**Operator:** Greetings, and welcome to the Sun Hydraulics Corporation Third Quarter 2017 Financial Results Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. If anyone should require Operator assistance during the conference, please press star, zero on your telephone keypad. As a reminder, this conference is being recorded.

I would now like to turn the conference over to Ms. Karen Howard, Investor Relations for Sun Hydraulics. Thank you, Ms. Howard. You may now begin.

**Karen Howard:** Thank you, Manny, and good morning, everyone. We certainly appreciate your time today for our third quarter 2017 financial results conference call. On the line with me are Wolfgang Dangel, our President and Chief Executive Officer, and Tricia Fulton, our Chief Financial Officer. Wolfgang and Tricia will be reviewing the results that were published in the press release distributed after yesterday's market close. If you don't have that release, it's available on our website at www.sunhydraulics.com. You will also find slides there that will accompany our discussions today.

If you look to the slide deck on Slide 2, you'll find our Safe Harbor statement. As you may be aware, we will make some forward-looking statements during this presentation and also during the Q&A. These statements apply to future events that are subject to risks and uncertainties, as well as other factors that could cause actual results to differ materially from where we are today. These risks and uncertainties and other factors are provided in the earnings release as well as other documents filed by the Company with the Securities and Exchange Commission. These documents can be found at our website or at www.sec.gov.

I also want to point out that during today's call, we will discuss some non-GAAP financial measures, which we believe are useful in evaluating our performance. You should not consider the presentation of this additional information in isolation or as a substitute for results prepared in accordance with GAAP. We have provided reconciliations of comparable GAAP to non-GAAP measures in the tables that accompany today's earnings release, as well as in the slides.

Wolfgang will get started with some highlights for the quarter. Tricia will go through the detail of the financial results, and then we'll turn it back to Wolfgang for his perspective on our outlook before we open up the line for questions and answers.

With that, it is now my pleasure to introduce Wolfgang.

**Wolfgang H. Dangel:** Thank you, Karen, and good morning, everyone. Please turn to Slide 3. We continue to be very pleased with our team's performance as we are progressing through 2017. We've had a lot of exciting activities going on, especially as teams from our two business segments have been working closely together to execute our Vision 2025. I'll get more into that in a moment.

Let me start with highlighting the financial results for the quarter. Sales nearly doubled to $88 million compared with the 2016 third quarter. Enovation Controls contributed $30.8 million in the quarter, representing 34% growth over the 2016 third quarter on a pro forma basis. Consistent with the first half of the year, the significant Enovation Controls growth has been driven by strong demand in the Vehicle Technology business, specifically the recreational equipment market, as well as our Power Controls business, benefitting from economic improvement and stable oil prices.

The rest of our business also realized significant organic growth, up by 27% in the quarter over the prior year's third quarter. Sales in all of our markets around the globe grew considerably as our many initiatives are taking hold, which I'll talk about on my next slide. Our consolidated sales growth has been particularly strong in Asia, which increased 72% over the prior year third quarter. Included in that, our organic business in Asia grew 55%. The growth trends we realized in both of our segments continued through October.

Turning to the bottom line, earnings per share were $0.42 for the quarter, or $0.43 on a non-GAAP basis. This is more than double the 2016 third quarter EPS of $0.19. The non-GAAP number is calculated in the table at the end of both the slide deck and release. It excludes a small change in fair value of contingent consideration relating to the Enovation Controls acquisition, which Tricia will discuss in more detail.

Similarly, our Adjusted EBITDA more than doubled to $22.5 million, representing almost 26% of sales for the quarter. This result is a testament to many people within our global organization working hard every day to proactively service our customers and be as productive as possible.

Finally, given our stronger than expected sales growth in both segments, we are once again increasing our revenue guidance for 2017. We now expect consolidated revenue in the $330 million to $340 million range. That reflects an increase of about 3% on the top end of the range and 5% on the bottom end. You will notice that this infers that our fourth quarter could be our softest quarter of the year, which is impacted by normal seasonality within our Electronics segment. This results from several of our OEMs having extended scheduled shutdowns around the December holiday season. Also worth noting, in a steady economic climate, our Hydraulics segment frequently experiences seasonal fourth quarter softness due to buying patterns in the industry which we serve.

Please turn to Slide 4 and I will touch on some of the investments we have made in accordance with our Vision 2025 strategic plan. As you may know, historically our Hydraulics segment did not have any application experts in the field in the Americas, and only a limited number of field application experts in other parts of the globe. In our strategic planning, we identified that we may have opportunity to drive sales growth by establishing direct relationships with OEMs and better covering the marketplace. Accordingly, we have been adding sales application specialists in the field. We are up to eight in the Americas where in the past we had none. Additionally, we are up to 23 in the rest of the world compared with six previously.

I want to report to you that we have begun seeing the benefits of these investments in our sales growth we reported this quarter, and we anticipate that we will gain additional momentum as these engineers continue to get up to speed, and as we add more application specialists in select geographic pockets. Generally, it takes about three years to realize the expected return on our investments in such personnel.

Regarding our Electronics segment, while we have seen this in the past two quarters, we are again pleased to see significant growth, resulting in record sales in the third quarter. Since the acquisition closed last December, we have been executing the operational carve-out from the previously affiliated Enovation Controls businesses. As Tricia will note, we did make some temporary investments in inventory during this quarter to ensure that the movement of production lines between facilities would be seamless to our customers. I am pleased to report that the carve-out is about to be successfully completed.

We recently launched two new products for our Hydraulics segment as follows: the October 25 announcement of the availability of the XMD electro-hydraulic valve drivers was the result of the first joint engineering development project between our Electronics and Hydraulics segments. Recall that part of our strategic rationale for the Enovation Controls acquisition was to quickly obtain significant engineering talent with electronics knowledge that could transfer relevant knowledge to our Hydraulics engineering team. We are pleased with how quickly the team completed this project. These new products are Bluetooth-configurable, emphasize our commitment to operator safety and drive a wide range of electrically-operated hydraulic valves. Target markets include many industrial applications as well as off-highway equipment used in a variety of industries, including agriculture, forestry, construction, marine, earth-moving, and material handling.

Announced last week, our second new product launch introduced a new line of Sun FLex™ electro-hydraulic cartridge valve products. This is the first of three phases and we expect to finalize the other two in 2018. We're especially excited about these 16 new solenoid operated cartridge valves and coils as they enhance our existing electro-hydraulic products and have been proven to outperform comparable valves in the marketplace. These products are ideally suited for a wide variety of demanding applications in a broad array of industries serving both the mobile and industrial hydraulics marketplace. Sun FLex™ represents our largest new product launch in nearly a decade.

Our strategic goal for our Hydraulics segment includes the introduction of more smart components and intelligent-control systems. A significant portion of our R&D is spent on the development of such products and systems and we expect this to continue.

Another strategic investment that we are making involves our organization in China. Previously, both our Hydraulics and our Electronics segments had a sales presence in the Shanghai/ Hangzhou area, each of them in a small office. We have taken the step to combine them administratively, which creates efficiency, and moved into a larger co-located facility. The new facility houses our sales and engineering functions and warehouses inventory, allowing us to grow and service the China region from within that region, which is one of our strategic goals for all geographies. This will complement the expanded production facility that we are building in South Korea, which we spoke about last quarter. We have made the initial payment for the land, and the project is progressing as planned.

With that overview, I will now turn the call over to Tricia to review the financial results for the quarter and year-to-date in a bit more detail.

**Tricia L. Fulton:** Thank you, Wolfgang, and good morning, everyone. I am starting on Slide 6 with the review of our third quarter consolidated results. Third quarter sales were $88 million, up 95% compared to last year's quarter. This includes $30.8 million for the Enovation Controls business, indicating that the organic business grew 27%. Most of our products did not have any price increases in 2016 or 2017, so pricing had an immaterial impact on the comparability. Foreign currency translation had a favorable $200,000 impact for the quarter.

I will now touch on sales by region, which are designated here in the sales bar chart. We inserted the table in the back of the press release as well as the supplemental slides summarizing this information. As we've previously noted, we started experiencing progressive improvement in all of our geographic markets a little over a year ago and that has continued to the present time. We realized year-over-year third quarter growth in each region.

In the Americas, sales more than doubled over the third quarter of 2016 to $52.1 million, driven by the Enovation Controls business as well as organic growth. The Enovation Controls business is heavily weighted to the U.S., driving our sales to the Americas market up to 59% of the consolidated total. EMEA realized 36% growth to $19 million, and the Asia-Pacific region was up 72% to $16.9 million. Our organic business grew 21%, 15%, and 55% in the Americas, EMEA and APAC respectively. We have made investments in sales and marketing, including the additional sales application specialists in the field, which we believe are generating sales to complement the market expansion.

Regarding profitability, our consolidated Adjusted EBITDA more than doubled to $22.5 million, representing 25.5% of sales in this year's third quarter. That was up from 21.7% in last year's third quarter. The improvement was driven by the increase in sales and the leverage realized on our fixed-cost base in both cost of goods sold and SEA. Those benefits were partially offset by higher costs associated with product development activities, inefficiencies that resulted from the carve-out, and public company audit and SOX implementation expense.

Turning to the bottom line, adjusted earnings per share were $0.43, more than double last year's third quarter of $0.19. I want to mention a few items that impacted our consolidated results reported in our earnings release. First, our amortization expense, most of which resulted from the Enovation Controls acquisition, amounted to $2 million pretax in the third quarter. Net of tax, that amounts to $0.05 per share. I also want to point out that we realized $1.4 million of incremental net interest expense, primarily due to the cash and debt used for the acquisition. Net of tax, this amounts to approximately $0.04 per share.

Finally, we reported an additional $700,000 pretax of contingent consideration which, net of tax, amounts to approximately $0.02 per share. We reflected this item as an adjustment to arrive at non-GAAP net income and EPS as shown in the reconciliation at the end of both the earnings release and the slide deck. Based on the accounting rules, this represents an adjustment to the additional purchase price for the Enovation Controls business in accordance with the earn-out in the purchase agreement.

Please turn to Slide 7 for a review of our Hydraulics segment third quarter operating results. Sales grew 28% to $56.6 million with particular strength in the APAC and Americas regions, continuing the trend realized last quarter. We saw a 55% year-over-year growth for the quarter in the APAC region and 23% in the Americas region. Gross profit increased by 50% to $22.9 million on the higher sales, driving gross margin up to 40.4%. This compares favorably to last year, which realized 34.4% gross margin. The improvement resulted primarily from leverage on the higher sales volume, although there was a minor unfavorable impact on our Sarasota operations from Hurricane Irma.

SEA expenses increased by $1.8 million to $9.3 million to support our growth initiatives, including the addition of new talent. Operating income increased 75% to $13.5 million or 23.8% operating margin, compared with 17.4% operating margin in last year's third quarter. Similar to the improved gross margin on our higher sales volume, we realized further leverage on our SEA expenses. This drove the operating margin improvement.

Please turn to Slide 8 for a review of our Electronics segment third quarter operating results. As a reminder, the 2016 Electronics segment numbers include only a very small HCT business and the 2017 numbers include both our Enovation Controls business as well as HCT. Enovation Controls contributed $30.8 million of the segment's $31.4 million third quarter 2017 sales. On a pro forma basis, Enovation Controls realized 34% growth over the pre-acquisition 2016 third quarter. Similar to the strong pro forma growth realized in the last quarter, we attribute this to our proactive sales initiatives as well as new products and overall increasing market demand in the power controls and recreational vehicle end-markets.

The segment generated 42.8% gross margin and 19% operating margin in the quarter. Compared with the trailing second quarter, this period was impacted by higher costs associated with product development activities, inefficiencies that resulted from the carve-out, and public company audit and SOX implementation expenses.

Please turn to Slide 9 for a review of our year-to-date consolidated results. Sales of $258.7 million were up 76% over the same period last year. This includes $85.2 million for the Enovation Controls business, indicating that the organic business grew approximately 18%. Foreign currency translation had an unfavorable $1.7 million impact year-to-date compared with last year.

Regarding profitability, our consolidated Adjusted EBITDA nearly doubled to $69.9 million, representing 27% of sales in the first three quarters of 2017. That was up from 25% last year. Turning to the bottom line, adjusted earnings per share were $1.33, up from $0.75 last year.

As I noted for the quarter, I want to mention some items that impacted our consolidated year-to-date results reported in our earnings release. To begin with, in the first quarter of this year, we recorded $1.8 million pretax for amortization of the inventory step-up. It is included in cost of sales and, net of tax, amounts to $0.04 per share. This is reflected as an adjustment to arrive at non-GAAP net income and EPS, as shown in the reconciliation at the end of both the earnings release and slide deck.

Next, our amortization expense amounted to $6.4 million. Net of tax, that amounts to $0.16 per share. Third, we realized $3.8 million of incremental net interest expense. Net of tax, this amounts to approximately $0.09 per share. Finally, we recorded $8.9 million pretax of contingent consideration which, net of tax, amounts to approximately $0.21 per share. This item is also reflected as an adjustment to arrive at non-GAAP net income and EPS.

Please turn to Slide 10 for a year-to-date review of the Hydraulics segment. Sales grew 19% to $171.6 million, with particular strength in the APAC and Americas regions, which grew 36% and 17% respectively. Gross profit increased by 33% to $70.5 million on the higher sales, driving gross margin up to 41.1%. This compares favorably to last year, which realized 36.8% gross margin. Operating income increased 44% to $43.6 million or 25.4% operating margin, compared to 21% operating margin for the first three quarters of 2016. Like the quarter, our improved profitability is benefiting from the leverage realized on our fixed costs with higher sales volumes.

Please turn to Slide 11 for a year-to-date review of our Electronics segment. Enovation Controls contributed $85.2 million of the segment's $87.1 million of sales for the first three quarters of 2017. On a pro forma basis, Enovation Controls realized 38% over the same period last year. The segment generated 44.7% gross margin and 21.4% operating margin in the first three quarters of 2017. As Wolfgang indicated, this sales growth and profitability is exceeding our initial expectations. We're very pleased with the team's attention and focus to attaining or exceeding their goals.

Please turn to Slide 12 for a review of our cash flow and capital structure. During the first three quarters of 2017, we generated $38.4 million of cash from operating activities compared with $31.3 million in the first three quarters of 2016. The increase was due to higher net income, partially offset by an increase in working capital. We have needed additional working capital during 2017, especially inventory, to support the sales growth as well as the Enovation Controls carve-out. To ensure that we didn't interrupt our ability to meet customer demands, we carried extra inventory as production lines were being shut down and then set up in their new location.

Total debt was $116 million at September 30, 2017, down from $124 million at July 1, 2017, and $140 million at December 31, 2016. We repaid an additional $8 million of debt during the third quarter of 2017, after having repaid $16 million during the first quarter. We had $184 million of available capacity under our revolving credit facility at September 30, 2017.

As we previously mentioned would occur in our fourth quarter, in October we paid $17 million to the former owners of Enovation Controls as the first of three payments earned as contingent consideration, or earn-out. The next two payments are due in July 2018 and April 2019. Other than that and our regular quarterly dividend, our primary use of cash is for capital expenditures and acquisitions to support our Vision 2025.

We finished the quarter with $84.9 million of cash and short-term investments, and $116 million of debt or $31.1 million of net debt. Our net debt to net capitalization was down to 10%. At the end of 2016, we had $81 million in cash and short-term investments and $140 million of debt, or $59 million of net debt. That had our net debt to net capitalization at 20%. Our strong cash flow profile has allowed us to make considerable improvement in that metric during the year.

Wolfgang, I'd like to turn it back to you for your perspective on outlook before we open the line for Q&A.

**Wolfgang H. Dangel:** Thanks, Tricia. Please turn to Slide 14. The economies in nearly all regions around the globe and nearly all sectors are performing very well and seem to be growing at an accelerated rate. Leading indicators point to continued acceleration into early or mid-2018 and then slowing growth for the remainder of the year. The growth in U.S. industrial production is supported by strong consumer spending and increasing demand for industrial goods. It appears that the U.S. total industry capacity utilization rate may have peaked in May 2017, supporting the theory of slowing growth in 2018.

As we look around the globe, industrial production is currently growing at an accelerated rate in Canada, Brazil and Europe. However, India and China are both reportedly experiencing slowing growth currently. Looking towards next year, other than India, which is expecting accelerating growth, slowing growth is expected in all other global regions by the end of 2018.

As our cartridge valves are important to the construction machinery sector, we look to the status of the U.S. construction market. Currently, single-unit housing starts are accelerating, but multi-unit housing starts are in a recession. Those trends are expected to shift in 2018, but the overall construction industry is expected to expand, which bodes well for Sun.

U.S. manufacturing production is growing at an accelerated rate despite some weakness in the auto industry. This economic activity is benefiting us, given our current concentrations in material handling and general industrial applications. While production is expected to continue to grow in 2018, it's expected to be at a slower rate. Indicators for the North American electronics sectors as published by the Institute of Printed Circuits Association also suggest growth, but with some anticipated volatility. In addition to growth resulting from the execution of our strategic initiatives, Sun is enjoying the benefit of broad economic growth globally.

Please turn to Slide 15 for additional thoughts regarding our outlook. We generally have visibility for about one quarter or so. Accordingly, given our recent trends and expectation for the remainder of the year, we have raised our revenue guidance, which I will address on the next slide. Since this is our first year with the Enovation Controls business and the establishment of our Electronics segment, I want to be sure you understand the seasonality of that business. It is typical for most of the OEMs that our Vehicle Technologies business services to schedule extended shutdowns around the December holiday season. Accordingly, that has a significant impact on our expected fourth quarter sales for the Electronics segment. However, this is normal and we don't have any reason to believe that growth will not bounce back in the first quarter of 2018, while recognizing that the significant growth rates experienced in 2017 are not expected to be sustained.

For those of you who know our historical hydraulics business well, you know that in a stable economic environment, our fourth quarter may be seasonally weaker given purchasing patterns in our industry. However, in 2017, given the strong economic growth being realized as well as the benefits from our strategic initiatives, we do not expect this to be the case.

In September, we announced that we will combine the Enovation Controls and HCT businesses into our facility in Tulsa, which is our North American competency center for the Electronics segment. HCT's operations in Nevada City, California, will be closed at the end of 2017 and moved to Tulsa. The cost associated with closing the location, including severance payments to employees and moving equipment and inventory, is approximately $1.2 million, which will be expensed as restructuring charges in Q4. We believe the combination of these two businesses will provide opportunity for integration of the HCT products into Enovation Controls' system. Additionally, the establishment of new, modernized production lines for the HCT products will drive efficiencies in the manufacturing processes and cost improvement.

Finally, I want to comment on the devastating hurricanes that affected so many people and businesses during this past quarter. Regarding the impact on Sun and our employees specifically, we were relieved that we regained power within a couple of days and proceeded to get our operations back up and running. All in all, I estimate that we lost about five production days in September and are working to make that up as we progress through the fourth quarter.

From a demand standpoint, I am pleased to report that the diversity and breadth of our customer base, both from an industry sector and geographic perspective, have resulted in minimal impact to Sun. On the other hand, as the reconstruction and refurbishment continues in the hurricane-affected regions, there may be incremental demand for Sun products in the mid-term, say, the next couple of quarters.

Please proceed to Slide 16 where we summarized our guidance for 2017. As I mentioned earlier, our trends thus far this year have led us to increase our revenue guidance modestly which, other than updating our depreciation guidance, is the only category that changed from last quarter. You can see here that we increased our consolidated revenue guidance by $10 million at the top end of the range and $15 million at the bottom end. This represents about a 3% to 5% increase over the guidance that we provided last quarter. Both of our business segments are driving this increase as you can see here. We did lower our depreciation guidance by about $1 million due to timing of the closing on the purchase of the Tulsa building, which will be later in 2017's fourth quarter.

With that, let's open up the lines for questions-and-answers.

**Operator:** Thank you. We will now be conducting a question-and-answer session. If you would like to ask a question, please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star, two if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys.

Our first question is from Mig Dobre of Robert W. Baird. Please go ahead.

**Joe Grabowski:** Good morning, everyone. It's Joe Grabowski on for Mig this morning.

**Wolfgang H. Dangel:** Good morning, Joe.

**Joe Grabowski:** Good morning. Starting off on Hydraulics, the sales growth in the Asia-Pacific has continued to accelerate. I know you touched upon it in your prepared remarks, but can you update us on the Asia-Pac initiatives, what “inning” you're in on those, and can sales growth continue to accelerate at these strong rates?

**Wolfgang H. Dangel:** Yes. Just to give you an update on some of the major initiatives, it's pretty much in alignment with what I reported earlier. We have been intensifying customer contact and activities in the marketplace. We have been adding people with application engineering skillsets to the team. Last, but not least, I would also attribute some of the staggering growth we have seen there on the Hydraulics side, to a rebounding of the construction machinery sector in China. In a nutshell, from an internal perspective, it's probably much more activity in the marketplace and adding additional strength to a pretty capable existing team.

**Joe Grabowski:** Got it, okay, thanks for that color. Then switching to the Electronics segment, Q3 sales were about $34.5 million and the guidance implies Q4 sales of $18 million to $23 million. I know you talked about seasonality in Q4, but that's more seasonality than I would've expected. Anything else going on there or is that really the magnitude of the Q4 seasonality?

**Wolfgang H. Dangel:** Oh, that's pretty much the only reason there.

**Joe Grabowski:** Okay.

**Wolfgang H. Dangel:** As we mentioned earlier on, we are expecting shutdowns of some of the OEMs in December and that's pretty much the only impact that we are seeing.

**Joe Grabowski:** Okay, got it. Then a big part of the Vision 2025 target is incremental sales from M&A, and now that we're about a year out from the announcement of the Enovation acquisition, any color on how the M&A pipeline is looking?

**Wolfgang H. Dangel:** Yes, that has been an ongoing activity as we reported during earlier webcasts, and we are filling the pipeline with prospects. Some of them are at various stages of discussions, but we have embedded the whole modus operandi of becoming acquisitive into our daily activities. We have built up team resources and competence within Sun, and the overall activity, I have to say, I'm pretty pleased where we are at this point.

**Joe Grabowski:** Got it and then a final question, the $1.2 million of restructuring expense in Q4, does that flow through SG&A? Is it included in the margin guidance for the year, and assuming it does flow through SG&A, how will Q4 SG&A compare to Q3?

**Tricia L. Fulton:** The majority of it will flow through SEA. There is a small part that will flow through cost of goods sold as well. However, we will segregate it as restructuring charges for reporting purposes. Given the relative immateriality, it is included in the margin guidance.

**Joe Grabowski:** Got it, okay. Congratulations on a solid quarter.

**Wolfgang H. Dangel:** Thank you, Joe.

**Operator:** Thank you. Our next question is from Joe Mondillo with Sidoti & Co. Please go ahead.

**Joe Mondillo:** Hi, good morning everyone.

**Wolfgang H. Dangel:** Good morning, Joe.

**Joe Mondillo:** In the press release, you cited that going forward growth may be decelerating. I just wanted to understand that. Is that just the comps just get a little tougher and so, because of that, the growth will decelerate? Or, are you seeing any pockets anywhere that indicate to you that things may be slowing compared to this pretty good 2017 we've seen?

**Wolfgang H. Dangel:** I think it's two-fold, Joe. On one hand, I want to be careful of not creating the impression that we can continue with some of the staggering growth numbers we have seen in certain pockets. We just talked about Asia-Pacific a minute ago. Secondly, the tailwind of the economy is still expected to be strong heading into 2018. As I've pointed out on numerous occasions, our challenge is always to have clear visibility. We have good visibility for about a quarter. We have mid of November now, so let's say we can probably pretty well evaluate what is going to happen in Q1, but it's difficult to give a precise forecast for Q2, Q3 and Q4 next year.

Overall, I think the economy is doing fine. We are not seeing any specific pockets that would concern us. First and foremost, I am less concerned about the economy. I am actually very excited about our strategic initiatives folding out the way they are, and us taking a grip on certain situations here. We are definitely seeing progress in so many areas that I think the combination of both the macroeconomic environment plus the rollout of the strategic initiatives, make me feel comfortable as far as 2018 is concerned.

**Joe Mondillo:** Okay, great. Then regarding Enovation accretion, I know you gave some information regarding that, but how accretive was Enovation including the non-cash amortization?

**Tricia L. Fulton:** It was accretive by about $0.11 without considering interest expense. Including the impact of the interest expense, it was accretive by about $0.08.

**Joe Mondillo:** Okay, and then looking at the fourth quarter, with such a fall-off in revenue at the Electronics segment, I imagine gross margins will fall off pretty significantly as well. How do you manage that or how does the business look seasonally on more of a bottom line or margin perspective?

**Tricia L. Fulton:** The gross margins overall likely won't change a lot for the Electronics segment, due to the high level of variable costs in cost of goods sold for that segment. We will likely see a decrease in the operating margins in the fourth quarter in the Electronics segment on the lower sales, but there will be some variable expenses that also go down with sales that will help those margins not drop as much as what we would see on the incremental revenue drop. But given their relatively high fixed SEA costs, we do expect an unfavorable impact on the operating margin given the lower sales.

**Joe Mondillo:** Okay. Just looking at the Hydraulics segment, in past strong recoveries like we're seeing here in '17 compared to '16, the third quarter has not been as seasonally weak on a profitability standpoint. I thought maybe that was going to take place again here just given the strength that we're seeing, given the 25% revenue growth. I was just wondering, is there anything you saw that was a little surprising that maybe profitability wasn't as strong given the strength in revenue, or was that in line with what you were looking at?

**Tricia L. Fulton:** Yes, we talked about it a little bit in the prepared remarks. We did see some inefficiencies in the Electronics segment, despite the incremental increase in the sales, that were related to the carve-out, as well as a few SEA things like audit fees and SOX. Certainly we believe that those inefficiencies going forward can be overcome and were related to the carve-out specifically. We did recognize also that it was down just a bit.

**Wolfgang H. Dangel:** Maybe, Joe, if I may add, the only impact on the Hydraulics side that you are referring to is probably attributed to the hurricane as I mentioned earlier. At the end of the day, we lost about five manufacturing days, which is a full week. That was the only negative impact.

**Joe Mondillo:** Yes, that's a good point. Is there any way for you to quantify what you lost regarding that?

**Wolfgang H. Dangel:** No, we didn't make an estimate there. As I said, it's probably tailwind in the fourth quarter coming in. There is reconstruction, and we see in those hurricane-affected areas an increase in demand for our products. I can't quantify exactly what that would be for the five days. The five days is an estimate. As you can imagine, you are ramping down, preparing for the hurricane, you're weathering the storm, and then you are ramping up again. It's an estimate when I said we probably lost five days of manufacturing as a whole, but we didn't quantify it.

**Joe Mondillo:** Okay. Then one last question for me, just regarding the balance sheet and cash flow. Do you anticipate being more aggressive starting in 2018 in terms of debt pay-down?

**Tricia L. Fulton:** Yes, we plan to pay down the debt as quickly as we can with available cash. We have some pretty significant cash outlays related to capital expenditures this year that have kept us from doing more there. Certainly as we normalize on the capital expenditures side, I think there will be available cash to pay that down more quickly.

**Joe Mondillo:** Okay, and then regarding cap ex, it's obviously going to be inflated in 2017. Looking at 2018 do you have any idea what that looks like in 2018 yet?

**Tricia L. Fulton:** We estimate going forward as part of Vision 2025 that our cap ex will be 4% to 5% of sales.

**Joe Mondillo:** Okay, thanks a lot, appreciate it.

**Operator:** Thank you. As a reminder ladies and gentlemen, it is star, one if you would like to ask a question. The next question is from Jon Braatz with Kansas City Capital. Please go ahead.

**Jon Braatz:** Good morning Wolfgang, Tricia.

**Wolfgang H. Dangel:** Good morning, Jon.

**Jon Braatz:** During the quarter, you announced the launch of a couple new product lines within the electro-hydraulic sector. Wolfgang, how does that improve your position? Where did you stand in that segment in the marketplace, and how much will that improve your competitive position in the marketplace, and how significant can these products be?

**Wolfgang H. Dangel:** Excellent question, Jon. It's a substantial expansion of our existing product offering in terms of aligning with the electrification trends that we have seen in the industry. We are seeing a strong shift from hydro-mechanical valves to electro-hydraulic valves. This expansion is significant for us because it will give us access to additional customers, and it will help us to pull through a higher content per machine with existing customers. It is significant moving forward. As I said, I would probably describe this as the most significant product launch over the past decade here in the Company.

**Jon Braatz:** Wolfgang, is there any way you can quantify for us the opportunity that you're looking at with the introduction of these products?

**Wolfgang H. Dangel:** Looking at the hydraulic—electro-hydraulics offerings in the marketplace, we can probably say that about a third of the market is to be allocated to that specific bucket. Our position in the past has been reasonably weak in that area. We always talk about a $2 billion market in total. If you say a third of that is in electro-hydraulics, let's say it is $600 - $700 million, I think we would probably target a double-digit market share, in the range of 10% to 15% in that area. If you do the math there, that could be significant incremental revenue for the Company.

**Jon Braatz:** Thank you very much.

**Operator:** Thank you, and once again, ladies and gentlemen, please press star, one if you would like to ask a question and we'll be pausing to take any questions that were submitted through the webcast.

There is another question from the line of Joe Mondillo of Sidoti & Co. Please go ahead.

**Joe Mondillo:** Hi, guys. I just had one follow-up question, regarding the profitability and margins that you saw at Enovation. They looked like they were pretty strong for what I would consider the third quarter as a little seasonably weak quarter. Obviously revenue was really good in the quarter. Just wondering if you could help us understand the normalized seasonality in maybe not as strong of a growth year like we're seeing here.

**Tricia L. Fulton:** Well, if you look back historically in the previous two quarters at the margins on the Electronics side, the gross margins in particular were a little bit weak in the third quarter. Again, that goes back to the reasons that we've talked about previously. The second quarter margins were higher on those incremental sales. From a seasonality perspective, the third quarter tends to be a little bit stronger for them just given that there are some model year rollouts mid-year.

I think that's a little bit of what we're seeing here. If you go back to the pro forma 2016 numbers, we saw the same thing last year, but again, Q4 then is seasonally weaker due to the shutdowns, which again affects operating margins.

**Joe Mondillo:** Okay, and that's on a revenue perspective you're referring to or—?

**Tricia L. Fulton:** Yes.

**Joe Mondillo:** What about the margin generally on a seasonal perspective?

**Tricia L. Fulton:** Well, the margins really should flow from the revenues. There is no seasonality change in the margins, per se. It's all driven by what the revenues are doing, unless there's something extraordinary that's happening or something different that's happening, like we saw this quarter with the inefficiencies.

**Joe Mondillo:** Right, okay. Thank you.

**Operator:** Thank you. There are no further questions in the queue at this time. I would like to turn the conference back over to Management for closing remarks.

**Wolfgang H. Dangel:** Thank you. Thanks again for your participation this morning and thank you to all of the hardworking Sun employees who are driving these results. We look forward to meeting some of you at the Baird Conference this week and then updating all of you on our full year results in February. Thank you very much and have a great day. Bye-bye.

**Operator:** Thank you. Ladies and gentlemen, this does conclude today's teleconference. You may disconnect your lines at this time and thank you for your participation.