

THE FPDA MOTION & CONTROL NETWORK

Fluid Power Survey Results August 2014



CLEVELAND
RESEARCH COMPANY

Highlights



Background:

- The July survey had 40 respondents comprised of 31 distributors and 9 manufacturing firms.

Summary Thoughts:

- Sales in our fluid power survey grew 7% in the July accelerating from 6% growth in June as underlying demand continues to improve driven by strong oil & gas activity. The 2014 outlook of 5-6% implies growth of 7-8% in the remaining 5 months of the year which appears reasonable given improved sales, order and backlog growth rates but we expect weakening ag markets to limit additional upside to the calendar 2014 outlook.

Highlights:

- The July FPDA Index produced a reading of 64.9 (best reading since May-2012) up meaningfully from June's reading of 59.0. The broader ISM improved to 57.1, better than the 55.3 reading in June.
- Our fluid power survey indicates sales improved in July growing 7%, up from 6% growth in June as sales exceeded expectations for the first time since May-2012.
- 2014 outlook remained unchanged with sources forecasting 5-6% growth in 2014 implying 7-8% in the remaining 5 months after ~4% growth YTD. Further upside to the outlook is likely limited by weakening ag markets.

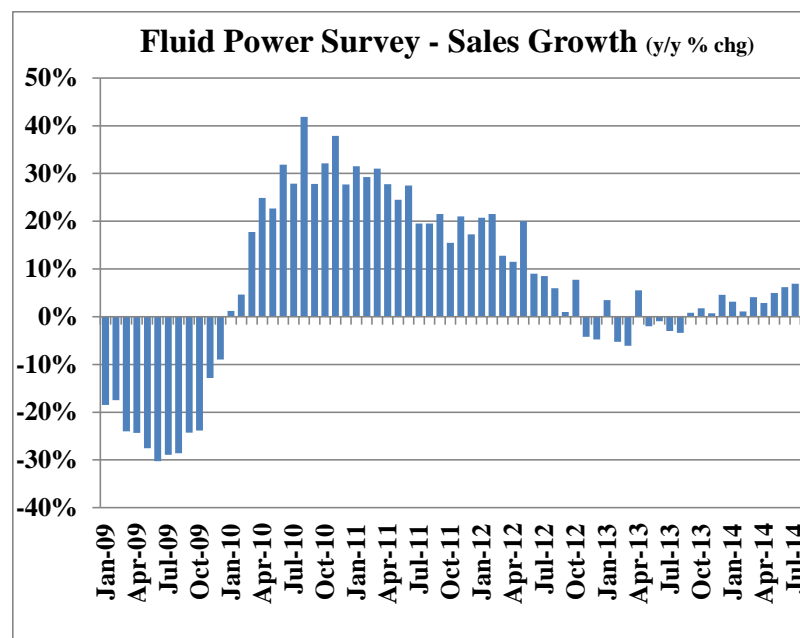
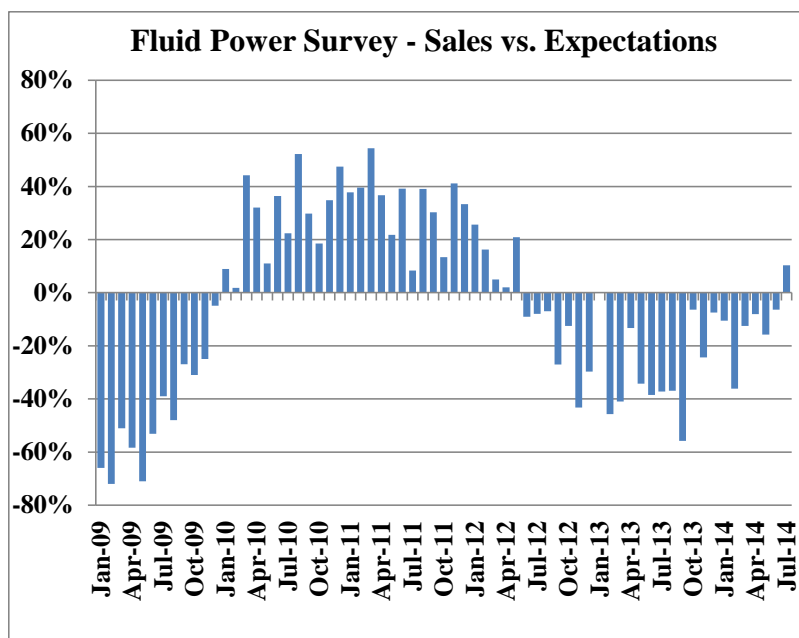
July FPDA Index

- The July FPDA Index produced a reading of 64.9 (best reading since May-2012) up meaningfully from June's reading of 59.0. The broader ISM improved to 57.1 better than the 55.3 reading in June.
- The FPDA Index is similar in construction to the widely followed ISM Purchasing Manager's Index. These are both seasonally adjusted diffusion indexes which measure the month-to-month change in each of the categories listed below. A reading of 50 indicates no change and the further above or below 50 indicates a faster or slower rate of change.

Fluid Power Index																					
Index	Feb-13	Mar-13	Apr-13	May-13	Jun-13	Jul-13	Aug-13	Sep-13	Oct-13	Nov-13	Dec-13	Jan-14	Feb-14	Mar-14	Apr-14	May-14	Jun-14	Jul-14	Direction	Rate of Change	Trend (months)
Sales	38.9	68.1	66.6	43.1	35.5	55.0	60.9	38.2	77.3	33.0	59.6	70.8	56.4	57.8	63.9	48.5	59.4	72.2	Growing	Faster	2
Prices	58.6	52.6	54.9	52.4	54.6	66.1	57.2	58.2	61.6	65.9	63.9	79.8	60.4	57.6	55.7	57.3	58.4	60.6	Growing	Faster	50
Orders	32.0	47.9	71.4	37.9	34.2	57.9	56.1	44.1	71.3	37.0	55.0	77.7	50.6	59.4	56.0	54.0	56.3	71.6	Growing	Faster	8
Backlog	61.3	37.9	48.4	47.1	38.5	44.9	41.1	41.3	52.2	47.2	53.0	67.6	65.7	59.5	61.1	59.5	54.0	63.9	Growing	Faster	8
Outlook	51.6	43.3	46.7	62.1	38.5	43.8	47.7	42.7	52.2	50.0	62.9	63.5	56.6	57.5	52.8	50.0	55.0	58.5	Growing	Faster	10
Inventory	50.0	53.1	45.0	40.9	46.2	45.1	47.7	51.2	55.3	39.2	48.6	55.1	55.4	60.0	65.3	58.6	56.5	58.8	Growing	Faster	7
Supplier Deliveries	58.3	47.5	51.7	46.8	54.0	53.5	55.5	57.7	58.7	58.7	62.2	51.9	55.9	53.7	52.6	65.9	62.2	59.4	Growing	Slower	14
Employment	55.3	53.3	49.2	51.1	42.5	49.9	53.2	53.5	55.1	54.8	55.3	61.7	60.5	56.7	57.6	56.5	60.9	62.5	Growing	Faster	12
Accounts Receivable	40.3	46.7	46.6	50.0	41.0	45.0	43.0	46.5	45.5	47.2	45.6	39.7	46.1	47.5	40.5	47.2	45.2	45.6	Slowing	Faster	14
Overall FPDA Index	46.9	54.0	56.8	44.0	42.5	52.3	54.7	49.0	63.6	44.5	56.1	63.5	55.8	57.5	59.1	56.7	59.0	64.9	Growing	Faster	7
Memo: ISM PMI Index	54.2	54.2	50.7	49.0	50.9	55.4	55.7	56.2	56.4	57.3	57.0	51.3	53.2	53.7	54.9	55.4	55.3	57.1	Growing	Faster	14

July Sales Accelerate as Oil & Gas Activity Remains Strong

Sales in our July fluid power survey grew 7%, accelerating from the 6% growth in June led by still strong oil & gas activity. Notably, sales exceeded expectations for the first time since May 2012 with a net 10% of participants reporting sales beat expectations up from the net 6% who reported sales below expectations in June. In addition to strong oil & gas activity sources report construction activity improved in July.



Monthly Sales Growth – July 2014

Total						
	2009	2010	2011	2012	2013	2014
January	-19%	1%	32%	21%	4%	3%
February	-18%	5%	29%	22%	-5%	1%
March	-24%	18%	31%	13%	-6%	4%
April	-24%	25%	28%	12%	6%	3%
May	-28%	23%	25%	20%	-2%	5%
June	-30%	32%	28%	9%	-1%	6%
July	-29%	28%	20%	9%	-3%	7%
August	-29%	42%	20%	6%	-3%	
September	-24%	28%	22%	1%	1%	
October	-24%	32%	17%	8%	2%	
November	-13%	38%	21%	-4%	1%	
December	-9%	28%	17%	-5%	5%	

Distributors						
	2009	2010	2011	2012	2013	2014
January	-16%	-6%	28%	26%	1%	3%
February	-17%	-2%	28%	24%	-6%	3%
March	-22%	12%	33%	16%	-5%	5%
April	-22%	17%	27%	10%	6%	1%
May	-27%	18%	31%	21%	-3%	4%
June	-29%	25%	27%	10%	-1%	7%
July	-29%	23%	23%	13%	-2%	8%
August	-28%	38%	25%	6%	-5%	
September	-24%	22%	29%	5%	1%	
October	-25%	22%	20%	13%	1%	
November	-14%	31%	28%	2%	2%	
December	-14%	21%	24%	4%	4%	

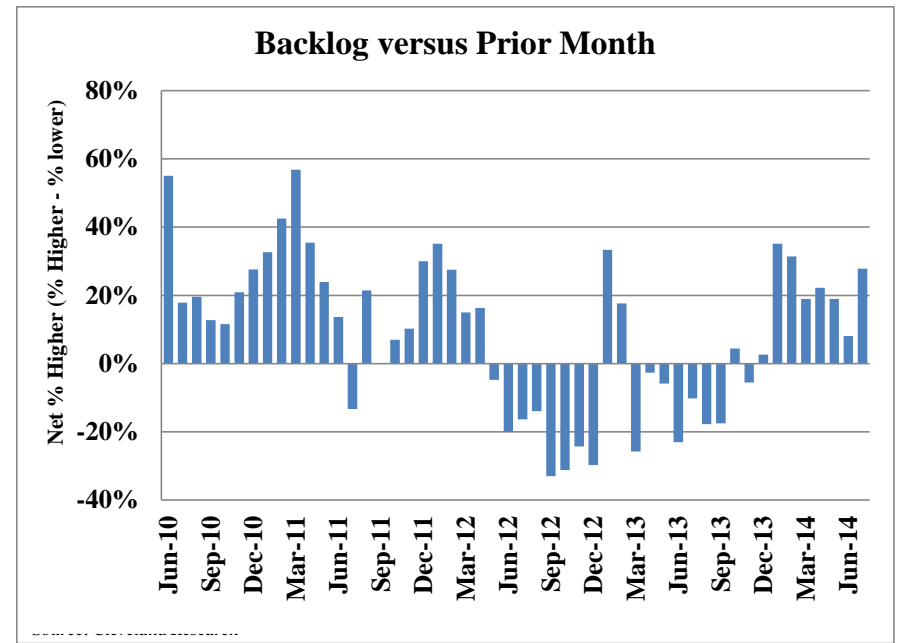
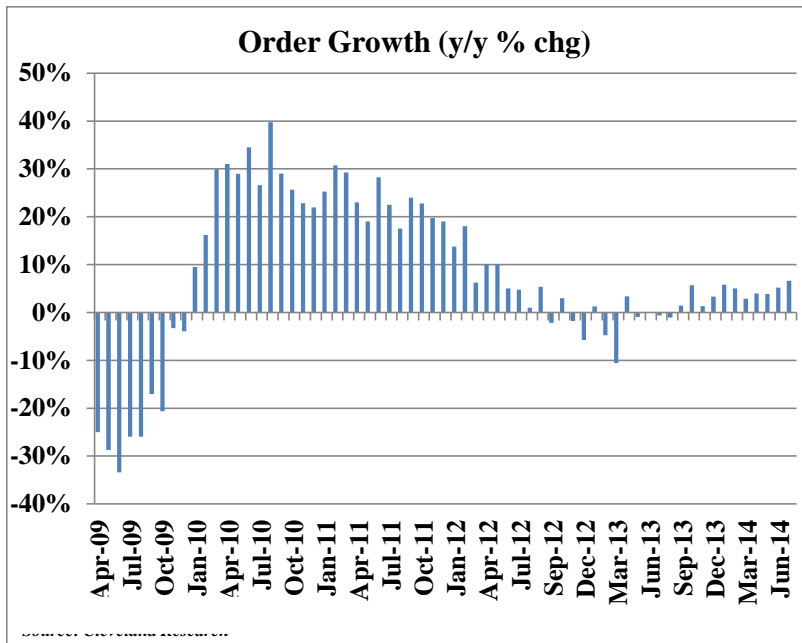
Manufacturers						
	2009	2010	2011	2012	2013	2014
January	-21%	9%	35%	17%	7%	3%
February	-18%	11%	31%	19%	-5%	-1%
March	-26%	24%	30%	10%	-7%	3%
April	-27%	32%	29%	13%	5%	4%
May	-28%	28%	18%	19%	-1%	6%
June	-32%	39%	28%	8%	0%	6%
July	-29%	33%	17%	5%	-4%	6%
August	-29%	46%	14%	6%	-2%	
September	-24%	34%	14%	-3%	1%	
October	-22%	42%	14%	3%	2%	
November	-12%	44%	15%	-10%	-1%	
December	-4%	28%	5%	-8%	5%	

Percent Positive / Negative Growth															
	<u>May-13</u>	<u>Jun-13</u>	<u>Jul-13</u>	<u>Aug-13</u>	<u>Sep-13</u>	<u>Oct-13</u>	<u>Nov-13</u>	<u>Dec-13</u>	<u>Jan-14</u>	<u>Feb-14</u>	<u>Mar-14</u>	<u>Apr-14</u>	<u>May-14</u>	<u>Jun-14</u>	<u>Jul-14</u>
Positive Sales Growth	35%	42%	42%	43%	34%	47%	47%	54%	69%	59%	62%	59%	53%	67%	76%
Flat Sales	15%	11%	12%	11%	10%	19%	12%	16%	11%	14%	18%	16%	18%	14%	7%
Negative Sales Growth	50%	47%	46%	46%	56%	34%	41%	30%	20%	27%	21%	24%	29%	19%	17%
Net % (Positive - Negative)	-15%	-5%	-4%	-2%	-22%	13%	6%	24%	49%	32%	41%	35%	24%	48%	59%

Results vs. Expectations															
	<u>May-13</u>	<u>Jun-13</u>	<u>Jul-13</u>	<u>Aug-13</u>	<u>Sep-13</u>	<u>Oct-13</u>	<u>Nov-13</u>	<u>Dec-13</u>	<u>Jan-14</u>	<u>Feb-14</u>	<u>Mar-14</u>	<u>Apr-14</u>	<u>May-14</u>	<u>Jun-14</u>	<u>Jul-14</u>
Better than expected	11%	13%	12%	9%	12%	28%	11%	25%	18%	11%	25%	19%	21%	21%	38%
In line with expectations	45%	36%	39%	46%	21%	38%	54%	43%	53%	42%	38%	54%	42%	52%	34%
Worse than expected	45%	51%	49%	46%	67%	34%	35%	33%	29%	47%	38%	27%	37%	27%	28%
Net % (Better - Worse)	-34%	-38%	-37%	-37%	-56%	-6%	-24%	-8%	-11%	-36%	-13%	-8%	-16%	-6%	10%

Orders and Backlog Continue to Trend Positively

July orders were up 7%, better than the 5% last month while backlogs grew 5%, up from 3% in June.



Order and Backlog Growth Trends

Total						
	2009	2010	2011	2012	2013	2014
January		9%	25%	14%	1%	6%
February		16%	31%	18%	-5%	5%
March		30%	29%	6%	-11%	3%
April	-25%	31%	23%	10%	3%	4%
May	-29%	29%	19%	10%	-1%	4%
June	-33%	34%	28%	5%	0%	5%
July	-26%	27%	23%	5%	-1%	7%
August	-26%	40%	18%	5%	-1%	
September	-17%	29%	24%	-2%	1%	
October	-21%	26%	25%	3%	4%	
November	-3%	23%	20%	-2%	1%	
December	-4%	18%	18%	-6%	3%	

Distributors						
	2009	2010	2011	2012	2013	2014
January		1%	25%	13%	3%	6%
February		12%	31%	19%	-7%	4%
March		29%	30%	10%	-6%	4%
April	-25%	30%	29%	8%	5%	3%
May	-27%	28%	27%	5%	-2%	5%
June	-30%	28%	33%	1%	-2%	7%
July	-28%	20%	25%	8%	1%	9%
August	-26%	34%	29%	6%	-1%	
September	-20%	29%	30%	1%	3%	
October	-21%	25%	25%	-4%	4%	
November	-2%	28%	21%	-1%	-1%	
December	-10%	27%	21%	5%	5%	

Manufacturers						
	2009	2010	2011	2012	2013	2014
January		18%	25%	15%	-1%	5%
February		21%	31%	17%	-3%	6%
March		31%	29%	3%	-15%	2%
April	-25%	32%	18%	12%	2%	5%
May	-31%	30%	12%	15%	0%	3%
June	-37%	41%	24%	10%	2%	3%
July	-24%	34%	20%	2%	-2%	5%
August	-26%	46%	7%	5%	-1%	
September	-14%	29%	19%	-5%	0%	
October	-20%	26%	23%	10%	4%	
November	-4%	17%	19%	-3%	4%	
December	3%	17%	1%	-11%	1%	

Total						
	2009	2010	2011	2012	2013	2014
January			25%	22%	1%	1%
February			32%	18%	-2%	3%
March			40%	15%	-5%	2%
April			31%	16%	-6%	4%
May			25%	10%	-2%	3%
June		24%	29%	8%	-7%	3%
July		29%	25%	7%	-4%	5%
August		37%	17%	6%	-3%	
September		37%	24%	4%	-3%	
October		34%	22%	-1%	1%	
November		32%	26%	-3%	0%	
December		25%	19%	-3%	2%	

Distributors						
	2009	2010	2011	2012	2013	2014
January			22%	30%	0%	1%
February			35%	22%	-2%	2%
March			39%	24%	-2%	4%
April			36%	25%	-6%	4%
May			37%	11%	-3%	4%
June		29%	32%	11%	-6%	5%
July		24%	29%	12%	-5%	6%
August		29%	36%	7%	-5%	
September		37%	33%	9%	-6%	
October		24%	26%	-4%	1%	
November		23%	29%	-3%	-2%	
December		20%	27%	2%	2%	

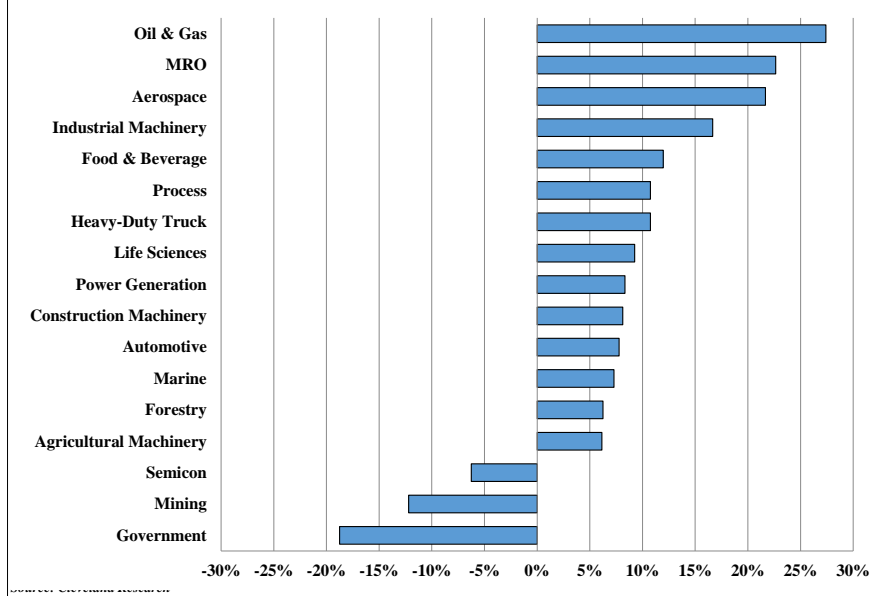
Manufacturers						
	2009	2010	2011	2012	2013	2014
January			28%	13%	1%	1%
February			30%	13%	-1%	3%
March			41%	7%	-8%	1%
April			27%	7%	-6%	3%
May			14%	10%	0%	2%
June		20%	25%	6%	-7%	2%
July		34%	22%	3%	-3%	4%
August		45%	-1%	6%	-1%	
September		37%	16%	-1%	1%	
October		45%	19%	3%	0%	
November		41%	23%	-4%	1%	
December		30%	1%	-6%	1%	

Oil & Gas Activity Remains Strong

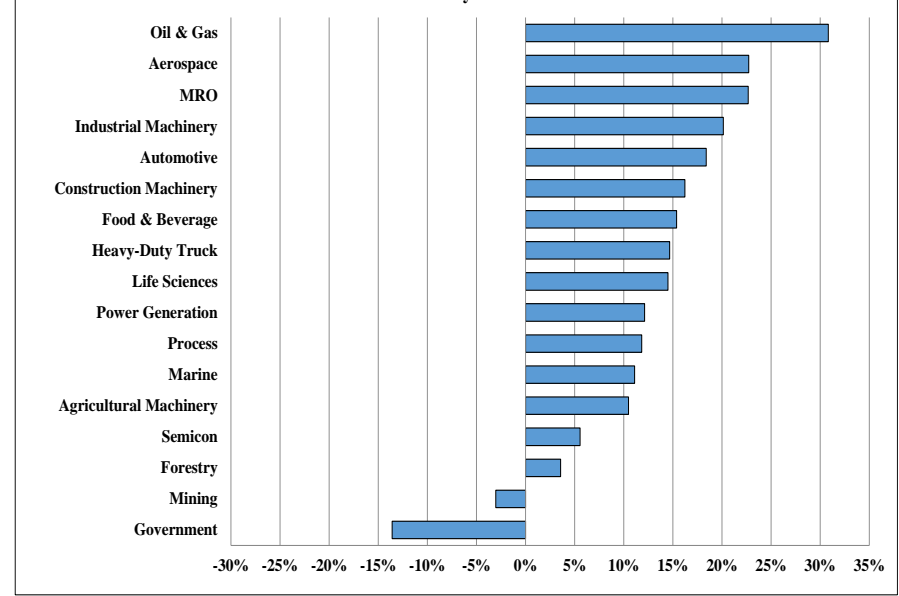
End Market Highlights – Strength Led by Oil & Gas

End market trends improved in July as 15 out of 17 end markets ranked in positive territory up from 14 in June as all end markets with the exception of forestry improved on a sequential basis. Oil & gas remained the strongest reported end market followed by aerospace and MRO while government and mining were the two weakest reported markets. Anecdotally, we are hearing of better activity in metals markets which supports the sequential improvement in July mining trends.

End Market Ranking (Net % Strong - Weak)
June

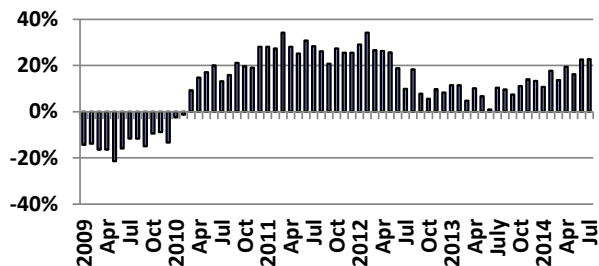


End Market Ranking (Net % Strong - Weak)
July

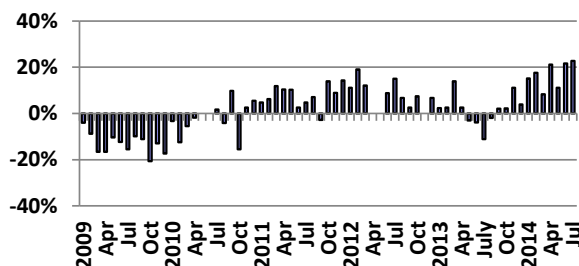


End Market Trends

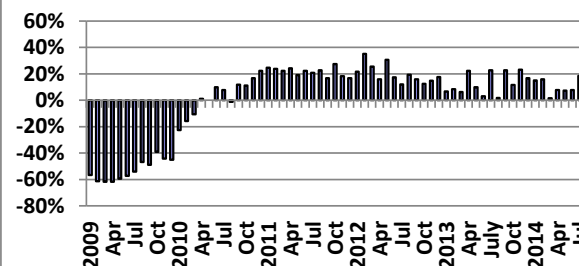
Maintenance, Repair and Operations (MRO)



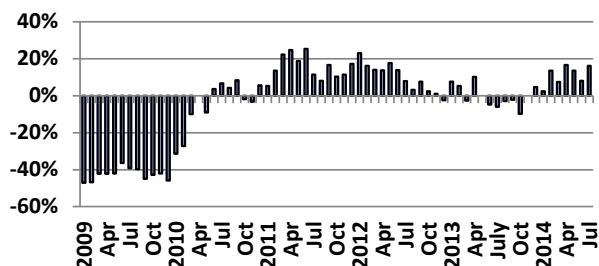
Aerospace



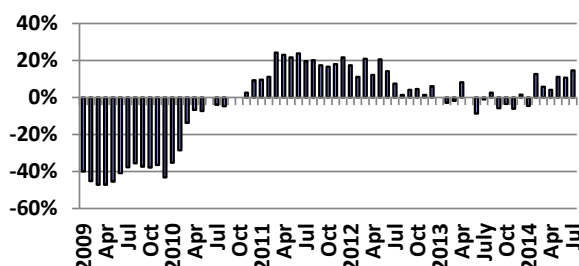
Automotive



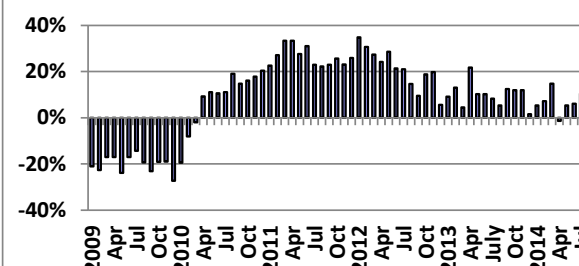
Construction Machinery



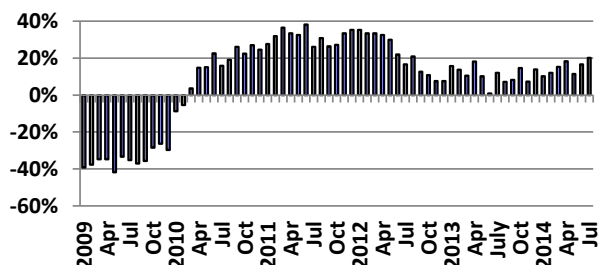
Heavy-Duty Truck



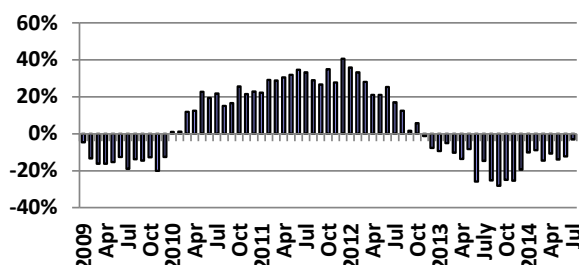
Agricultural Machinery



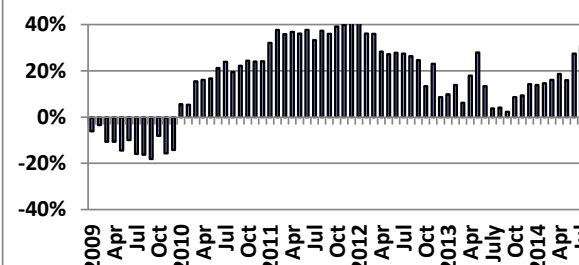
Industrial Machinery



Mining

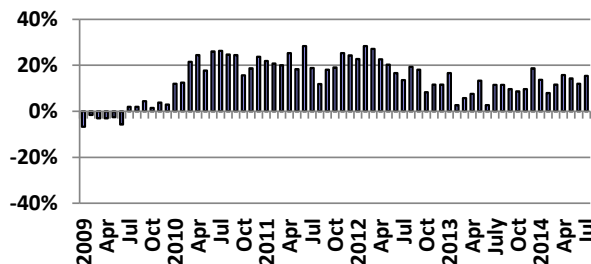


Oil & Gas

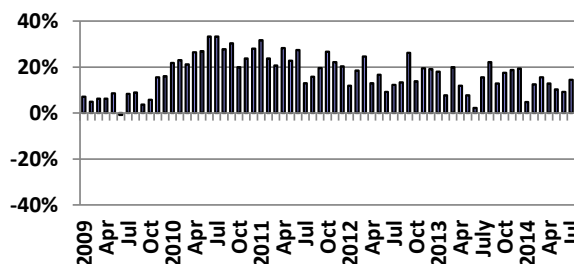


End Market Trends

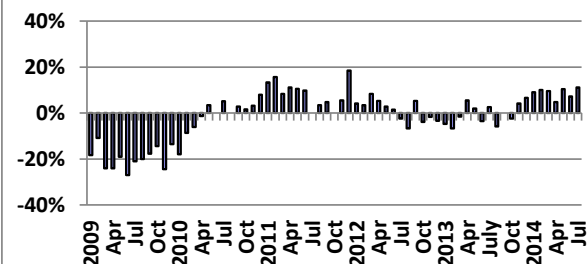
Food & Beverage



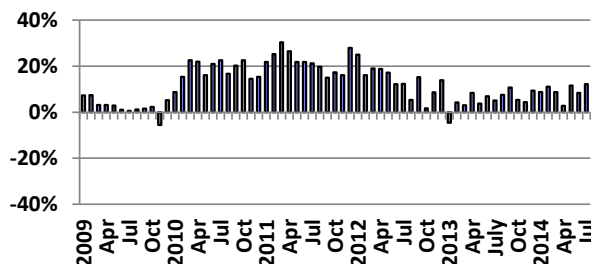
Life Sciences



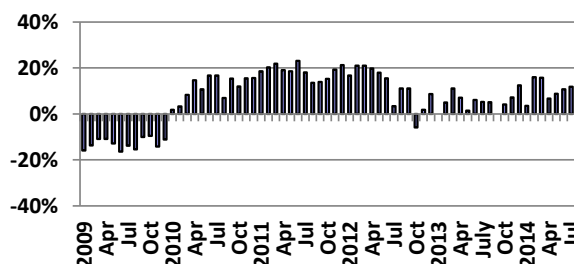
Marine



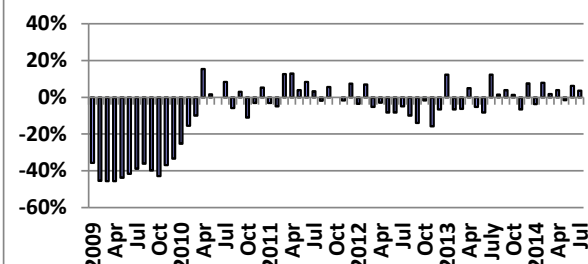
Power Generation



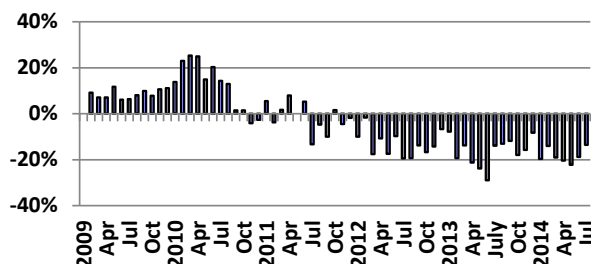
Process



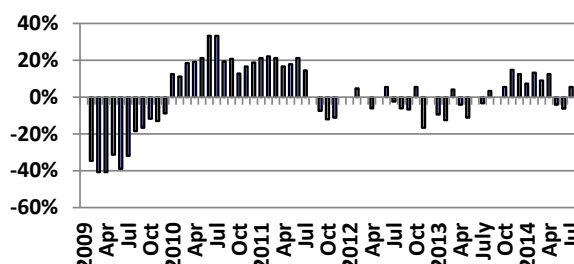
Forestry



Government



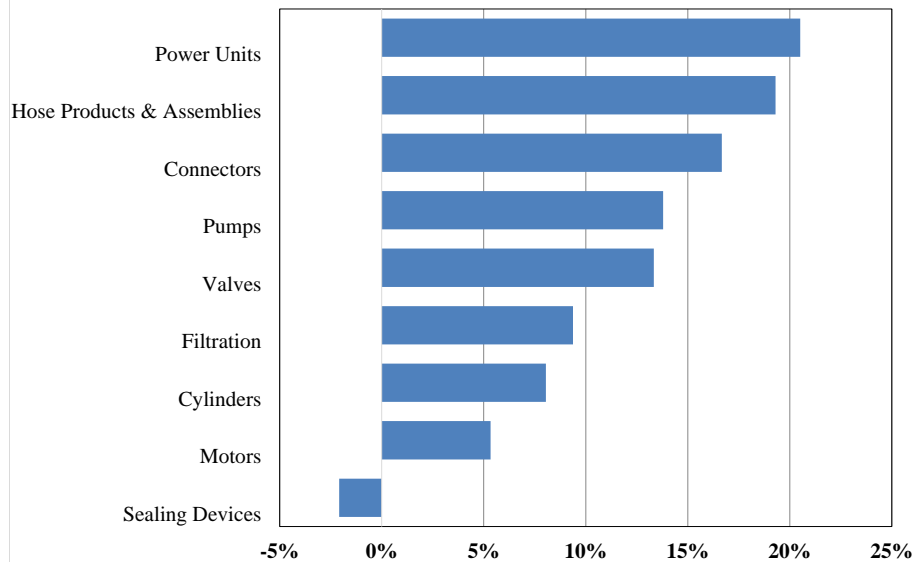
Semicon



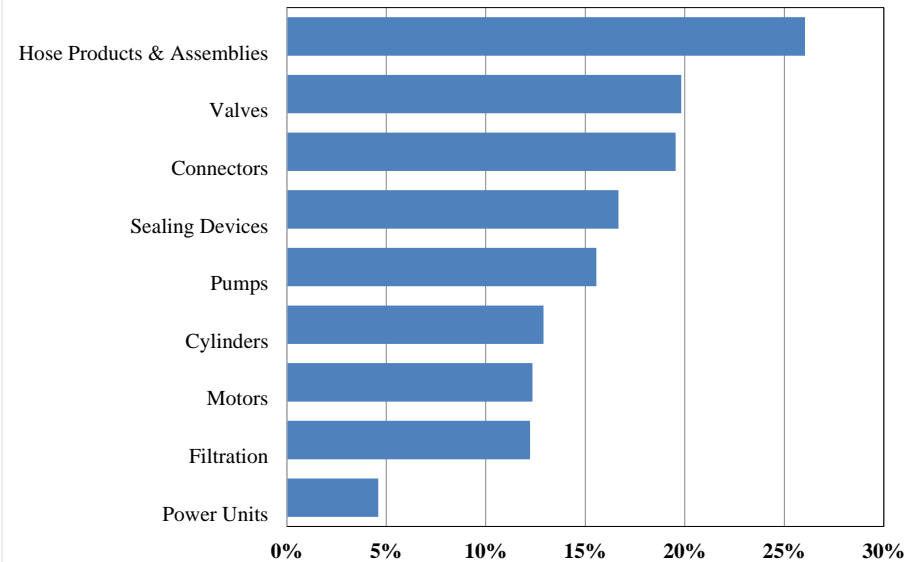
Product Category Ranking

All nine product categories were higher in July, with hose products & assemblies, valves and connectors reported as the strongest product categories while motors, filtration and power units were reported as the relative weakest in the month.

Product Category Ranking (Net % Strong - Weak)
June 2014



Product Category Ranking (Net % Strong - Weak)
July 2014



2014 Outlook

Sources Continue to Forecast 5-6% Growth in 2014, Upside Likely Limited by Deteriorating Ag Markets

Sources in our August fluid power survey continue to forecast 5-6% growth in 2014 implying sales will accelerate to up 7-8% following ~4% growth through the first seven months. Supporting the implied acceleration are strengthening order and backlog trends which both posted the strongest YTD growth in July, up 7% (up 5% in June) and 5% (up 3% in June), respectively as orders from construction accelerated. At this time implied 2H acceleration (largely driven by oil & gas) appears reasonable but upside to the 2014 outlook will likely be muted by the deterioration of ag markets specifically among OEM's.

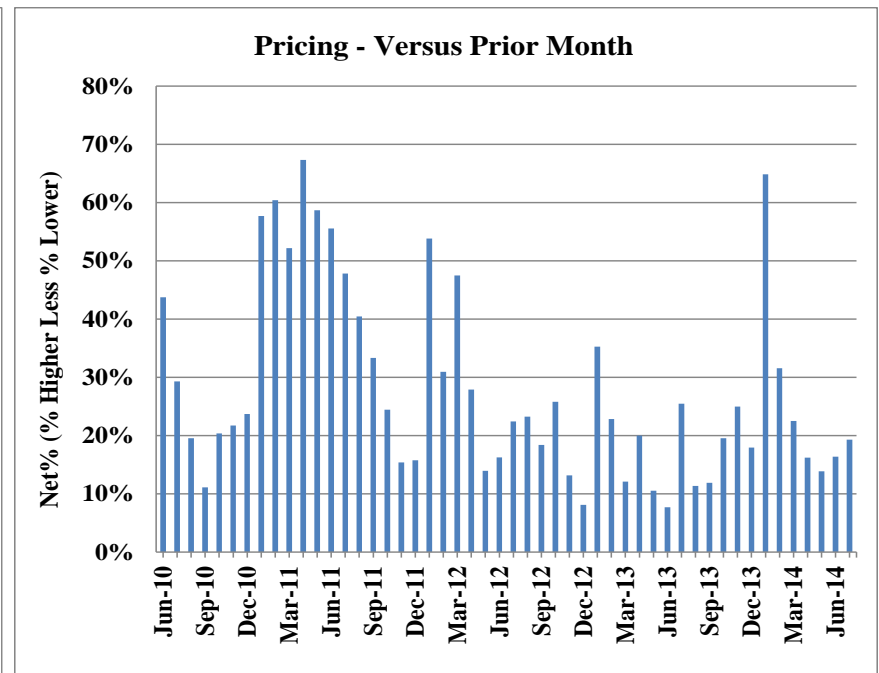
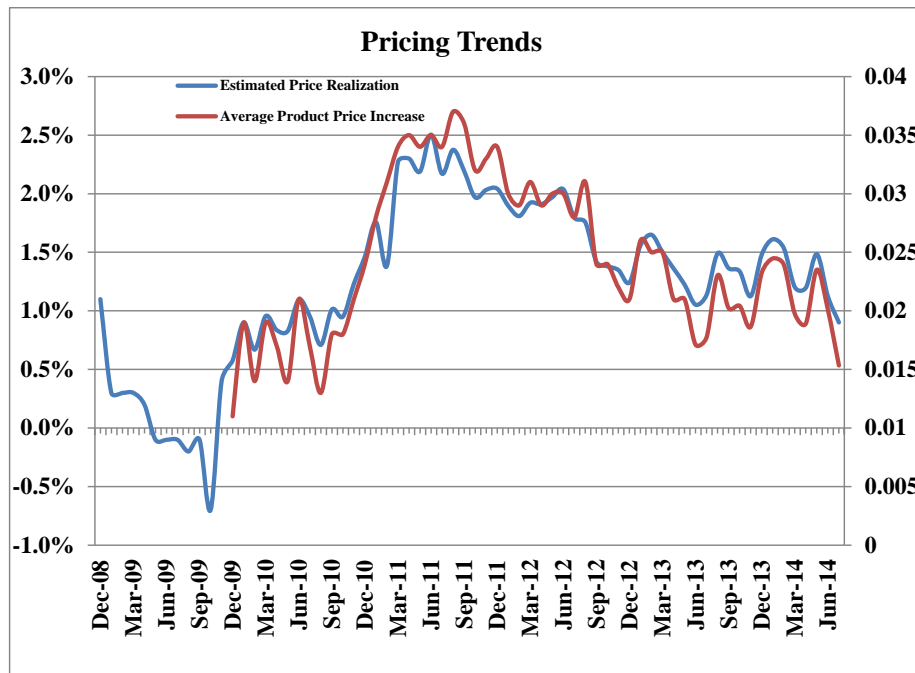
Deteriorating N. America ag markets are primarily driven by lower farmer cash receipts expected in 2014 and meaningful reductions in Section 179/Bonus Depreciation levels which have incentivized a large number of farmers to purchase new equipment each year. Further compounding the issue is the significant amount of used inventory created by the tax incentivized purchasing over the last decade. Due to these headwinds our capital equipment team is forecasting N. America ag equipment revenues to be down ~15% in 2014 and DE recently lowered its 2014(fiscal) Ag & Turf revenue forecast to down 10% (previously down 7%). Additionally, DE announced on 8-15-14 it will be laying off 600 employees at its ag equipment factories in response to current market demand.

Fluid Power Outlook													
	2012	2013	2014 Outlook										
Sales Growth (y/y)	Actual Results	Actual Results	Sept-13	Oct-13	Nov-13	Dec-13	Jan-14	Feb-14	Mar-14	Apr-14	May-14	Jun-14	Jul-14
Overall	8%	0%	3%	4-5%	4-5%	5-6%	5-6%	6%	6%	6%	6%	6%	6%
Distributors	8%	0%	4%	5%	4-5%	6%	7%	6%	6%	6%	6%	6%	6%
Manufacturers	8%	0%	3%	4%	3%	5%	4%	6%	5%	5%	5%	5%	5%

Price Contribution Trends

Price Realization Deteriorates in July

We are hearing average product price increases were 1.5% in July, below the 2.0% in June as price realization also deteriorated to 0.9%, down from 1.1% in June.

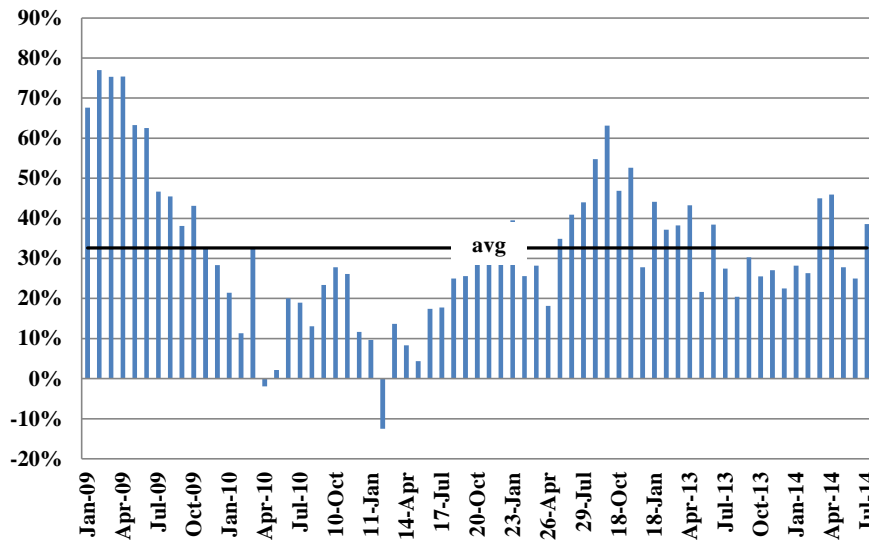


Inventory Trends

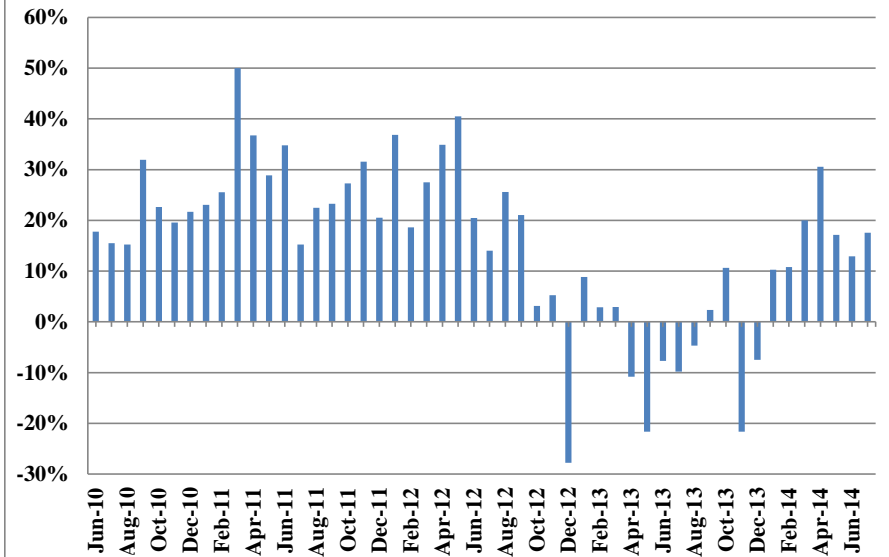
July Inventories Move Up

Inventory levels grew a little in July with a net 18% of sources reporting higher inventories in the month up from 13% last month. At this time distributors appear less comfortable with current levels as a net 39% reported inventories were “too high” jumping up from the 25% in June, and above the long run average of 33%.

Inventory Levels - Net % "Too High"

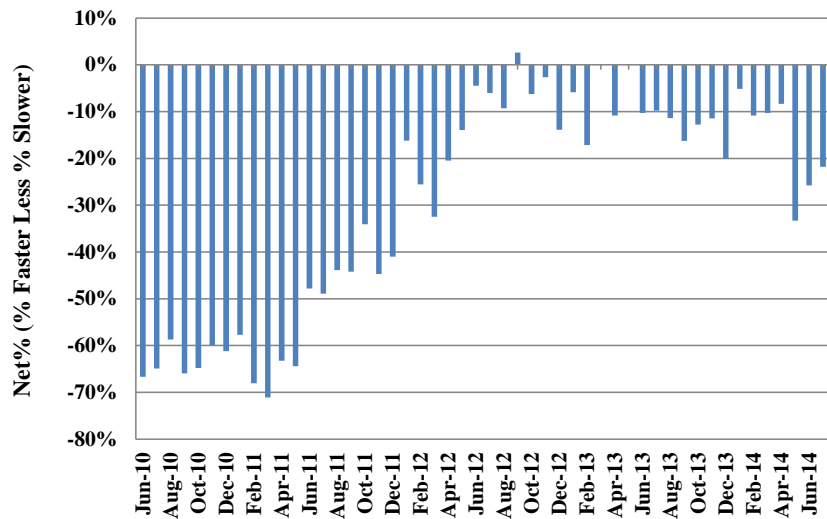


Inventory Levels - Versus Prior Month

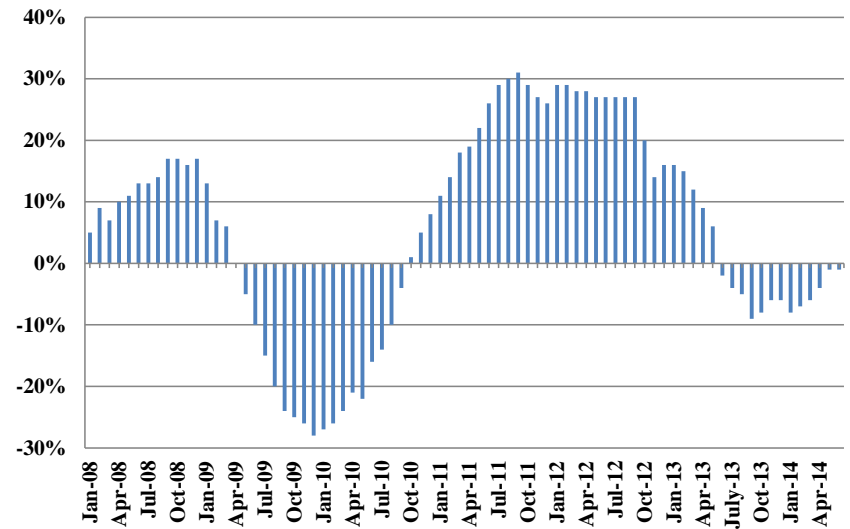


Inventory Levels

Supplier Deliveries - Versus Prior Month



Inventory Levels - Versus Last Year



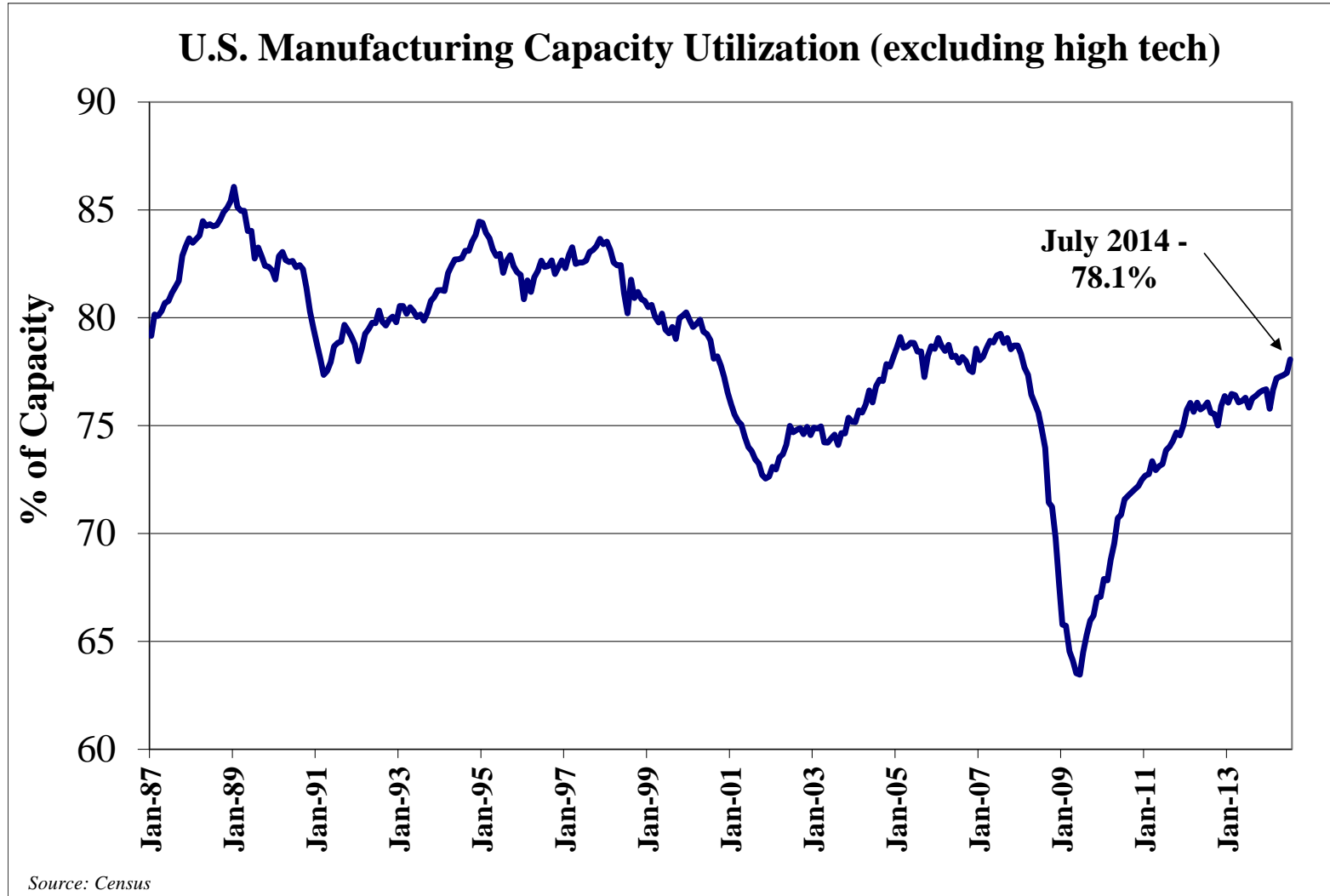
Macroeconomic Indicators

ISM, Industrial Production, Capacity Utilization, Non-Res Construction
Forecasts, Resi Construction Indicators, Commodity Prices, Heavy Truck &
Automotive Data

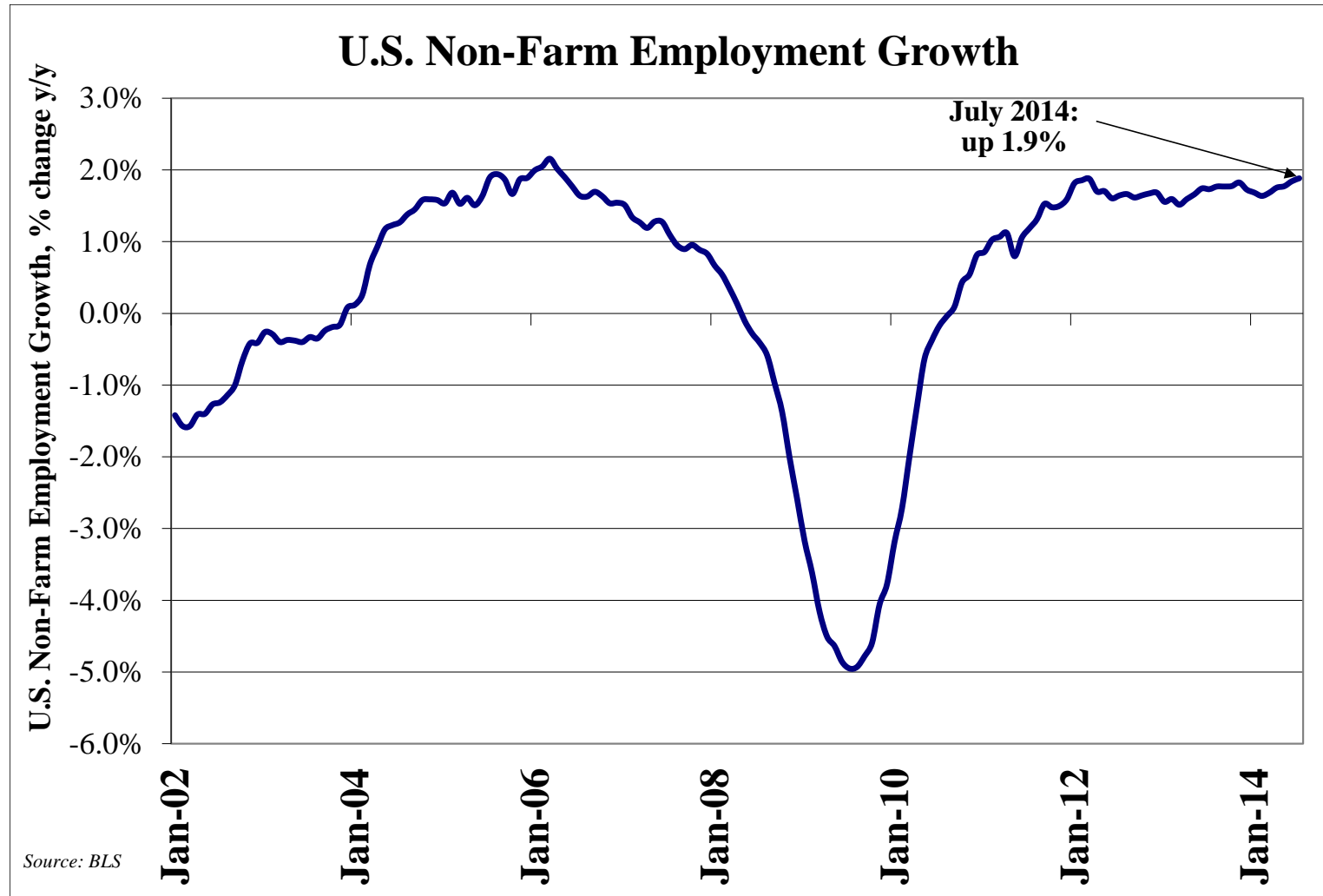
Manufacturing IP: Up 4.8% y/y in July



Capacity Utilization: Up to 78.1% in July



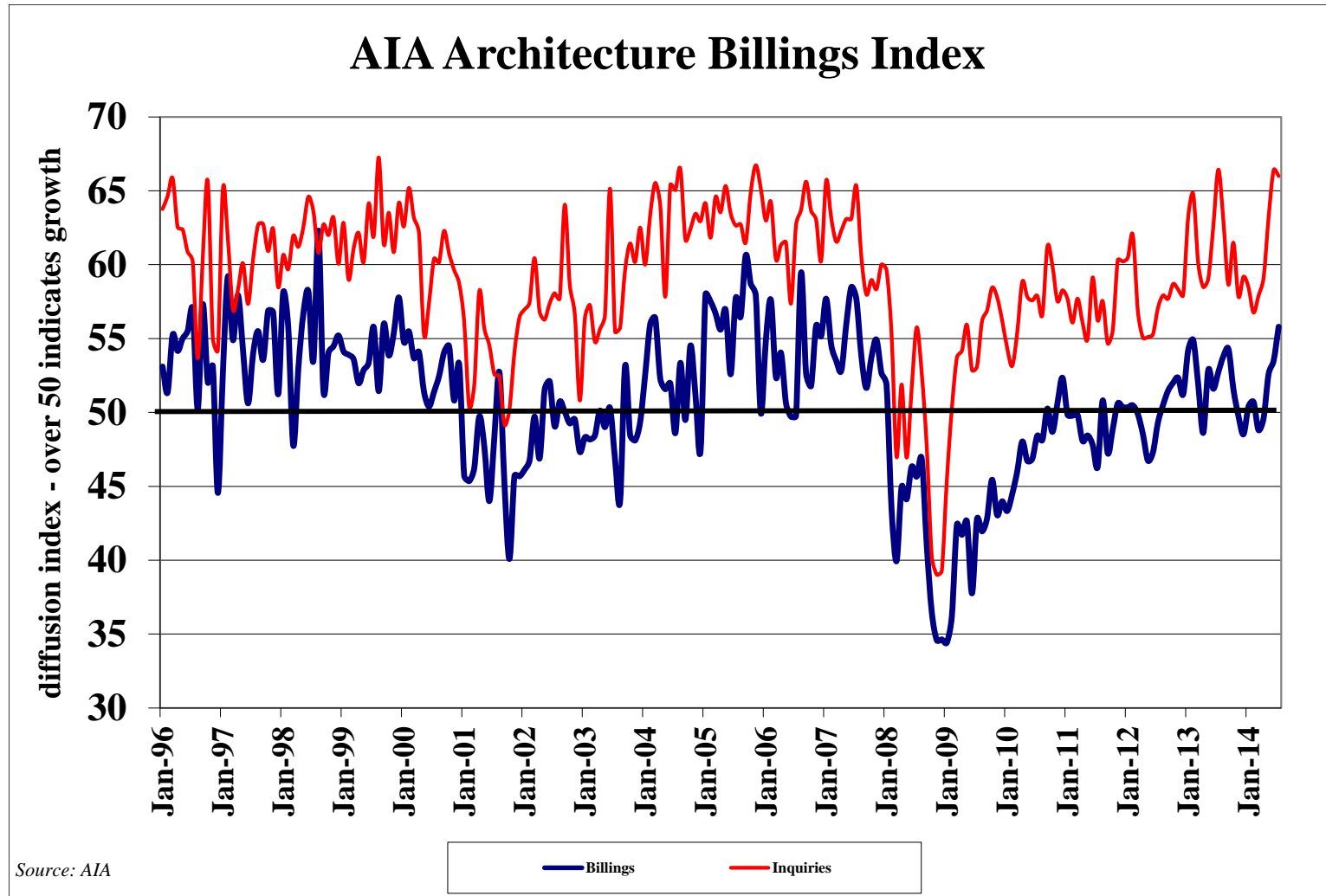
Non-Farm Employment: Up 1.9 % y/y in July



Manufacturing Employment: Up 1.5% in July



AIA Billings Index – Billings Improve in July



McGraw Hill

Updates Forecast

- McGraw Hill recently increased its 2014 non-residential building starts forecast (in dollars) to up 9% y/y from 8% growth 90-days ago, and the up 12% y/y forecast for non-residential building starts in square footage is unchanged. The most positive revisions are in the religious buildings, office/bank buildings, warehouses, dorms, government buildings, and hospitals categories, while the forecast for hotels/motels and parking garages declined the most from the prior forecast. The current forecast anticipates growth in non-residential building starts will accelerate in 2015 and 2016, to 14% and 16% growth, respectively. The chart on the next page details the current forecast from McGraw Hill.

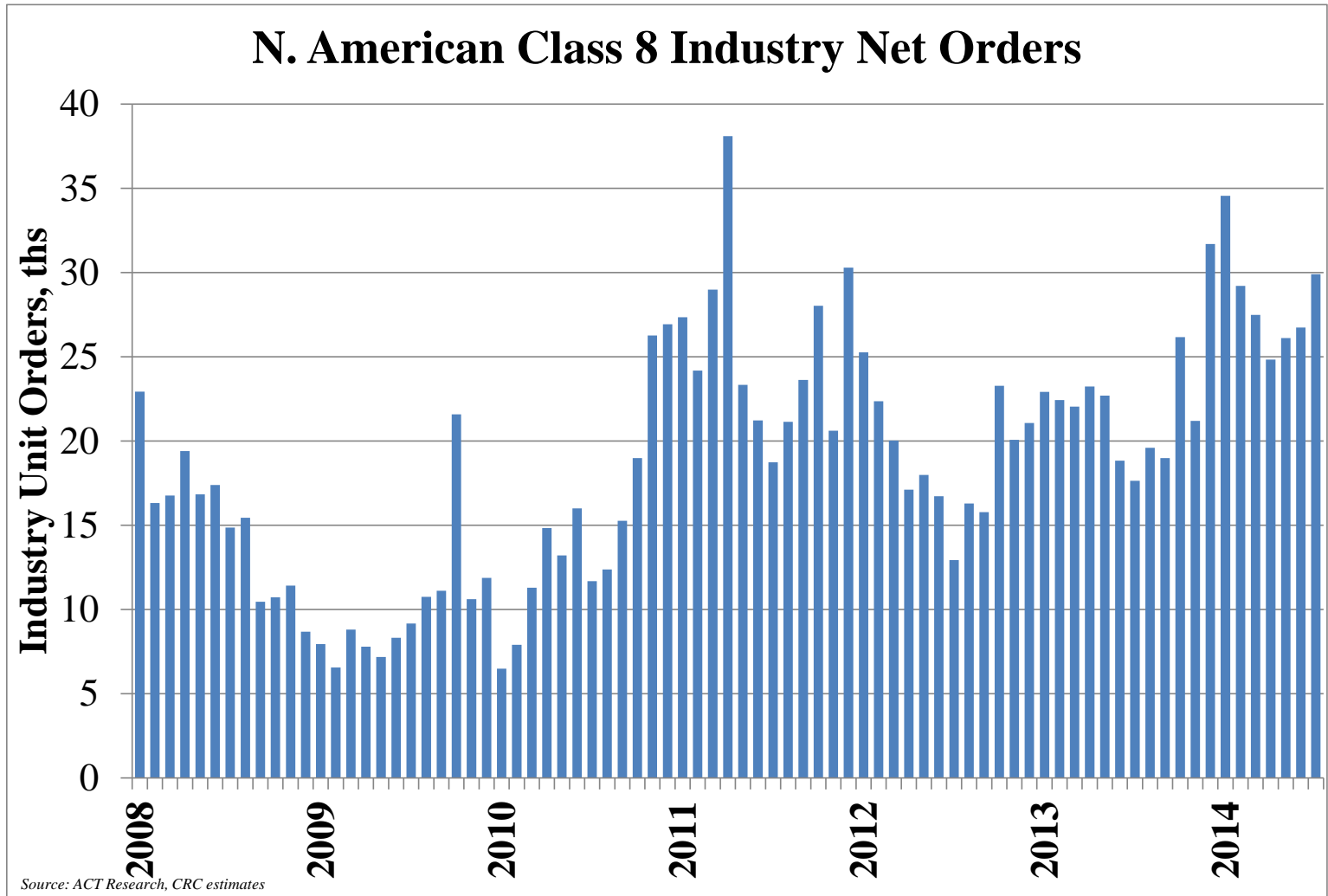
Non-Res Starts: Forecast

McGraw-Hill Construction Starts History and Forecast

U.S. Starts Forecast (Value \$mm)	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E
Amusement, Social and Recreational Bldgs	0%	-14%	-4%	-12%	-17%	28%	6%	18%	24%	1%
Dormitories	16%	-5%	1%	-15%	5%	-7%	3%	8%	8%	9%
Government Service Buildings	7%	15%	-32%	-14%	-9%	-24%	-6%	13%	11%	14%
Hospitals and Other Health Treatment	23%	-33%	16%	-7%	-3%	-4%	4%	14%	17%	10%
Hotels and Motels	-9%	-64%	-28%	58%	25%	31%	11%	21%	12%	-7%
Manufacturing Plants, Warehouses, Labs	44%	10%	-5%	74%	-25%	42%	7%	8%	14%	3%
Miscellaneous Nonresidential Buildings	19%	16%	29%	-29%	-10%	1%	7%	15%	14%	5%
Office and Bank Buildings	-15%	-28%	-18%	-3%	0%	21%	18%	19%	16%	11%
Parking Garages and Automotive Services	-21%	-47%	9%	26%	22%	25%	12%	12%	8%	1%
Religious Buildings	-5%	-7%	-29%	-10%	-10%	-5%	1%	10%	12%	17%
Schools, Libraries, and Labs (nonmfg)	9%	-17%	-3%	-11%	-12%	1%	4%	11%	23%	17%
Stores and Restaurants	-27%	-40%	-5%	3%	15%	6%	15%	21%	17%	4%
Warehouses (excl. manufacturer owned)	-22%	-58%	-16%	23%	27%	33%	27%	12%	8%	-3%
Nonresidential Building Starts (\$mm)	242,186	168,877	162,640	165,654	158,222	174,082	189,473	216,522	251,990	271,614
% change y/y	1%	-30%	-4%	2%	-4%	10%	9%	14%	16%	8%
Nonresidential Building Starts (sqr ft)	1,377	773	678	703	774	845	943	1,076	1,220	1,269
% change y/y	-18%	-44%	-12%	4%	10%	9%	12%	14%	13%	4%
Single Family Housing Starts	1,203	951	978	905	1,146	1,424	1,762	2,248	2,687	2,614
% change y/y	-42%	-21%	3%	-7%	27%	24%	24%	28%	20%	-3%
Nonbuilding Starts (bridges, highways, etc, \$mm)	152,486	144,769	148,329	150,515	162,823	144,800	129,300	135,100	146,900	162,700
% change y/y	9%	-5%	2%	1%	8%	-11%	-11%	4%	9%	11%

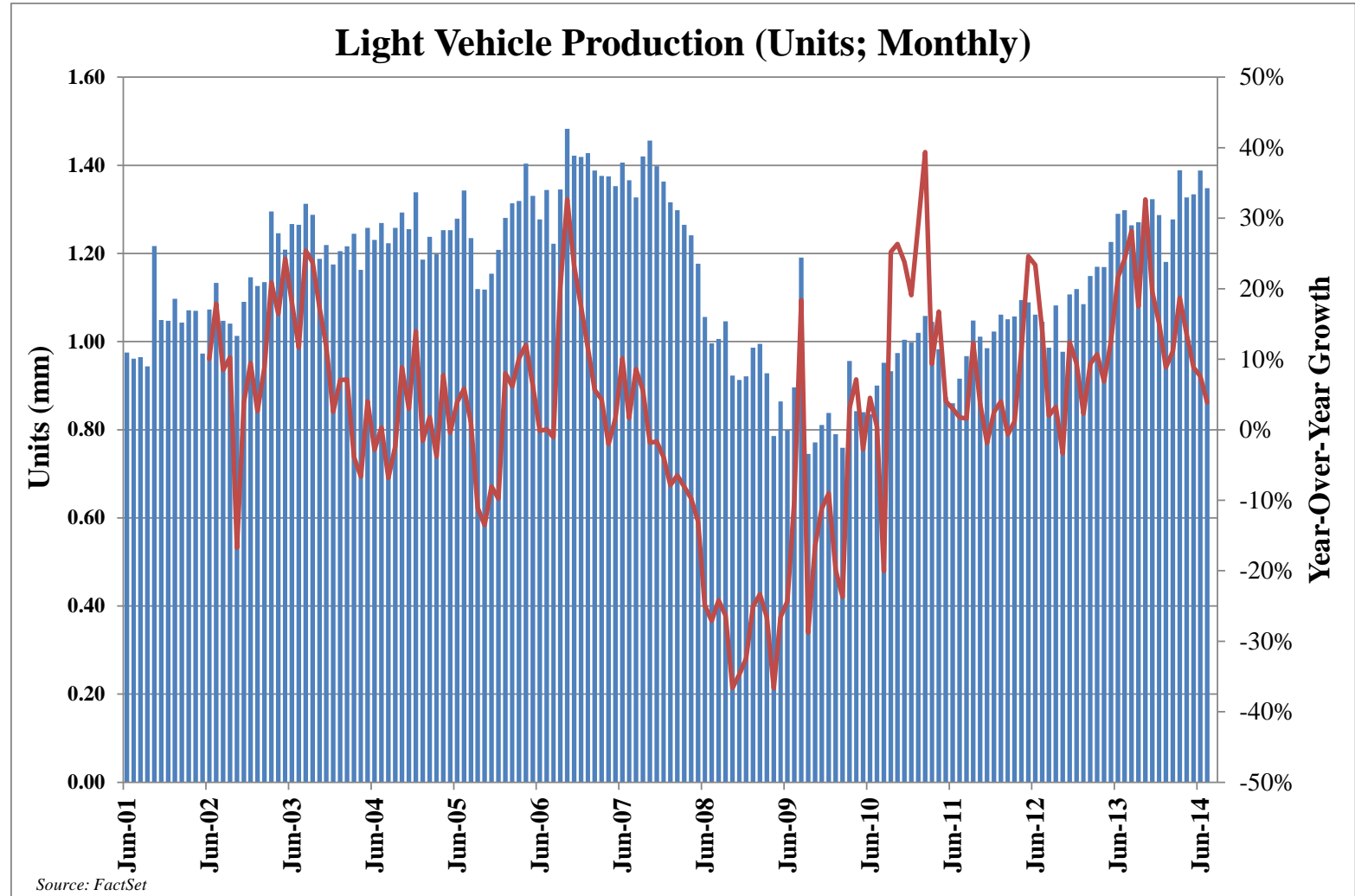
Source: MHC (1Q14 fcst)

Heavy Truck Orders Tick Up to ~30k Units in July



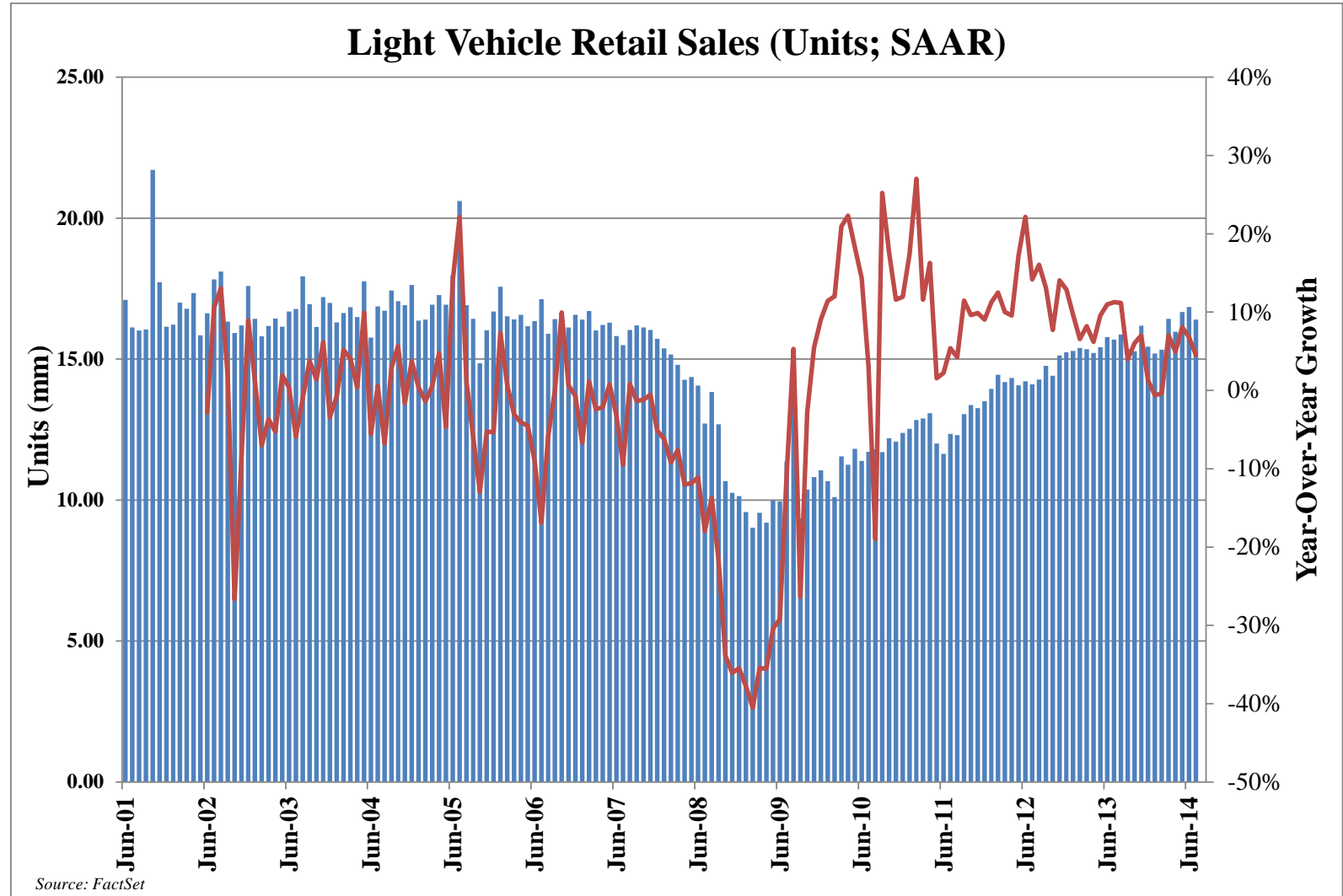
Light Vehicle Production

up 4% y/y in July



Light Vehicle Retail Sales

~16.4mm SAAR in July



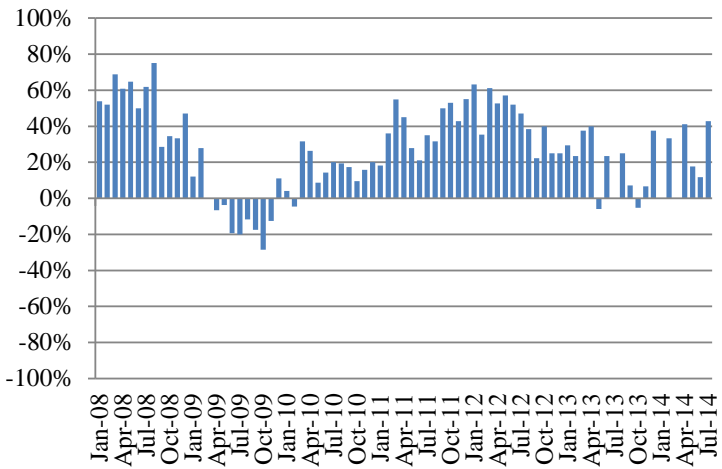
Appendix

Long term end market trends

Industrial Survey

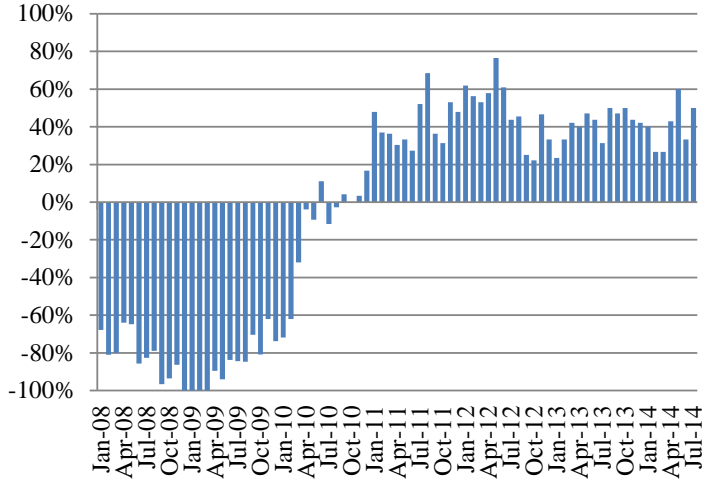
End Market Trends

Aerospace



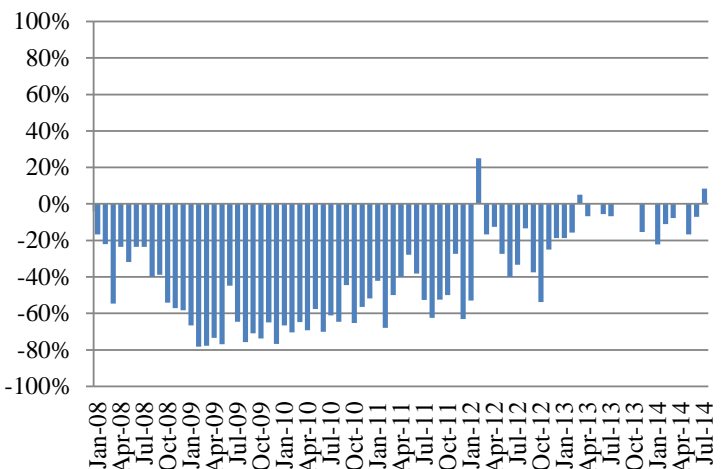
Source: CRC survey

Automotive



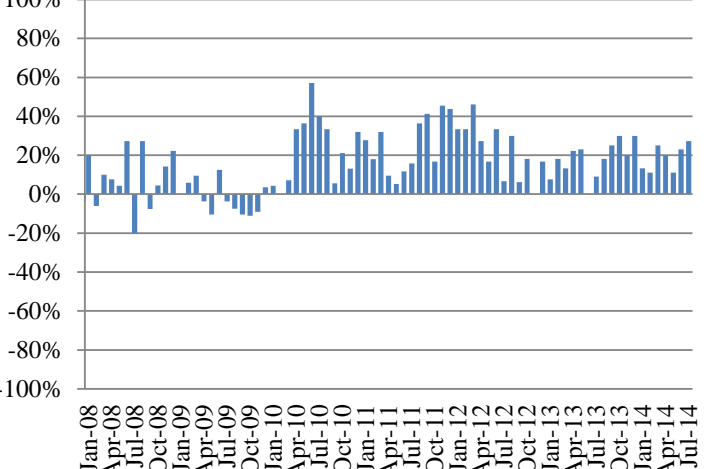
Source: CRC survey

Contractor



Source: CRC survey

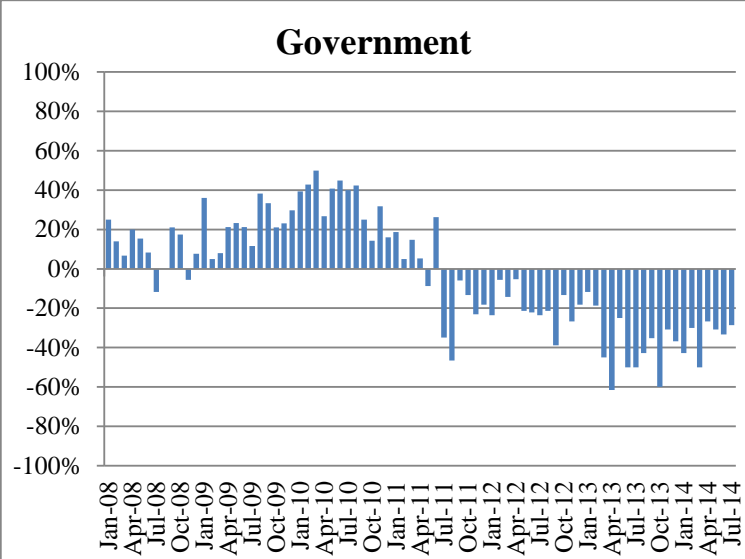
Food



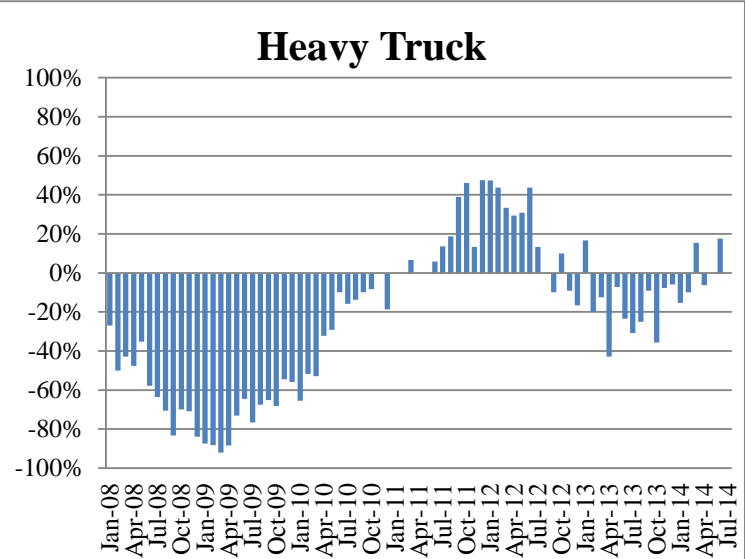
Source: CRC survey

Industrial Survey

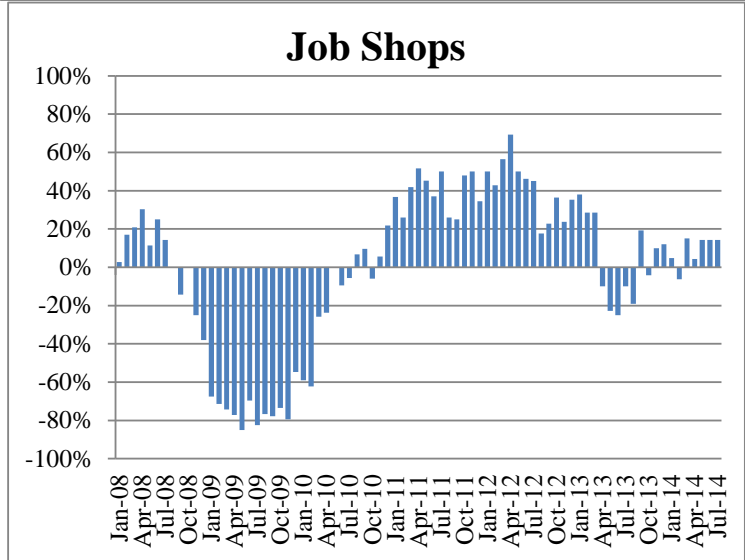
End Market Trends



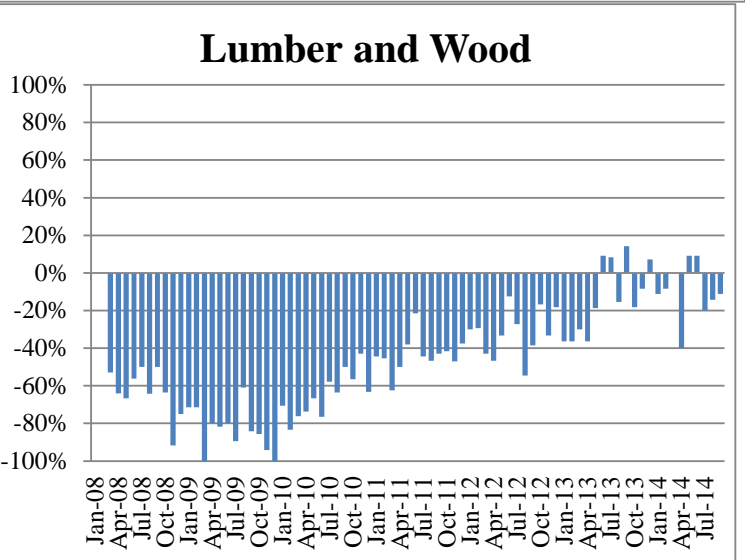
Source: CRC survey



Source: CRC survey



Source: CRC survey

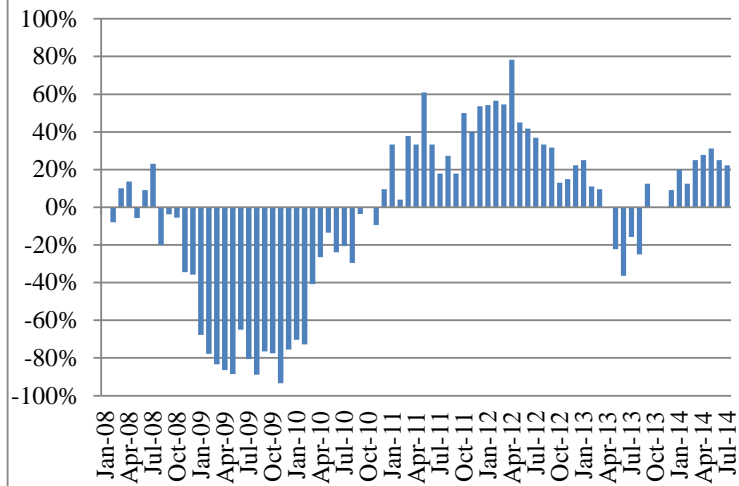


Source: CRC survey

Industrial Survey

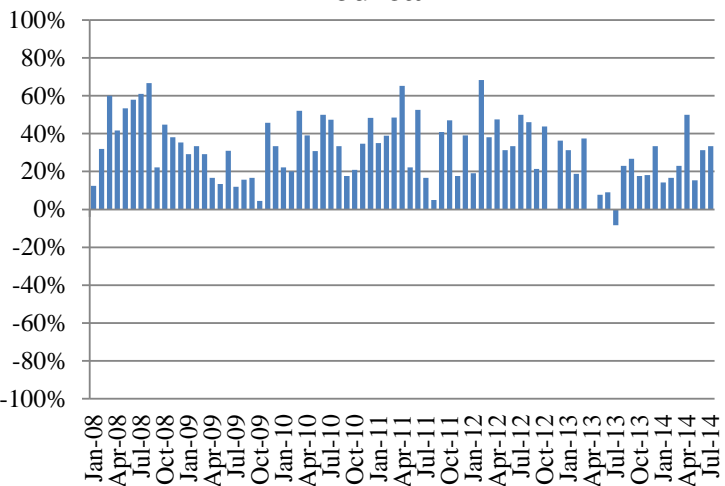
End Market Trends

Machine Tool



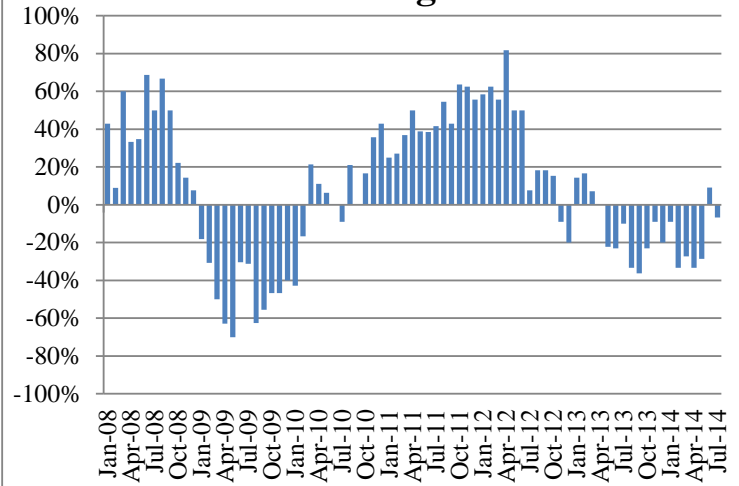
Source: CRC survey

Medical



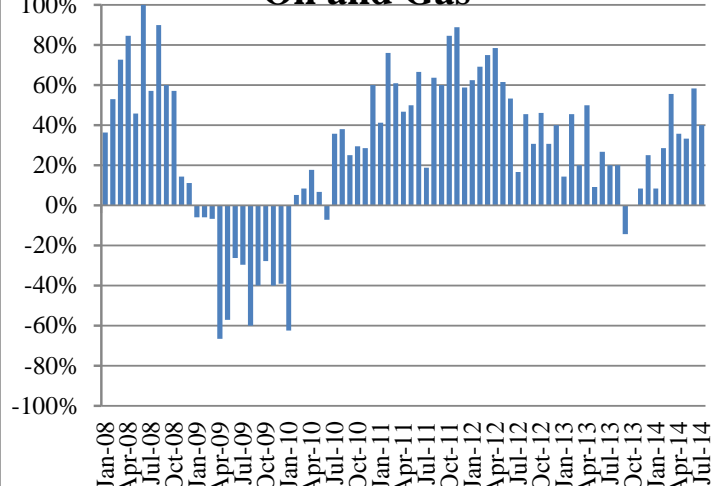
Source: CRC survey

Mining



Source: CRC survey

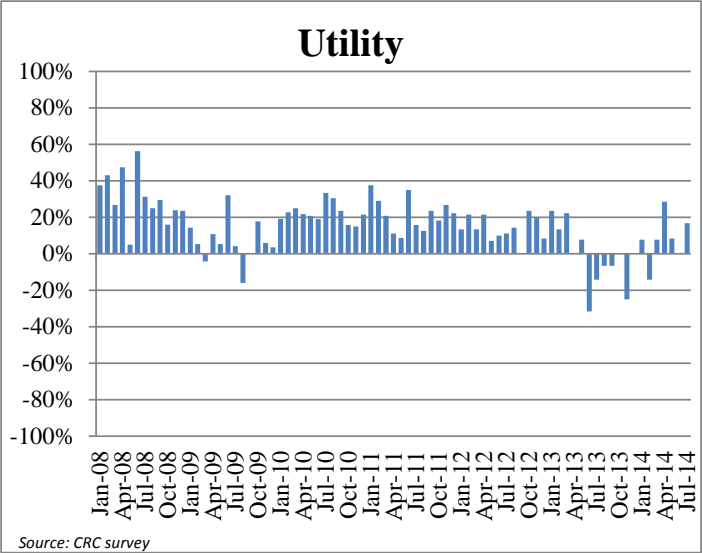
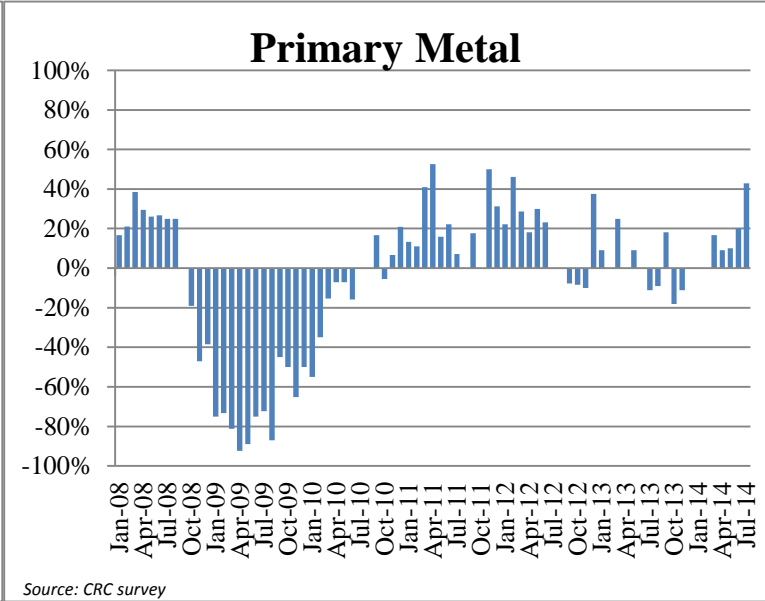
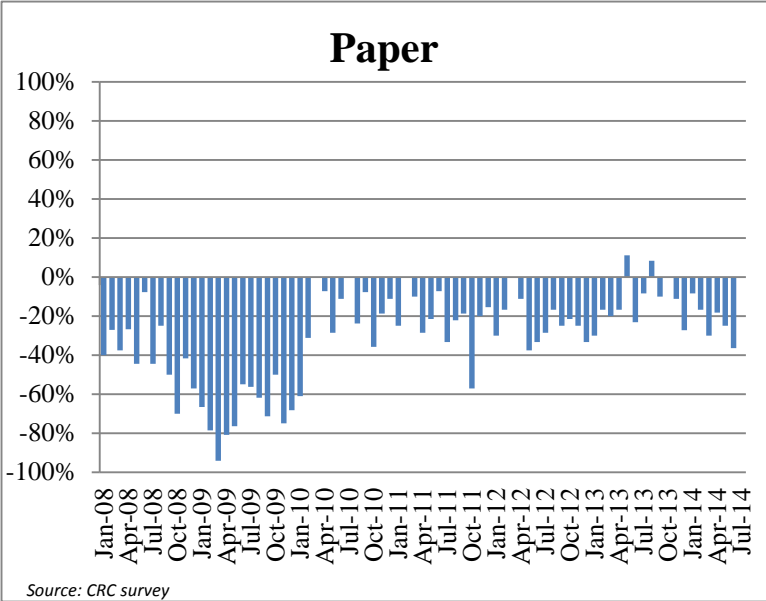
Oil and Gas



Source: CRC survey

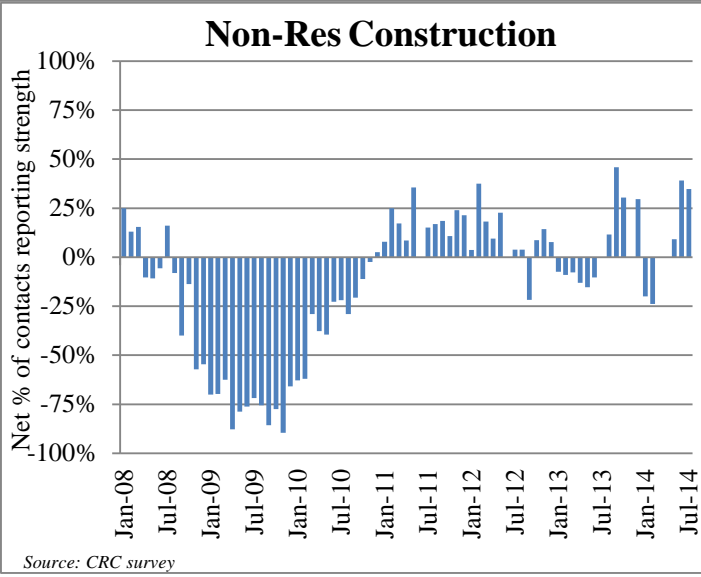
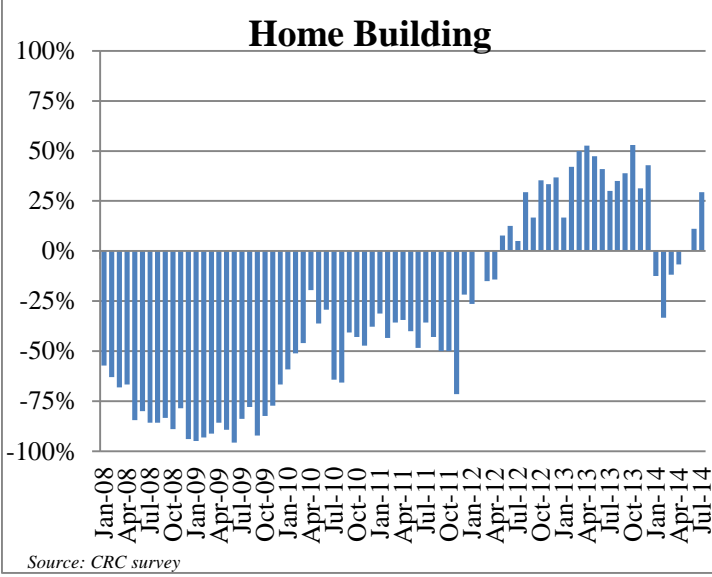
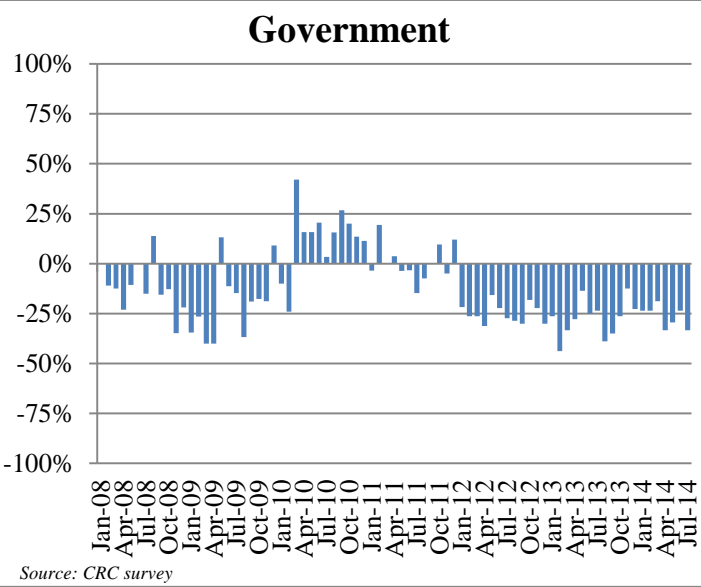
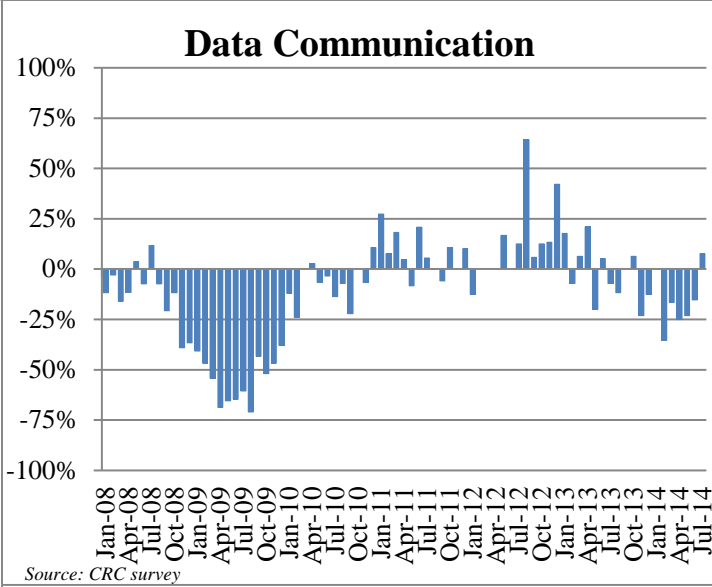
Industrial Survey

End Market Trends



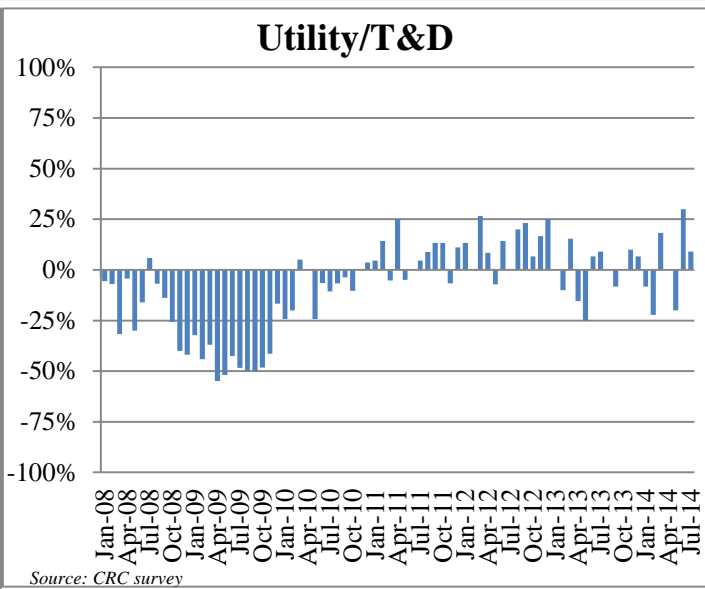
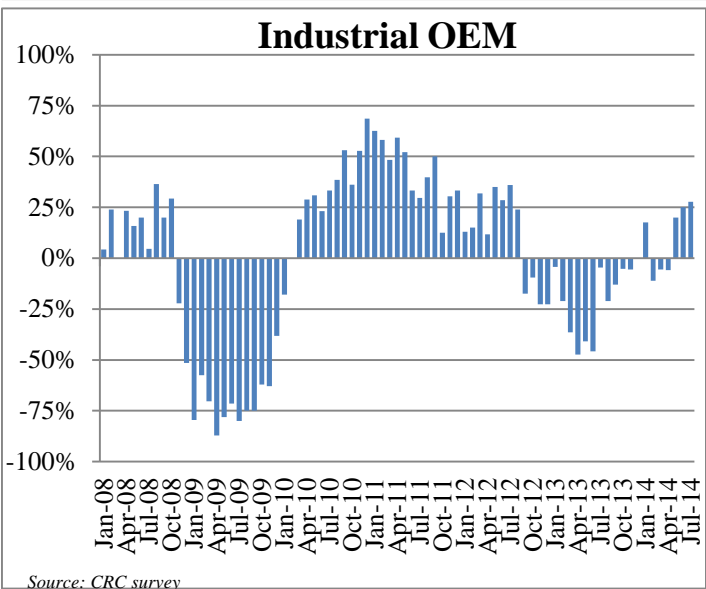
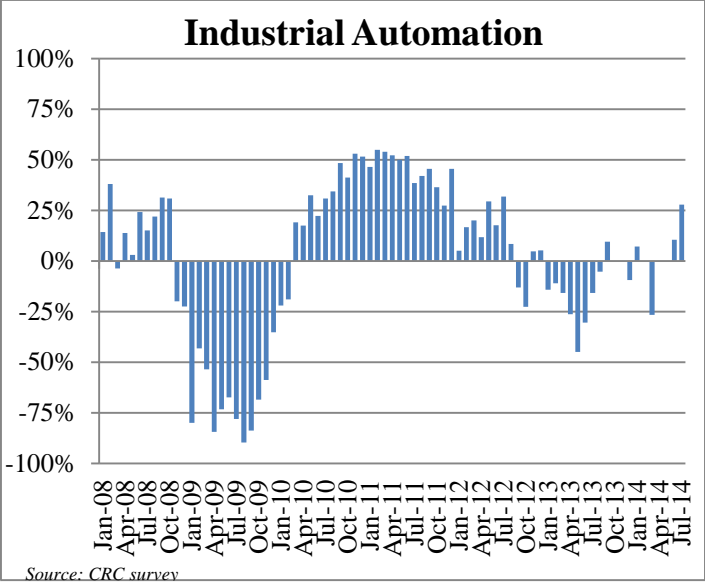
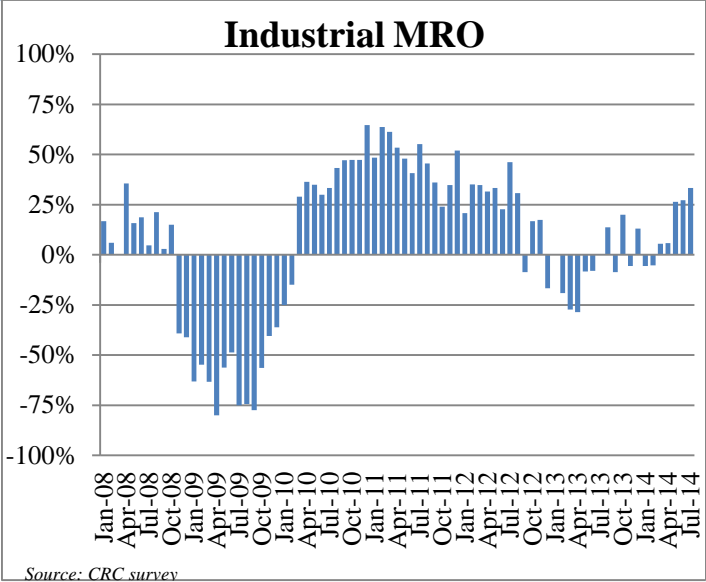
Electrical Survey

End Market Trends



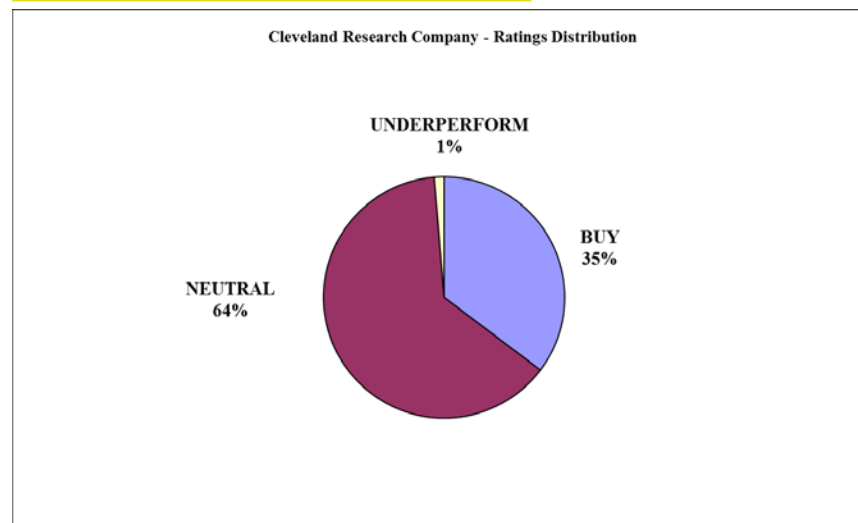
Electrical Survey

End Market Trends



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Underperform: The stock's total return is expected to underperform the market due to weak fundamentals and a lack of catalysts.

Neutral: The stock is expected to be in line with the market due to full valuation and/or a lack of catalysts.

Valuation and Risk: Price targets are established under various valuation methods including P/E, P/S, EV/EBITDA on financial estimates based on forward earnings. Price targets are not established for every stock. The price target's effectiveness may be affected by various outside factors. Risk assessments can be found in the most recent research on these stocks.

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