting these improvements, operating income increased 49.1% for 2006 to \$103.3 million, or 17.1% of sales, from \$69.2 million, or 14.1% of sales, for 2005. Primarily as a result

of this growth, net earnings for 2006 increased to \$73.0 million, or \$4.83 per diluted share, from \$44.5 million, or \$3.03 per diluted share, for 2005. Our results for 2006 included a net benefit of \$0.14 per diluted share comprised of a benefit of \$0.30 per diluted share associated with the finalization of various tax estimates and tax initiatives; an expense of \$0.12 per diluted share cost related to SFAS 123R (Expensing of Stock Options) and an expense of \$0.04 per diluted share to dispose of inventories and fixed assets related to a portion of our trailer business.

Our financial position also strengthened during 2006, as our increased profitability generated 284% growth in cash flow from operations to \$67.4 million for 2006. After capital expenditures of approximately \$31 million for 2006 and a 67.9% increase in our cash dividend to \$9.2 million for 2006, our cash and cash equivalents more than doubled to \$57.8 million at the end of 2006 from \$25.9 million at the end of 2005. Shareholders' equity increased 25.7% during 2006, and with no bank debt at the end of the year, we continued to have full availability on our \$27.5 million credit facility.

After three years of strong profitable growth for Lufkin, the decline in oil and other commodity prices in the fourth quarter of 2006, as well as increased uncertainty in the economic environment, tempered the momentum we experienced throughout the first three quarters of the year. Based on our customers' indications, we are cautiously optimistic about growth in demand for 2007 and our

prospects for continued profitable growth. With long industry experience, we also recognize the volatility inherent in the energy markets and the impact the macro environment can have on any company's plans or expectations. Our focus, therefore, remains on building sustainable leadership in each of our markets through steady expansion, high quality products and outstanding customer service. We are confident that in the future, as in the past, successful execution of this focus will enable us to achieve our goals for long-term growth in earnings per diluted share and shareholder value.

Oil Field – Our oil field business again led our financial results, with growth in sales of 30.7% for 2006 to \$401.2 million. This growth reflected strong demand for our pumping units for both oil and natural gas applications in North American, South America, the Middle East and other international markets. With bookings outpacing production in the first half of 2006, our oil field backlog rose to \$91.0 million at the end of the second quarter. As additional manufacturing capacity became available in the U.S., Canada and Argentina, coupled with some softening of demand, backlogs were down to \$67.1 million at year end, helping to drive oil field sales to over \$100 million for each of the third and fourth quarters.

Given the premium on extending the life of producing wells, both our oil field automation and services businesses also grew significantly for 2006, up 66% and 18% from 2005, respectively. To relieve a primary bottleneck

for our automation business, we reorganized the team to support the addition of new employees. We also focused on expanding the worldwide oil field services team. Reflecting the growing international oil field opportunity for Lufkin, we experienced substantial automation and services sales growth outside the U.S. for 2006, and we expect this trend to continue for 2007.

Through strong oil field sales, the division produced operating leverage that more than offset increased expense and reduced productivity associated with capacity expansions. A key component of our manufacturing operating leverage for 2006 was the high capacity utilization at our foundry, which provided most of its output for internal use instead of third party commercial applications. The combination of these factors resulted in an increase in the oil field gross margin, to 27.3% for 2006 from 24.9% for 2005.

Power Transmission

– Bookings for the power transmission division rose to a record level for 2006, with sales, which grew 17% to \$124.9 million for 2006 from 2005, increasing on a comparable-quarter basis for each consecutive quarter of the year. In addition, the power transmission backlog, which expanded 79% during 2006 to record \$95.6 million at the end of 2006 from the end of 2005, also increased. Similar to

our oil field business, sales rose for each of our power transmission businesses, domestically and internationally and across nearly all the industrial markets we serve.

Global energy demand dominated our orders for high speed gears, with applications in oil and gas production, transportation and refining increasing substantially. Both our U.S. and France manufacturing operations were heavily engaged in meeting this demand, and each added capacity during the year. Our low speed gears used primarily in industrial applications reflected rising commodity prices through much of 2006, as gear applications in industries producing or handling commodity materials, such as rubber, steel, aluminum, increased demand. Due in part to increasing lead times on new projects, we also experienced 23% growth in our gear repair and retrofit business, as companies around the world refurbished existing machinery or brought mothballed production capacity into operation.

The record level of power transmission production Lufkin accomplished during 2006 generated economies of scale resulting in an expanded gross margin for the year of 32.8% compared with 30.3% for 2005. In addition to the business represented by our backlog, we believe our power transmission business is well positioned to

expand bookings and margins further. Our confidence is based on our growth into one of the world's leading providers of power transmission products and services through short production lead times. In addition, in spite of short-term volatility, energy demand is expected to grow over the longer term. In addition, demand for electricity generation in developing countries around the world is growing rapidly, with tremendous market opportunity in China and India, among other countries. We are also successfully increasing sales of power transmission products and services in international oil and gas markets, such as the Middle East, West Africa and South America.

Trailer – Operating and financial results for our trailer business for 2006 reflected the continued softness in the van trailer segment and our decision in the third quarter to exit that business. Through this decision, we are able to focus our trailer resources on expanding our capacity to manufacture our more profitable flat bed trailer and specialized dump trailer product lines, for which demand has remained robust. In addition, we are converting a portion of our trailer manufacturing capacity to production of products for our oil field business, whose facilities in Lufkin are adjacent to the trailer factory.

Sales for the trailer division totaled \$79.4 million for 2006, an increase of 1.1% from 2005. The trailer backlog at the end of 2006 was \$18.4 million compared with \$25.5 million at the end of 2005, partially due to an \$6 million reduction in van backlog related to the exit decision. As mentioned above, we also disposed of inventories and fixed assets related to the van business at an approximate cost of \$950,000, or \$0.04 per diluted share after tax.

The growth we have consistently achieved in sales of flat and dump trailers is partially attributable to innovative new product introductions that are often designed to meet specific needs of customers. Although these markets are smaller than the van market, the value-added nature of this design enables us to differentiate our products on other qualities in addition to price. The improved profit potential of the trailer division after exiting the van business is evident in the 290 basis point improvement in gross margin, excluding the disposal costs discussed above, to 8.6% for 2006 from 5.7% for 2005. In addition, lead times for flat bed trailers and dump trailers had become extended during 2006, and the completion of the conversion of the van manufacturing lines to these products in early 2007 supports the acceleration of our trailer sales efforts.

Summary – The key to leveraging the strong 2006 market conditions we have described in this letter into the substantial profitable growth we achieved for the year was execution, every day, by people throughout our organization. As we look forward to 2007 with less visibility than we enjoyed at the start of 2006, we remain confident in Lufkin's market positioning, its business model and resources, and its people. In essence, we are cautiously optimistic about growth in 2007, but we have little doubt about our ability to drive long-term growth and increased shareholder value. We thank all the people of Lufkin for their continuous work to strengthen this Company. In closing, we also wish to thank our Board of Directors for their disciplined oversight and commitment and you, our fellow shareholder, for your investment in the Company

Sincerely,



Douglas V. Smith
President and Chief Executive
Officer



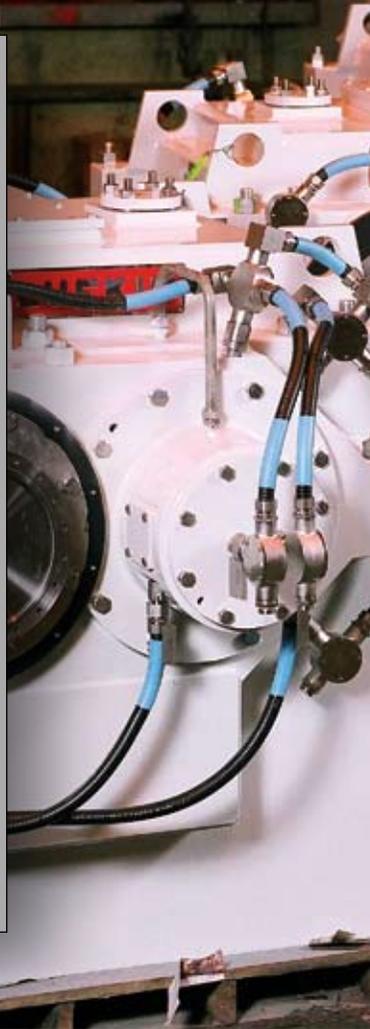


OIL FIELD and
POWER TRANSMISSION
DIVISIONS

LUFKIN
LUFKIN INDUSTRIES

2006

ANNUAL REPORT



OIL FIELD DIVISION

The Oil Field Division is a vertically integrated global leader in the manufacture, installation and service of beam lift pumping units. The Company commands a significant share of its markets, which include capital equipment, automation technology equipment and service. To serve these markets, Lufkin operates manufacturing facilities in three countries and has an international network of service centers, sales offices or sales representation affiliations in over 40 countries

The Company produces beam lift pumping units that address the particular well-depth and fluid-production characteristics of each application. In addition to the market for oil wells, Lufkin pumping units are used to lift water off of natural gas wells. Lufkin can provide a full system including design, installation, and field maintenance.

Lufkin also sells oil field automation equipment that reduces the cost of operating and maintaining pumping equipment by automating the operation of the pumping units using software and instrumentation. In addition to automating pumping units, Lufkin supplies control equipment to automate gas injection and progressive cavity pump wells. Sales of a Lufkin controller combined with a variable frequency drive system grew substantially this year. Lufkin is a world leader in the sale of rod pump automation

controllers, offering products with advanced technological features that differentiate them from other products currently in the market.

Lufkin supports its pumping unit equipment products business with its service organization, through which the Company installs repairs and maintains equipment. A natural extension of its pumping unit and automation businesses, the expansion of the Company's service capabilities has been an integral part of its strategy to become an integrated provider of oil field beam lift products and services. Lufkin has service centers in the U.S.A., Canada, Argentina, Oman and Egypt. These service centers install, optimize, maintain, and repair Lufkin equipment.

Another aspect of the Company's vertical integration capabilities, Lufkin operates a gray and ductile iron foundry capable of producing high quality captive and commercial castings ranging in size from 100 pounds to 15 tons for pumping units and for external customers for the heavy equipment, valve and machine tool markets. Having a captive foundry resource has enhanced the Company's competitive position by reducing lead times for production of oil field and power transmission castings, thus enabling the Company to respond to tight customer delivery and quality requirements.

POWER TRANSMISSION DIVISION

Lufkin is one of the world's leading suppliers of mechanical power transmission products and services. The power transmission division's products are primarily highly engineered, precision gears that function as speed increasers or

speed reducers. They range in weight from 300 pounds to 250 tons and transmit power from 20 to 85,000 horsepower. Lufkin is able to provide full product engineering and manufacturing in both the US and Europe through modern, capable factories. The division differentiates itself through its engineering excellence, superior customer service, product reliability, rapid delivery and strong after sales support.

The market for power transmission products is divided into high-speed and low-speed gear units. One of the primary markets for Lufkin's high-speed gears is in oil and gas applications in which the gearbox is used to convert power to drive compressors and pumps. Our gear products are found on land and offshore platforms for gas compression or oil transmission. They are used in the production of liquefied natural gas (LNG), in petrochemical and refining processes and in electrical power generation application.

In all these applications, the consequences of equipment failure could be both costly and disruptive. Consequently, Lufkin's expertise in engineering, metallurgy and manufacturing combine to produce products with a proven history of reliability and long service life. Reliability and safety translate into increased production and superior utilization levels that add value to the users and provide Lufkin with a strong competitive advantage. In addition to our product strengths, Lufkin offers the logistical advantage of design, manufacturing and mechanical testing capabilities in both Europe and the U.S. We are the only gear manufacturer able to offer that level of global support.

The power transmission division delivered a record year in both sales and order intake. Sales of \$125 million were up 17% from \$107 million in 2005. In spite of record shipments, new order intake of \$167 million resulted in a year end backlog of \$95.6 million, up 79% from the \$53.4 million backlog at the end of 2005.

The growth in the division continued to be driven by strong markets, coupled with our strategy to expand the division's global reach. Strong energy markets drove the demand for our high-speed turbo gears. These gears are used in compressor, pump and generating applications in oil and gas production, processing, transportation and refining processes. New orders from the oil and gas production sector nearly doubled from the 2005 level of \$30 million to \$58.6 million, following a 75% growth in this sector from 2004 to 2005. Bookings from the oil refining sector rose from \$10.9 million in 2005 to \$15.8 million in 2006. This 45.6% growth follows a year in which bookings for this sector increased 58%. Investment in this sector continues to be driven by both capacity expansions to address the growing, global demand for gasoline and diesel, as well as the environmental requirements in both Europe and the U.S. to reduce the sulfur level in both gasoline and diesel fuels.

Bookings from the Petrochemical sector also showed continued growth from 2005 levels of \$12.2 million, rising 15% to \$14.1 million during 2006 as prices for Chemical products recovered and producers stepped up investment in process related equipment.

New product designs and improved sales focus resulted in a similar 45% increase in bookings from the power generation segment of our business. In 2005, bookings from this sector were \$12.2 million, as compared to \$17.7 million in 2006. Again, this followed a year in

which bookings from this sector more than doubled. Lufkin Industries supplies gearboxes for use with both Steam and Gas turbines that are used in electrical power generation applications. Environmental concerns continue to encourage industrial users who have waste heat to utilize that heat in cogeneration applications.

Lufkin Industries also supply low-speed gear products for mining, metals processing and marine propulsion applications. While demand from both mining and metals processing declined during 2006 from the record levels booked during 2005, bookings from these sectors remained strong compared to historic booking levels. Demand, however, from the marine propulsion sector rose sharply from \$3.9 million in 2005 to \$9.3 million in 2006. Much of the Marine demand came from fleet expansions to transport coal on the US inland waterways and for articulated tug barges, as well as offshore supply vessels.

Our strategy to expand our sales organization in Europe and Asia continues to open new opportunities for our Power Transmission products. This is complemented by our manufacturing and engineering organizations that enable Lufkin Industries to offer superior products and services on the shortest lead times in the industry. Our unique position as the only turbo gear manufacturer with manufacturing, design and mechanical test facilities in North America and Europe enables full product support in both the Eastern and Western Hemispheres. Although we believe we are well positioned for future growth, we continue to explore promising expansion opportunities to profitably grow our Power Transmission business.



TRAILER
DIVISION



2006

ANNUAL REPORT



TRAILER DIVISION

Lufkin has served its core trailer market in the South Central United States for over 65 years. Over this time, it has built the same reputation for high quality, reliability, innovative design and competitive pricing that are the hallmarks of its other businesses. In keeping with the Company's announcement at the end of the third quarter to exit the dry freight van business, Lufkin has chosen to expand its capabilities for the more profitable platform, dump and specialty trailer models.

During 2006, the trailer division designed a new high capacity, ultra-light, quarter frame dump trailer which is slated for field testing in the first quarter 2007. It also designed an insulated bottom dump trailer for the construction market which is currently being field tested. These new products enhance Lufkin's market position and its profitability, and the Company expects to continue leveraging its strong design and production capabilities in response to demand for new products that arise from changes in materials, manufacturing techniques or customer needs.

According to analysts who track the industry, 2006 trailer sales increased to 277,000 from 251,000 for 2005, still substantially below the industry's record shipments of 303,000 units in 1999, illustrating both the potential and challenges presented by the industry. Some

analysts expect the market to decline slightly in 2007 to 265,000 units based on mixed economic indicators at the end of the year and a shortage of funds available to truckers arising from the large pre-buy of tractors in response to new Clean Air Act regulations.

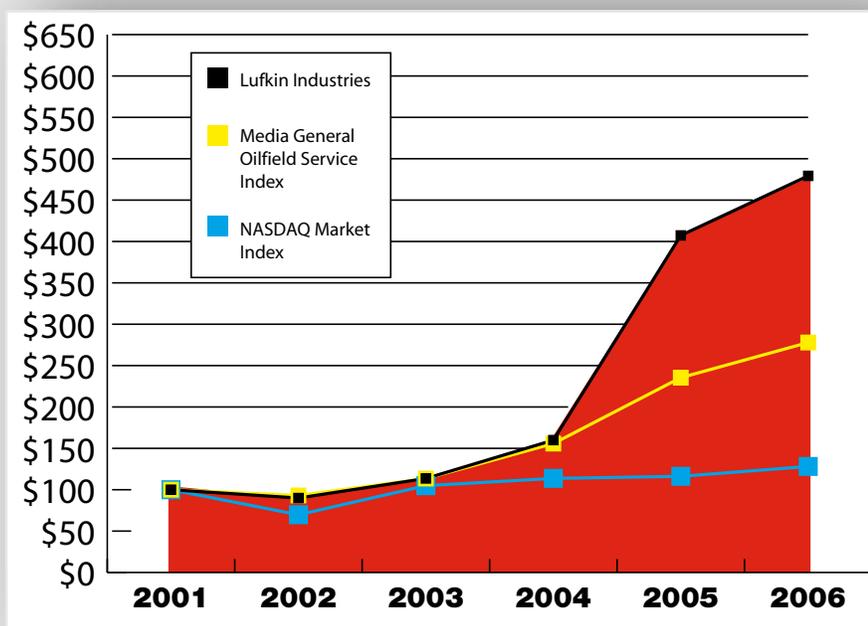
The trailer division's strategy for long-term growth in a cyclical industry is based on the expertise it has developed through many economic cycles. Lufkin continues to maintain and enhance its market position through its strong design and production capabilities, as well as through consistent efforts to broaden its base of customers. It also continues its strong cost controls, with a focus on maintaining the technical and production capacity to meet the demands of a challenging market. Based on expected steady growth in the transportation industry during the second half of 2007, the ongoing aging of transportation fleets and strong opportunities for specialty trailers, the division anticipates positive momentum for 2007.

Market Price of and Dividends on the Registrant's Common Equity and Related Stockholder Matters

Performance Graph:

The following performance graph compares the performance of the Company's common stock to the NASDAQ Market Value Index and to the Media General Oilfield Services Index (which includes the Company) for the last five years. The graph assumes that the value of the investment in the Company's common stock and each index was \$100 at December 31, 2001 and reinvestment of dividends.

COMPARISON OF CUMULATIVE TOTAL RETURN OF ONE OR MORE COMPANIES, PEER GROUPS, INDUSTRY INDEXES AND/OR BROAD MARKETS



Performance Graph data provided by R. R. Donnelley Financial.

	Fiscal Year Ending					
	12/31/01	12/31/02	12/31/03	12/31/04	12/31/05	12/31/06
Lufkin Industries	100.00	89.96	113.58	159.96	407.32	479.31
Media General Oilfield Service Index	100.00	93.04	113.49	155.77	235.41	279.90
NASDAQ Market Index	100.00	69.75	104.88	113.70	116.19	128.12



The performance graph will not be deemed to be soliciting material under the proxy rules or incorporated by reference into any filing except to the extent that the Company specifically incorporates it.



BOARD
MEMBERS



2006
ANNUAL REPORT



Douglas V. Smith
Chairman of the Board
Chairman –
Executive Committee
Board member since 1993



S. W. Henderson, III
Member –
Executive Committee
Compensation Committee
Nominating/Governance
Committee
Board member since 1971



H. J. Trout, Jr.
Chairman –
Pension Committee
Member –
Executive Committee
Nominating/Governance
Committee
Board member since 1980



Thomas E. Wiener
Member –
Executive Committee
Pension Committee
Nominating/Governance Committee
Board member since 1987



B. H. O'Neal
Chairman – Compensation Committee
Member –
Audit Committee
Nominating/Governance Committee
Board member since 1992



John H. Lollar
Chairman – Audit Committee
Member –
Compensation Committee
Board member since 1997



J. T. Jongebloed
Chairman –Nominating/
Governance Committee
Member –
Audit Committee
Compensation Committee
Board member since 2002



John F. Anderson
Member –
Executive Committee
Pension Committee
Board member since 2003



Suzanne V. Baer
Member –
Audit Committee
Pension Committee
Board member since 2005



Larry M. Hoes
Board member since 2006

Corporate Officers

D. V. Smith

*CEO,
President, Chairman*

L. M. Hoes

*Executive Vice President,
COO*

J. F. Glick

*Vice President,
General Manager –
Power Transmission Division*

S. H. Semlinger

*Vice President,
General Manager – Trailer Division*

P. G. Perez

*Vice President,
General Counsel
Corporate Secretary*

R. D. Leslie

*Vice President,
Treasurer, CFO*

Key Locations

Corporate Offices

*P. O. Box 849
Lufkin, TX 75902-0849
936-634-2211*

Houston Sales

Oil Field/Power Transmission

*450 Gears Road, Suite 550
Houston, TX 77067
281-875-6500*

Trailer Sales

*7 Miles S. Highway 69 S.
Lufkin, TX 75901
800-324-3812*

Foundry Sales

*P. O. Box 849
Lufkin, TX 75902-0849
936-634-2211*

Oil Field Domestic Service

Headquarters/Sales

*P. O. Box 849
Lufkin, TX 75902-0849
936-634-2211*

Gear Repair and Service

Headquarters/Sales

*711 Industrial Blvd.
Lufkin, TX 75904
936-634-2211*

Lufkin France

*Avenue des Chavannes
70220 Fougerolles, France
(33) 384-49-64-00*

Lufkin Canada Sales & Services

*1050 McDougall Place, 808-4th Ave. S. W.
Calgary, Alberta T2P 3E8
403-234-7692*

Lufkin Middle East

*5 Road 281, Corner of 265
New Maadi
Cairo, Egypt
202-754-8828*

Lufkin Argentina Sales & Services

*656 Reconquista 6th Floor A
1003 Buenos Aires, Argentina
(54) 297-448-1750*

Lufkin Automation

*11375 West Sam Houston Parkway
Suite 800
Houston, TX 77031
281-495-1100*

Lufkin & Partners, LLC

*Way 3312, Bld. 63 Flat 5-D Floor 5
Al-Khuwair
Sultanate of Oman
968 24475 5733*

Common Stock Transfer Agent

Computershare Investor Services, LLC

*2 North LaSalle Street
Chicago, IL 60602
866-781-1368*

Auditors

Deloitte & Touche, LLP

*333 Clay Street, Suite 2300
Houston, TX 77002-4196
713-982-2000*