Capturing

VALUE

2014 ANNUAL REPORT

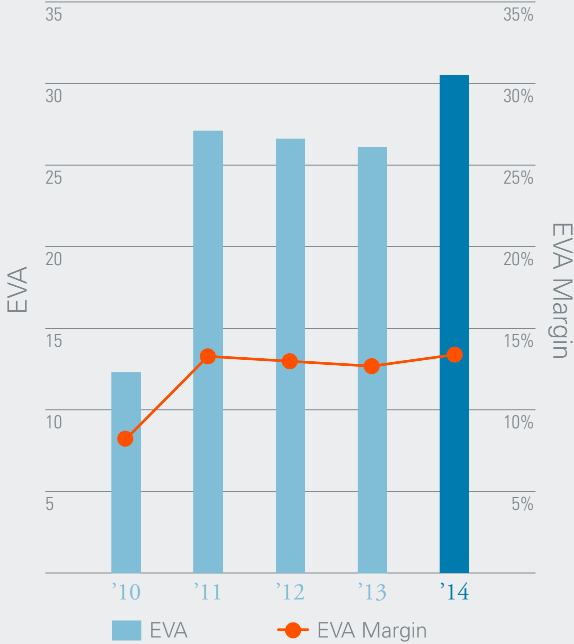
Measuring Value Last year, we began using EVA®[1], or economic value added, to guide our decision making and communicate the value that we create and capture for shareholders. We believe EVA is the best measure for determining how well we are running our business because it incorporates our cost of capital, or the opportunity cost to shareholders. EVA also promotes decision making for long-term sustainable results, which mirrors our own approach. To increase EVA, we must earn a return on capital employed greater than our cost of capital. We accomplish this through profitable growth, operating efficiency and asset management. Long-term, this drives value for shareholders.

Once again in 2014, we succeeded in capturing value. Our top line grew by 11%, enabling us to better absorb our fixed costs and better employ our asset base. That in turn led to a 14% increase in our bottom line and a 17% increase in EVA. With our third facility in Sarasota fully operational, we have the infrastructure in place to continue to grow. As our top line expands further, we will be able to create incremental growth at the bottom line and increase EVA.

The investments we made in new products and markets during 2014 will also drive future growth for Sun. We are excited about our partnership with Sturman Industries, which provides us the opportunity to bring Sturman's digital valve technology to the fluid power industry. This is an innovative technology with numerous possibilities for existing and new customers and markets. While the partnership did not create EVA in 2014, we expect it to spur EVA growth over the long term.

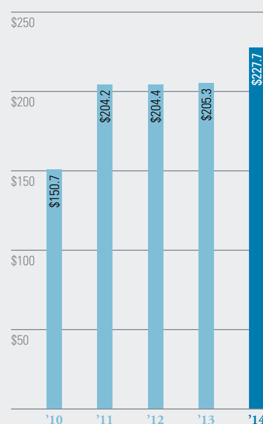
When it comes to EVA margin (EVA/sales), Sun ranks near the top among public companies, and we are committed to capturing further value for shareholders. Our plan for growing EVA has three components: pursue profitable end market growth, focus on continuous operational improvement, and implement prudent investments.

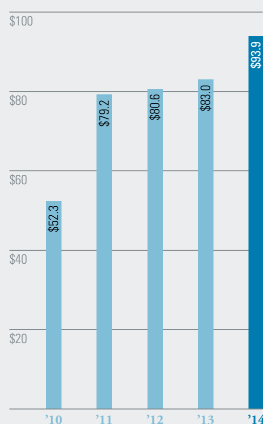
1 EVA is measured as net operating profit after taxes less a charge for capital equal to 11% multiplied by our average net operating assets.

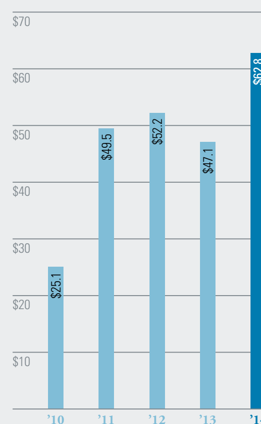


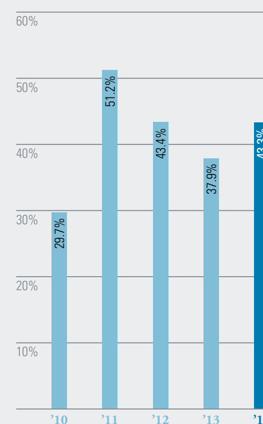
Financial Highlights

Year Ended	**Dec. 27, 2014**	Dec. 28, 2013	Dec. 29, 2012	Dec. 31, 2011	Jan. 1, 2011
(in thousands except per share data)					
Statement of Operations:					
Net sales	**$227,673**	$205,267	$204,367	$204,171	$150,695
Gross profit	**93,892**	82,961	80,572	79,215	52,343
Operating income	**64,071**	56,171	54,409	55,269	31,039
Income before income taxes	**65,742**	57,172	55,853	57,586	31,643
Net income	**$ 43,775**	$ 37,984	$ 37,398	$ 37,677	$ 21,400
Basic net income per common share	**$ 1.65**	$ 1.45	$ 1.44	$ 1.47	$ 0.84
Diluted net income per common share	**$ 1.65**	$ 1.45	$ 1.44	$ 1.47	$ 0.84
Dividends per common share	**$ 1.45**	$ 0.45	$ 1.48	$ 0.40	$ 0.57
Other Financial Data:					
Depreciation and amortization	**$ 8,718**	$ 7,227	$ 7,186	$ 6,721	$ 6,873
Capital expenditures	**10,667**	17,935	13,359	10,143	3,856
Balance Sheet Data:					
Cash and cash equivalents	**$ 56,843**	$ 54,912	$ 34,478	$ 42,834	$ 33,206
Working capital	**119,815**	115,038	90,198	89,744	66,150
Total assets	**222,764**	213,478	175,121	167,528	132,034
Total debt	**—**	—	—	—	—
Shareholders' equity	**198,259**	191,428	155,273	145,276	115,024
% of Sales:					
Gross profit	**41.2%**	40.4%	39.4%	38.8%	34.7%
Operating income	**28.1%**	27.4%	26.6%	27.1%	20.6%
Net Income	**19.2%**	18.5%	18.3%	18.5%	14.2%









THIS IS HOW WE CAPTURE...

VALUE

Dear Shareholders,

If you do the right things and run your business for long-term success, you will get the financial results you desire. This principle permeates everything we do—from the way we develop products to the way we conduct our relationships with shareholders, employees, customers and channel partners. We never sacrifice long-term success for short-term results. It is because of this long-term orientation that we have begun using economic value added (EVA®) as a way to guide decision making and communicate our performance. We believe that EVA is the metric that best summarizes our success in creating and capturing long-term value for our shareholders.

Whether we look at EVA or the traditional accounting metrics, 2014 was a record year for Sun. Taking advantage of a healthy macroeconomic environment, we produced EVA of $30.5 million in 2014, a gain of 17% from 2013. Our EVA margin (defined as EVA/sales) grew by 70 basis points to 13.4%. As for the traditional metrics, sales grew by 11% to $228 million; gross margin grew by 80 basis points to 41.2%; and earnings grew by 14% to $1.65 per share. Fueling this double-digit growth was the increased penetration we achieved in all our major global geographic markets. Our strong performance coupled with our ability to generate cash led to a special one-time cash dividend of $1.00 per share in October 2014, and to a shared distribution for shareholders and employees in March 2015. The total amount we returned to shareholders for 2014 was $38.4 million.

We were extremely pleased with our results as 2014 progressed, but knew that we could not rest on our laurels. So, during the year, we increased our investments for future growth, focusing on key geographic markets and product development to remain at the forefront of innovation. Ultimately, these investments will ensure that we continue to create and capture long-term value for stakeholders.

Ten years ago, $42 million of our sales were outside North America. Today, $117 million of our sales are outside North America. We have achieved much of that gain by focusing on expanding our presence in Asian markets, particularly China. Because we believe Asia continues to provide an opportunity for significant future growth, in 2014 we relocated a senior leader from Sun to Shanghai to further develop the region. We expect to add additional marketing and engineering resources in Asia to grow our customer base and maintain our market- leading brand.

We released several new products during 2014, including electrically actuated cartridge valves, electronics and enhancements to Sun QuickDesign™, our web-based tool that designs a custom integrated package in a matter of minutes. Also last year, we entered into a strategic partnership with Sturman Industries to utilize Sturman's digital valve technology to develop and produce next-generation electro-hydraulic valves. These valves are smaller and lighter, use less power and operate faster. Sun will be the first to bring this technology to the fluid power market. Additionally, with our new releases and the Sturman valves, Sun will also be able to enter new markets and to expand its offering of complete system solutions.

Product development is ongoing. Already in 2015, we released a line of embedded amplifiers that utilize Bluetooth technology. These amplifiers provide wireless configuration, from your iPhone® or other smart device, that will benefit a broad range of applications, where cost, reliability, and ease of use are critical. We expect to release more new offerings throughout 2015.

We have completed our first full year of operations in our new Sarasota facility. This plant increases our U.S. manufacturing footprint by 50%, providing the necessary space for Sun to grow for the foreseeable future. We have consolidated the design, production and assembly operations for our U.S. integrated package business at the new facility. Custom integrated packages combine standard cartridge valves and electronics to provide unique system solutions for customer applications. Our integrated packages are smaller, lighter and more highly optimized than are those from other suppliers, often creating a competitive advantage for the machinery and equipment housing them. These system solutions will be an important driver of growth for Sun and a source of added value.

So, to sum up, 2014 was a great year for our company. Our workforce and channel partners remained focused on providing the right products and services to our customers when and where they wanted them. The result was solid top- and bottom-line growth, capturing value for shareholders. At the same time, our leadership, engineering and marketing teams around the world were attentive to investments and new business opportunities. We will continue to look for opportunities, whether through strategic partnership or acquisition, to deliver a broader range of products, services and new technologies to the market. We are in a strong position financially to seek out and take advantage of opportunities in the market. But in doing so, we will keep our eyes fixed on creating lasting shareholder value.

Allen J. Carlson
President and CEO

THIS IS HOW WE PROVIDE...

ENDLESS SOLUTIONS

Sun Hydraulics serves its multiple markets with a product line of over 2.5 million discrete components. Our product breadth and depth is unmatched in the industry. This scope, combined with our custom integrated package design and our production capabilities, means we can address any challenge in the marketplace. The result is a differentiated solution, creating value for customers.

Creating and capturing value is in Sun's DNA. This basic instinct is evidenced by our marketing strategy, the diversity of our end markets, and the vast number of customers we serve. The design, performance and reliability of our products create and capture value as well. We combine superior service with premium product offerings to make Sun a partner of choice.

A Medley of Markets Sun Hydraulics serves a global customer base of equipment manufacturers in the capital goods industries. Sun follows a simple marketing strategy—market to the end-use customer and sell through distribution. Our worldwide distributors provide technical value-added engineering services to customers. They typically carry all the components of a hydraulic system to provide a complete hydraulic solution for a customer. In North America, third-party distributors are our sales force. In other parts of the world, our foreign subsidiaries and third-party distributors sell directly to customers.

Approximately 50% of our sales are to customers in North America, 30% in Europe and 20% in the Asia/Pacific region. Long-term, we expect to see growth and market share gains in all three of these regions, but believe our sales will ultimately be split evenly among them. In any given year, our geographic diversity helps us balance the effects of the ever-changing economies of the world, without relying on any one region.

The Asia/Pacific region, and specifically China, has been and will remain an area offering significant long-term future growth for Sun. We continue to invest in this region by adding sales and marketing resources to expand the adoption of our products and maintain our industry-leading brand.

Geographic diversity is one part of Sun's equation. The other is end-market diversity. We make approximately 60% of our sales to mobile markets and 30% to industrial markets. Mobile markets are characterized by applications where the equipment is not fixed in place, the operating environment is often unpredictable, and duty cycles are generally moderate to low. Industrial markets are characterized by equipment that is fixed in place, typically in a controlled environment, and that operates at higher pressures and duty cycles. We make the remaining 10% of our sales to end markets that do not fit easily into the other two categories. An example would

Jetting Systems is a specialist designer and manufacturer of high pressure water-jet cleaning systems. Its truck-mounted system for removing rubber deposits from jet runways uses a Sun custom solution for the truck's hydraulic controls. Our solution includes a custom integrated package, cylinder-mounted controls, and an electronic controller that interfaces between the operator controls and Sun's electrically actuated valves. This comprehensive product matrix provides a one-stop solution for the customer.

Herbert, a leading manufacturer of innovative solutions for the tire industry, produces hydraulically driven tire-curing presses used in making automobile, motorcycle, truck, and airplane tires. Herbert incorporates Sun's electrically actuated proportional valves in its presses to control the equipment's movement. Our ability to offer a unique, high-quality solution that is both compact and cost-efficient makes Sun the supplier of choice for these presses, which are sold throughout the world.

be applications in alternative energy, such as wind power. Wind power is a demanding application where performance and reliability are crucial for maximizing power generation and eliminating expensive maintenance costs. The reliability of our products has made us a leader in this field.

Our end-user markets are broken down further into 41 capital goods categories. In the mobile sector, we make a large portion of our sales, just over 10%, to cylinder manufacturers. A portion of these cylinders end up in aerial work platforms, with the remainder sold to a host of original equipment manufacturers across all industries. On the industrial side, we make nearly 10% of our sales to manufacturers of power units. Like cylinders, power units are used in many different industries.

Sun's other major end markets include oil and gas, utilities, cranes, construction, mining, agriculture, metal cutting/forming and alternative energy. This diversity of end markets allows us to withstand a downturn in any one or even multiple sectors. Mining, for example, has been constrained for the past three years. Despite this weakness in a major market, Sun has been able to grow. Diversity helps Sun create and capture long-term value.

Customer Diversity Because we serve so many different types of markets, we have many different types of customers. Our products can be found just about anywhere —in a blueberry harvester, a Ferris wheel, an aerial works platform, a city bus, a tire-curing press, an airport runway cleaning system, an energy-efficient vehicle.

Sun's largest end-use customer represents approximately 3% of total sales. We have several other large customers that each represent between 0.5% to 1% of sales. However, the majority of end-use customers individually account for even smaller proportions of total sales.

Operationally, Sun has the ability to serve both large and small customers. Everything we produce is made to order and we have no minimum-order quantity. We will design and sell one custom application solution, or thousands. We want our entire customer base, big and small, to have easy access to our products. OEMs use Sun's high-performance products to differentiate their equipment in the market.

THIS IS HOW WE DELIVER...

PERFORMANCE

Our cartridge valves operate more precisely and reliably at higher pressures and flow rates than do competitive products. And our expansive product line gives us the opportunity to offer unique, highly optimized integrated package solutions for customer applications.

Lightning Hybrids makes innovative hydraulic hybrid-drive systems for fleet vehicles, including shuttle buses and delivery trucks. Its systems offer the benefits of lower fuel usage, less emissions, reduced brake wear and increased vehicle power, while providing a driver-friendly experience. Lightning Hybrids selected Sun as a key supplier because of our ability to deliver small-quantity orders, meet fast-changing system and design requirements, and provide hassle-free service and superior delivery reliability.

Daily, there are new market and customer opportunities for hydraulics to solve design problems. Sun stands ready to capitalize on these opportunities.

Premium Products Our cartridge valves utilize a floating-construction design, which allows them to operate more precisely and reliably at higher pressures and flow rates than do competitive products. This design, coupled with the most expansive product line in the industry, enables us to make highly optimized integrated package solutions for customer applications. The equipment manufacturer benefits by getting a custom-designed solution that has a single part number and that is also lighter and smaller, which saves valuable space in the machine. Our performance characteristics, particularly durability and tolerance of high operating pressures, are the reasons we can use the same products for both mobile and industrial applications.

We utilize common parts to maximize automation in the manufacture of our high-quality products. Automation, in turn, improves operating efficiency, which drives value. We have an integrated supply channel that supports our made-to-order production. This aids our ability to maximize throughput while keeping on-hand inventory to a minimum, which also drives value.

Premium Service We pride ourselves on more than just offering a great product. Everyone at Sun continually focuses on serving our customers. We make our products to order and schedule everything based on the customer's requested ship date. In any given week, we expedite 15% of our orders, which results in a shortened lead time. On-time delivery is a key internal metric for Sun. We believe our delivery reliability helps us gain market share, particularly during the expansion phase of a business cycle.

Sun offers all the benefits and resources of a global company while being able to provide local support. We have the best global network of authorized distributors in the industry. Our distribution partners are an extension of Sun and have the technical hydraulics expertise to solve the most difficult customer challenges.

FINANCIAL SECTION

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SELECTED CONSOLIDATED FINANCIAL DATA

The following summary should be read in conjunction with the consolidated financial statements and related notes contained herein. See Management's Discussion and Analysis of Financial Condition and Results of Operations and Business.

The Company reports on a fiscal year that ends on the Saturday closest to December 31st. Each quarter consists of thirteen weeks.

Year ended	**Dec. 27, 2014**	Dec. 28, 2013	Dec. 29, 2012	Dec. 31, 2011	Jan. 1, 2011
(in thousands except per share data)					
Statement of Operations:					
Net Sales	**$227,673**	$205,267	$204,367	$204,171	$150,695
Gross Profit	**93,892**	82,961	80,572	79,215	52,343
Operating Income	**64,071**	56,171	54,409	55,269	31,039
Income before income taxes	**65,742**	57,172	55,853	57,586	31,643
Net income	**$ 43,775**	$ 37,984	$ 37,398	$ 37,677	$ 21,400
Basic net income per common share	**$ 1.65**	$ 1.45	$ 1.44	$ 1.47	$ 0.84
Diluted net income per common share	**$ 1.65**	$ 1.45	$ 1.44	$ 1.47	$ 0.84
Dividends per common share	**$ 1.45**	$ 0.45	$ 1.48	$ 0.40	$ 0.57
Other Financial Data:					
Depreciation and amortization	**$ 8,718**	$ 7,227	$ 7,186	$ 6,721	$ 6,873
Capital expenditures	**10,667**	17,935	13,359	10,143	3,856
Balance Sheet Data:					
Cash and cash equivalents	**$ 56,843**	$ 54,912	$ 34,478	$ 42,834	$ 33,206
Working capital	**119,815**	115,038	90,198	89,744	66,150
Total assets	**222,764**	213,478	175,121	167,528	132,034
Total debt	**—**	—	—	—	—
Shareholders' equity	**198,259**	191,428	155,273	145,276	115,024

All stock prices and dividends are adjusted for a three-for-two stock split, effected in the form of a 50% stock dividend, which was effective on July 15, 2011.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

Sun is a leading designer and manufacturer of high-performance screw-in hydraulic cartridge valves and manifolds, which control force, speed and motion as integral components in fluid power systems. The Company sells its products globally through wholly-owned subsidiaries and independent distributors. Sales outside the United States for the year ended December 27, 2014, were approximately 57% of total net sales.

Approximately two-thirds of product sales are used by the mobile market, which is characterized by applications where the equipment is not fixed in place, the operating environment is often unpredictable, and duty cycles are generally moderate to low. Some examples of the mobile market include equipment used in off-road construction, agriculture, fire and rescue, utilities, oil fields, and mining.

The remaining one-third of sales are used by industrial markets, which are characterized by equipment that is fixed in place, typically in a controlled environment, and which operates at higher pressures and duty cycles. Power units, automation machinery, metal cutting machine tools and plastics machinery are some examples of industrial equipment. The Company sells to both markets with a single product line.

In recent periods, the Company's products have been used by emerging markets that have characteristics of both the mobile and industrial markets and do not conveniently fit either classification exclusively. These markets include alternative energy equipment including wind, wave and solar equipment, animatronics and staging for theater and cinema. The Company sells to these markets the same products used in its traditional markets.

Management and Operations Philosophy

Since its inception, Sun has operated as an entrepreneurial enterprise, with an emphasis on individual employee empowerment and a disinclination to create bureaucracy, a formal management structure or administrative impediments to innovation, efficiency and customer service. Accordingly, the Company's organization, management structure, and reporting and decision-making systems are highly unified and unlayered.

In addition to representative and sales offices located throughout the world, Sun has three subsidiaries outside the United States (in the U.K., Germany and Korea) and one U.S. subsidiary. These entity distinctions arose out of historical considerations or as the result of acquisitions. Nevertheless, and increasingly as it has developed into a global enterprise, the Company is operated and managed on a consolidated basis. Much of the Company's primary financial and operations data is reported from Sun's various legal entities, which are separate taxpayers and, in many cases, subject to statutory audits in the countries in which they are organized. This information from Sun locations around the world is then compiled and aggregated, with appropriate consolidating entries, on a monthly basis. However, we do not manage or make decisions based on the individual legal entity information. Instead, this is done on the basis of the consolidated information.

Sun has always employed a leadership model in which all management personnel have line responsibilities and participate across functional lines and in multiple areas, including geographical areas. Through a common vision, shared values and networks of informal, overlapping relationships, the Company has emphasized a unified approach. The CEO oversees the Company with a constant focus on consolidated results.

With oversight from its Board of Directors and an emphasis on transparent communication across the entire Company, Sun's operating strategy and business is based upon the creation and manufacture of a comprehensive line of functional products which are sold, through distribution and directly, worldwide for use in a host of mobile and industrial applications. This unified focus places a premium on the delivery of Sun products for fluid power solutions anywhere in the world in the most efficient manner, with little regard for traditional geographic or entity differentiation. Instead, Sun's management looks at where products are sold—the Americas, Europe (which includes the Middle East and Africa), and Asia/Pacific. Decisions as to resource allocation, expansion of facilities and personnel, and capital investment are all made based on information on "sales to" customers, not information about "sales from" Sun subsidiary entities. This reflects the fact that sales are routinely specified, originated or sold beyond and regardless of entity or geographic boundaries. In particular, many of the sales in Europe and Asia come directly from the U.S. and never pass through one of Sun's subsidiary entities in those regions.

Management's focus is on overall Company performance and the evaluation of opportunities for additional "sales to" customers. Sun's CEO truly acts as the chief executive for the entire business; he and the other management leaders oversee operations worldwide, without an intermediate reporting bureaucracy in each location in which Sun has a legal entity. Using "shared offices," leadership responsibilities are disbursed throughout the Company, with minimal formal reporting relationships and maximum collaboration among employees worldwide. By focusing on total net orders and total net sales, not individual legal entity performance, Sun is able to better serve its customers. This philosophy permeates not only the management approach to decision-making, but also the Company's compensation system, which is based on company-wide performance, and not individual or entity-level management-by-objective criteria.

Industry Conditions

Demand for the Company's products is dependent on demand for the capital goods into which the products are incorporated. The capital goods industries in general, and the fluid power industry specifically, are subject to economic cycles. According to the National Fluid Power Association (the fluid power industry's trade association in the United States), the United States index of shipments of hydraulic products increased 6% in 2014, after decreasing 5% in 2013 and increasing 1% in 2012.

The Company's order trend has historically tracked closely to the United States Purchasing Managers Index (PMI), with the PMI providing a six to ten months leading indication of business conditions. A PMI above 50 indicates economic expansion in the manufacturing sector and when below 50, it indicates economic contraction. The index decreased to 55.1 in December 2014, from 56.1 (seasonally adjusted) in December 2013. Although down in December on a year over year basis, the index showed considerable strength in the manufacturing sector for much of 2014. The index in January 2015 was 53.1, indicating growth, albeit at a slower rate, for the 20th consecutive month.

Results for the 2014 fiscal year

	Dec. 27, 2014	Dec. 28, 2013	Increase
(in millions except net income per share)			
Twelve Months Ended			
Net sales	**$227.7**	$205.3	11%
Net income	**$ 43.8**	$ 38.0	15%
Net income per share:			
Basic	**$ 1.65**	$ 1.45	14%
Diluted	**$ 1.65**	$ 1.45	14%
Three Months Ended			
Net sales	**$ 54.8**	$ 49.1	12%
Net income	**$ 10.3**	$ 8.3	24%
Net income per share:			
Basic	**$ 0.39**	$ 0.32	22%
Diluted	**$ 0.39**	$ 0.32	22%

Demand was strong throughout the fourth quarter. All geographic end markets expanded in the quarter, led by robust demand in North America, which was up 18%. Asia/Pacific and Europe were each up 5%. For the year, the Company was able to drive double digit top and bottom line growth. Its performance led the Board to once again declare a shared distribution, recognizing the importance of both employees and shareholders.

The Company made significant investments for future growth in 2014, and management is seeing positive signs as a result. With the addition of its third U.S. facility, the larger physical footprint provides the capacity to grow and drive operational improvements. This leads to faster response times to better satisfy customers. New products, including prototype valves utilizing the new licensed Sturman technology, are creating interesting opportunities with both existing and new customers. Product development efforts increase the Company's capabilities and enhance its offering of integrated package solutions. Management anticipates continued product development and new product releases in 2015.

Despite some headwinds, 2015 is off to a good start. The breadth and depth of the Company's product line lends itself well to serving diverse end-user markets and eliminating reliance on any one industry. Geographically, there are pockets of strength, including North America and parts of Europe. In China, the Company has expanded its customer base, which mitigates a slowdown in Asia/Pacific. Management believes it is well positioned to respond to business conditions in 2015. Diverse end markets, coupled with ongoing investment in products and marketing efforts prepare Sun for future business growth. The Company also has the infrastructure in place and a strong balance sheet to capitalize on opportunities. The Company ended 2014 with cash and marketable securities of $100.5 million, and zero dollars of long-term debt.

Dividends

The Company declared quarterly dividends of $0.09 per share during 2014. These dividends were paid on the 15th day of the month following the date of declaration. Additionally, in 2014, the Company declared a shared distribution cash dividend of $0.09 per share that was paid on March 31, 2014, to shareholders of record on March 15, 2014.

In light of the Company's strong cash position, ability to generate ongoing cash, and strong financial performance in the first half of 2014, the Company declared a special cash dividend of $1.00 per share that was paid on October 24, 2014, to shareholders of record as of October 10, 2014.

In February 2015, the Board elected to once again apportion a shared distribution for employees and shareholders based on the Company's 2014 results. The shared distribution consists of a 10.0% contribution of salaries to all eligible employees, most of which will be paid into retirement plans via Sun Hydraulics stock, and a $0.09 per share dividend to shareholders, totaling approximately $6.1 million. The shared distribution concept was introduced in 2008 as a way to reward both shareholders and employees when Sun has a successful year.

The shared distribution dividend will be issued to shareholders of record on March 15, 2015, with payment on March 31, 2015.

Outlook

First quarter 2015 revenues are expected to be approximately $55 million, down 3% from the first quarter of 2014, primarily driven by a strong U.S. Dollar against the Euro. Earnings per share are estimated to be $0.40 to $0.42 compared to $0.43 in the same period a year ago. The first quarter will look similar on the top line to the fourth quarter, but operationally the Company expects to drive more profit to the bottom line.

Results of Operations

The following table sets forth, for the periods indicated, certain items in the Company's statements of operations as a percentage of net sales.

For the year ended	**Dec. 27, 2014**	Dec. 28, 2013	Dec. 29, 2012	Dec. 31, 2011	Jan. 1, 2011
Net sales	**100.0%**	100.0%	100.0%	100.0%	100.0%
Gross profit	**41.2%**	40.4%	39.4%	38.8%	34.7%
Operating income	**28.1%**	27.4%	26.6%	27.1%	20.6%
Income before income taxes	**28.9%**	27.9%	27.3%	28.2%	21.0%

COMPARISON OF YEARS ENDED DECEMBER 27, 2014 AND DECEMBER 28, 2013

Net Sales

Net sales were $227.7 million, an increase of $22.4 million, compared to $205.3 million in 2013. Demand for our products in 2014 was primarily driven by increased demand in all major global end markets, which primarily include capital goods equipment. Price increases, effective October 1, 2013 and December 1, 2014, contributed approximately 2% to sales. Exchange rates had a positive impact on sales in both 2014 and 2013 of approximately $1.6 million and $1.1 million, respectively. New product sales (defined as products introduced within the last five years) continue to make up 10%–15% of total sales.

Asia/Pacific sales increased 8.5% or $3.6 million, to $45.9 million in 2014, primarily related to demand from Korea and China. Exchange rates had a $0.8 million positive impact on Asia/Pacific sales in 2014. EAME sales increased 13.1% or $8.0 million, to $69.2 million in 2014, primarily related to demand in Germany and the United Kingdom. Significant increases were also noted in Austria, Ireland, and Spain. Additionally, currency had a $0.8 million positive impact to EAME sales in 2014. Sales to the Americas increased 10.6% or $10.8 million, to $112.5 million in 2014, driven by U.S. demand.

Gross Profit

Gross profit increased $10.9 million or 13.2% to $93.9 million in 2014, compared to $83.0 million in 2013. Gross profit as a percentage of net sales increased to 41.2% in 2014, compared to 40.4% in 2013.

The increase in gross profit was primarily attributable to increased sales volume in the current period of approximately $7.0 million. Pricing added approximately $5.0 million to gross profit. This was partially offset by increased material and overhead expenses, related to indirect labor costs including overtime, building maintenance and repairs, and depreciation on our new facility.

Selling, Engineering, and Administrative Expenses

Selling, engineering and administrative expenses in 2014 were $29.8 million, a $3.0 million, or 11.3%, increase, compared to $26.8 million in 2013. The change for 2014 was related to increases in compensation, including stock compensation and currency effects, of approximately $1.0 million. The remainder is primarily made up of outside services of $0.6 million and marketing efforts in Asia and R&D, each totaling approximately $0.5 million.

Operating Income

Operating income increased $7.9 million or 14.1% to $64.1 million in 2014, compared to $56.2 million in 2013, with operating margins of 28.1% and 27.4% for 2014 and 2013, respectively.

The Company derives its operating income based on the consolidated results of its legal entities. The Company has made the decision to consolidate engineering and manufacturing for the most part in the U.S. The Company's foreign subsidiaries primarily act as part of our sales and distribution channel. This structure results in different operating margins between the legal entities due to the mix of products, channels to market, and industries present in different geographic regions.

Products manufactured in the U.S. are sold worldwide. Pricing, operations and cost structure are the primary reasons that operating income in the U.S. is higher than foreign subsidiary operating income, which we expect will continue. Our German and U.K. entities act as value add distributors. These entities sell to both end use customers in their respective regions, as well as to third-party distributors in certain parts of Europe. U.K. margins have historically been lower than Germany margins. This is due to the fact that, in the U.K., we manufacture iron manifolds for the European market. This results in higher overhead costs primarily related to machinery and equipment, and the employment of nearly twice as many people as in Germany. Margins are lowest in our Korean entity. Korea, more than any other subsidiary, sells direct to large OEM customers where pricing pressure is most pronounced.

The U.S. legal entity contributed $52.3 million to our consolidated operating income during 2014 compared to $45.5 million during 2013, an increase of $6.8 million. Increased revenue contributed approximately $4.7 million to operating income, while margin expansion, primarily related to pricing, contributed $2.1 million. Increased revenue volume was driven by sales to North America, China, and to Europe, specifically Spain. Increasingly, the U.S. legal entity ships products directly to customers around the world. Third-party export sales from the U.S. were $60.1 million in 2014 compared to $54.2 million in 2013. As demand strengthens internationally, the U.S. legal entity will benefit from these direct export sales.

Our Korean subsidiary contributed $1.2 million to our consolidated operating income during 2014 compared to $1.8 million during 2013, a decrease of $0.6 million. Margins contracted from 9.3% in 2013 to approximately 5.6% in 2014, representing a $0.8 million decrease in operating income. The decrease was primarily related to increased material, labor and overhead costs. The decrease in operating income was partially offset by higher revenue.

Our German subsidiary contributed $6.6 million to our consolidated operating income during 2014 compared to $5.5 million during 2013, an increase of $1.1 million. Higher volume added approximately $0.6 million, with the remainder resulting from margin expansion. Operating margins were 23.2% and 21.2%, in 2014 and 2013, respectively. The margin growth was attributable to material cost decreases related to purchases of material in U.S. Dollars and a strengthening Euro during the first half of the year.

Our U.K. subsidiary contributed $3.9 million to our consolidated operating income during 2014 compared to $3.5 million during 2013, an increase of $0.4 million. Higher volume contributed $0.6 million, which was partially offset by a decrease in margins from 19.8% to 18.9%.

Interest Income, Net

Net interest income for 2014 was $1.6 million compared to net interest income of $1.0 million for 2013. Total average cash and marketable securities for 2014 was $97.2 million compared to total average cash and marketable securities for 2013 of $82.9 million. Interest derived from investments in corporate and municipal bonds, mutual funds, certificates of deposit, and money market funds increased approximately $0.3 million in 2014. The remaining increase is related to interest received on a tax refund at our German subsidiary.

Foreign Currency Transaction (Gain) Loss, Net

Net foreign currency transaction gain was $0.8 million in 2014 compared to a minimal gain in 2013. The current year gain was primarily derived in the fourth quarter, which resulted from a strengthening U.S. Dollar against the Euro and assets held in U.S. Dollars at our German subsidiary.

Miscellaneous (Income) Expense, Net

Net miscellaneous expense was $0.7 million in 2014 compared to minimal income in 2013. The current and prior year periods included losses on the disposal of assets. The prior year amounts were offset by a gain resulting from the acquisition of WhiteOak Controls, and an incentive received for the activation of our thermal storage energy building on our new facility.

Income Taxes

The provision for income taxes for the year ended December 27, 2014, was 33.4% of pretax income compared to a provision of 33.6% for the year ended December 28, 2013. The change was primarily due to the relative levels of income and different tax rates in effect among the countries in which the Company sells its products. The provisions were affected by discrete items related to a reserve for uncertain tax positions from previous years. Excluding these discrete items, the effective rate would have been approximately 33.1% and 33.3% for the years ended December 27, 2014 and December 28, 2013, respectively.

COMPARISON OF YEARS ENDED DECEMBER 28, 2013 AND DECEMBER 29, 2012

Net Sales

Net sales were $205.3 million, an increase of $0.9 million, compared to $204.4 million in 2012. Demand for our products in 2013 was primarily driven by increased demand in our international end markets, which primarily include capital goods equipment. Price increases, effective July 1, 2012 and October 1, 2013, contributed approximately 2% to sales. Exchange rates had a positive impact on sales in 2013 of approximately $1.1 million compared to a negative effect in the prior year of approximately $2.3 million. New product sales (defined as products introduced within the last five years) continue to make up 10%–15% of total sales.

Asia/Pacific sales increased 7.0% or $2.8 million, to $42.3 million in 2013, primarily related to demand from Korea and China. These amounts were partially offset from declines in Australia. Exchange rates had a $0.6 million positive impact on Asia/Pacific sales in 2013. EAME sales increased 1.9% or $1.1 million, to $61.2 million in 2013, resulting from the general economic improvement in Europe. Additionally, currency had a $0.5 million positive impact to EAME sales in 2013. Sales to the Americas decreased 2.9% or $3.0 million, to $101.7 million in 2013, due to weaker demand in the first three quarters of the year.

Gross Profit

Gross profit increased $2.4 million or 3.0% to $83.0 million in 2013, compared to $80.6 million in 2012. Gross profit as a percentage of net sales increased to 40.4% in 2013, compared to 39.4% in 2012.

The increase in gross profit was attributed to price increases in July 2012 and October 2013, totaling approximately $4.6 million and decreases in material costs as a percent of sales of approximately $0.2 million. These amounts were partially offset by increased labor costs of $0.5 million related primarily to the addition of Seungwon, and overhead costs as a percent of sales of approximately $0.4 million. Additionally, sales volume, excluding pricing, reduced gross profit approximately $1.5 million.

Selling, Engineering, and Administrative Expenses

Selling, engineering, and administrative expenses in 2013 were $26.8 million, a $0.6 million, or 2.4%, increase, compared to $26.2 million in 2012. The change for 2013 was related to increases in compensation of approximately $0.7 million, primarily related to stock compensation, and amounts associated with Seungwon of approximately $0.3 million that were not present in the prior year. These amounts were partially offset by reduced professional fees of approximately $0.2 million.

Operating Income

Operating income increased $1.8 million or 3.2% to $56.2 million in 2013, compared to $54.4 million in 2012, with operating margins of 27.4% and 26.6% for 2013 and 2012, respectively.

The Company derives its operating income based on the consolidated results of its legal entities. The Company has made the decision to consolidate engineering and manufacturing for the most part in the U.S. The Company's foreign subsidiaries primarily act as part of our sales and distribution channel. This structure results in different operating margins between the legal entities due to the mix of products, channels to market, and industries present in different geographic regions.

Products manufactured in the U.S. are sold worldwide. Pricing, operations and cost structure are the primary reasons that operating income in the U.S. is higher than foreign subsidiary operating income, which we expect will continue. Our German and U.K. entities act as value add distributors. These entities sell to both end use customers in their respective regions, as well as to third-party distributors in certain parts of Europe. U.K. margins have historically been lower than Germany margins. This is due to the fact that, in the U.K., we manufacture iron manifolds for the European market. This results in higher overhead costs primarily related to machinery and equipment, and the employment of nearly twice as many people as in Germany. Margins are lowest in our Korean entity. Korea, more than any other subsidiary, sells direct to large OEM customers where pricing pressure is most pronounced.

The U.S. legal entity contributed $45.5 million to our consolidated operating income during 2013 compared to $44.4 million during 2012, an increase of $1.1 million. Increased revenue contributed approximately $0.8 million to operating income, while margin expansion, primarily related to pricing, contributed $0.4 million. Increased revenue volume was driven by sales to China, and to Europe, specifically Norway, the Netherlands, and Italy. Increasingly, the U.S. legal entity ships products directly to customers around the world. Third-party export sales from the U.S. were $54.2 million in 2013 compared to $50.2 million in 2012. As demand strengthens internationally, the U.S. legal entity will benefit from these direct export sales.

Our Korean subsidiary contributed $1.8 million to our consolidated operating income during 2013 compared to $1.2 million during 2012, an increase of $0.6 million. Margins expanded from approximately 7% in 2012 to approximately 9% in 2013, representing $0.5 million of the increased operating income. Margins were impacted by reduced material costs related to items purchased in U.S. Dollars and a strengthening Korean Won. These amounts were partially offset by cost increases associated with Seungwon.

Our German subsidiary contributed $5.5 million to our consolidated operating income during 2013 compared to $5.4 million during 2012, an increase of $0.1 million. The increase was related to volume as margins remained flat at approximately 21%. Material cost decreases related to purchases of material in U.S. Dollars and a strengthening Euro were offset by increased overhead and selling, engineering, and administration costs primarily related to trade show and compensation expenses.

Our U.K. subsidiary contributed $3.5 million to our consolidated operating income during 2013 compared to $3.7 million during 2012, a decrease of $0.2 million. Decreased volume reduced operating income approximately $0.5 million. This was partially offset by improved margins of approximately $0.3 million. Margins improved from approximately 18% in 2012 to approximately 20% in 2013. The increase in margins was primarily related to decreased material costs which were partially offset by fixed overhead costs as a percent of sales.

Interest Income, Net

Net interest income for 2013 was $1.0 million compared to net interest income of $1.4 million for 2012.Total average cash and marketable securities for 2013 was $82.9 million compared to total average cash and marketable securities for 2012 of $86.9, excluding the dividend payment on December 28, 2012. Although total cash and marketable securities remained high in 2013, interest rates and investment returns remain at low levels. Interest is primarily derived from investments in corporate and municipal bonds, mutual funds, certificates of deposit, and money market funds.

Foreign Currency Transaction (Gain) Loss, Net

Net foreign currency transaction gain was minimal in 2013 compared to $0.1 million in 2012. The U.S. Dollar weakened against the Euro and the Korean Won at times during 2013, resulting in foreign currency transaction gains at our German and Korean locations. These amounts were partially offset at our U.K. location due to a strengthening U.S. Dollar against the British Pound at times during 2013.

Miscellaneous (Income) Expense, Net

Net miscellaneous (income) expense was minimal in 2013 and 2012. During the current year, costs associated with the relocation of our Kansas operations of approximately $0.7 million were offset by a gain of $0.5 million as a result of remeasuring to fair value our 40% equity interest in WhiteOak Controls held before the business combination, and an incentive received for the activation of our thermal storage energy building on our new facility of approximately $0.5 million.

Income Taxes

The provision for income taxes for the year ended December 28, 2013, was 33.6% of pretax income compared to a provision of 33.0% for the year ended December 29, 2012. The change was primarily due to the relative levels of income and different tax rates in effect among the countries in which the Company sells its products. The provisions were affected by discrete items related to a reserve for uncertain tax positions from previous years. Excluding these discrete items, the effective rate would have been approximately 33.3% and 31.8% for the years ended December 28, 2013 and December 29, 2012, respectively.

Liquidity and Capital Resources

Historically, the Company's primary source of capital has been cash generated from operations, although short-term fluctuations in working capital requirements have been met through borrowings under revolving lines of credit as needed. The Company's principal uses of cash have been paying operating expenses, paying dividends to shareholders, making capital expenditures, and servicing debt.

Net cash flow from operations in 2014 was $62.8 million, compared to $47.1 million in 2013 and $52.2 million in 2012. The $15.7 million increase in the Company's net cash flow from operations in 2014 was due primarily to increased net income of $5.8 million. Changes in aggregate tax balances increased cash $2.8 million in the current year, compared to a minimal change in the prior year. Changes in inventory and accounts receivable decreased cash $0.7 million in the current year compared to a decrease in cash of $4.4 million in the prior year. The change is related to better management of days sales outstanding and inventory turns with improved business conditions. Days sales outstanding remained flat at 28 days in 2014. Inventory turns increased to 9.6 in 2014 from 9.3 in 2013. Cash on hand increased $1.9 million from $54.9 million in 2013 to $56.8 million in 2014. Investments in marketable securities increased $4.6 million from $38.7 million in 2013 to $43.4 million in 2014.

The $5.1 million decrease in the Company's net cash flow from operations in 2013 was due primarily to changes in accounts receivable and inventory. Changes in inventory and accounts receivable reduced cash $4.4 million in the current year compared to an increase in cash of $2.2 million in the prior year. These changes were primarily related to improved business conditions in the fourth quarter of 2013.

Capital expenditures were $10.7 million in 2014, compared to $17.9 million in 2013 and $13.4 million in 2012. In 2014, approximately $3.2 million was for improvements to, and reconfiguring of, the Company's Manatee County facility originally constructed in 1997. Changes to this facility are expected to create operational efficiencies and productivity gains with regard to the Company's high-volume cartridge valve line. The remainder is made up primarily of purchases of machinery and equipment. Included in capital expenditures for 2013 and 2012 were approximately $10.6 million and $7.3 million, respectively, relating to the new Sarasota facility. Additionally, approximately $1.4 million and $1.0 million for an expansion and update of our U.K. facility was included in 2013 and 2012, respectively.

Capital expenditures for 2015 are estimated to be $8.0 million, primarily consisting of purchases of machinery and equipment.

Effective August 1, 2011, the Company entered into a credit and security agreement in the U.S. with Fifth Third Bank (the "Bank"). The agreement provides for three separate credit facilities totaling $50 million.

Facility A is a $15 million unsecured revolving line of credit and requires monthly payments of interest. Facility A has a floating interest rate of 1.45% over the 30-day LIBOR Rate (as defined).

Facility B is an accordion feature to increase the revolving line of credit to a $35 million secured revolving line of credit. Facility B will be secured by the Company's U.S. assets, including its manufacturing facilities, and requires monthly payments of interest. Facility B will bear interest at the 30-day LIBOR Rate or the Bank's Base Rate (as defined), at the Company's discretion, plus a margin based on the Borrower's Funded Debt to EBITDA Leverage Ratio (as defined). The LIBOR Margin ranges from 1.45% to 2.25% and the Bank's Base Rate ranges from -0.25% to 0.00%.

Facility C provided for a $15 million construction and term loan. The Company did not activate Facility C for the construction of its new Sarasota factory and access to this facility is now expired.

Facility A or Facility B (if activated) is payable in full on August 1, 2016. Maturity may be accelerated by the Bank upon an Event of Default (as defined). Prepayment may be made without penalty or premium at any time upon the required notice to the Bank.

Facility A is subject to debt covenants (capitalized terms are defined therein) including: 1) Minimum Tangible Net Worth of not less than $92 million, increased annually by 50% of Net Income, and 2) Minimum EBITDA of not less than $5 million; and requires the Company to maintain its primary domestic deposit accounts with the bank.

If Facility B is activated, covenant 2 above will automatically terminate and two additional covenants will be required: 1) Funded Debt to EBITDA ratio equal to or less than 3.0:1.0, and 2) EBIT to Interest Expense ratio of not less than 2.5:1.0.

The Company did not have any amounts drawn on Facilities A, B, or C for the periods ended December 27, 2014 and December 28, 2013.

As a result of the acquisition of Seungwon on October 18, 2012, the Company acquired a loan equal to $169. The Company paid and cancelled the loan during the fourth quarter of 2012.

Except as noted below, the Company declared the following regular quarterly dividends to shareholders of record on the last calendar day of the respective quarter, paid on the 15th day of each month following the date of declaration:

	2014	2013	2012
First quarter	**$0.090**	$0.090	$0.090
Second quarter	**0.090**	0.090	0.090
Third quarter	**0.090**	0.090	0.090
Fourth quarter	**0.090**	0.090	0.090

In addition to the regular quarterly dividends, the Company declared shared distribution cash dividends in 2014, 2013 and 2012, equal to $0.09, $0.09 and $0.12, respectively. The 2014 dividend was paid on March 31, 2014, to shareholders of record on March 15, 2014, the 2013 dividend was paid on March 31, 2013, to shareholders of record on March 15, 2013, the 2012 dividend was paid on March 31, 2012, to shareholders of record on March 22, 2012. The shared distribution was introduced in 2008 as a way to reward both shareholders and employees when the Company has a successful year. The Board of Directors also declared a shared distribution cash dividend of $0.09 per share, payable on March 31, 2015, to shareholders of record as of March 15, 2015.

The Board of Directors, in 2014, declared a special one-time cash dividend of $1.00 per share, payable October 24, 2014 to shareholders of record as of October 10, 2014. In declaring the special dividend, the Board of Directors cited the Company's strong cash position, ability to generate ongoing cash, and strong financial performance in the first half of 2014 as reasons for its decision.

In light of the Company's cash position, its current and perceived uses for cash, and an anticipated increase in income tax rates on corporate dividends as of January 1, 2013, the Board of Directors in December 2012 declared a special one-time cash dividend of $1.00 per share to shareholders of record as of December 14, 2012. In anticipation of the expected tax law changes in 2013, the payment date for both the special dividend and the regular quarterly dividend of $0.09 per share was December 28, 2012.

The Company paid dividends totaling $38.4 million, $9.4 million, and $40.9 million for the years ended December 27, 2014, December 28, 2013, and December 29, 2012, respectively.

The declaration and payment of future dividends is subject to the sole discretion of the Board of Directors, and any determination as to the payment of future dividends will depend upon the Company's profitability, financial condition, capital needs, acquisition opportunities, future prospects and other factors deemed pertinent by the Board of Directors.

The Company believes that cash generated from operations and its borrowing availability under the revolving Line of Credit will be sufficient to satisfy the Company's operating expenses and capital expenditures for the foreseeable future. In the event that economic conditions were to severely worsen for a protracted period of time, the Company would have several options available to ensure liquidity in addition to increased borrowing. Capital expenditures could be postponed since they primarily pertain to long-term improvements in operations. Additional operating expense reductions also could be made. Finally, the dividend to shareholders could be reduced or suspended.

OTHER MATERIAL COMMITMENTS. Our contractual obligations and debt obligations as of December 27, 2014, are summarized in the table below (in thousands):

	Payments due by period				
Contractual Obligations	Total	2015	2016–2017	2018–2019	Thereafter
Operating Leases	$1,265	$470	$703	$41	$51
Other long-term liabilities[(1)]	272	272	—	—	—
Total contractual obligations	$1,537	$742	$703	$41	$51

(1) Other long term-liabilities consist of a liability associated with the acquisition of Seungwon for a holdback amount of approximately $272,000.

Critical Accounting Policies and Estimates

The Company currently only applies judgment and estimates which may have a material effect on the eventual outcome of assets, liabilities, revenues and expenses for impairment of long-lived assets, inventory, goodwill, accruals, income taxes, and fair value of short-term investments. The following explains the basis and the procedure for each account where judgment and estimates are applied.

Revenue Recognition

The Company reports revenues, net of sales incentives, when title passes and risk of loss transfers to the customer. The effect of material nonrecurring events related to product liabilities is provided for when they become known. The Company has not experienced any material product liabilities in the past.

Short-term Investments

The Company's short-term investments have been classified and accounted for as available-for-sale. Management determines the appropriate classification of its investments at the time of purchase and reevaluates the designation at each balance sheet date. The Company may or may not hold securities with stated maturities greater than 12 months until maturity. As management views these securities as available to support current operations, the Company classifies securities with maturities beyond 12 months as current assets under the caption short-term investments in the accompanying Consolidated Balance Sheets. The Company's short-term investments are carried at fair value, with the unrealized gains and losses, net of tax, reported as a component of shareholder's equity. Realized gains and losses on sales of short-term investments are generally determined using the specific identification method, and are included in miscellaneous (income) expense in the Consolidated Statements of Operations.

Fair Value Measurements

The Company applies fair value accounting guidelines for all financial assets and liabilities and non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). Under these guidelines, fair value is defined as the price that would be received for the sale of an asset or paid to transfer a liability (i.e., an exit price) in an orderly transaction between market participants at the measurement date. The guidance establishes a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value as follows:

Level 1—Quoted prices in active markets for identical assets or liabilities.

Level 2—Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets or liabilities in active markets or quoted prices for identical assets or liabilities in inactive markets.

Level 3—Unobservable inputs that are supported by little, infrequent, or no market activity and reflect the Company's own assumptions about inputs used in pricing the asset or liability.

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The Company's valuation techniques used to measure the fair value of marketable equity securities were derived from quoted prices in active markets for identical assets or liabilities. The valuation techniques used to measure the fair value of all other financial instruments were valued based on quoted market prices or model driven valuations using significant inputs derived from or corroborated by observable market data.

Impairment of Long-Lived Assets

Long-lived assets, such as property and equipment, and purchased intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of the asset is measured by comparison of its carrying amount to future net cash flows the asset is expected to generate. If such assets are considered impaired, the impairment to be recognized is measured as the amount by which the carrying amount of the asset exceeds its fair value.

Inventory

The Company offers a wide variety of standard products and as a matter of policy does not discontinue products. On an ongoing basis, component parts found to be obsolete through design or process changes are disposed of and charged to material cost. The Company reviews on-hand balances of products and component parts against specific criteria. Products and component parts without usage or that have excess quantities on hand are evaluated. An inventory reserve is then established for the full inventory carrying value of those products and component parts deemed to be obsolete or slow moving. See Note 5 to the Financial Statements for inventory reserve amounts.

Goodwill

Goodwill, which represents the excess of the purchase price of acquisition over the fair value of the net assets acquired, is carried at cost. Goodwill is tested for impairment annually or more often if events or circumstances indicate a reduction in the fair value below the carrying value. The carrying value of assets is calculated at the reporting unit. An impairment loss is recorded to the extent that the fair value of the goodwill within the reporting unit is less than its carrying value.

The Company completed its annual goodwill impairment testing and determined that the carrying amount of goodwill was not impaired. See Note 7 to the Financial Statements for goodwill amounts.

Accruals

The Company makes estimates related to certain employee benefits and miscellaneous accruals. Estimates for employee benefit accruals are based on management's assessment of estimated liabilities related to workers' compensation, health care benefits and annual contributions to an employee stock ownership plan ("ESOP") established in 2004 as part of the Company's retirement plan. Estimates for miscellaneous accruals are based on management's assessment of estimated liabilities for costs incurred.

The Company accrues for health care benefit costs under a self-funded plan. The Company purchases re-insurance for both specific and aggregate stop losses on claims that exceed $155 thousand on an individual basis and approximately $7.2 million on an aggregate basis.

Income Taxes
The Company's income tax policy provides for a liability approach under which deferred income taxes are provided for based upon enacted tax laws and rates applicable to the periods in which the taxes become payable. These differences result from items reported differently for financial reporting and income tax purposes, primarily depreciation, accrued expenses and reserves.

The Company reports a liability for unrecognized tax benefits resulting from uncertain tax positions taken or expected to be taken in a tax return. The Company recognizes potential interest and penalties related to its unrecognized tax benefits in income tax expense. The Company files U.S. federal income tax returns as well as income tax returns in various states and foreign jurisdictions. The Company is no longer subject to income tax examinations by tax authorities for years prior to 2005 for the majority of tax jurisdictions.

The Company's federal returns are currently under examination by the Internal Revenue Service (IRS) in the United States for the periods 2005 through 2012. Audit outcomes and the timing of audit settlements are subject to significant uncertainty. It is reasonably possible that within the next twelve months the Company will resolve some or all of the matters presently under consideration for 2005 through 2012 with the IRS and that there could be significant increases or decreases to unrecognized tax benefits. See Note 13 to the Financial Statements for income tax amounts, including reserves.

Off Balance Sheet Arrangements
The Company does not engage in any off balance sheet financing arrangements. In particular, the Company does not have any material interest in variable interest entities, which include special purpose entities and structured finance entities.

The Company used the equity method of accounting to account for its 40% equity investment in WhiteOak until April 2013 when the Company acquired the remaining 60% of the capital stock of WhiteOak. WhiteOak was merged into HCT. This investment was not material to the financial statements of the Company for the years ended December 28, 2013 and December 29, 2012.

Seasonality
The Company generally has experienced increased sales during the second quarter of the year, largely as a result of the order patterns of our customers. As a result, the Company's second quarter net sales, income from operations and net income historically are the highest of any quarter during the year.

Inflation
The impact of inflation on the Company's operating results has been moderate in recent years, reflecting generally lower rates of inflation in the economy. While inflation has not had, and the Company does not expect that it will have, a material impact upon operating results, there is no assurance that the Company's business will not be affected by inflation in the future.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to market risk from changes in interest rates on borrowed funds, which could affect its results of operations and financial condition. The Company's interest rate on its debt financing remains variable based upon the Company's leverage ratio. The Company had no variable-rate debt outstanding at December 27, 2014 and December 28, 2013.

The Company's exposure to foreign currency exchange fluctuations relates primarily to the direct investment in its facilities in the United Kingdom, Germany, and Korea. The Company does not use financial instruments to hedge foreign currency exchange rate changes.

MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

MARKET INFORMATION

The Common Stock of the Company has been trading publicly under the symbol SNHY on the Nasdaq Global Select Market since the Company's initial public offering on January 9, 1997. The following table sets forth the high and low closing sale prices of the Company's Common Stock as reported by the Nasdaq Global Select Market and the dividends declared for the periods indicated.

	High	Low	Dividends declared
2014			
First quarter	**$44.740**	**$34.990**	**$0.180**
Second quarter	**44.310**	**36.660**	**0.090**
Third quarter	**42.110**	**35.910**	**1.090**
Fourth quarter	**42.940**	**33.840**	**0.090**
2013			
First quarter	$33.160	$26.080	$0.180
Second quarter	33.610	29.640	0.090
Third quarter	36.300	30.000	0.090
Fourth quarter	43.270	34.950	0.090

HOLDERS

There were 174 shareholders of record of Common Stock on February 19, 2015. The number of recordholders was determined from the records of the Company's transfer agent and does not include beneficial owners of Common Stock whose shares are held in the names of securities brokers, dealers, and registered clearing agencies. The Company believes that there are approximately 13,000 beneficial owners of Common Stock.

DIVIDENDS

Quarterly dividends of $0.09 per share were paid on the 15th day of each month following the date of declaration.

In addition to the regular quarterly dividends, the Company declared shared distribution cash dividends in 2014 and 2013 equal to $0.09 per share. The 2014 dividend was paid on March 31, 2014, to shareholders of record on March 15, 2014, and the 2013 dividend was paid on March 31, 2013, to shareholders of record on March 15, 2013.

In light of the Company's strong cash position, ability to generate ongoing cash, and strong financial performance in the first half of 2014, the Company declared a special cash dividend of $1.00 per share that was paid on October 24, 2014, to shareholders of record as of October 10, 2014.

The Company's Board of Directors declared a shared distribution cash dividend of $0.09 per share, payable on March 31, 2015, to shareholders of record as of March 15, 2015.

The Company's Board of Directors currently intends to continue to pay a quarterly dividend of $0.09 per share during 2015. However, the declaration and payment of future dividends is subject to the sole discretion of the Board of Directors, and any determination as to the payment of future dividends will depend upon the Company's profitability, financial condition, capital needs, acquisition opportunities, future prospects and other factors deemed pertinent by the Board of Directors.

STOCK SPLIT

On June 9, 2011, the Company declared a three-for-two stock split, effected in the form of a 50% stock dividend, to shareholders of record on June 30, 2011, payable on July 15, 2011. The Company issued approximately 8,500,000 shares of common stock as a result of the stock split.

The effect of this stock split on outstanding shares, earnings per share and dividends per share has been retroactively applied to all periods presented.

EQUITY COMPENSATION PLANS

Information called for by Item 5 of Regulation S-K is provided in Note 14 of our 2014 Audited Financial Statements.

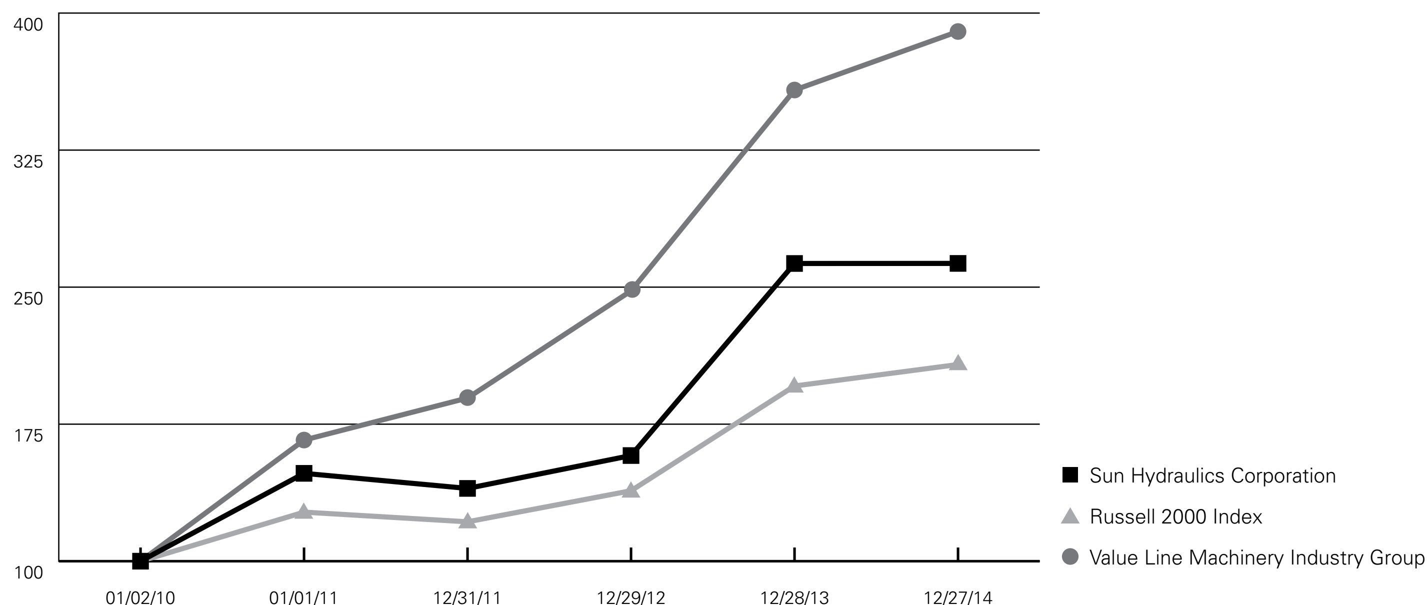
ISSUER PURCHASES OF EQUITY SECURITIES

The Company did not repurchase any of its stock during the fourth quarter of 2014.

FIVE-YEAR STOCK PERFORMANCE GRAPH

The following graph compares cumulative total return among Sun, the Russell 2000 Index and the Value Line Machinery Industry Group, from January 2, 2010 to December 27, 2014, assuming $100 invested in each on January 2, 2010. Total return assumes reinvestment of any dividends for all companies considered within the comparison. The stock price performance shown in the graph is not necessarily indicative of future price performance.

Comparison of 5-Year Cumulative Total Return
Among Sun Hydraulic Corporation, the Russell 2000 Index and
Value Line Machinery Industry Group



	1/2/2010	1/1/2011	12/31/2011	12/29/2012	12/28/2013	**12/27/2014**
Sun Hydraulics Corporation	100.00	148.08	139.83	157.82	262.94	**262.98**
Russell 2000 Index	100.00	126.85	121.56	138.56	195.89	**207.64**
Value Line Machinery Industry Group	100.00	166.30	189.30	247.94	357.88	**389.91**

FORWARD-LOOKING STATEMENTS

This Annual Report contains "forward-looking statements" (within the meaning of the Private Securities Litigation Reform Act of 1995) that are based on current expectations, estimates, forecasts, and projections about us, our beliefs, and assumptions made by us, including (i) our strategies regarding growth, including our intention to develop new products; (ii) our financing plans; (iii) trends affecting our financial condition or results of operations; (iv) our ability to continue to control costs and to meet our liquidity and other financing needs; (v) the declaration and payment of dividends; and (vi) our ability to respond to changes in customer demand domestically and internationally, including as a result of standardization. In addition, we may make other written or oral statements, which constitute forward-looking statements, from time to time. Words such as "may," "expects," "projects," "anticipates," "intends," "plans," "believes," "seeks," "estimates," variations of such words, and similar expressions are intended to identify such forward-looking statements. Similarly, statements that describe our future plans, objectives or goals also are forward-looking statements. These statements are not guarantees of future performance and are subject to a number of risks and uncertainties, including those discussed below and elsewhere in this report. Our actual results may differ materially from what is expressed or forecasted in such forward-looking statements, and undue reliance should not be placed on such statements. All forward-looking statements are made as of the date hereof, and we undertake no obligation to update any forward-looking statements, whether as a result of new information, future events or otherwise.

Factors that could cause actual results to differ materially from what is expressed or forecasted in such forward-looking statements include, but are not limited to: (i) conditions in the capital markets, including the interest rate environment and the availability of capital; (ii) changes in the competitive marketplace that could affect our revenue and/or cost bases, such as increased competition, lack of qualified engineering, marketing, management or other personnel, and increased labor and raw materials costs; (iii) new product introductions, product sales mix and the geographic mix of sales nationally and internationally. Further information relating to factors that could cause actual results to differ from those anticipated is included but not limited to information under the headings Item 1 "Business," Item 1A. "Risk Factors" and Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Form 10-K for the year ended December 27, 2014. The Company disclaims any intention or obligation to update or revise forward-looking statements, whether as a result of new information, future events or otherwise.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and
Stockholders of Sun Hydraulics Corporation:

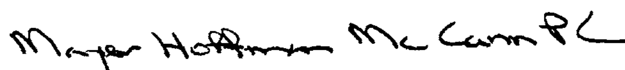
We have audited the accompanying consolidated balance sheets of Sun Hydraulics Corporation (a Florida Corporation) and subsidiaries (collectively, the Company) as of December 27, 2014 and December 28, 2013, and the related consolidated statements of operations, comprehensive income (loss), shareholders' equity, and cash flows for each of the years in the three-year period ended December 27, 2014. We also have audited Sun Hydraulics Corporation and subsidiaries' internal control over financial reporting as of December 27, 2014 based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall consolidated financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sun Hydraulics Corporation and subsidiaries as of December 27, 2014 and December 28, 2013, and the results of its operations and its cash flows for each of the years in the three-year period ended December 27, 2014, in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, Sun Hydraulics Corporation and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 27, 2014, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).



February 24, 2015
Clearwater, Florida

CONSOLIDATED BALANCE SHEETS

	December 27, 2014	December 28, 2013
(in thousands, except share data)		
Assets		
Current assets:		
Cash and cash equivalents	**$ 56,843**	$ 54,912
Restricted cash	**319**	334
Accounts receivable, net of allowance for doubtful accounts of $172 and $117	**17,501**	16,984
Inventories	**14,098**	13,853
Income taxes receivable	**—**	954
Deferred income taxes	**467**	474
Short-term investments	**43,353**	38,729
Other current assets	**2,966**	2,816
Total current assets	**135,547**	129,056
Property, plant and equipment, net	**77,716**	75,731
Goodwill	**5,141**	5,221
Other assets	**4,360**	3,470
Total assets	**$222,764**	$213,478
Liabilities and shareholders' equity		
Current liabilities:		
Accounts payable	**$ 4,873**	$ 4,630
Accrued expenses and other liabilities	**7,908**	7,016
Income taxes payable	**559**	—
Dividends payable	**2,392**	2,372
Total current liabilities	**15,732**	14,018
Deferred income taxes	**8,501**	7,747
Other noncurrent liabilities	**272**	285
Total liabilities	**24,505**	22,050
Commitments and contingencies	**—**	—
Shareholders' equity:		
Preferred stock, 2,000,000 shares authorized, par value $0.001, no shares outstanding	**—**	—
Common stock, 50,000,000 shares authorized, par value $0.001, 26,572,774 and 26,352,692 shares outstanding	**27**	26
Capital in excess of par value	**73,499**	65,391
Retained earnings	**128,818**	123,420
Accumulated other comprehensive income (loss)	**(4,085)**	2,591
Total shareholders' equity	**198,259**	191,428
Total liabilities and shareholders' equity	**$222,764**	$213,478

The accompanying Notes to the Consolidated Financial Statements are an integral part of these financial statements.

CONSOLIDATED STATEMENTS OF OPERATIONS

For the year ended	**December 27, 2014**	December 28, 2013	December 29, 2012
(in thousands, except per share data)			
Net sales	**$227,673**	$205,267	$204,367
Cost of sales	**133,781**	122,306	123,795
Gross profit	**93,892**	82,961	80,572
Selling, engineering and administrative expenses	**29,821**	26,790	26,163
Operating income	**64,071**	56,171	54,409
Interest (income) expense, net	**(1,592)**	(967)	(1,368)
Foreign currency transaction (gain) loss, net	**(764)**	(27)	(116)
Miscellaneous (income) expense, net	**685**	(7)	40
Income before income taxes	**65,742**	57,172	55,853
Income tax provision	**21,967**	19,188	18,455
Net income	**$ 43,775**	$ 37,984	$ 37,398
Basic net income per common share	**$ 1.65**	$ 1.45	$ 1.44
Weighted average basic shares outstanding	**26,456**	26,206	25,944
Diluted net income per common share	**$ 1.65**	$ 1.45	$ 1.44
Weighted average diluted shares outstanding	**26,456**	26,206	25,971
Dividends declared per share	**$ 1.450**	$ 0.450	$ 1.480

The accompanying Notes to the Consolidated Financial Statements are an integral part of these financial statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

Year ended	**December 27, 2014**	December 28, 2013	December 29, 2012
(in thousands)			
Net income	**$ 43,775**	$ 37,984	$ 37,398
Other comprehensive income (loss)			
Foreign currency translation adjustments	**(6,005)**	2,010	2,397
Unrealized gain (loss) on available-for-sale securities	**(671)**	(22)	326
Total other comprehensive income (loss)	**$ (6,676)**	$ 1,988	$ 2,763
Comprehensive income	**$ 37,099**	$ 39,972	$ 40,121

The accompanying Notes to the Consolidated Financial Statements are an integral part of these financial statements.

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

(in thousands)	Preferred shares	Preferred stock	Common shares	Common stock	Capital in excess of par value	Retained earnings	Accumulated other comprehensive income	Total
Balance, December 31, 2011	—	$—	25,756	$26	$48,944	$ 98,426	$(2,120)	$145,276
Shares issued, Restricted Stock			89					
Shares issues, other comp			56					
Shares issued, ESPP			35		700			700
Shares issued, shared distribution			159		4,407			4,407
Stock-based compensation					3,263			3,263
Tax benefit of stock-based compensation					88			88
Dividends declared						(38,582)		(38,582)
Net income						37,398		37,398
Other comprehensive income (loss)							2,723	2,723
Balance, December 29, 2012	—	$—	26,095	$26	$57,402	$ 97,242	$ 603	$155,273
Shares issued, Restricted Stock			90					
Shares issues, other comp			27					
Shares issued, ESPP			35		859			859
Shares issued, shared distribution			106		3,486			3,486
Stock-based compensation					3,341			3,341
Tax benefit of stock-based compensation					303			303
Dividends declared						(11,806)		(11,806)
Net income						37,984		37,984
Other comprehensive income (loss)							1,988	1,988
Balance, December 28, 2013	—	$—	26,353	$26	$65,391	$123,420	$ 2,591	$191,428
Shares issued, Restricted Stock			102	1				1
Shares issues, other comp			19					
Shares issued, ESPP			25		846			846
Shares issued, shared distribution			74		3,226			3,226
Stock-based compensation					3,899			3,899
Tax benefit of stock-based compensation					137			137
Dividends declared						(38,377)		(38,377)
Net income						43,775		43,775
Other comprehensive income (loss)							(6,676)	(6,676)
Balance, December 27, 2014	**—**	**$—**	**26,573**	**$27**	**$73,499**	**$128,818**	**$(4,085)**	**$198,259**

The accompanying Notes to the Consolidated Financial Statements are an integral part of these financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the year ended	**December 27, 2014**	December 28, 2013	December 29, 2012
(in thousands)			
Cash flows from operating activities:			
Net income	**$ 43,775**	$ 37,984	$ 37,398
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	**8,718**	7,227	7,186
(Gain) Loss on disposal of assets	**171**	462	193
Gain on investment in business	**—**	(528)	—
Stock-based compensation expense	**3,899**	3,047	2,333
Deferred director and phantom stock unit expense (income)	**35**	70	20
Stock compensation income tax benefit	**(137)**	(303)	(88)
Allowance for doubtful accounts	**55**	(7)	26
Provision for slow moving inventory	**(37)**	—	112
Provision for deferred income taxes	**1,265**	291	325
(Increase) decrease in, net of acquisition:			
Accounts receivable	**(572)**	(3,210)	1,903
Inventories	**(208)**	(1,226)	268
Income taxes receivable	**1,091**	77	(520)
Other current assets	**(150)**	(167)	(650)
Other assets	**69**	383	240
Increase (decrease) in, net of acquisition:			
Accounts payable	**243**	24	(742)
Accrued expenses and other liabilities	**4,118**	3,155	4,547
Income taxes payable	**559**	—	—
Other noncurrent liabilities	**(48)**	(156)	(353)
Net cash provided by operating activities	**62,846**	47,123	52,198
Cash flows from investing activities:			
Investment in business, net of cash acquired	**—**	(923)	(1,140)
Investment in licensed technology	**(1,075)**	—	—
Capital expenditures	**(10,667)**	(17,935)	(13,359)
Proceeds from dispositions of equipment	**37**	230	56
Purchases of short-term investments	**(51,236)**	(28,356)	(40,495)
Proceeds from sale of short-term investments	**44,765**	26,764	32,912
Net cash used in investing activities	**(18,176)**	(20,220)	(22,026)
Cash flows from financing activities:			
Repayment of debt	**—**	—	(169)
Stock compensation income tax benefit	**137**	303	88
Proceeds from stock issued	**846**	859	700
Dividends to shareholders	**(38,357)**	(9,435)	(40,900)
Change in restricted cash	**15**	(5)	(272)
Net cash used in financing activities	**(37,359)**	(8,278)	(40,553)
Effect of exchange rate changes on cash and cash equivalents	**(5,380)**	1,809	2,025
Net increase (decrease) in cash and cash equivalents	**1,931**	20,434	(8,356)
Cash and cash equivalents, beginning of period	**54,912**	34,478	42,834
Cash and cash equivalents, end of period	**$ 56,843**	$ 54,912	$ 34,478
Supplemental disclosure of cash flow information:			
Cash paid:			
Income taxes	**$ 19,693**	$ 19,123	$ 18,739
Supplemental disclosure of noncash transactions:			
Common stock issued for shared distribution through accrued expenses and other liabilities	**$ 3,226**	$ 3,486	$ 4,407
Common stock issued for deferred director's compensation through other noncurrent liabilities	**$ —**	$ 294	$ 930
Unrealized gain (loss) on available-for-sale securities	**$ (671)**	$ (22)	$ 326

The accompanying Notes to the Consolidated Financial Statements are an integral part of these financial statements.

1. BUSINESS

Sun Hydraulics Corporation, and its wholly-owned subsidiaries, design, manufacture, and sell screw-in cartridge valves and manifolds used in hydraulic systems. The Company has facilities in the United States, the United Kingdom, Germany, Korea, France, China, and India. Sun Hydraulics Corporation ("Sun Hydraulics"), with its main offices located in Sarasota, Florida, designs, manufactures, and sells its products primarily through distributors. Sun Hydraulik Holdings Limited ("Sun Holdings"), a wholly-owned subsidiary of Sun Hydraulics, was formed to provide a holding company for the European market operations; its wholly-owned subsidiaries are Sun Hydraulics Limited (a British corporation, "Sun Ltd.") and Sun Hydraulik GmbH (a German corporation, "Sun GmbH"). Sun Ltd. operates a manufacturing and distribution facility located in Coventry, England, and Sun GmbH operates a manufacturing and distribution facility located in Erkelenz, Germany. Sun Hydraulics Korea Corporation ("Sun Korea"), a wholly-owned subsidiary of Sun Hydraulics, located in Incheon, South Korea, operates a manufacturing and distribution facility. In 2012, Sun Korea acquired Seungwon Solutions Corporation ("Seungwon"), also located in Incheon, South Korea, a component supplier to Sun Korea and third parties. Sun Hydraulics (France) ("Sun France"), a liaison office located in Bordeaux, France, is used to service the French market. Sun Hydraulics established Sun Hydraulics China Co. Ltd., a representative office in Shanghai in January 2011, to develop new business opportunities in the Chinese market. Sun Hydraulics (India), a liaison office in Bangalore, India, is used to develop new business opportunities in the Indian market. In 2011, Sun Hydraulics purchased the outstanding shares of High Country Tek, Inc. ("HCT") it did not already own. HCT, now a wholly-owned subsidiary of Sun Hydraulics, is located in Nevada City, California, and designs and manufactures ruggedized electronic/hydraulic control solutions for mobile equipment markets. In 2013, Sun Hydraulics purchased the remaining 60% of WhiteOak Controls Inc. ("WhiteOak"), which was merged into HCT (see Note 8). WhiteOak, designs and produces complementary electronic control products.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts and operations of Sun Hydraulics and its direct and indirect subsidiaries. All significant intercompany accounts and transactions are eliminated in consolidation. The Company used the equity method of accounting for its investment in WhiteOak until April 1, 2013, when it acquired the remaining 60% of WhiteOak (see Note 8). The Company did not have a majority ownership in or exercise control over this entity prior to that date.

Critical Accounting Policies and Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates are used in the determination of impairment of long-lived assets, inventory, goodwill, accruals, income taxes, and fair value of short-term investments.

Cash, Cash Equivalents and Short-term Investments

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

The Company's short-term investments have been classified and accounted for as available-for-sale. Management determines the appropriate classification of its investments at the time of purchase and reevaluates the designation at each balance sheet date. The Company may or may not hold securities with stated maturities greater than 12 months until maturity. As management views these securities as available to support current operations, the Company classifies securities with maturities beyond 12 months as current assets under the caption short-term investments in the accompanying Consolidated Balance Sheets. The Company's short-term investments are carried at fair value, with the unrealized gains and losses, net of tax, reported as a component of shareholder's equity. Realized gains and losses on sales of short-term investments are generally determined using the specific identification method, and are included in miscellaneous (income) expense in the Consolidated Statements of Operations.

Accounts Receivable

The Company sells to most of its customers on a recurring basis, primarily through distributors with which the Company maintains long-term relationships. As a result, bad debt experience has not been material. The allowance for doubtful accounts is determined on a specific identification basis by a review of those accounts that are significantly in arrears. There can be no assurance that a distributor or a large direct sale customer with overdue accounts receivable balances will not develop financial difficulties and default on payment. See the consolidated balance sheets for allowance amounts.

Inventory

Inventories are valued at the lower of cost or market, with cost determined on a first-in, first-out basis. The Company offers a wide variety of standard products and as a matter of policy does not discontinue products. On an ongoing basis, component parts found to be obsolete through design or process changes are disposed of and charged to material cost. The Company reviews on-hand balances of products and component parts against specific criteria. Products and component parts without usage or that have excess quantities on hand are evaluated. An inventory reserve is then established for the full inventory carrying value of those products and component parts deemed to be obsolete or slow moving. See Note 5 to the Financial Statements for inventory reserve amounts.

Property, Plant and Equipment

Property, plant and equipment is stated at cost. Expenditures for repairs and improvements that significantly add to the productive capacity or extend the useful life of an asset are capitalized. Repairs and maintenance are expensed as incurred.

Depreciation is computed using the straight-line method over the following useful lives:

	Years
Computer Equipment	3–5
Machinery and equipment	4–12
Furniture and fixtures	4–10
Leasehold and land improvements	5–15
Buildings	25–40

Gains or losses on the retirement, sale, or disposition of property, plant and equipment are reflected in the Consolidated Statement of Operations in the period in which the assets are taken out of service.

Fair Value Measurements
The Company applies fair value accounting guidelines for all financial assets and liabilities and non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). Under these guidelines, fair value is defined as the price that would be received for the sale of an asset or paid to transfer a liability (i.e., an exit price) in an orderly transaction between market participants at the measurement date. The guidance establishes a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value as follows:

Level 1—Quoted prices in active markets for identical assets or liabilities.

Level 2—Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets or liabilities in active markets or quoted prices for identical assets or liabilities in inactive markets.

Level 3—Unobservable inputs that are supported by little, infrequent, or no market activity and reflect the Company's own assumptions about inputs used in pricing the asset or liability.

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The Company's valuation techniques used to measure the fair value of marketable equity securities were derived from quoted prices in active markets for identical assets or liabilities. The valuation techniques used to measure the fair value of all other financial instruments were valued based on quoted market prices or model driven valuations using significant inputs derived from or corroborated by observable market data.

Goodwill
Goodwill, which represents the excess of the purchase price of acquisition over the fair value of the net assets acquired, is carried at cost. Goodwill is tested for impairment annually or more often if events or circumstances indicate a reduction in the fair value below the carrying value. The carrying value of assets is calculated at the reporting unit. An impairment loss is recorded to the extent that the fair value of the goodwill within the reporting unit is less than its carrying value.

The Company completed its annual goodwill impairment testing and determined that the carrying amount of goodwill was not impaired. See Note 7 to the Financial Statements for goodwill amounts.

Impairment of Long-Lived Assets
Long-lived assets, such as property and equipment, and purchased intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of the asset is measured by comparison of its carrying amount to future net cash flows the asset is expected to generate. If such assets are considered impaired, the impairment to be recognized is measured as the amount by which the carrying amount of the asset exceeds its fair value.

Accruals
The Company makes estimates related to certain employee benefits and miscellaneous accruals. Estimates for employee benefit accruals are based on management's assessment of estimated liabilities related to workers' compensation, health care benefits and annual contributions to an employee stock ownership plan ("ESOP"), established in 2004 as part of the Company's retirement plan. Estimates for miscellaneous accruals are based on management's assessment of estimated liabilities for costs incurred.

The Company accrues for health care benefit costs under a self-funded plan. The Company purchases re-insurance for both specific and aggregate stop losses on claims that exceed $155 on an individual basis and approximately $7,200 on an aggregate basis.

Revenue Recognition
The Company reports revenues, net of sales incentives, when title passes and risk of loss transfers to the customer. The effect of material nonrecurring events is provided for when they become known.

Shipping and Handling Costs
Shipping and handling costs billed to distributors and customers are recorded in revenue. Shipping costs incurred by the Company are recorded in cost of goods sold.

Foreign Currency Translation and Transactions
The Pound Sterling is the functional currency of Sun Ltd. The Euro is the functional currency of Sun GmbH. The South Korean Won is the functional currency of Sun Korea. The U.S. Dollar is the functional currency for Sun Hydraulics and the reporting currency for the consolidated group. The assets and liabilities of Sun Ltd., Sun GmbH, and Sun Korea are translated at the exchange rate in effect at the balance sheet date, and income and expense items are translated at the average annual rate of exchange for the period. The resulting unrealized translation gains and losses are included as a component of shareholders' equity designated as "accumulated other comprehensive income (loss)." Realized gains and losses from foreign currency transactions are included in the Consolidated Statement of Operations.

Income Taxes
The Company's income tax policy provides for a liability approach under which deferred income taxes are provided for based upon enacted tax laws and rates applicable to the

periods in which the taxes become payable. These differences result from items reported differently for financial reporting and income tax purposes, primarily depreciation, accrued expenses and reserves.

The Company reports a liability for unrecognized tax benefits resulting from uncertain tax positions taken or expected to be taken in a tax return. The Company recognizes potential interest and penalties related to its unrecognized tax benefits in income tax expense.

Stock-Based Compensation

All share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as an expense in earnings over the requisite service period. Benefits of tax deductions in excess of recognized compensation costs are reported as a financing cash inflow.

3. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following tables provide information regarding the Company's assets and liabilities measured at fair value on a recurring basis at December 27, 2014 and December 28, 2013.

	December 27, 2014			
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value
Assets				
Level 1:				
Equity securities	**$ 2,145**	**$ 65**	**$ (282)**	**$ 1,928**
Mutual funds	**3,106**	**2**	**(227)**	**2,881**
Subtotal	**$ 5,251**	**$ 67**	**$ (509)**	**$ 4,809**
Level 2:				
Corporate fixed income	**$33,740**	**$ 6**	**$ (868)**	**$32,878**
Municipal bonds	**2,441**	**—**	**(33)**	**2,408**
Certificates of deposit and time deposits	**2,439**	**—**	**—**	**2,439**
Asset-backed securities	**842**	**—**	**(23)**	**819**
Subtotal	**$39,462**	**$ 6**	**$ (924)**	**$38,544**
Total	**$44,713**	**$ 73**	**$(1,433)**	**$43,353**
Liabilities				
Level 1:				
Phantom stock units	**$ 30**	**$ —**	**$ —**	**$ 30**
Total	**$ 30**	**$ —**	**$ —**	**$ 30**

	December 28, 2013			
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value
Assets				
Level 1:				
Equity securities	$ 2,049	$137	$ (64)	$ 2,122
Mutual funds	3,865	19	(1)	3,883
Subtotal	$ 5,914	$156	$ (65)	$ 6,005
Level 2:				
Corporate fixed income	$25,240	$126	$ (250)	$25,116
Municipal bonds	2,775	1	(28)	2,748
Certificates of deposit and time deposits	4,014	1	—	4,015
Asset-backed securities	974	—	(129)	845
Subtotal	$33,003	$128	$ (407)	$32,724
Total	$38,917	$284	$ (472)	$38,729
Liabilities				
Level 1:				
Phantom stock units	$ 38	$ —	$ —	$ 38
Total	$ 38	$ —	$ —	$ 38

The Company recognized a net realized gain on investments during the twelve months ended December 27, 2014 of $182 and a net realized loss of $1 during the twelve months ended December 28, 2013. As of December 27, 2014, gross unrealized losses related to individual securities that had been in a continuous loss position for 12 months or longer were not significant. The Company considers these unrealized losses in market value of its investments to be temporary in nature. When evaluating an investment for other-than-temporary impairment, the Company reviews factors such as the length of time and extent to which fair value has been below its cost basis, the financial condition of the issuer and any changes thereto, and the Company's intent to sell, or whether it is more likely than not it will be required to sell, the investment before recovery of the investment's cost basis. During the twelve months ended December 28, 2013, the Company recognized an impairment charge of $61, which is included in the net realized loss for that period. This resulted from the deterioration of the financial condition of an issuer of a corporate bond security.

Maturities of investments at December 27, 2014 are as follows:

	Adjusted Cost	Fair Value
Due in less than one year	$19,309	$19,229
Due after one year but within five years	14,019	13,611
Due after five years but within ten years	2,794	2,510
Due after ten years	3,340	3,194
Equity securities	2,145	1,928
Mutual funds	3,106	2,881
Total	$44,713	$43,353

The Company reports deferred director stock units and phantom stock units as a liability. All remaining deferred stock units were issued in 2013. The Company recognized expense relating to these liabilities of $35 and $70, for the periods ended December 27, 2014 and December 28, 2013, respectively. Phantom stock units vest over a period of three years.

The Company did not have any fair value adjustments for assets and liabilities measured at fair value on a nonrecurring basis during the period ended December 27, 2014.

4. RESTRICTED CASH

On December 27, 2014 and December 28, 2013, the Company had restricted cash of $319 and $334, respectively. Restricted cash reserves for customs and excise taxes in the U.K. operation were $47 and $50 at December 27, 2014 and December 28, 2013, respectively. The restricted amount was calculated as an estimate of two months of customs and excise taxes for items coming into the Company's U.K. operations and is held with Lloyds TSB in the U.K. Restricted cash of $272 and $284 at December 27, 2014 and December 28, 2013, respectively, represents the holdback of the purchase price associated with the acquisition of Seungwon on October 18, 2012.

5. INVENTORIES

	December 27, 2014	December 28, 2013
Raw materials	**$ 6,329**	$ 6,037
Work in process	**3,979**	4,258
Finished goods	**4,433**	4,238
Provision for slow-moving inventory	**(643)**	(680)
Total	**$ 14,098**	$ 13,853

6. PROPERTY, PLANT AND EQUIPMENT

	December 27, 2014	December 28, 2013
Machinery and equipment	**$ 94,702**	$ 92,549
Office furniture and equipment	**9,417**	7,969
Buildings	**45,604**	30,771
Leasehold and land improvements	**2,664**	2,644
Land	**10,104**	7,490
	$162,491	$141,423
Less: Accumulated depreciation	**(91,375)**	(86,484)
Construction in progress	**6,600**	20,792
Total	**$ 77,716**	$ 75,731

Depreciation expense for the years ended December 27, 2014, December 28, 2013, and December 29, 2012 totaled $7,717, $6,511, and $6,514, respectively.

7. GOODWILL AND INTANGIBLE ASSETS

A summary of changes in goodwill at December 27, 2014 and December 28, 2013 is as follows:

Balance, December 29, 2012	$4,472
Acquisitions	726
Currency translation	23
Balance, December 28, 2013	$5,221
Acquisitions	—
Currency translation	(80)
Balance, December 27, 2014	**$5,141**

Valuation models reflecting the expected future cash flow projections are used to value reporting units. A valuation of the reporting unit at December 27, 2014 indicated that there was no impairment of the carrying value of the goodwill at Sun Korea. A valuation of the reporting unit at September 27, 2014 indicated that there was no impairment of the carrying value of the goodwill at HCT. As of December 27, 2014, no factors were identified that indicated impairment of the carrying value of goodwill at HCT.

In 2014, the Company entered into a licensing agreement with Sturman Industries, Inc., recognizing an intangible asset of $1,075. The agreement is for licensed technology to be used with the Company's electrically actuated hydraulic cartridge valves, and lasts for a period of fifteen years from the date of the first sale. The Company recognized $2,658 and $746 in identifiable intangible assets as a result of the acquisitions of HCT and WhiteOak, respectively. Intangible assets are held in other assets on the balance sheet. At December 27, 2014 and December 28, 2013, intangible assets consisted of the following:

	December 27, 2014			December 28, 2013		
	Gross carrying amount	**Accumulated amortization**	**Net carrying amount**	Gross carrying amount	Accumulated amortization	Net carrying amount
Definite-lived intangibles:						
Trade Name	**$ 774**	**$(264)**	**$ 510**	$ 774	$(184)	$ 590
Non-compete agreement	**11**	**(10)**	**1**	11	(4)	7
Technology	**868**	**(216)**	**652**	868	(130)	738
Customer relationships	**1,751**	**(272)**	**1,479**	1,751	(179)	1,572
Licensing agreement	**1,075**	**(11)**	**1,064**	—	—	—
	$4,479	**$(773)**	**$3,706**	$3,404	$(497)	$2,907

Total amortization expense for the years 2015 through 2019, which includes anticipated amortization under the new licensing agreement entered into in 2014, is presented below.

Year:	
2015	$ 389
2016	471
2017	471
2018	471
2019	471
Total	$2,273

Intangible assets are evaluated for impairment whenever events or circumstances indicate that the undiscounted net cash flows to be generated by their use over their expected useful lives and eventual disposition may be less than their net carrying value. No such events or circumstances occurred during the twelve months ended December 27, 2014.

8. ACQUISITIONS

On April 1, 2013, the Company acquired the remaining 60% of the capital stock of WhiteOak that it did not already own for $1,000. WhiteOak has been merged into HCT and relocated to HCT's facility in California. HCT manufactures, markets, sells and has design control for all current WhiteOak products. The combination of HCT and WhiteOak gives Sun full ownership of the technology to develop the next generation of Sun's electronic control products.

The Company recorded approximately $726 in goodwill, $746 in definite-lived intangible assets, and $12 in transaction costs related to the acquisition. Of the $746 of acquired intangible assets, $18 was assigned to the WhiteOak trade name (1-year useful life), $11 was assigned to non-compete agreements (2-year useful life), $276 was assigned to customer relationships (15-year useful life), and $441 was assigned to technology (10-year useful life). Additionally, the Company recorded a gain of $528 as a result of remeasuring to fair value its 40% equity interest in WhiteOak held before the business combination. This gain is included in miscellaneous income on the Company's Consolidated Statement of Operations.

On October 18, 2012, the Company, through Sun Korea, purchased all of the outstanding stock of Seungwon Solutions Corporation ("Seungwon") for approximately $1,458. Seungwon is a component supplier, and approximately 80% of its sales are to Sun Korea.

The Company recorded approximately $1,731 in goodwill and approximately $80 in transaction costs related to the acquisition.

The results of operations of WhiteOak and Seungwon have been included in the Company's consolidated results since the dates of acquisition. Supplemental pro forma information and disclosure of acquired assets and liabilities have not been provided as these acquisitions did not have a material impact on the consolidated financial statements individually or in the aggregate.

9. OTHER ASSETS

	December 27, 2014	December 28, 2013
Definite-lived intangibles, net of amortization of $773 and $497	**$3,706**	$2,907
Loan acquisition costs, net of amortization of $59 and $42	**27**	44
Deposits with suppliers	**425**	129
Notes receivable	**106**	337
Other	**96**	53
Total	**$4,360**	$3,470

10. ACCRUED EXPENSES AND OTHER LIABILITIES

	December 27, 2014	December 28, 2013
Compensation and benefits	**$5,878**	$5,546
Self-insurance liability	**744**	703
Other	**1,286**	767
Total	**$7,908**	$7,016

11. LONG-TERM DEBT

Effective August 1, 2011, the Company entered into a credit and security agreement in the U.S. with Fifth Third Bank (the "Bank"). The agreement provides for three separate credit facilities totaling $50,000.

Facility A is a $15,000 unsecured revolving line of credit and requires monthly payments of interest. Facility A has a floating interest rate of 1.45% over the 30-day LIBOR Rate (as defined).

Facility B is an accordion feature to increase the revolving line of credit to a $35,000 secured revolving line of credit. Facility B will be secured by the Company's U.S. assets, including its manufacturing facilities, and requires monthly payments of interest. Facility B will bear interest at the 30-day LIBOR Rate or the Bank's Base Rate (as defined), at the Company's discretion, plus a margin based on the Borrower's Funded Debt to EBITDA Leverage Ratio (as defined). The LIBOR Margin ranges from 1.45% to 2.25% and the Bank's Base Rate ranges from (0.25)% to 0.00%.

Facility C is a $15,000 construction and term loan. The Company did not activate Facility C for the construction of its new Sarasota factory and access to this facility is now expired.

Facility A or Facility B (if activated) is payable in full on August 1, 2016. Maturity may be accelerated by the Bank upon an Event of Default (as defined). Prepayment may be made without penalty or premium at any time upon the required notice to the Bank.

Facility A is subject to debt covenants (capitalized terms are defined therein) including: 1) Minimum Tangible Net Worth of not less than $92,000, increased annually by 50% of Net Income, and 2) Minimum EBITDA of not less than $5,000; and requires the Company to maintain its primary domestic deposit accounts with the bank. At December 27, 2014, the Company was in compliance with all debt covenants related to Facility A as follows:

Covenant	Required Ratio/Amount	Actual Ratio/Amount
Minimum Tangible Net Worth	$170,417	$191,069
Minimum EBITDA	Not less than $5 million	$ 72,132

If Facility B is activated, covenant 2 above will automatically terminate and two additional covenants will be required: 1) Funded Debt to EBITDA ratio equal to or less than 3.0:1.0, and 2) EBIT to Interest Expense ratio of not less than 2.5:1.0. As of December 27, 2014, the Company had not activated Facility B.

The Company did not have any amounts drawn on Facilities A, B, or C for the periods ended December 27, 2014, and December 28, 2013.

12. DIVIDENDS TO SHAREHOLDERS

The Company declared dividends of $38,377, $11,806, and $38,582 to shareholders in 2014, 2013, and 2012, respectively.

Except as noted below, the Company declared the following regular quarterly dividends to shareholders of record on the last day of the respective quarter, paid on the 15th day of each month following the date of declaration:

	2014	2013	2012
First quarter	**$0.090**	$0.090	$0.090
Second quarter	**0.090**	0.090	0.090
Third quarter	**0.090**	0.090	0.090
Fourth quarter	**0.090**	0.090	0.090

In addition to the regular quarterly dividends, the Company declared shared distribution cash dividends in 2014, 2013 and 2012, equal to $0.09, $0.09 and $0.12, respectively. The 2014 dividend was paid on March 31, 2014, to shareholders of record on March 15, 2014, the 2013 dividend was paid on March 31, 2013, to shareholders of record on March 15, 2013, and the 2012 dividend was paid on March 31, 2012, to shareholders of record as of March 22, 2012. The shared distribution was introduced in 2008 as a way to reward both shareholders and employees when the Company has a successful year. The Board of Directors declared a shared distribution cash dividend of $0.09 per share, payable on March 31, 2015, to shareholders of record as of March 15, 2015.

In 2014, the Company declared a special one-time cash dividend of $1.00 per share paid on October 24, 2014, to shareholders of record as of October 10, 2014. In declaring the special dividend, the Board of Directors cited the Company's strong cash position, ability to generate ongoing cash, and strong financial performance in the first half of 2014 as reasons for its decision.

In light of the Company's cash position, its current and perceived uses for cash, and an anticipated increase in income tax rates on corporate dividends as of January 1, 2013, the Board of Directors in December 2012 declared a special one-time cash dividend of $1.00 per share to shareholders of record as of December 14, 2012. In anticipation of the expected tax law changes in 2013, the payment date for both the special dividend and the regular quarterly dividend of $0.09 per share was December 28, 2012.

13. INCOME TAXES

Deferred income tax assets and liabilities are provided to reflect the future tax consequences of differences between the tax basis of assets and liabilities and their reported amounts in the financial statements.

For financial reporting purposes, income before income taxes includes the following components:

For the year ended	**December 27, 2014**	December 28, 2013	December 29, 2012
United States	**$52,713**	$46,314	$44,957
Foreign	**13,029**	10,858	10,896
Total	**$65,742**	$57,172	$55,853

The Company derives its pretax income based on the consolidated results of its legal entities. The Company has made the decision to consolidate engineering and manufacturing for the most part in the U.S. The Company's foreign subsidiaries primarily act as part of our sales and distribution channel, resulting in different pretax income levels. Products manufactured in the U.S. are sold worldwide and are the primary reason that pretax income in the U.S. is higher than foreign pretax income. The U.S. legal entity had third-party export sales of $60,052, $54,213, and $50,231 for the years 2014, 2013, and 2012, respectively. Foreign pretax income is impacted by the level of foreign manufacturing, sales at varying market levels, as well as direct sales to large OEM customers.

The components of the income tax provision (benefit) are as follows:

For the year ended	**December 27, 2014**	December 28, 2013	December 29, 2012
Current tax expense (benefit):			
United States	**$17,897**	$15,634	$15,396
State and local	**1,249**	950	924
Foreign	**2,574**	2,466	1,788
Total Current	**21,720**	19,050	18,108
Deferred tax expense (benefit):			
United States	**112**	158	545
State and local	**(7)**	6	12
Foreign	**142**	(26)	(210)
Total Deferred	**247**	138	347
Total income tax provision	**$21,967**	$19,188	$18,455

The reconciliation between the effective income tax rate and the U.S. federal statutory rate is as follows:

For the year ended	**December 27, 2014**	December 28, 2013	December 29, 2012
U.S. federal taxes at the statutory rate	**$23,010**	$20,010	$19,549
Increase (decrease)			
Foreign tax credit	**(432)**	(433)	(358)
Domestic production activity deduction	**(1,793)**	(1,632)	(1,483)
Foreign income taxed at lower rate	**(957)**	(1,013)	(901)
Nondeductible items	**392**	302	411
State and local taxes, net	**1,242**	957	935
Change in reserve	**193**	168	710
Other	**312**	829	(408)
Income tax provision	**$21,967**	$19,188	$18,455

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income taxes. The temporary differences that give rise to significant portions of the deferred tax assets and liabilities as of December 27, 2014 and December 28, 2013 are presented below:

	December 27, 2014	December 28, 2013
Deferred tax assets:		
Current:		
Accrued expenses and other	**$ 467**	$ 474
Total current deferred tax assets	**467**	474
Noncurrent:		
Accrued expenses and other	**2,863**	2,414
Total noncurrent deferred tax assets	**2,863**	2,414
Deferred tax liabilities:		
Noncurrent:		
Depreciation	**(10,265)**	(8,867)
Other	**(1,099)**	(1,294)
Total noncurrent deferred tax liabilities	**(11,364)**	(10,161)
Net noncurrent deferred tax liability	**$ (8,501)**	$ (7,747)

A valuation allowance to reduce the deferred tax assets reported is required if, based on the weight of the evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized. For the fiscal years ended 2014 and 2013, management has determined that a valuation allowance was not required.

The Company intends and has the ability to indefinitely reinvest the earnings of its non-U.S. subsidiaries, which reflect full provision for non-U.S. income taxes, to expand its international operations. These earnings relate to ongoing operations and, at December 27, 2014, cumulative earnings were approximately $72 million. Accordingly, no provision has been made for U.S. income taxes that might be payable upon repatriation of such earnings. In the event any earnings of non-U.S. subsidiaries are repatriated, the Company will provide U.S. income taxes upon repatriation of such earnings, which will be offset by applicable foreign tax credits, subject to certain limitations.

The Company prescribes a recognition threshold and measurement attribute for an uncertain tax position taken or expected to be taken in a tax return.

The following is a roll-forward of the Company's unrecognized tax benefits:

Unrecognized tax benefits—December 31, 2011	$ 609
Increases from positions taken during prior periods	710
Settled Positions	(124)
Lapse of statute of limitations	—
Unrecognized tax benefits—December 29, 2012	$1,195
Increases from positions taken during prior periods	168
Settled positions	(241)
Lapse of statute of limitations	—
Unrecognized tax benefits—December 28, 2013	$1,122
Increases from positions taken during prior periods	193
Settled positions	(159)
Lapse of statute of limitations	—
Unrecognized tax benefits—December 27, 2014	**$1,156**

At December 27, 2014, the Company had an unrecognized tax benefit of $1,156 including accrued interest. If recognized, the unrecognized tax benefit would have a favorable effect on the effective tax rate in future periods. The Company recognizes interest and penalties related to income tax matters in income tax expense. Interest related to the unrecognized tax benefit has been recognized and included in income tax expense. Interest accrued as of December 27, 2014 is not considered material to the Company's consolidated financial statements.

The Company files U.S. federal income tax returns as well as income tax returns in various states and foreign jurisdictions. The Company is no longer subject to income tax examinations by tax authorities for years prior to 2005 for the majority of tax jurisdictions.

The Company's federal returns are currently under examination by the Internal Revenue Service (IRS) in the United States for the periods 2005 through 2012. To date, there have not been any significant proposed adjustments that have not been accounted for in the Company's consolidated financial statements.

Audit outcomes and the timing of audit settlements are subject to significant uncertainty. It is reasonably possible that within the next twelve months the Company will resolve some or all of the matters presently under consideration for 2005 through 2012 with the IRS and that there could be significant increases or decreases to unrecognized tax benefits.

14. STOCK-BASED COMPENSATION

The Company's 2006 Stock Option Plan ("2006 Plan") provides for the grant of incentive stock options and nonqualified stock options for the purchase of up to an aggregate of 1,125,000 shares of the Company's common stock by officers, employees and directors of the Company. Under the terms of the plan, incentive stock options may be granted to employees at an exercise price per share of not less than the fair value per common share on the date of the grant (not less than 110% of the fair value in the case of holders of more than 10% of the Company's voting stock). Nonqualified stock options may be granted at the discretion of the Company's Board of Directors.

The maximum term of an option may not exceed 10 years, and options become exercisable at such times and in such installments as determined by the Board of Directors. No awards have been granted under the 2006 Plan.

The Company's 2001 Restricted Stock Plan provides for the grant of restricted stock of up to an aggregate of 928,125 shares of the Company's common stock to officers, employees, consultants and directors of the Company. Under the terms of the plan, the minimum period before any shares become nonforfeitable may not be less than six months. The 2001 Restricted Stock Plan expired in 2011 and was replaced in September 2011 with the 2011 Equity Incentive Plan ("2011 Plan"). The 2011 Plan provides for the grant of up to an aggregate of 1,000,000 shares of restricted stock, restricted share units, stock appreciation rights, dividend or dividend equivalent rights, stock awards and other awards valued in whole or in part by reference to or otherwise based on the Company's common stock, to officers, employees and directors of the Company. The 2011 Plan was approved by the Company's shareholders at the 2012 Annual Meeting. At December 27, 2014, 732,062 shares remained available to be issued through the 2011 Plan. Compensation cost is measured at the date of the grant and is recognized in earnings over the period in which the shares vest. Restricted stock expense for the twelve months ended December 27, 2014 and December 28, 2013, totaled $2,961 and $2,234, respectively.

The following table summarizes restricted stock activity for the years ended December 27, 2014, December 28, 2013, and December 29, 2012:

	Number of shares	Weighted average grant-date fair value
Nonvested balance at December 31, 2011	154	$24.25
Granted	89	25.41
Vested	(72)	21.95
Forfeitures	(2)	26.12
Nonvested balance at December 29, 2012	169	$25.81
Granted	90	37.64
Vested	(81)	28.08
Forfeitures	(2)	26.50
Nonvested balance at December 28, 2013	176	$32.13
Granted	103	35.79
Vested	(87)	30.60
Forfeitures	(1)	25.41
Nonvested balance at December 27, 2014	**191**	**$34.81**

The Company had $5,600 of total unrecognized compensation cost related to restricted stock awards granted under the 2011 Plan as of December 27, 2014. That cost is expected to be recognized over a weighted average period of 1.79 years.

The Company maintains an Employee Stock Purchase Plan ("ESPP"), in which most employees are eligible to participate. Employees in the United States who choose to participate are granted an opportunity to purchase common stock at 85 percent of market value on the first or last day of the quarterly purchase period, whichever is lower. Employees in the United Kingdom, under a separate plan, are granted an opportunity to purchase common stock at market value, on the first or last day of the quarterly purchase period, whichever is lower, with the Company issuing one additional free share of common stock for each six shares purchased by the employee under the ESPP. The ESPP authorizes the issuance, and the purchase by employees, of up to 1,096,875 shares of common stock through payroll deductions. No U.S. employee is allowed to buy more than $25 of common stock in any year, based on the market value of the common stock at the beginning of the purchase period, and no U.K. employee is allowed to buy more than the lesser of £1.5 or 10% of his or her annual salary in any year. Employees purchased 25,238 shares at a weighted average price of $33.52, and 34,653 shares at a weighted average price of $24.80, under the ESPP during the twelve months ended December 27, 2014 and December 28, 2013, respectively. The Company recognized $173 and $206 of compensation expense during the twelve months ended December 27, 2014 and December 28, 2013, respectively. At December 27, 2014, 653,393 shares remained available to be issued through the ESPP and the U.K. plan.

The Nonemployee Director Equity and Deferred Compensation Plan (the "Plan") originally was adopted by the Board of Directors and approved by the shareholders in 2004, and amended in 2008. Under the Plan, Directors who were not officers of the Company were paid 375 shares of Company common stock and $3 in cash fees for attendance at each meeting of the Board of Directors, as well as each meeting of each Board Committee on which they served when the committee meeting was not held within one day of a meeting of the Board of Directors. Committee Chairmen received additional fees equal to 25% of normal compensation and the Chairman of the Board was paid twice the amount of normal compensation, with such additional compensation payable in Company common stock. Prior to June 7, 2011, Directors were able to elect under the Plan to receive all or part of their cash fees in Company stock and to defer receipt of their fees until a subsequent year. When so deferred, the shares of stock were converted to deferred stock units. Deferred stock units are treated as liabilities. At December 27, 2014, there were zero deferred stock units outstanding. The Plan has now been terminated, and no further issuance of shares will be made under the Plan.

In March 2012, the Board reviewed its non-employee director compensation policy and determined that compensating Directors solely in Company stock would further align the interests of the Board and the shareholders. Accordingly, the Board of Directors adopted the Sun Hydraulics Corporation 2012 Nonemployee Director Fees Plan (the "2012 Directors Plan"), which was approved by the shareholders of the Company at its 2012 annual meeting.

Under the 2012 Directors Plan, as compensation for attendance at each Board meeting and each meeting of each committee of the Board on which he or she serves when the committee meeting is not held within one day of a meeting of the Board, each Nonemployee Director will be paid 500 shares of Common Stock. The Chairman's fee is twice that of a regular director, and the fee for the chairs of each Board Committee is 125% that of a regular director. The Board has the authority to change from time to time, in any manner it deems desirable or appropriate, the share compensation to be awarded to all or any one or more Nonemployee Directors, provided that, with limited exceptions, such changes are subject to prior shareholder approval. The aggregate number of shares which may be issued during any single calendar year is limited to 25,000 shares. The 2012 Directors Plan authorizes the issuance of up to 270,000 shares of common stock. At December 27, 2014, 222,749 shares remained available for issuance under the 2012 Directors Plan.

Directors were granted 17,500 and 16,500 shares for the twelve months ended December 27, 2014 and December 28, 2013, respectively. The Company recognized director stock compensation expense of $677 and $592 for the twelve months ended December 27, 2014 and December 28, 2013, respectively.

15. EARNINGS PER SHARE

The following table represents the computation of basic and diluted net income per common share (in thousands, except per share data):

	December 27, 2014	December 28, 2013	December 29, 2012
Net income	**$43,775**	$37,984	$37,398
Basic weighted average number of common shares outstanding	**26,456**	26,206	25,944
Basic net income per common share	**$ 1.65**	$ 1.45	$ 1.44
Effect of dilutive stock options and deferred director stock units	**—**	—	27
Diluted weighted average number of common shares outstanding	**26,456**	26,206	25,971
Diluted net income per common share	**$ 1.65**	$ 1.45	$ 1.44

16. EMPLOYEE BENEFITS

The Company has a defined contribution retirement plan covering substantially all of its eligible United States employees. Employer contributions under the retirement plan amounted to approximately $4,325, $4,066, and $4,309 during 2014, 2013, and 2012, respectively.

The Company provides supplemental pension benefits to its employees of foreign operations in addition to mandatory benefits included in local country payroll tax statutes. These supplemental pension benefits amounted to approximately $415, $327, and $330 during 2014, 2013, and 2012, respectively.

The Company uses an Employee Stock Ownership Plan ("ESOP") as the discretionary match portion of its 401(k) retirement plan. The Company contributes to the ESOP for all eligible United States employees. Under the ESOP, which is 100% company funded, the Company allocates common stock to each participant's account. The allocation is generally a percentage of a participant's compensation as determined by the Board of Directors on an annual basis.

In May 2008, the Board introduced the concept of a shared distribution dividend. The shared distribution dividend rewards the majority of employees through a contribution into their retirement accounts and concurrently rewards shareholders with a special cash dividend. As a result of the shared distribution, the Company contributed 63,647 and 91,158 shares into the ESOP in March 2014 and March 2013, respectively. In 2014, the Company accrued an amount equal to 10.0% of eligible wages in accordance with the shared distribution dividend announced in February 2015.

The Company incurred retirement benefit expense under the ESOP of approximately $3,021, $2,881, and $3,011 during 2014, 2013 and 2012, respectively. These amounts are included in the total employer contributions to the retirement plan noted above.

There are no restrictions on the shares contributed to the ESOP. This allows participants to sell their shares to enable diversification within their individual 401(k) accounts. The Company does not have any repurchase obligations under the ESOP.

During 2008, the Company developed plans for international employees to participate in the shared distributions. The Company's foreign operations recognized total expense of approximately $673, $551, and $633 in 2014, 2013, and 2012, respectively, relating to shared distributions. The Company's U.K. employees received 5,643 and 7,366 shares in March 2014 and March 2013, respectively, into a share incentive plan. In Korea, employees received their shared distribution in the form of cash, which was deposited into a Company retirement plan. In Germany, employees received 4,699 and 7,015 shares in March 2014 and March 2013, respectively. The remainder was paid in cash.

Due to tax provisions in some foreign jurisdictions which make stock awards difficult, the Company sometimes awards deferred cash bonuses to key employees of its foreign operations. The deferred cash bonuses are similar to phantom stock units, in that such bonuses are tied to the value of the Company's common stock. Awards are recognized over the deferral period as variable plan awards. The Company recognized approximately $35, $70 and $44 of compensation expense in 2014, 2013 and 2012, respectively, related to the awards.

17. ACCUMULATED OTHER COMPREHENSIVE INCOME

Changes in Accumulated Other Comprehensive Income by Component Twelve Months Ended December 27, 2014

	Unrealized Gains and Losses on Available-for-Sale Securities	Foreign Currency Items	Total
Balance at December 28, 2013	$(188)	$ 2,779	$ 2,591
Other comprehensive income (loss) before reclassifications	(556)	(6,005)	(6,561)
Amounts reclassified from accumulated other comprehensive income	(115)	—	(115)
Net current period other comprehensive income (loss)	(671)	(6,005)	(6,676)
Balance at December 27, 2014	**$(859)**	**$(3,226)**	**$(4,085)**

Reclassifications Out of Accumulated Other Comprehensive Income

Details about Accumulated Other Comprehensive Income Components	**Twelve months ended December 27, 2014**	Affected Line Item in the Consolidated Statements of Operations
Unrealized gains and losses on available-for-sale securities		
Realized gain/(loss) on sale of securities	**$182**	Miscellaneous (income) expense, net
	182	Total before tax
	(67)	Tax benefit
	$115	Net of tax
Total reclassifications for the period	**$115**	

18. SEGMENT REPORTING

The individual subsidiaries comprising the Company operate predominantly in a single industry as manufacturers and distributors of hydraulic components. Given the similar nature of products offered for sale, the type of customers, the methods of distribution and how the Company is managed, the Company determined that it has only one operating and reporting segment for both internal and external reporting purposes.

Geographic Region Information:

Net sales are measured based on the geographic destination of sales. Total and long-lived assets are shown based on the physical location of the assets. Long-lived assets primarily include net property, plant and equipment:

	2014	2013	2012
Net sales			
Americas	**$112,515**	$101,690	$104,987
Europe	**69,241**	61,246	59,818
Asia/Pacific	**45,917**	42,331	39,562
Total	**$227,673**	$205,267	$204,367
Total assets			
Americas	**$145,816**	$138,828	$110,392
Europe	**59,439**	58,388	50,054
Asia/Pacific	**17,509**	16,262	14,675
Total	**$222,764**	$213,478	$175,121
Long-lived assets			
Americas	**$ 73,315**	$ 70,479	$ 60,240
Europe	**9,233**	9,745	8,085
Asia/Pacific	**4,669**	4,198	4,351
Total	**$ 87,217**	$ 84,422	$ 72,676

19. COMMITMENTS AND CONTINGENCIES

The Company is not a party to any legal proceedings other than routine litigation incidental to its business. In the opinion of management, the amount of ultimate liability with respect to these actions will not materially affect the results of operations, financial position or cash flows of the Company.

OPERATING LEASES—The Company leases manufacturing facilities, production support facilities and office space in various locations around the world. Total rental expense for the years ended 2014, 2013 and 2012 was approximately $137, $265 and $297, respectively. The following table summarizes our minimum lease payments in excess of one year as of December 27, 2014.

Future minimum lease payments on operating leases are as follows:

2015	$ 470
2016	384
2017	319
2018	20
2019	21
Thereafter	51
Total minimum lease payments	$1,265

INSURANCE—The Company accrues for health care benefit costs under a self-funded plan. The Company purchases re-insurance for both specific and aggregate stop losses on claims that exceed $155 on an individual basis and approximately $7,200 on an aggregate basis. The Company records a liability for all unresolved claims at the anticipated cost to the Company at the end of the period based on management's assessment. The Company believes it has adequate reserves for all self-insurance claims.

20. UNAUDITED QUARTERLY FINANCIAL INFORMATION

Quarterly Results of Operations

For the quarter ended	**Dec. 27, 2014**	Sep. 27, 2014	Jun. 28, 2014	Mar. 29, 2014
(in thousands, except per share data)				
Net sales	**$54,803**	$55,011	$61,050	$56,809
Gross profit	**21,778**	22,291	25,756	24,067
Operating income	**14,333**	14,635	18,377	16,726
Income before income taxes	**15,370**	15,001	18,424	16,947
Net income	**$10,327**	$ 9,877	$12,186	$11,385
Basic net income per common share	**$ 0.39**	$ 0.37	$ 0.46	$ 0.43
Diluted net income per common share	**$ 0.39**	$ 0.37	$ 0.46	$ 0.43

For the quarter ended	Dec. 28, 2013	Sep. 28, 2013	Jun. 29, 2013	Mar. 30, 2013
Net sales	$49,050	$49,369	$55,788	$51,060
Gross profit	19,442	19,614	23,401	20,504
Operating income	12,403	13,074	16,761	13,932
Income before income taxes	12,707	12,794	17,516	14,154
Net income	$ 8,343	$ 8,275	$11,790	$ 9,575
Basic net income per common share	$ 0.32	$ 0.32	$ 0.45	$ 0.37
Diluted net income per common share	$ 0.32	$ 0.32	$ 0.45	$ 0.37

21. NEW ACCOUNTING PRONOUNCEMENTS

In August 2014, the FASB issued guidance on Disclosure of Uncertainties About an Entity's Ability to Continue as a Going Concern. The guidance requires management to perform interim and annual assessments of an entity's ability to continue as a going concern within one year of the date the financial statements are issued and provides guidance on determining when and how to disclose going concern uncertainties in the financial statements. Certain disclosures will be required if conditions give rise to substantial doubt about an entity's ability to continue as a going concern. The guidance applies to all entities and is effective for annual and interim reporting periods ending after December 15, 2016, with early adoption permitted. The Company does not expect that the adoption of this guidance to have a material impact on the Company's consolidated financial statements.

In May 2014, the FASB issued guidance on Revenue from Contracts with Customers, to clarify the principles used to recognize revenue for all entities. The core principle of the new guidance is that an entity will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard provides a five-step analysis of transactions to determine when and how revenue is recognized. Additionally, the guidance requires disaggregated disclosures related to the nature, amount, timing, and uncertainty of revenue that is recognized. The guidance is effective for annual and interim periods beginning after December 15, 2016. Early adoption is not permitted. The Company is currently evaluating the effects, if any, adoption of this guidance will have on the Company's consolidated financial statements.

In April 2014, the FASB issued guidance on Reporting Discontinued Operations and Disposals of Components of an Entity, which changes the criteria for determining which disposals can be presented as discontinued operations and modifies related disclosure requirements. The guidance is effective for annual and interim periods beginning after December 15, 2014, with early adoption permitted. This guidance did not have a material impact on the Company's consolidated financial statements.

22. SUBSEQUENT EVENTS

Subsequent to year end, the Company's Korean facility qualified as being held for sale. Sun Korea and Seungwon consolidated their operations into one leased facility. The new facility provides increased space for growth and production efficiencies. The carrying amount of the assets held for sale were $335 at December 27, 2014. The Company has received a letter of intent from a prospective buyer, and anticipates that a sale will be completed within the first half of 2015. The Company expects to recognize a gain on this sale in the period in which it is completed.

CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Company's management, with the participation of the Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of the Company's "disclosure controls and procedures" (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report, have concluded that our disclosure controls and procedures are effective and are designed to ensure that the information we are required to disclose is recorded, processed, summarized and reported within the necessary time periods. Our disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in reports that we file or submit pursuant to the Securities Exchange Act of 1934, as amended, is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Management's Report on Internal Control over Financial Reporting

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Internal control over financial reporting includes those policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;
- provide reasonable assurance that transactions are recorded, as necessary, to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Management, with the participation of the Chief Executive Officer and Chief Financial Officer, conducted an evaluation of the effectiveness of the Company's internal control over financial reporting based on the criteria set forth in *Internal Control—Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation under the *Internal Control—Integrated Framework,* management, with the participation of the Chief Executive Officer and Chief Financial Officer, concluded that the internal control over financial reporting was effective as of December 27, 2014.

Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting during the quarter ended December 27, 2014, that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We have issued our report dated February 24, 2015, accompanying the consolidated financial statements included in the Annual Report of Sun Hydraulics Corporation on Form 10-K for the years ended December 27, 2014, December 28, 2013, and December 29, 2012. We hereby consent to the incorporation by reference of said report in the Registration Statements of Sun Hydraulics Corporation of Forms S-8 (File No. 333-30801, effective July 3, 1997, File No. 333-83269, effective July 20, 1999, File No. 333-62816, effective June 12, 2001, File No. 333-66008 effective, July 27, 2001, File No. 333-119367, effective September 29, 2004, File No. 333-124174, effective April 19, 2005, File No. 333-158245, effective March 27, 2009, File No. 333-177448, effective October 21, 2011, and File No. 333-184840, effective November 9, 2012).

Mayer Hoffman McCann P.C.

February 24, 2015
Clearwater, Florida

SHAREHOLDER INFORMATION

Corporate Officers

Allen J. Carlson
President, CEO

Tricia L. Fulton
Chief Financial Officer

Mark B. Bokorney
Officer

Steven Hancox
Officer

Tim A. Twitty
Officer

Directors

Marc Bertoneche, PhD
Professor, Business Administration
University of Bordeaux

Allen J. Carlson
President, CEO
Sun Hydraulics Corporation

Wolfgang H. Dangel
Consultant, Schaeffler Holding Company

John S. Kahler
President, CEO *retired*
Cincinnati Incorporated

Christine L. Koski
President, CEO
nMetric LLC

Philippe Lemaitre
Chairman of the Board
Sun Hydraulics Corporation
Chairman, President, CEO *retired*
Woodhead Industries, Inc.

Alexander Schuetz
CEO
Knauf Engineering GmbH

David N. Wormley, PhD
Dean, Engineering School *retired*
Pennsylvania State University

Legal Counsel

Shumaker, Loop & Kendrick, LLP
Tampa, Florida

Auditors

Mayer Hoffman McCann P.C.
Clearwater, Florida

Corporate Headquarters

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Investor Relations

If you wish to be placed on Sun Hydraulics' email list for periodic news and financial releases, please send your request to investor@sunhydraulics.com or visit Sun's website to sign up.

The Company's Annual Reports, Forms 10-K, 10-Q, 3, 4, 5, and press releases are available at the Investor Relations section of Sun's website, www.sunhydraulics.com, or by request from corporate headquarters.

If you would like a hard copy of Form 10-K, a copy will be provided without charge upon request to:

Investor Relations
Sun Hydraulics Corporation
1500 West University Parkway
Sarasota, FL 34243

Transfer Agent

Computershare
Campton, Massachusetts

Common Stock Information

The Common Stock of Sun Hydraulics Corporation is traded on the NASDAQ Global Select Market under the symbol SNHY.

As of April 6, 2015, there were 175 shareholders of record. The number of record holders was determined from the records of the Company's transfer agent and does not include beneficial owners of common stock whose shares are held in the name of various securities brokers, dealers and registered clearing agencies. The Company believes that there are approximately 13,000 beneficial owners of common stock.

As of April 6, 2015, the closing price per share of SNHY stock was $41.19 and there were 26,686,293 shares outstanding.

Shareholders Annual Meeting

The annual meeting of shareholders will be held at 10:00 AM Eastern Time on Monday, June 1, 2015, at:

Sun Hydraulics Corporation
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