

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 29, 2001

Commission file number 0-21835

**SUN HYDRAULICS CORPORATION**  
(Exact Name of Registration as Specified in its Charter)

**Florida**  
(State or Other Jurisdiction of  
Incorporation or Organization)  
**1500 West University Parkway**  
**Sarasota, Florida**  
(Address of Principal Executive Offices)

**59-2754337**  
(I.R.S. Employer  
Identification No.)  
**34243**  
(Zip Code)

**941/362-1200**  
(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:  
Securities registered pursuant to Section 12(g) of the Act:

None

Common Stock, Par Value \$.001 per share  
(Title of Class)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

The aggregate market value of the voting stock held by non-affiliates of the Registrant on February 27, 2002, was \$27,579,344 based upon the closing sale price of \$7.60 on the Nasdaq Stock Market's National Market for that date. As of February 27, 2002, there were 6,424,171 shares outstanding.

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## **PART I**

### **ITEM 1. BUSINESS**

*Certain statements contained in this "Item 1. Business" that are not historical facts are "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934. See "Item 7. Forward-Looking Information."*

#### **Overview**

The Company 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 innovative floating construction of the Company's screw-in cartridge valves and the design of the cavities in which they are installed provides demonstrable performance and reliability advantages compared to other available screw-in cartridge valves. The Company designs and manufactures one of the most comprehensive lines of screw-in hydraulic cartridge valves and manifolds in the world. The Company has generated a profit every year since 1972 and has paid a dividend every quarter since its public offering in 1997. The Company believes that its success is primarily a result of its innovative product design, consistent high quality, superior product performance and the breadth of the markets it serves.

The Company sells its products primarily through a global network of independent fluid power distributors to a diverse universe of end users, for use in various "mobile" applications, such as construction, agricultural and utility equipment (approximately 66% of net sales), and a broad array of "industrial" applications, such as machine tools and material handling equipment (approximately 34% of net sales). While many of the Company's end users are subject to cyclical demand for their products, the Company mitigates this exposure through the wide variety of applications and industries it serves. In 2001, sales to the Company's largest distributor represented less than 8.5% of net sales, and approximately 45% of the Company's net sales were outside the United States.

The Company was organized as a Florida corporation in 1986 to take over the operations of the business of the Company's predecessor, Suninco, Inc. (f/k/a Sun Hydraulics Corporation). Suninco, Inc. was founded in 1970 by Robert E. Koski for the specific purpose of developing and promoting screw-in cartridge valve technology. The address of the Company's executive offices is 1500 West University Parkway, Sarasota, Florida 34243, its telephone number is (941) 362-1200, and its website address is [www.sunhydraulics.com](http://www.sunhydraulics.com).

## **Industry Background**

Fluid power is one of three basic technologies, along with electrical and mechanical, utilized to achieve power transmission and motion control. Due to its mechanical advantage, fluid power is widely employed to move and position materials, control machines, vehicles and equipment, and improve industrial efficiency and productivity. Fluid power can perform work on very light loads with a high degree of accuracy or develop enormous forces to move and position materials and equipment that weigh many tons.

Screw-in hydraulic cartridge valves first appeared in the late 1950s as an alternative to conventional forms of hydraulic valving. Conventional hydraulic valves are generally larger in size, typically manufactured from cumbersome iron castings, relatively limited in their ability to interface with machinery and equipment, and are usually simple devices designed to control a single task. Screw-in cartridge valves represent a miniaturization of hydraulic valves, providing the same functional characteristics as conventional valves, but in a smaller package size. In addition to being lighter-weight and more compact, screw-in cartridge valves frequently offer significant advantages in interface flexibility and cost over conventional hydraulic valves.

Screw-in cartridge valves have achieved greater marketplace acceptance in recent years as hydraulic system design engineers increasingly use them to develop multiple-function control systems. A number of screw-in cartridge valves can be grouped together in a manifold, creating a hydraulic control system that is functionally analogous to an electronic integrated circuit. End users can utilize screw-in

cartridge valves and custom manifolds to design an optimal solution for control of their fluid power systems that significantly reduces assembly time and expense.

## Strategy

The Company's objective is to enhance its position as one of the world's leading designers and manufacturers of screw-in hydraulic cartridge valves and manifolds by (i) broadening the market for screw-in cartridge valve applications, (ii) continuing the geographic expansion of its markets, and (iii) selectively expanding its product lines. Key elements of the Company's strategy include the following:

*Deliver Value Through High-Quality, High-Performance Products.* The Company's products are designed with operating and performance characteristics that exceed those of many functionally similar products. Overall, the Company's products provide high value because they generally operate at higher flow rates and pressures than competitive offerings of the same size. The Company tests 100% of its screw-in cartridge valves to ensure the highest level of performance on a consistent basis.

*Offer a Wide Variety of Standard Products.* The Company currently offers one of the most comprehensive lines of non-solenoid screw-in cartridge valves and manifolds in the world and has recently released solenoid screw-in cartridge valves. The Company is committed to producing functionally superior, standard products that contain a high degree of common content to minimize work in process and maximize manufacturing efficiency. Products are designed for use by a broad base of industries to minimize the risk of dependence on any single market segment or customer. The Company, expands its business through the development of new products that are complementary to its existing products.

*Expand the Product Line.* The Company is continuously engaged in new product development programs to offer new and better cartridge valve solutions to its customers. New cartridge products generally fit into existing cavities, often allowing them to be installed in existing standard manifolds. In 1999, the Company introduced the first products in a new range of electrically actuated (solenoid) cartridge valves. The new solenoid cartridge valves establish a foundation to expand this range of products into other electrically actuated control valves, including proportional controls. With the introduction of these products, the Company believes it gains the opportunity to obtain sales for which it previously could not compete, and further believes that the solenoid cartridge valves will help increase sales of the Company's other cartridge valve and manifold products.

*Capitalize on Custom Manifold Opportunities.* Because fluid power system design engineers are increasingly incorporating screw-in cartridge valves into custom control systems, the Company concentrates its efforts in custom manifolds in two ways. The Company designs and manufactures manifolds, which incorporate the Company's screw-in cartridge valves for sale to original equipment manufacturers ("OEMs"). The Company's internally-developed, proprietary expert system software allows the Company to manufacture manifolds efficiently in low quantities. The Company encourages competitive manifold manufacturers to utilize the Company's screw-in cartridge valves in their manifold designs. The Company sells tooling for machining its cavities, allowing independent manifold manufacturers easily to incorporate the Company's screw-in cartridge valves into their designs.

*Expand Global Presence.* The Company intends to continue to increase its global presence through expansion of its distribution network and its international manufacturing capabilities. In addition to operating units in the United States, England, Germany, Korea and a joint venture in China, the Company has strong distributor representation in most developed and developing markets, including Canada, Western Europe, Taiwan, Singapore, Australia, and Japan. In 2001, the Company generated approximately 45% of its net sales outside the United States. Key areas for expansion where the Company has minimal presence include Central and South America, China and Eastern Europe. The Company believes that further expansion of its international manufacturing facilities will enhance its competitive position in certain foreign markets. In addition, custom manifolds provide an opportunity for operating units and distributors to offer significant value-added content through the local production of manifolds that incorporate the Company's screw-in cartridge valves. This strategy helps minimize potential tariffs and duties that could inflate the price of the Company's products in foreign markets.

*Maintain a Horizontal Organization with Entrepreneurial Spirit.* The Company believes that maintaining its horizontal management structure is critical to retaining key personnel and an important factor in attracting top talent from within the hydraulic valve and manifold industry. The Company strives to maintain its horizontal management structure that encourages communication, creativity, and entrepreneurial spirit and individual responsibility among employees. Employee initiatives have led to continuous process improvements, resulting in considerable operating efficiencies and quality control, as well as the maintenance of a safe and comfortable working environment. The Company believes that a lack of job titles and direct formal reporting responsibilities eliminates perceived barriers to advancement and reduces the potential for adversarial relationships to arise within the organization. A workplace without walls in the Company's offices as well as on the shop floor encourages informal employee consultation and provides the opportunity for all personnel to interface across functional areas.

*Leverage Manufacturing Capability and Know-how as Competitive Advantages.* The Company believes that one of its competitive advantages is its ability to manufacture products to demanding specifications. The Company's strong process capability allows it to machine parts to exacting dimensional tolerances, resulting in the high performance characteristics of its screw-in cartridge valves. The Company has the ability to control manufacturing processes to replicate products consistently and can, if desired, manufacture most of the components of its products with the exception of springs, elastomer seals, and electrical coils. The Company has in-house heat treatment capability to provide consistent and reliable control of this critical operation. Many of the processes discovered and/or developed by the Company often allow cartridge valve design engineers to create new products that otherwise may not have been considered.

*Sell Through Distributors.* Due to the variety of potential customers and the Company's desire to avoid unnecessary bureaucracy, the sales function has been performed primarily by independent distributors. The Company has approximately 75 distributors, 52 of which are located outside the United States, and a majority of which have strong technical backgrounds or capabilities, which enable them to develop practical, efficient, and cost-effective fluid power systems for their customers. Many of these distributors sell products manufactured by other companies that allow them to provide a complete hydraulic system to the customer. The Company provides a high level of technical support to its distributors through open access to the Company's engineering staff, technical documentation, and technical training programs. In addition, the Company maintains close relationships with many OEMs and end users of its products to help it understand and predict future needs for fluid power control devices and to test and refine new product offerings.

*Brand Label and License Manufacturing where desirable.* Two areas the Company has not historically exploited to increase the market penetration of its products are brand labeling and manufacturing licensing agreements. In 1999, the Company entered into a non-exclusive supply agreement with Bosch Rexroth, A.G., a German full-line hydraulic component and systems manufacturer, under which the Company will manufacture selected products carrying the Rexroth logo. In addition, the Company has a non-exclusive licensing agreement whereby Rexroth may manufacture some of the Company's products for use in its own fluid power systems. Company sales to Rexroth have increased under the supply agreement; however, Rexroth has produced only prototype quantity valves under the manufacturing agreement. The Company may also consider entering into similar agreements with other manufacturers of fluid power components if it deems it to be of strategic benefit.

## **Products**

### ***Screw-in Cartridge Valves***

The Company designs and manufactures high-performance, screw-in hydraulic cartridge valves in up to five size ranges, suitable for flows from one to 400 gallons per minute and continuous operating pressures up to 5,000 pounds per square inch. The floating construction pioneered by the Company provides demonstrable performance and reliability advantages compared to most competitors' product offerings due to its self-alignment characteristic that accommodates potential manufacturing deviations common in the thread-making operations of screw-in cartridge valves and manifolds. This floating construction significantly differentiates the Company from most of its competitors, which design and manufacture rigid screw-in cartridge valves that fit an industry common cavity. The floating construction of the Company's screw-in cartridge valves eliminates the tendency of working parts inside the cartridge

valves to bind when screwed into the manifold, which leads to unnecessary stress and, often, premature failure. Recently some competitors have begun to manufacture products that fit the Company's cavity. Strategically, the Company believes the markets for its products will expand more rapidly if other sources are available for products that fit the Company's cavity. The Company believes the recent supply and manufacturing agreements with Bosch Rexroth are a strong endorsement of its design principles.

### ***Manifolds***

A manifold is a solid block of metal, usually aluminum or ductile iron, which is machined to create threaded cavities and channels into which screw-in cartridge valves can be installed and through which the hydraulic fluid flows. The manifolds manufactured by the Company are described below:

*Standard Manifolds.* The variety of standard, catalogued manifolds offered by the Company is unmatched by any screw-in cartridge valve competitor. These products allow customers easily to integrate the Company's screw-in cartridge valves into their systems in many different ways. Once designed, standard manifolds require minimal, if any, maintenance engineering over the life of the product.

*Custom Manifolds.* Custom manifolds are designed for a customer-specific application and typically combine many different screw-in cartridge valves in a single package or multiple packages. The Company's internally-developed, proprietary expert system software allows the Company to manufacture manifolds efficiently in low volumes. The innovative design of the Company's screw-in cartridge valves allows manifolds to be physically smaller for certain applications than functionally similar manifolds containing competitors' screw-in cartridges that fit industry common cavities. The Company believes many of the custom manifolds that incorporate cartridge valves which fit industry common cavities require testing after assembly. The Company does not routinely test manifolds that contain its screw-in cartridge valves because of the inherent reliability of the cartridge valves and believes this provides a significant competitive advantage. Custom manifolds provide many benefits to end users and equipment manufacturers, including reduced assembly time, reduced leakage points, neater packaging, potentially fewer hose and fitting connections, and more control functions in a single location.

### **Engineering**

The Company believes that it is critical for engineers to play an important role in all aspects of the Company's business, including design, manufacturing, sales and marketing and technical support. When designing products, engineers work within a disciplined set of design parameters that often results in repeated incorporation of existing screw-in cartridge valve components in new functional products. The Company's focus on engineering has served as the foundation of its ability to offer the expansive range of screw-in cartridge valves that it brings to market.

During product development, engineers work closely with manufacturing personnel to define the processes required to manufacture the product reliably and consistently. The close link between engineering and manufacturing helps smooth the transition from design to market. Design changes to facilitate manufacturing processes are sometimes considered but not if product performance levels would be compromised. The Company practices a continuous improvement process, which it believes is largely attributable to its horizontal management structure that empowers employees and encourages their creative contribution. At various times the Company may incorporate design changes in a product to improve its performance or life expectancy. All of the Company's engineers provide application support to customers and distributors.

## **Manufacturing**

The Company is a process intensive manufacturing operation that extensively utilizes computer numerically controlled (“CNC”) machinery to manufacture its products. Where commercial machinery is not available for specific manufacturing or assembly operations, the Company often designs and builds its own machinery to perform these tasks. The Company makes extensive use of automated handling and assembly technology (robotics) where possible to perform repetitive tasks, thus promoting manufacturing efficiencies and workplace safety. The Company has its own electric heat treatment furnaces to provide consistent and reliable control of this important operation.

At its Sarasota, Florida, facilities, the Company has extensive testing facilities that allow its design engineers to test fully all cartridge valve products at their maximum rated pressure and flow rates. A metallurgist and complete metallurgical laboratory support the Company’s design engineers and in-house heat treatment. The resident engineers at the Company’s other facilities also utilize test equipment.

The Company employs a build-to-order philosophy and relies on its distributors to purchase and maintain sufficient inventory to meet their customers’ demands. With this build-to-order philosophy, most raw materials, including aluminum and steel, are delivered on a just-in-time basis. These and other raw materials are commercially available from multiple sources.

The Company controls most critical finishing processes in-house but does rely on a small network of outside manufacturers to machine cartridge components to varying degrees of completeness. Many high-volume machining operations are performed exclusively at outside suppliers. The Company is very selective in establishing its supplier base and attempts to develop and maintain long-term relationships with suppliers. The Company continually reviews all of its suppliers to improve the quality of incoming parts and to assess opportunities for better control of both price and quality. Manufacturing processes at the existing facilities in the United States, England and Korea are certified to ISO 9002. The United States is in the process of having its manufacturing and design processes certified to ISO 9001. Completion of the certification is expected in 2002.

## **Sales and Marketing**

The Company’s products are sold globally, primarily through independent fluid power distributors. Distributors are supported with product education programs conducted by the Company at its facilities. Technical support is provided by each of the Company’s manufacturing operations (Florida, England, Germany, Korea, and China). Included in the Company’s sales and marketing staff are hydraulic engineers who have significant experience in the fluid power industry. Discount pricing structures encourage distributors to buy in moderate to high volumes to ensure there is a local inventory of products in the marketplace.

The Company currently has approximately 75 distributors, 52 of which are located outside the United States and a majority of which have strong technical backgrounds or capabilities, which enable them to develop practical, efficient, and cost-effective fluid power systems for their customers. In 2001, sales to the Company’s largest distributor represented less than 8.5% of net sales and net sales outside of the United States represented approximately 45% of total net sales.

In addition to distributors, the Company sells directly to other companies within the hydraulic industry under a pricing program that does not undermine the primary distributors’ efforts. Companies that participate in this program utilize the Company’s products in a value-added application, integrating the Company’s screw-in cartridge valves into other fluid power products or systems of their manufacture. Management believes this strategy strengthens the Company by encouraging other manufacturers to buy from the Company. The “goodwill” relationships that result from this strategy also help to keep the Company abreast of technological advances within the fluid power industry, aiding in new product development.

In 1999, the Company signed a non-exclusive supply agreement with Rexroth, a German manufacturer of fluid power components and systems, which allows Rexroth to purchase the Company’s standard products for incorporation into its hydraulic systems. Rexroth is one of the largest hydraulic manufacturers of fluid power systems in the world and has significant presence in all major markets.

Through this relationship, the Company believes that it will gain entry into new markets, both geographically and for new applications. Management anticipates that it will evaluate similar agreements with other manufacturers' of fluid power components when to do so would be of strategic benefit.

While the Company principally sells its products through distributors, it provides end users with technical information via the internet website and catalogues. This program is intended to provide design engineers with all information necessary to specify and obtain the Company's products. In December, 2001, the Company launched a new website which disseminates product information quickly and is widely available to help stimulate global demand and pull product through the distribution channel. The time from the engineering release of products to their appearance in the marketplace has been drastically reduced. The Company will continue to invest in this technology as one of the best ways to keep its broad product offering available to provide hydraulic control solutions for customers around the world.

## **Customers**

Management does not believe that the loss of any one customer would have a material adverse effect on the Company's business. End-users are classified by whether their primary applications for the Company's products are "mobile" or "industrial."

Mobile applications involve equipment that generally is not fixed in place and is often operated in an uncontrolled environment, such as construction, agricultural and utility equipment. Mobile customers were the original users of screw-in cartridge valves due to the premium that these industries place on considerations of space, weight, and cost. Mobile customers currently account for approximately 66% of the Company's net sales.

Industrial applications involve equipment that generally is fixed in place in a controlled environment. Examples include presses, injection molding equipment, and machine tools. The requirements of the industrial marketplace are more demanding than most mobile applications since industrial equipment typically operates at significantly higher cycles. The Company's products are designed to withstand these operating imperatives, and industrial applications currently account for approximately 34% of the Company's net sales. Many conventional valve designs are still used in industrial applications and represent substitution opportunities for the Company's products.

The Company's distributors are not authorized to approve the use of its products in any of the following applications, (i) any product that comes under the Federal Highway Safety Act, such as steering or braking systems for passenger-carrying vehicles or on-highway trucks, (ii) aircraft or space vehicles, (iii) ordnance equipment, (iv) life support equipment, and (v) any product that, when sold, would be subject to the rules and regulations of the United States Nuclear Regulatory Commission. These "application limitations" have alleviated the need for the Company to maintain the internal bureaucracy necessary to conduct business in these market segments.

## **Competition**

The hydraulic valve industry is highly fragmented and intensely competitive. The Company has a large number of competitors, some of which are full-line producers and others that are niche suppliers similar to the Company. Most competitors market globally. Full-line producers have the ability to provide total hydraulic systems to customers, including components functionally similar to those manufactured by the Company. There has been increasing consolidation activity within the industry in recent years, with large, full-line producers filling out their product lines by acquiring or entering into relationships with other hydraulics companies, and management expects there will be further consolidation in the future. The Company believes that it competes based upon quality, reliability, price, value, speed of delivery and technological characteristics.

Most of the Company's screw-in cartridge valve competitors produce screw-in cartridge valves that fit an industry common cavity that sometimes allows their products to be interchangeable. The industry common cavity is not currently supported by any national or global standards organizations, although there is an ongoing effort to standardize a modified version of this cavity in the United States. The International Standards Organization (ISO) has developed a standard screw-in cartridge cavity that is different from the industry common cavity, but the Company is not aware of any major competitor that



currently produces a full line of standard products conforming to the ISO standard. The Company does not manufacture a product that fits either the industry common or the ISO standard cavity. A few competitors manufacture selected screw-in cartridge valves that fit the Company's cavity. The Company believes the majority of these products are load control valves. To help expand market opportunities, the Company, in late 1999, entered into a non-exclusive sales agreement and a non-exclusive license agreement with Rexroth, under which products will be brand-labeled for, or manufactured under, license by Rexroth using the Company's unique cavity. Management believes that increased use of the Company's cavity will be beneficial in the long term because, although competition will increase, markets and applications for the Company's products also will increase.

## **Employees**

As of December 29, 2001, the Company had 537 full-time employees in the United States, 89 in England, 22 in Germany, and 30 in Korea. The Company continues to focus its efforts in designing and manufacturing standard products, allowing it to maintain over 90% of its employees in manufacturing, distribution, and engineering functions. No employees are represented by a union in any of the Company's operating units, and management believes that relations with its employees are good.

Employees are paid either hourly or with an annual salary at rates that are competitive with other companies in the industry and in its geographic areas. Management believes that the combination of competitive salary, above average health and retirement plans, and a safe and pleasant working environment discourages employee turnover and encourages efficient, high-quality production. Nevertheless, due to the nature of the Company's manufacturing business, it is often difficult to attract skilled personnel.

## **Patents and Trademarks**

The Company believes that the growth of its business will be dependent upon the quality and functional performance of its products and its relationship with the marketplace, rather than the extent of its patents and trademarks. The Company's principal trademark is registered internationally in the following countries: Argentina, Australia, Brazil, Canada, Chile, China, France, Germany, Italy, Japan, Korea, Mexico, Peru, Spain, Sweden, Switzerland, the United Kingdom and the United States. While the Company believes that its patents have significant value, the loss of any single patent would not have a material adverse effect on the Company.

## **Business Risk Factors**

*In addition to the other information in this Form 10-K Report, the following should be considered in evaluating the Company's business and its prospects:*

**Potential Marketplace Adoption of Industry Standard.** The Company's screw-in cartridge valves fit into a unique cavity for which, to date, few other manufacturers have designed products. Accordingly, the Company's screw-in cartridge valves are not interchangeable with those of other manufacturers. Most competitive manufacturers produce screw-in cartridge valves that fit into an industry common cavity. There is an ongoing effort in the United States to produce a new standard for screw-in hydraulic cartridge valve cavities based on the industry common cavity. Additionally, the International Standards Organization ("ISO") has an existing industry standard for screw-in hydraulic cartridge valve cavities, which is different from the Company's cavity and the industry common cavity. In the Company's view, the industry common cavity as well as the suggested standardized form of this cavity and the ISO standard cavity fail to address critical functional requirements, which could result in performance and safety problems of significant magnitude for end users. No major competitor has converted its products to fit the ISO standard cavity. Any move by a substantial number of screw-in cartridge valve and manifold manufacturers toward the adoption of ISO standard or another standard, based on the existing industry common cavity, could have a material adverse effect on the Company's business, financial condition and results of operation. See "Business — Competition."

**Risks Relating to Growth Strategy.** In pursuing its growth strategy, the Company intends to expand its presence in its existing markets and enter new geographic markets. In addition, the Company may pursue acquisitions and joint ventures to complement its business. Many of the expenses arising from the Company's expansion efforts may have a negative effect on operating results until such time, if at all, these expenses are offset by increased revenues. The Company initiated capacity expansion programs during 1997-1999, including the construction of new manufacturing facilities in the United States and Germany, plant improvements in England, equipment purchases and, through acquisition, a facility in Korea. The Company, during 1999 and 2000, also completed the implementation of new accounting and manufacturing computer software systems at its Florida and U.K. facilities, and reconfigured its manufacturing units at its two Florida facilities. In addition to monetary expense, these matters required significant attention from senior management and contributed to the Company's past delivery problems. Management has now refocused its efforts on improving delivery times and customer responsiveness, reducing manufacturing costs, and achieving greater profitability. There can be no assurance that the Company will be able to improve its market share or profitability, recover its expenditures for these capital improvements, or successfully implement its growth strategy. See "Business — Strategy."

The Company's expansion strategy also may require substantial capital investment for the construction of new facilities and their effective operation. The Company may finance the acquisition of additional assets using cash from operations, bank, or institutional borrowings, or through the issuance of debt or equity securities. There can be no assurance that the Company will be able to obtain financing from bank or institutional sources or through the equity or debt markets or that, if available, such financing will be on terms acceptable to the Company.

**Dependence on Key Employees and Skilled Personnel.** The Company's success depends, to a significant extent, upon a number of key individuals. The loss of the services of one or more of these individuals could have a material adverse effect on the business of the Company. The Company's future operating results depend to a significant degree upon the continued contribution of its key technical personnel and skilled labor force. Competition for management and engineering personnel is intense, and the Company competes for qualified personnel with numerous other employers, some of whom have greater financial and other resources than the Company. The Company conducts a substantial part of its operations at its facilities in Sarasota, Florida. The Company's continued success depends on its ability to attract and retain a skilled labor force at this location. While the Company has been successful in attracting and retaining skilled employees in the past, there can be no assurance that the Company will continue to be successful in attracting and retaining the personnel it requires to develop, manufacture and market its products and expand its operations. See "Business — Employees."

**Competition.** The hydraulic valve and manifold industry is highly fragmented and intensely competitive, with the Company facing competition from a large number of competitors, some of which are full-line producers and others that are niche suppliers like the Company. Full-line producers have the ability to provide total hydraulic systems to customers, including components functionally similar to those manufactured by the Company. The Company believes that it competes based upon quality, reliability, price, value, speed of delivery and technological characteristics. Many of the Company's screw-in cartridge valve competitors are owned by corporations, which are significantly larger than the Company and have greater financial resources than the Company. There can be no assurance that the Company will continue to be able to compete effectively with these companies.

The manifold business is also highly fragmented and intensely competitive. All of the major screw-in cartridge valve manufacturers either manufacture manifolds or have sources that they use on a regular basis. In addition, there are a number of independent manifold suppliers that produce manifolds incorporating various manufacturers' screw-in cartridge valves, including those made by the Company. Finally, there are many small, independent machine shops that produce manifolds at very competitive prices. Competition in the manifold business is based upon quality, price, relationships based on proximity to the customer, and speed of delivery. Many of the Company's competitors have very low overhead structures and there can be no assurance that the Company will continue to be able to compete effectively with these companies.

In addition, the Company competes in the sale of hydraulic valves and manifolds with certain of its customers. Generally, these customers purchase special purpose valves from the Company to meet a specific need in a system, which cannot be filled by any valve made by such customer. To the extent that

the Company introduces new valves in the future that increase the competition between the Company and such customer, such competition could adversely affect the Company's relationships with these customers.

**Cyclical**ity. The capital goods industry in general, and the hydraulic valve and manifold industry in particular, is subject to economic cycles. The Company experienced a downturn in 2001 which had a material adverse effect on the Company's business and results of operation.

**International Sales.** In 2001, approximately 45% of the Company's net sales were outside of the United States. The Company is expanding the scope of its operations outside the United States, both through direct investment and distribution, and expects that international sales will continue to account for a significant portion of net sales in future periods. International sales are subject to various risks, including unexpected changes in regulatory requirements and tariffs, longer payment cycles, difficulties in receivable collections, potentially adverse tax consequences, trade or currency restrictions and, particularly in emerging economies, potential political and economic instability and regional conflicts. Furthermore, the Company's international operations generate sales in a number of foreign currencies, particularly British pounds, the Euro, or the Korean Won. Therefore, the Company's financial condition and results of operation are affected by fluctuations in exchange rates between the United States dollar and these currencies. Any or all of these factors could have a material adverse effect on the Company's business, financial condition, and results of operations.

**Environmental Compliance.** The Company's operations involve the handling and use of substances that are subject to federal, state and local environmental laws and regulations that impose limitations on the discharge of pollutants into the soil, air and water and establish standards for their storage and disposal. Management believes that the Company's current operations are in substantial compliance with applicable environmental laws and regulations, the violation of which could have a material adverse effect on the Company. There can be no assurance, however, that currently unknown matters, new laws and regulations, or stricter interpretations of existing laws or regulations will not materially affect the Company's business or operations in the future.

**Risk of Product Liability.** The application of many of the Company's products entails an inherent risk of product liability. There can be no assurance that the Company will not face any material product liability claims in the future or that the product liability insurance maintained by the Company at such time will be adequate to cover such claims.

**Technological Change.** The fluid power industry and its component parts are subject to technological change, evolving industry standards, changing customer requirements and improvements in and expansion of product offerings. If technologies or standards used in the Company's products become obsolete, the Company's business, financial condition and results of operations will be adversely affected. Although the Company believes that it has the technological capabilities to remain competitive, there can be no assurance that developments by others will not render the Company's products or technologies obsolete or noncompetitive. See "Business — Strategy."

**Raw Materials.** The primary raw materials used by the Company in the manufacture of its products are aluminum, ductile iron, and steel. There can be no assurance that prices for such materials will remain stable. If the Company is unable to pass through any price increases to its customers, the operating results of the Company will be adversely affected.

**Parts Suppliers.** The Company's largest expense in the cost of sales is purchased cartridge valve parts. There is no assurance that the Company's manufacturing costs and output would not be materially and adversely affected by operational or financial difficulties experienced by one or more of its suppliers.

**Payment of Dividends.** Although the Company has paid a cash dividend each quarter since its Common Stock has been publicly traded, there can be no assurance that funds will be funds available for this purpose in the future. The declaration and payment of dividends is subject to the sole discretion of the Board of Directors of the Company and will depend upon the Company's profitability, financial condition, capital needs, future prospects and other factors deemed relevant by the Board of Directors, and may be restricted by the terms of the Company's credit agreements.

**Certain Anti-takeover Provisions.** The Company's Articles of Incorporation provides for a classified Board of Directors. In addition, the Articles of Incorporation gives the Board of Directors the authority, without further action by the shareholders, to issue and fix the rights and preferences of a new class, or classes, of preferred stock. These and other provisions of the Articles of Incorporation and the Company's Bylaws may deter or delay changes in control of the Company, including transactions in which shareholders might otherwise receive a premium for their shares over then current market prices. In addition, these provisions may limit the ability of shareholders to approve transactions that they may deem to be in their best interests.

**Control by Certain Shareholders and Management.** Members of the Koski family, including two Directors, Robert E. Koski, the Company's founder and former Chairman, and Christine L. Koski, own or control approximately 42% of the outstanding shares of Common Stock. Accordingly, the members of the Koski family have the ability to control the election of the Company's Directors and the outcome of certain corporate actions requiring shareholder approval and to control the business of the Company. Such control could preclude any acquisition of the Company and could adversely affect the price of the Common Stock. Additionally, all Directors and Executive Officers of the Company as a group beneficially own or control approximately 50% of the outstanding shares of Common Stock. See Item 12. Security Ownership of Certain Beneficial Owners and Management.

## ITEM 2. PROPERTIES

The Company's major locations include facilities in the United States, United Kingdom, Germany, and Korea, as set forth below.

The Company owns a 66,000 square foot facility in Sarasota, Florida, which houses manufacturing, design, marketing and other administrative functions. The Sarasota facility does not have any financial encumbrances and is well suited for the design, testing and manufacture of the Company's products.

The Company also owns a 60,000 square foot manufacturing facility in Manatee County, Florida, which is encumbered by a mortgage loan due December 1, 2011. Under the mortgage loan, monthly payments of principal with interest of 6.5% on the unpaid balance are required. At December 29, 2001, \$4.4 million was outstanding under this credit facility. The Manatee County facility, constructed in 1997, has a productive capacity similar to the Sarasota facility.

The close proximity of the United States facilities allows for quick change and the ability to shift resources, including machinery and people, to effectively meet changing business requirements. The Company believes the combined productive capacity of these facilities is approximately \$100 million. The Company estimates its combined current capacity utilization to be approximately 65%.

The Company also owns vacant land in Manatee County, Florida, for future expansion requirements. There is no mortgage on this property and the Company believes the land to be well suited to add over 30,000 square feet of manufacturing capacity.

The Company owns a 10,000 square foot manufacturing facility in Incheon, Korea, free of any encumbrances. This facility is operating at approximately 75% of capacity.

The Company owns a 25,000 square foot manufacturing facility in Coventry, England, free of any encumbrances. This facility has a productive capacity of approximately \$15 million and currently, is operating at 75% of its productive capacity. The Company is expanding the United Kingdom facility adding an additional 12,000 square feet. The expansion is expected to be complete in the second quarter of 2002.

The Company's 45,000 square foot facility in Erkelenz, Germany has a mortgage loan which is due September 30, 2008, and has a fixed interest rate of 6.05%. At December 29, 2001, the principal balance was \$1.1 million. This facility is well suited to house equipment used for manufacturing and testing of the Company's products. Currently, a small portion of the manufacturing area is utilized. The productive capacity of this facility if fully equipped is believed to be approximately \$40.0 million.

The Company believes that its properties have been adequately maintained, are generally in good condition, and are suitable and adequate for its business as presently conducted. The extent of utilization of the Company's properties varies from time to time and among its facilities.

### **ITEM 3. LEGAL PROCEEDINGS**

The Company from time to time is involved in routine litigation incidental to the conduct of its business. The Company does not believe that any pending litigation will have a material adverse effect on its consolidated financial position or results of operations.

### **ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

There were no matters submitted to a vote of the security holders of the Company through the solicitation of proxies or otherwise during the fourth quarter of the fiscal year ended December 29, 2001.

## PART II

### ITEM 5. MARKET FOR REGISTRANT'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS

#### *Market Information*

The Common Stock of the Company has been trading publicly under the symbol SNHY on the Nasdaq National 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 in the Nasdaq National Market for the periods indicated:

	High	Low
1999		
First quarter	\$ 9.750	\$6.375
Second quarter	9.500	6.750
Third quarter	9.250	6.875
Fourth quarter	8.000	5.750
2000		
First quarter	\$12.000	\$5.875
Second quarter	9.000	7.203
Third quarter	8.813	8.000
Fourth quarter	8.000	6.250
2001		
First quarter	\$ 7.688	\$6.500
Second quarter	8.000	7.050
Third quarter	8.130	7.350
Fourth quarter	8.000	6.800

#### *Holdings*

There were 104 shareholders of record of Common Stock on February 27, 2002. 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 names of securities brokers, dealers, and registered clearing agencies. The Company believes that there are approximately 2,000 beneficial owners of Common Stock.

#### *Dividends*

The Company declared cash dividends of \$0.04 per share to shareholders of record on the last day of each calendar quarter during 2001 and 2000. These dividends were paid on the 15th day of each month following the date of declaration.

The Company's Board of Directors currently intends to continue to pay a quarterly dividend of at least \$0.04 per share during 2002. 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, future prospects and other factors deemed pertinent by the Board of Directors.

### ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The following summary should be read in conjunction with the consolidated financial statements and related notes contained herein. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Item 1. Business."

As of January 1, 1999, the Company changed from a calendar reporting year ending on December 31st to a fiscal year which will end on the Saturday closest to December 31st. Each quarter consists of two 4-week periods and one 5-week period.

	Year Ended				
	Dec 29, 2001	Dec 30, 2000	Jan 1, 2000	Dec 31, 1998	Dec 31, 1997
(in thousands except per share data)					
<b>Statement of Income Data:</b>					
Net sales	\$ 64,983	\$ 79,967	\$70,449	\$ 72,720	\$ 64,947
Gross profit	14,625	21,465	16,416	19,234	19,479
Operating income	2,060	7,356	4,038	7,688	8,302
Income before income taxes	1,312	5,919	2,664	8,520	7,264
Net income	\$ 950	\$ 3,921	\$ 1,831	\$ 5,647	\$ 4,710
Basic net income per common share	\$ 0.15	\$ 0.61	\$ 0.29	\$ 0.89	\$ 0.75
Diluted net income per common share	\$ 0.14	\$ 0.60	\$ 0.28	\$ 0.87	\$ 0.73
Dividends per common share	\$ 0.16	\$ 0.16	\$ 0.16	\$ 0.16	\$ 0.14
<b>Other Financial Data:</b>					
Depreciation and amortization	\$ 5,426	\$ 5,594	\$ 5,043	\$ 4,387	\$ 3,706
Capital expenditures	4,022	4,374	7,897	8,137	6,490
<b>Balance Sheet Data:</b>					
Cash and cash equivalents	\$ 3,611	\$ 2,698	\$ 1,122	\$ 1,592	\$ 1,249
Working capital	12,778	12,658	8,717	5,629	6,100
Total assets	61,750	64,374	64,074	61,019	53,389
Total debt	10,663	12,012	14,342	11,907	9,564
Shareholders' equity	43,738	43,836	41,176	40,015	35,000

Quarterly Results of Operations  
(in thousands)

	For the Quarter Ended							
	Dec 29, 2001	Sep 29, 2001	Jun 30, 2001	Mar 31, 2001	Dec 29, 2000	Sep 29, 2000	Jun 30, 2000	Mar 31, 2000
Net sales	\$13,361	\$15,119	\$17,533	\$18,970	\$17,537	\$20,137	\$22,060	\$20,233
Gross profit	1,809	3,270	4,217	5,316	4,721	5,486	6,176	5,082
Operating income (loss)	(949)	295	842	1,859	1,377	1,887	2,653	1,439
Income (loss) before income taxes	(1,096)	202	620	1,585	1,021	1,550	2,148	1,200
Net income (loss)	(\$662)	\$ 151	\$ 429	\$ 1,033	\$ 667	\$ 1,021	\$ 1,376	\$ 857

## **ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

### ***Overview***

Sun Hydraulics Corporation 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, primarily through independent distributors. Approximately 66% of product sales are used by the mobile market, 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. The remaining 34% of sales are used by industrial markets, which are characterized by equipment that is fixed in place, typically in a controlled environment, with higher pressures and duty cycles. The Company sells to both markets with a single product line. In 2001, the Company generated approximately 45% of its net sales outside of the United States.

### ***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), United States shipments of hydraulic products decreased 16.4% in 2001 compared to 2000. Historically the Company's orders trend has tracked closely to the United States measure of manufacturing capacity utilization. At the end of 2001, this measure was at its lowest level in eighteen years.

### ***Results for the 2001 fiscal year***

Net sales for the year ended December 29, 2001, were \$65.0 million, a decrease of 18.7% compared to net sales of \$80.0 million for the year ended December 30, 2000. Net income for 2001 was \$1.0 million, or 1.5 % of net sales, compared to \$3.9 million, or 4.9% of net sales, for 2000. Basic and diluted earnings per share for the year ended 2001, were \$0.15 and \$0.14 respectively, compared to \$0.61 and \$0.60 for the year ended December 30, 2000.

### ***Cash Flow***

Net cash generated from operations for the year was \$7.3 million. Capital expenditures for the year were \$4.0 million, debt decreased \$1.4 million, and \$1.0 million was paid to shareholders in dividends. Cash on hand at December 29, 2001, was \$3.6 million, an increase of \$0.9 million for the year.

### ***Results for the fourth quarter of 2001***

Net sales for the fourth quarter ended December 29, 2001, were \$13.4 million, a decrease of 23.4% compared to net sales of \$17.5 million for the fourth quarter of 2000. Net loss for the quarter ended December 29, 2001, was in the company's forecasted range at \$0.7 million, compared to net income of \$0.7 million for the fourth quarter of 2000. Net loss for the quarter included a pretax charge of \$0.3 million for slow moving inventory. Both basic and diluted net loss per share for the fourth quarter of 2001 were \$0.10.

### ***Management Comments***

Management believes that the Company's diversified customer base and global presence helped to mitigate the adverse financial effects of the significant downturn in the manufacturing sector. During 2001, the Company was able to keep the workforce intact, continue investments in productivity improvements, and strengthen its marketing efforts.

### ***Outlook***



Orders for the first 8 weeks of the 2002 fiscal year were at a rate 30% higher than the fourth quarter and 12% higher than the third quarter of 2001. The Company estimates that sales for the first quarter of 2002 will be approximately 12% higher than the previous quarter and that net income will approach breakeven.

Management believes that the current upturn in orders is likely to continue in 2002. If the rate of recovery in 2002 is similar to the rate of decline in 2001, 2002 sales will be approximately \$70.0 million, an 8% increase over 2001, which should produce net income per share of approximately \$0.40.

### Other Highlights

In December 2001, the Company launched a new website which disseminates product information quickly and is widely available to help stimulate global demand and pull product through the distribution channel. The time from the engineering release of products to their appearance in the marketplace has been drastically reduced. The Company will continue to invest in this technology as one of the best ways to keep its broad product offering available to provide hydraulic control solutions for customers around the world.

### Results of Operations and Segment Information

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

	For the Year Ended				
	Dec 29, 2001	Dec 30, 2000	Jan 1, 2000	Dec 31, 1998	Dec 31, 1997
Net sales	100.0%	100.0%	100.0%	100.0%	100.0%
Gross profit	22.5%	26.8%	23.3%	26.4%	30.0%
Operating income	3.2%	9.2%	5.7%	10.6%	12.8%
Income before income taxes	1.5%	7.4%	3.8%	11.7%	11.3%

Segment information is as follows:

	United States	Korea	United Kingdom	Germany	Elimination	Consolidated
2001						
Sales to unaffiliated customers	\$43,158	\$4,244	\$11,248	\$6,333	\$ —	\$ 64,983
Intercompany sales	10,326	—	1,544	37	(11,907)	—
Operating income (loss)	667	(20)	1,257	95	61	2,060
Identifiable assets	44,463	1,764	11,257	5,861	(1,595)	61,750
Depreciation and amortization	4,219	177	725	305	—	5,426
Capital expenditures	1,939	72	1,357	654	—	4,022
2000						
Sales to unaffiliated customers	\$55,488	\$5,537	\$13,026	\$5,916	\$ —	\$ 79,967
Intercompany sales	11,232	—	1,814	29	(13,075)	—
Operating income (loss)	5,021	307	1,834	281	(87)	7,356
Identifiable assets	48,717	1,966	10,285	4,757	(1,351)	64,374
Depreciation and amortization	4,283	166	874	271	—	5,594
Capital expenditures	3,213	450	762	(51)	—	4,374
1999						
Sales to unaffiliated customers	\$50,327	\$4,202	\$10,858	\$5,062	\$ —	\$ 70,449
Intercompany sales	8,354	—	2,016	43	(10,413)	—
Operating income	2,492	81	1,059	354	52	4,038
Identifiable assets	49,539	857	8,044	5,902	(268)	64,074
Depreciation and amortization	3,802	112	827	302	—	5,043
Capital expenditures	5,953	119	1,323	502	—	7,897

## ***Comparison of Years Ended December 29, 2001 and December 30, 2000***

### ***Net Sales***

Net sales for 2001 were \$65.0 million, a decrease of \$15.0 million, or 18.7%, from \$80.0 million in 2000. Domestic net sales decreased 25.9%, or \$12.5 million, in 2001, compared to 2000. The primary reason for the decrease was the prolonged decline in the United States manufacturing sector, evidenced by the United States manufacturing capacity utilization index, which was at an eighteen year low at the end of 2001. International net sales decreased 7.7%, or \$2.5 million, with decreases across all markets except Germany.

### ***Gross Profit***

Gross profit decreased to \$14.6 million, or 32.1%, in 2001, compared to \$21.5 million in 2000. Gross profit as a percentage of net sales decreased to 22.5% in 2001, compared to 26.8% in 2000. The decrease in gross profit as a percentage of net sales was due to fewer sales dollars available to cover indirect manufacturing costs, despite an overall decrease in these costs. The decrease in gross profit as a percentage of net sales was also due to a loss of productivity in the U.S. operations. Management decided to maintain production headcount despite reduced production requirements in order to preserve its long-term investment in the workforce.

### ***Selling, Engineering, and Administrative Expenses***

Selling, engineering and administrative expenses decreased \$1.5 million, or 10.6%, to \$12.6 million in 2001, compared to \$14.1 million in 2000. \$0.7 million of the decrease was due to significantly reduced spending for product catalogues. The new company website significantly reduces the amount of product information required to be published. The balance of the decrease was due to lower wage and warranty expenses as well as reductions in many discretionary expense categories such as outside services and travel.

### ***Interest Expense***

Interest expense was \$0.9 million and \$1.1 million in 2001 and 2000, respectively. There was no interest expense on the unsecured line of credit in 2001 since the outstanding balance remained at \$0 for the entire year. This resulted in a decrease in interest expense of \$0.1 million from 2000 to 2001. Interest expense on the Company's long-term mortgages and other debt also decreased \$0.1 million.

### ***Miscellaneous (Income) Expense***

Miscellaneous income was \$0.1 million in 2001, compared to miscellaneous expense of \$0.3 million in 2000. The \$0.4 million change was due to a decrease in equity losses on the joint venture in China, a decrease in foreign currency exchange losses, and a decrease in loss on sale of fixed assets.

### ***Income Taxes***

The provision for income taxes for the year ended December 29, 2001, was 27.6% of pretax income compared to 33.8% for the year ended December 30, 2000. The decrease was due to a change in the relative levels of income and different tax rates in effect among the countries in which the Company sells its products.

## ***Comparison of Years Ended December 30, 2000 and January 1, 2000***

### ***Net Sales***

Net sales for the year were \$80.0 million, an increase of \$9.5 million, or 13.5%, over 1999. This increase was due to strong orders in the first half of the year across all business segments. North American net sales increased 9.8% over 1999. European operations increased 19.0% over 1999. Net sales to Asian distributors increased 27.3% and Korean net sales increased 31.8% over 1999.

### ***Gross Profit***

Gross profit increased to \$21.5 million in 2000, compared to \$16.4 million in 1999. Gross profit as a percentage of net sales increased to 26.8% in 2000, compared to 23.3% in 1999. The increase in gross profit as a percent of sales was primarily due to prime manufacturing cost reductions in the United States operation resulting from lower material costs and increased productivity.

### ***Selling, Engineering, and Administrative Expenses***

Selling, engineering and administrative expenses increased \$1.7 million, or 14.0%, to \$14.1 million in 2000, compared to \$12.4 million in 1999. \$0.4 million of the increase was for product catalogues and \$0.3 million of the increase was related to systems and network development costs. The balance of the increase was primarily due to wage and fringe benefit increases.

### ***Interest Expense***

Interest expense was \$1.1 million and \$1.0 million in 2000 and 1999, respectively. The interest expense related to the unsecured line of credit, long-term mortgages and related party debt decreased \$0.2 million, while interest on the secured line of credit in the United States, which was converted to a four year note on July 23, 2000 (See Note 8 to the Financial Statements), increased \$0.3 million.

### ***Miscellaneous (Income) Expense***

Miscellaneous expense was \$0.3 million in 2000, compared to \$0.4 million in 1999. The \$0.1 decrease was due to a decrease in equity losses on the joint venture in China and a decrease in foreign currency exchange losses.

### ***Income Taxes***

The provision for income taxes for the year ended December 30, 2000, was 33.8% of pretax income compared to 31.3% for the year ended January 1, 2000. This increase was due to Korean tax provision requirements that were not previously believed to be applicable. In both years, tax savings were realized in the United States from the Sun Hydraulics Foreign Sales Corporation.

### ***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 to pay operating expenses, pay dividends to shareholders, make capital expenditures, and service debt.

Net cash flow from operations in 2001 was \$7.3 million, compared to \$9.5 million in 2000 and \$5.6 million in 1999. The decrease in the Company's net cash flow from operations in 2001, compared to 2000, was due primarily to the decrease in net income of \$3.0 million and lower accounts receivable and inventory, partially offset by income taxes receivable. The increase in the Company's net cash flow from operations in 2000, compared to 1999, was due primarily to an increase in net income of \$2.1 million and an increase in depreciation and amortization of \$0.6 million.

Capital expenditures were \$4.0 million in 2001, compared to \$4.4 million in 2000 and \$7.9 million in 1999. Capital expenditures in the year 2002 are projected to be \$6.4 million and will include approximately \$2.6 million to cover the cost of an expansion of the United Kingdom operation.

The Company has \$10.7 million in outstanding debt secured by buildings and equipment. The Company has three revolving lines of credit totaling \$9.5 million with various banks. There were no outstanding balances on these credit facilities at December 29, 2001. Lines of credit in Germany and the U.K. totaling \$2.0 million expire in 2002, while the line of credit in the U.S. expires in 2004.

The Company declared quarterly dividends of \$0.04 per share to shareholders of record on the last day of each calendar quarter in 2001 and 2000. These dividends were paid on the 15th day of each

month following the date of declaration. The Company's Board of Directors currently intends to continue to pay a quarterly dividend of at least \$0.04 per share during 2002. 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, 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 its revolving lines 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 the following 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.

### ***Critical Accounting Policies and Estimates***

It is the Company's accounting policy to report revenues when products are shipped and expenses when costs are incurred. The effect of material non-recurring events is provided for when they become known. 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 accounts receivable, inventory and goodwill. The following explains the basis and the procedure for each asset account where judgment and estimates are applied.

#### ***Accounts Receivable***

The Company sells to most of its customers on a recurring basis, primarily through distributors with whom the Company maintains long-term relationships. As a result, bad debt experience is not material. The reserve for bad debts is determined on a specific identity basis by a review of those accounts that are significantly in arrears. There is no assurance that overdue accounts receivable balances of a distributor or a large direct sale customer will not develop financial difficulties and default on payment.

#### ***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.

#### ***Goodwill***

The Company acquired its Korean operations in September 1998 using the purchase method. As a result, goodwill is reflected on the consolidated balance sheet. A valuation based on the cash flow method was performed at December 29, 2001, and it was determined that the value of the goodwill and the net assets in the accounts exceeded the estimated cash flow valuation. There is no assurance that the value of the acquired company will not decrease in the future due to changing business conditions.

### ***New Accounting Pronouncements***

In June 2001, Statement of Financial Standards No. 141, "Business Combinations" ("SFAS 141"), and Statement of Financial Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"), were issued. SFAS 141 requires that all business combinations initiated after June 30, 2001 be accounted for using the purchase method of accounting, and that identifiable intangible assets acquired in a business combination be recognized as an asset apart from goodwill, if they meet certain criteria. The impact of the adoption of SFAS 141 on the Company's reported operating results, financial position and existing financial statement disclosure is not expected to be material.

SFAS 142 applies to all goodwill and identified intangible assets acquired in a business combination. Under the new standard, all goodwill and indefinite-lived intangible assets, including those acquired before initial application of the standard, will not be amortized but will be tested for impairment at

least annually. The new standard is effective for fiscal years beginning after December 15, 2001. Adoption of FAS 142 effective January 1, 2002 will result in the elimination of approximately \$60 of annual amortization, subject to the identification of separately recognized intangibles, which would continue to be amortized under the new rules. The Company does not expect to recognize any impaired goodwill as of January 1, 2002.

In July 2001, Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" (SFAS 143), which requires the recognition of a liability for an asset retirement obligation in the period in which it is incurred. When the liability is initially recorded, the carrying amount of the related long-lived asset is correspondingly increased. Over time, the liability is accreted to its present value and the related capitalized charge is depreciated over the useful life of the asset. SFAS 143 is effective for fiscal years beginning after June 15, 2002. The impact of the adoption of SFAS 143 on the Company's reported operating results, financial position and existing financial statement disclosure is not expected to be material.

In August 2001, Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"), was issued. This statement addresses the financial accounting and reporting for the impairment or disposal of long-lived assets and broadens the definition of what constitutes a discontinued operation and how results of a discontinued operation are to be measured and presented. The provisions of SFAS 144 are effective for financial statements issued for fiscal years beginning after December 15, 2001. The impact of the adoption of SFAS 144 on the Company's reported operating results, financial position and existing financial statement disclosure is not expected to be material.

### **Seasonality**

The Company generally has experienced reduced activity during the fourth quarter of the year, largely as a result of fewer working days due to holiday shutdowns. As a result, the Company's fourth quarter net sales, income from operations, and net income typically are the lowest 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.

### **FORWARD-LOOKING INFORMATION**

*Certain oral statements made by management from time to time and certain statements contained herein that are not historical facts are "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934 and, because such statements involve risks and uncertainties, actual results may differ materially from those expressed or implied by such forward-looking statements. Forward-looking statements, including those in Management's Discussion and Analysis of Financial Condition and Results of Operations are statements regarding the intent, belief or current expectations, estimates or projections of the Company, its Directors or its Officers about the Company and the industry in which it operates, and assumptions made by management, and include among other items, (i) the Company's strategies regarding growth, including its intention to develop new products; (ii) the Company's financing plans; (iii) trends affecting the Company's financial condition or results of operations; (iv) the Company's ability to continue to control costs and to meet its liquidity and other financing needs; (v) the declaration and payment of dividends; and (vi) the Company's ability to respond to changes in customer demand domestically and internationally, including as a result of standardization. Although the Company believes that its expectations are based on reasonable assumptions, it can give no assurance that the anticipated results will occur.*

*Important factors that could cause the actual results to differ materially from those in the forward-looking statements include, among other items, (i) the economic cyclicalities of the capital goods industry in general and the hydraulic valve and manifold industry in particular, which directly affect customer orders,*

*lead times and sales volume; (ii) conditions in the capital markets, including the interest rate environment and the availability of capital; (iii) changes in the competitive marketplace that could affect the Company's 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; (iv) changes in technology or customer requirements, such as standardization of the cavity into which screw-in cartridge valves must fit, which could render the Company's products or technologies noncompetitive or obsolete; (v) new product introductions, product sales mix and the geographic mix of sales nationally and internationally; and (vi) changes relating to the Company's international sales, including changes in regulatory requirements or tariffs, trade or currency restrictions, fluctuations in exchange rates, and tax and collection issues. 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 "Business," particularly under the subheading, "Business Risk Factors" and "Management's Discussion and Analysis of Financial Conditions and Results of Operations" in this Form 10-K for the year ended December 29, 2001. 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.*

#### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE 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. At December 29, 2001, the Company had \$92 in variable-rate debt outstanding and, as such, the market risk is immaterial. The Company manages this risk by selecting unsecured debt financing at its lenders' prime rate less 1%, or the Libor rate plus 2.0%, whichever is the more advantageous.

## ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

### Index to financial statements:

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Board of Directors and Shareholders  
of Sun Hydraulics Corporation

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, shareholders' equity and comprehensive income, and of cash flows present fairly, in all material respects, the financial position of Sun Hydraulics Corporation and its subsidiaries at December 29, 2001, December 30, 2000, and January 1, 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 29, 2001, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP  
Tampa, FL  
March 1, 2002



**Sun Hydraulics Corporation**  
**Consolidated Balance Sheets**  
(in thousands)

	December 29, 2001	December 30, 2000
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 3,611	\$ 2,698
Accounts receivable, net of allowance for doubtful accounts of \$195 and \$163	4,755	6,112
Inventories	7,238	9,033
Taxes receivable	668	—
Other current assets	985	536
	<hr/>	<hr/>
Total current assets	17,257	18,379
Property, plant and equipment, net	43,555	44,984
Other assets	938	1,011
	<hr/>	<hr/>
<b>Total assets</b>	<b>\$ 61,750</b>	<b>\$ 64,374</b>
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities:		
Accounts payable	\$ 1,323	\$ 1,787
Accrued expenses and other liabilities	1,494	1,585
Long-term debt due within one year	1,405	1,779
Dividends payable	257	255
Taxes payable	—	315
	<hr/>	<hr/>
Total current liabilities	4,479	5,721
Long-term debt due after one year	9,258	10,233
Deferred income taxes	3,848	4,106
Other noncurrent liabilities	427	478
	<hr/>	<hr/>
Total liabilities	18,012	20,538
Commitments and contingencies (Note 14)	—	—
Shareholders' equity:		
Preferred stock, 2,000,000 shares authorized, par value \$0.001, no shares outstanding	—	—
Common stock, 20,000,000 shares authorized, par value \$0.001, 6,421,367 shares outstanding	6	6
Capital in excess of par value	24,502	24,486
Retained earnings	19,001	19,073
Accumulated other comprehensive income	229	271
	<hr/>	<hr/>
Total shareholders' equity	43,738	43,836
<b>Total liabilities and shareholders' equity</b>	<b>\$ 61,750</b>	<b>\$ 64,374</b>

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

**Sun Hydraulics Corporation**  
**Consolidated Statements of Operations**  
(in thousands, except per share data)

	For the year ended		
	December 29, 2001	December 30, 2000	January 1, 2000
<b>Net sales</b>	\$ 64,983	\$ 79,967	\$ 70,449
Cost of sales	50,358	58,502	54,033
<b>Gross profit</b>	<b>14,625</b>	<b>21,465</b>	<b>16,416</b>
Selling, engineering and administrative expenses	12,565	14,109	12,378
<b>Operating income</b>	<b>2,060</b>	<b>7,356</b>	<b>4,038</b>
Interest expense	878	1,114	954
Miscellaneous expense (income)	(130)	323	420
<b>Income before income taxes</b>	<b>1,312</b>	<b>5,919</b>	<b>2,664</b>
Income tax provision	362	1,998	833
<b>Net income</b>	<b>\$ 950</b>	<b>\$ 3,921</b>	<b>\$ 1,831</b>
<b>Basic net income per common share</b>	<b>\$ 0.15</b>	<b>\$ 0.61</b>	<b>\$ 0.29</b>
<b>Weighted average basic shares outstanding</b>	<b>6,392</b>	<b>6,385</b>	<b>6,380</b>
<b>Diluted net income per common share</b>	<b>\$ 0.14</b>	<b>\$ 0.60</b>	<b>\$ 0.28</b>
<b>Weighted average diluted shares outstanding</b>	<b>6,554</b>	<b>6,574</b>	<b>6,569</b>

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

**Sun Hydraulics Corporation**  
**Consolidated Statement of Shareholders' Equity and Comprehensive Income**  
**(in thousands)**

	Shares	Preferred Stock	Common stock	Capital in excess of par value	Retained earnings	Accumulated other comprehensive income	Total
Balance, December 31, 1998	6,361	\$ —	\$ 6	\$24,386	\$15,363	\$ 260	\$40,015
Exercise of Stock Options	22			75			75
Shares issued	2			13			13
Tax effect of non-qualified stock options				12			12
Dividends declared					(1,021)		(1,021)
Comprehensive income:							
Net income					1,831		1,831
Foreign currency translation adjustments						251	251
Comprehensive income							2,082
Balance, January 1, 2000	6,385	\$ —	\$ 6	\$24,486	\$16,173	\$ 511	\$41,176
Dividends declared					(1,021)		(1,021)
Comprehensive income:							
Net income					3,921		3,921
Foreign currency translation adjustments						(240)	(240)
Comprehensive income							3,681
Balance, December 30, 2000	6,385	\$ —	\$ 6	\$24,486	\$19,073	\$ 271	\$43,836
Shares issued, Restricted Stock	34						—
Shares issued, Unrestricted Stock	1			8			8
Shares issued, ESPP	1			8			8
Dividends declared					(1,022)		(1,022)
Comprehensive income:							
Net income					950		950
Foreign currency translation adjustments						(42)	(42)
Comprehensive income							908
Balance, December 29, 2001	6,421	\$ —	\$ 6	\$24,502	\$19,001	\$ 229	\$43,738

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

**Sun Hydraulics Corporation**  
**Consolidated Statements of Cash Flows**  
(in thousands)

	For the year ended		
	December 29, 2001	December 30, 2000	January 1, 2000
<b>Cash flows from operating activities:</b>			
Net income	\$ 950	\$ 3,921	\$ 1,831
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	5,426	5,594	5,043
(Gain)/Loss on disposal of assets	(2)	273	281
Compensation expense of stock options	—	—	13
Allowance for doubtful accounts	32	(33)	27
Allowance for slow moving inventory	314	24	28
Provision for deferred income taxes	(258)	(6)	468
(Increase) decrease in:			
Accounts receivable	1,325	181	(945)
Inventories	1,481	(926)	(34)
Income tax receivable	(668)	442	(687)
Other current assets	(449)	55	300
Other assets, net	30	19	30
Increase (decrease) in:			
Accounts payable	(464)	(925)	(165)
Accrued expenses and other liabilities	(91)	121	(601)
Dividends payable	2	—	—
Income taxes payable	(315)	315	—
Other liabilities	(51)	478	—
Net cash from operating activities	7,262	9,533	5,589
<b>Cash flows from investing activities:</b>			
Investment in acquisition and joint venture	—	(100)	—
Capital expenditures	(4,022)	(4,374)	(7,897)
Proceeds from dispositions of equipment	70	108	96
Net cash from investing activities	(3,952)	(4,366)	(7,801)
<b>Cash flows from financing activities:</b>			
Proceeds from debt	571	2,999	13,206
Repayment of debt	(1,920)	(5,329)	(10,769)
Proceeds from exercise of stock options	—	—	75
Proceeds from stock issued	16	—	—
Dividends to shareholders	(1,022)	(1,021)	(1,021)
Net cash from financing activities	(2,355)	(3,351)	1,491
Effect of exchange rate changes on cash and cash equivalents	(42)	(240)	251
Net increase (decrease) in cash and cash equivalents	913	1,576	(470)
Cash and cash equivalents, beginning of period	2,698	1,122	1,592
Cash and cash equivalents, end of period	\$ 3,611	\$ 2,698	\$ 1,122
<b>Supplemental disclosure of cash flow information:</b>			
Cash paid for:			
Interest	\$ 878	\$ 1,114	\$ 1,002
Income taxes	\$ 1,603	\$ 1,247	\$ 1,052

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

**SUN HYDRAULICS CORPORATION**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands except per share data)**

**1. BUSINESS**

Sun Hydraulics Corporation and its wholly-owned subsidiaries (the “Company”) 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, and China. Sun Hydraulics Corporation (“Sun Hydraulics”), with its main offices located in Sarasota, Florida, designs, manufactures and sells through independent distributors in the United States and other international markets. 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 Inchon, South Korea, operates a manufacturing and distribution facility. Sun Hydraulics Systems (Shanghai) Co., Ltd., (“Sun China”), a 50/50 joint venture between Sun Hydraulics and Links Lin, the owner of Sun Hydraulics Corporation’s Taiwanese distributor, is located in Shanghai, China, and operates a manufacturing and distribution facility.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

A summary of the significant accounting policies followed in the preparation of the Company’s consolidated financial statements is set forth below:

**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.

**Critical Accounting Policies and Estimates**

It is the Company’s accounting policy to report revenues when products are shipped and expenses when costs are incurred. The effect of material non-recurring events is provided for when they become known. 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 accounts receivable, inventory and goodwill. The following explains the basis and the procedure for each asset account where judgment and estimates are applied.

**Accounts Receivable**

The Company sells to most of its customers on a recurring basis, primarily through distributors with whom the Company maintains long-term relationships. As a result, bad debt experience is not material. The reserve for bad debts is determined on a specific identity basis by a review of those accounts that are significantly in arrears. There is no assurance that overdue accounts receivable balances of a distributor or a large direct sale customer will not develop financial difficulties and default on payment.

**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.

**Goodwill**

The Company acquired its Korean operations in September 1998 using the purchase method. As a result, goodwill is reflected on the consolidated balance sheet. A valuation based on the cash flow method was performed

at December 29, 2001, and it was determined that the value of the goodwill and the net assets in the accounts exceeded the estimated cash flow valuation. There is no assurance that the value of the acquired company will not decrease in the future due to changing business conditions.

### **Reclassification**

Certain amounts shown in the 1999 consolidated financial statements have been reclassified to conform with the 2000 and 2001 presentation. These reclassification did not have any effect on total assets, total liabilities, shareholders' equity or net income.

### **Management Estimates and Assumptions**

The preparation of financial statements in conformity with generally accepted accounting principles 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.

### **52 Week Fiscal Year**

Commencing in 1999, the Company implemented a fiscal year which ends on the Saturday nearest to the end of the month of December. Each quarter consists of two 4-week periods and one 5-week period.

### **Cash and Cash Equivalents**

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

### **Inventories**

Inventories are valued at the lower of cost or market, cost being determined on a first-in, first-out basis. Obsolete and excess inventory is evaluated and reserves are established based on specific criteria determined by management.

### **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	40

### **Valuation Assessment of Long-Lived Assets**

Management periodically evaluates long-lived assets for potential impairment and will reserve for impairment whenever events or changes in circumstances indicate the carrying amount of the assets may not be fully recoverable. As of December 29, 2001, management does not believe that any assets are impaired.

### **Other Assets**

Other assets consists of goodwill and an equity investment. Goodwill, which represents the excess of the purchase price of acquisition over the fair value of the net assets acquired and other acquisition costs are carried at cost, net of accumulated amortization and amortized on a straight-line basis over fifteen years. Beginning January 1, 2002, goodwill will be subject to at least an annual assessment for impairment by applying a fair-value-based test and will no longer be amortized. As of December 29, 2001, the Company had \$714 of goodwill, net of accumulated amortization of \$157. The equity investment represents the Company's joint venture in China. The equity investment was recorded at cost and has been adjusted for investment income or loss and dividend distributions for each quarterly period since its origin.

## Revenue Recognition

Sales are recognized when products are shipped. Sales incentives are granted to customers based upon the volume of purchases. These sales incentives are recorded at the time of sales as a reduction of gross sales.

## Foreign Currency Translation and Transactions

The Company follows the translation policy provided by Statement of Financial Accounting Standards No. 52, "Foreign Currency Translation." The Pound Sterling is the functional currency of Sun Ltd. The Euro is the functional currency of 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 monetary 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 in the component of shareholders' equity designated as "accumulated other comprehensive income." Realized gains and losses from foreign currency translations are included in miscellaneous (income) expense.

## Income Taxes

The Company follows the income tax policy provided by Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes." This Statement 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 and stock options.

## Stock-Based Compensation

The Company has elected to follow Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25) and related interpretations in accounting for its employee stock options. Under APB 25, because the exercise price of employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recorded. The Company has adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" (Statement 123).

## Earnings Per Share Computation

Earnings per share were computed as follows:

	2001	2000	1999
Net Income	\$ 950	\$3,921	\$1,831
Weighted-average shares outstanding — basic	6,392	6,385	6,380
Incremental shares from assumed conversions	162	189	189
Weighted-average shares outstanding — diluted	6,554	6,574	6,569
Earnings per share:			
Basic	\$ 0.15	\$ 0.61	\$ 0.29
Diluted	0.14	0.60	0.28

Outstanding diluted shares includes basic shares outstanding as well as outstanding, unexercised stock options.

## 3. FAIR VALUE OF INVESTMENTS

The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation. The following methods and assumptions were used to estimate the fair value of each class of financial instruments.

The carrying amounts of cash and cash equivalents, accounts receivable, other current assets, accounts payable, accrued expenses and other liabilities approximate fair value.

The carrying amount of long-term debt approximates fair value, as the interest rates on the debt approximate rates currently available to the Company for debt with similar terms and remaining maturities.

#### 4. INVENTORIES

	December 29, 2001	December 30, 2000
Raw materials	\$ 2,426	\$ 3,300
Work in process	2,773	3,145
Finished goods	2,039	2,588
Total	<u>\$ 7,238</u>	<u>\$ 9,033</u>

#### 5. PROPERTY, PLANT, and EQUIPMENT

	December 29, 2001	December 30, 2000
Machinery and equipment	\$ 42,871	\$ 41,443
Office furniture and equipment	6,904	8,755
Buildings	19,654	19,618
Leasehold and land improvements	1,149	1,038
Land	2,481	2,481
	<u>\$ 73,059</u>	<u>\$ 73,335</u>
Less: Accumulated depreciation	(32,381)	(29,476)
Construction in progress	2,877	1,125
Total	<u>\$ 43,555</u>	<u>\$ 44,984</u>

Depreciation expense for the years ended December 29, 2001, December 30, 2000, and January 1, 2000, totaled \$5,383, \$5,538, and \$4,993, respectively.

#### 6. OTHER ASSETS

	December 29, 2001	December 30, 2000
Goodwill, net of accumulated amortization of \$156 and \$113	\$ 715	\$ 758
Equity investment in joint venture	178	194
Other	45	59
Total	<u>\$ 938</u>	<u>\$ 1,011</u>

#### 7. ACCRUED EXPENSES AND OTHER LIABILITIES

	December 29, 2001	December 30, 2000
Compensation and benefits	\$ 672	\$ 1,161
Insurance	451	207
Other	371	217
Total	<u>\$ 1,494</u>	<u>\$ 1,585</u>



## 8. LONG-TERM DEBT

	December 29, 2001	December 30, 2000
\$3,872 three year note, secured by U.S. equipment, fixed interest rate of 5.3%, due December 23, 2005	\$ 3,872	\$ 5,167
\$4,425 10-year mortgage note with 20-year amortization schedule on the U.S. Manatee County facility, fixed interest rate of 6.5%, due December 1, 2011	4,412	4,575
\$2,400 12-year mortgage note on the German facility, fixed interest rate of 6.05%, due September 30, 2008	1,081	1,118
10-year notes, fixed interest rates ranging from 3.5-5.1%, secured by equipment in Germany, due between 2009 and 2011	1,058	811
Other	240	341
	<u>10,663</u>	<u>12,012</u>
Less amounts due within one year	(1,405)	(1,779)
Total	<u>\$ 9,258</u>	<u>\$ 10,233</u>

The remaining principal payments are due as follows: 2003 — \$1,464; 2004 — \$1,432; 2005 — \$1,511; 2006 — \$664; 2007 and thereafter — \$4,187.

The Company has three revolving lines of credit agreements totaling \$9,497 with various banks. Interest rates on these credit facilities are variable based on the prime rate in the U.S. and the equivalent rate in the U.K. and Germany, respectively. Lines of credit in Germany and the U.K. totaling \$2.0 million expire in 2002, while the line of credit in the U.S. expires in 2004. None of these arrangements contain pre-payment penalties. There were no outstanding balances on these credit facilities at December 29, 2001 or December 30, 2000.

Certain of these debt instruments are subject to debt covenants including 1) consolidated net working capital of not less than \$2,000 and a current ratio not less than 1.2:1.0 at all times during the term of the loan, 2) tangible net worth at a minimum of \$35,000 for the fiscal year 2001, with tangible net worth increases of at least 50% of net income for the immediately preceding fiscal year., and 3) consolidated debt service coverage ratio throughout the term of the loan at a minimum of 1.25:1.0 on a calendar year basis.

Effective December 1, 2001, the U.S. modified two existing loans in an effort to reduce the interest rate and adjust the term of each loan. Under the new terms, the mortgage loan on the Manatee county facility has a fixed interest rate of 6.5%, a 10-year term due on December 1, 2011, based on 20-year amortization, and had an outstanding balance of \$3.9 million at December 29, 2001. The equipment loan, secured by U.S. equipment, has a fixed interest rate of 5.3%, a 5-year term due on December 23, 2006, and had an outstanding balance of \$4.4 million at December 29, 2001.

## 9. DISTRIBUTIONS AND DIVIDENDS TO SHAREHOLDERS

The Company declared distributions of \$ 1,022, \$1,021, and \$1,021 to shareholders in 2001, 2000, and 1999, respectively.

On February 23, 2002, the Company declared a cash dividend of \$0.04 per share to

shareholders of record on March 31, 2002, payable on April 15, 2002. The Company declared quarterly dividends of \$0.04 per share to shareholders of record on the last day of each quarter in 2001 and 2000. These dividends were paid on the 15th day of each month following the date of declaration.

## 10. INCOME TAXES

Pretax income is taxed under the following jurisdictions:

	For the year ended		
	December 29, 2001	December 30, 2000	January 1, 2000
United States	\$ (283)	\$ 3,807	\$1,439
Foreign	1,595	2,112	1,325
<b>Total</b>	<b>\$ 1,312</b>	<b>\$ 5,919</b>	<b>\$2,764</b>

The income tax provision consists of the following:

	For the year ended		
	December 29, 2001	December 30, 2000	January 1, 2000
<b>Current tax expense:</b>			
United States	\$ 180	\$ 1,300	\$ 38
State and local	16	110	1
Foreign	424	594	326
<b>Total current</b>	<b>620</b>	<b>2,004</b>	<b>365</b>
<b>Deferred tax expense (benefit):</b>			
United States	(231)	—	573
State and local	(21)	—	51
Foreign	(6)	(6)	(156)
<b>Total deferred</b>	<b>(258)</b>	<b>(6)</b>	<b>468</b>
<b>Total income tax provision</b>	<b>\$ 362</b>	<b>\$ 1,998</b>	<b>\$ 833</b>

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

	For the year ended		
	December 29, 2001	December 30, 2000	January 1, 2000
U.S. federal taxes at statutory rate	\$ 446	\$ 2,012	\$ 940
Increase (decrease)			
Benefit of foreign sales corporation	—	(30)	(59)
Foreign income taxed at lower rate	(114)	(129)	(104)
Nondeductible items	36	70	27
State and local taxes, net	(6)	75	29
<b>Income tax provision</b>	<b>\$ 362</b>	<b>\$ 1,998</b>	<b>\$ 833</b>

Deferred tax assets and liabilities at fiscal year end are as follows:

	December 29, 2001	December 30, 2000	January 1, 2000
<b>Deferred taxes, non-current:</b>			
Assets			
Accrued expenses and reserves not currently deductible	\$ 354	\$ 161	\$ 109
Compensation expense recognized for book, not yet deductible for tax		329329	329
Deferred royalty income	158	177	—
	<u>841</u>	<u>667</u>	<u>438</u>
Deferred tax asset, non-current	841	667	438
Liabilities			
Depreciation	(4,689)	(4,773)	(4,563)
	<u>(4,689)</u>	<u>(4,773)</u>	<u>(4,563)</u>
Net deferred tax liability, non-current	\$ (3,848)	\$ (4,106)	\$(4,125)

## 11. STOCK OPTION PLANS

During 1996, the Company adopted the 1996 Stock Option Plan (the "Stock Option Plan"), which provides for the grant of incentive stock options and nonqualified stock options for the purchase of up to an aggregate of 1,000,000 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.

A summary of the Company's stock option plan for the years ended December 29, 2001, December 30, 2000, and January 1, 2000 is summarized as follows:

	Number of shares	Exercise price range	Weighted average exercise price
(share amounts are in thousands)			
Under option, December 31, 1998 (385 shares exercisable)	768	\$3.00-16.75	\$ 9.18
Exercised	(22)	\$ 3.00-3.47	\$ 3.39
Forfeitures	(80)	\$ 9.50	\$ 9.50
	<u>666</u>	<u>\$3.00-16.75</u>	<u>\$ 9.19</u>
Under option, January 1, 2000 (453 shares exercisable)	666	\$3.00-16.75	\$ 9.19
Granted	103	\$ 6.00-8.00	\$ 7.36
Forfeitures	(13)	\$10.0-16.75	\$ 15.19
	<u>756</u>	<u>\$3.00-16.75</u>	<u>\$ 7.84</u>
Under option, December 30, 2000 (526 shares exercisable)	756	\$3.00-16.75	\$ 7.84
Granted	25	\$ 7.00	\$ 7.00
Forfeitures	(105)	\$ 16.75	\$ 16.75
	<u>676</u>	<u>\$3.00-16.75</u>	<u>\$ 7.68</u>
Under option, December 29, 2001 (557 shares exercisable)	676	\$3.00-16.75	\$ 7.68

A summary of outstanding and exercisable options at December 29, 2001 is summarized as follows:

Options Outstanding				Options Exercisable	
Range of exercise prices	Number of shares	Weighted-average		Number of shares	Weighted average exercise price
		Remaining contractual life	Exercise price		
\$3.00	62,746	2.08	3.00	62,746	\$ 3.00
3.43-5.05	189,068	4.75	4.41	189,068	4.41
6.00	10,000	8.00	6.00	10,000	6.00
6.75	37,000	9.00	6.75	7,400	6.75
7.00	25,000	9.83	7.00	—	7.00
8.00	56,000	8.67	8.00	11,700	8.00
9.50	194,385	4.81	9.50	199,385	9.50
10.00	47,000	6.92	10.00	47,000	10.00
16.75	160,000	6.33	16.75	30,000	16.75

All options listed above vest over 5 years with a maximum term of 10 years.

During 2001, the Company adopted the 2001 Restricted Stock Plan, which provides for the grant of restricted stock of up to an aggregate of 275,000 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 non-forfeitable may not be less than six months. On the date of vesting, the Company records unearned compensation equal to the market value of the restricted shares on that date and, simultaneously, charges the unearned compensation to expense. The Company had 34,250 shares of restricted stock outstanding at December 29, 2001, and none of these shares were vested.

On July 12, 2001, the Company offered certain employees who held "underwater" options at a grant price of \$16.75 an opportunity to exchange those options for restricted stock on a 4:1 basis. This offer was not extended to Named Executive Officers. All employees who were made the offer accepted, and 105,000 options were cancelled in exchange for the issuance of 26,250 shares of restricted stock. One-half of the stock granted is restricted for one year and the other one-half for two years. None of the restricted stock issued in this transaction was vested at December 29, 2001.

During 2001, the Company adopted the Employee Stock Purchase Plan ("ESPP"), which became effective August 1, 2001. Most employees are eligible to participate. Employees who choose to participate are granted an option to purchase common stock at 85 percent of market value on the first or last day of the quarterly purchase period, whichever is lower. The ESPP authorizes the issuance, and the purchase by employees, of up to 325,000 shares of the common stock through payroll deductions. No employee is allowed to buy more than \$25,000 of common stock in any year, based on the market value of the common stock at the beginning of the purchase period. During 2001, employees purchased approximately 4,000 shares at a price of \$6.42, under the ESPP.

The Company has adopted the disclosure-only provisions of SFAS No. 123. Accordingly, no compensation cost has been recognized for the stock option plan other than for nonqualified stock options. Had compensation costs for the stock option plan been determined based on the fair value at the grant date for awards in 2001 and 2000 (there were no options granted in 1999) consistent with the provisions of SFAS No. 123, the Company's net income and earnings per share would have been reduced to the pro forma amounts indicated below:

	For the year ended		
	December 29, 2001	December 30, 2000	January 1, 2000
<b>Net income:</b>			
As reported	\$ 950	\$ 3,921	\$1,831
Pro forma	671	3,418	1,404
<b>Basic earnings per common share:</b>			
As reported	\$ 0.15	\$ 0.61	\$ 0.29
Pro forma	0.10	0.54	0.22
<b>Diluted earnings per common share:</b>			
As reported	\$ 0.14	\$ 0.60	\$ 0.28
Pro forma	0.10	0.52	0.21

These pro forma amounts may not be representative of future disclosures since the estimated fair value of stock options is amortized to expense over the vesting period and additional options may be granted in future years. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants in 2001, and 2000 (no options were granted in 1999): cumulative volatility of 40.0% for 2001 and 2000; dividend yields of 2.09%, and 2.41%, for 2001 and 2000, respectively; risk-free interest rate of 4.96%, and 5.11%, for 2001 and 2000, respectively; and expected terms of 6.50 years for 2001 and 3.00 to 6.50 years for 2000.

## 12. 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 \$715, \$1,195, and \$702 during 2001, 2000, and 1999, 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 \$215, \$110, and \$124 during 2001, 2000, and 1999, respectively.

## 13. SEGMENT REPORTING

The individual subsidiaries comprising the Company operate predominantly in a single industry as manufacturers and distributors of hydraulic components. Management bases its financial decisions by the geographical location of its operations. The subsidiaries are multinational with operations in the United States, the United Kingdom, Germany, and Korea. In computing earnings from operations for the foreign subsidiaries, no allocations of general corporate expenses, interest or income taxes have been made.

Identifiable assets of the foreign subsidiaries are those assets related to the operation of those companies. United States assets consist of all other operating assets of the Company.

Segment information is as follows:

	United States	Korea	United Kingdom	Germany	Elimination	Consolidated
<b>2001</b>						
Sales to unaffiliated customers	\$43,158	\$4,244	\$11,248	\$6,333	\$ —	\$ 64,983
Intercompany sales	10,326	—	1,544	37	(11,907)	—
Operating income (loss)	667	(20)	1,257	95	61	2,060
Identifiable assets	44,463	1,764	11,257	5,861	(1,595)	61,750
Depreciation and amortization	4,219	177	725	305	—	5,426
Capital expenditures	1,939	72	1,357	654	—	4,022
<b>2000</b>						
Sales to unaffiliated customers	\$55,488	\$5,537	\$13,026	\$5,916	\$ —	\$ 79,967
Intercompany sales	11,232	—	1,814	29	(13,075)	—
Operating income (loss)	5,021	307	1,834	281	(87)	7,356
Identifiable assets	48,717	1,966	10,285	4,757	(1,351)	64,374
Depreciation and amortization	4,283	166	874	271	—	5,594
Capital expenditures	3,213	450	762	(51)	—	4,374
<b>1999</b>						
Sales to unaffiliated customers	\$50,327	\$4,202	\$10,858	\$5,062	\$ —	\$ 70,449
Intercompany sales	8,354	—	2,016	43	(10,413)	—
Operating income	2,492	81	1,059	354	52	4,038
Identifiable assets	49,539	857	8,044	5,902	(268)	64,074
Depreciation and amortization	3,802	112	827	302	—	5,043
Capital expenditures	5,953	119	1,323	502	—	7,897

Net foreign currency gains (losses) reflected in results of operations were \$34, (\$39), and (\$168), for 2001, 2000, and 1999, respectively. Operating income (loss) is total sales and other operating income less operating expenses. In computing segment operating profit, interest expense and net miscellaneous income (expense) have not been deducted (added).

Included in U.S. sales to unaffiliated customers were export sales, principally to Canada and Asia, of \$5,964, \$7,134, and \$6,056, during 2001, 2000, and 1999, respectively.

#### 14. 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.

#### 15. NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, Statement of Financial Standards No. 141, "Business Combinations" ("SFAS 141"), and Statement of Financial Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"), were issued. SFAS 141 requires that all business combinations initiated after June 30, 2001 be accounted for using the purchase method of accounting, and that identifiable intangible assets acquired in a business combination be recognized as an asset apart from goodwill, if they meet certain criteria. The impact of the adoption of SFAS 141 on our reported operating results, financial position and existing financial statement disclosure is not expected to be material.

SFAS 142 applies to all goodwill and identified intangible assets acquired in a business combination. Under the new standard, all goodwill and indefinite-lived intangible assets, including that acquired before initial application of the standard, will not be amortized but will be tested for impairment at least annually. The new standard is effective for fiscal years beginning after December 15, 2001. Adoption of FAS 142 effective January 1, 2002 will result in the elimination of approximately \$60 of annual amortization, subject to the identification of separately recognized intangibles, which would continue to be amortized under the new rules. The Company does not expect to recognize any impaired goodwill as of January 1, 2002.

In July 2001, Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" (SFAS 143), which requires the recognition of a liability for an asset retirement obligation in the period in which it is incurred. When the liability is initially recorded, the carrying amount of the related long-lived asset is correspondingly increased. Over time, the liability is accreted to its present value and the related capitalized charge is depreciated over the useful life of the asset. SFAS 143 is effective for fiscal years beginning after June 15, 2002. The impact of the adoption of SFAS 143 on the Company's reported operating results, financial position and existing financial statement disclosure is not expected to be material.

In August 2001, Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"), was issued. This statement addresses the financial accounting and reporting for the impairment or disposal of long-lived assets and broadens the definition of what constitutes a discontinued operation and how results of a discontinued operation are to be measured and presented. The provisions of SFAS 144 are effective for financial statements issued for fiscal years beginning after December 15, 2001. The impact of the adoption of SFAS 144 on our reported operating results, financial position and existing financial statement disclosure is not expected to be material.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH  
ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None

**PART III.**

**ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY**

**Directors and Executive Officers**

The Board of Directors ("Board") of the Company currently consists of nine members. The Board is divided into three classes of Directors serving staggered three-year terms. Directors hold their positions until the annual meeting of shareholders in the year in which their term expires, and until their respective successors are elected and qualified or until their earlier resignation, removal from office or death. Executive Officers serve at the pleasure of the Board of Directors.

The following table sets forth the names and ages of the Company's Directors and Executive Officers and the positions they hold with the Company.

Name	Age	Position
Clyde G. Nixon	66	Chairman of the Board of Directors (term expiring in 2004)
Allen J. Carlson	51	President, Chief Executive Officer, Director (term expiring in 2003)
Jeffrey Cooper	60	Engineering Manager
Richard J. Dobbyn	58	Chief Financial Officer
Peter G. Robson	57	General Manager, Sun Hydraulics Limited
Marc Bertoneche	55	Director (term expiring in 2004), and a member of the Audit Committee
John S. Kahler	62	Director (term expiring in 2003), and a member of the Audit and Compensation Committees
Christine L. Koski	44	Director (term expiring in 2002)
Robert E. Koski	72	Director (term expiring in 2003), and a member of the Compensation Committee
Ferdinand E. Megerlin	62	Director (term expiring in 2004) and a member of the Compensation Committee
Taco van Tijn	78	Director (term expiring in 2002) and a member of the Audit Committee
David N. Wormley	62	Director (term expiring in 2002) and a member of the Compensation Committee



**Mr. Nixon** joined the Company in January 1988, and served as its President and Chief Executive Officer from November 1988 until May 2000, at which time he was named Chairman of the Board. From September 1985 to January 1988, he served as Vice President of Cross & Trecker Corporation and was President of Warner & Swasey Company, its wholly-owned subsidiary. From 1964 to 1985, he served in various management capacities with Brown & Sharpe Manufacturing Corporation, most recently as Vice President of its fluid power division and President of Double A Products Company, its wholly-owned subsidiary. Mr. Nixon is a graduate of Cornell University and the Harvard Business School, and is Past Chairman of the Board of the National Fluid Power Association. Mr. Nixon has over 33 years experience in the fluid power industry.

**Mr. Carlson** joined the Company in March 1996 and served as Vice President from January 2000 until May 2000, when he was named President and Chief Executive Officer. From October 1977 to March 1996, Mr. Carlson held various engineering, marketing and management positions for Vickers Incorporated, a wholly-owned subsidiary of Trinova Corporation. He is a graduate of the Milwaukee School of Engineering and the Advanced Management Program at the Harvard Business School. Mr. Carlson has over 30 years experience in the fluid power industry.

**Mr. Cooper** joined the Company in December 1990 as an engineer and has been Engineering Manager since September 1991. From August 1987 to December 1990, he was Engineering Manager, Mobile Valves, of Vickers, Incorporated, a wholly-owned subsidiary of Trinova Corporation, and from September 1979 to August 1986, he served as Vice President of Engineering for Double A Products Company. Mr. Cooper is an engineering graduate of Willesden College of Technology, London, England. Mr. Cooper has over 32 years experience in the fluid power industry.

**Mr. Dobbyn** joined the Company in October 1995 and was named Chief Financial Officer in July 1996. From June 1995 to October 1995, Mr. Dobbyn served as the Controller of Protek Electronics. From July 1994 to June 1995, he served as the Fiscal Director of a non-profit child care agency. From September 1984 to July 1994, Mr. Dobbyn was Senior Vice President-Finance and Administration for Loral Data Systems, formerly Fairchild Weston Systems, a Schlumberger company. Mr. Dobbyn is a Certified Public Accountant and a graduate of Boston College.

**Mr. Robson** has served as a Director of Sun Hydraulics Limited, Coventry, England, since May 1993, and has been employed by the Company as the General Manager of its United Kingdom operations since 1982. Mr. Robson is a Chartered Engineer and a graduate of Coventry University. Mr. Robson has over 34 years experience in the fluid power industry.

**Dr. Bertoneche** holds a chair as Professor in Business Administration at the University of Bordeaux in France, and has been on the Faculty of INSEAD, the European Institute of Business Administration in Fontainebleau, France, for more than 20 years. He has also been a visiting professor at Northwestern University and the Harvard Business School. Dr. Bertoneche has served as a Director of the Company since August 2001.

**Mr. Kahler** is the President, CEO and a Director of Cincinnati Incorporated. Mr. Kahler has served in various management positions with Cincinnati Incorporated since 1989. He is a graduate of Carnegie-Mellon University and the Harvard Business School. Mr. Kahler has served as a Director of the Company since May 1998.

**Ms. Koski** founded Koski Consulting Group, Inc. in June 2001 to work with start-up companies in the area of business strategy and marketing. In May 2001, Ms. Koski completed an Executive MBA degree from Southern Methodist University. From 1980 through 2001, Ms. Koski held various positions in sales, product management, purchasing, sales management, and international marketing management with Celanese A.G. or its former affiliates, including Celanese Ltd., Hoechst AG and Hoechst Celanese Chemical Group Ltd. Ms. Koski has served as a Director of the Company since May 2000.

**Mr. Koski** is a co-founder of the Company and served as its Chairman of the Board from the Company's inception in 1970 until his retirement in May of 2000. He was also its President and Chief Executive Officer from 1970 until November 1988. He is a graduate of Dartmouth College and past Chairman of the Board of the National Fluid Power Association. Mr. Koski has over 38 years experience in the fluid power industry, and has served as Chairman of the Fluid Power Systems and Technology Division of the American Society of Mechanical Engineers, and as a member of the Board of Directors of the National Association of Manufacturers.

**Dr. Megerlin** is Chairman and Joint Managing Director of Linde AG's Industrial Trucks and Hydraulics Division in Aschaffenburg, Germany. He is also Chairman of Linde's U.S. subsidiaries Linde Hydraulics Corp., Canfield, Ohio, and Linde Lift Truck Corp., Sommerville, South Carolina. Within VDMA, Germany's association for mechanical and plant engineering, Dr. Megerlin serves as Vice Chairman of the German Fluid Power Association. He is a mechanical engineer and received his Dipl-Ing (M.S.) degree from the Technical University of Karlsruhe, Germany, and his Dr.-Ing. (Ph.D.) from TH Aachen, Germany. Dr. Megerlin has over 30 years of experience in the fluid power industry. Dr. Megerlin has served as a Director of the Company since May 1998.

**Mr. van Tijn** is an attorney (solicitor), who has practiced law in London, England, since May 1977. Since June 1998, he has been a consultant with Rooks Rider. Mr. van Tijn has been a Director of the Company since February 1989, and the principal statutory officer of Sun Hydraulik Holdings Limited since January 1991.

**Dr. Wormley** is the Dean of the Engineering School at Pennsylvania State University, where he has taught since 1992. He previously was a member of the engineering faculty at the Massachusetts Institute of Technology. Dr. Wormley has served as a Director of the Company since December 1992. He is an engineer and earned his Ph.D. from the Massachusetts Institute of Technology.

No family relationships exist between any of the Company's Directors and executive officers, except that Ms. Koski is the daughter of Mr. Koski. There are no arrangements or understandings between Directors and any other person concerning service as a Director.

The Board of Directors has Audit and Compensation Committees. The Company does not have a Nominating Committee; instead, the entire Board of Directors functions as a Nominating Committee.

The Audit Committee was appointed in February 1997 and held four meetings in 2001. The functions of the Audit Committee are to recommend annually to the Board of Directors the appointment of the independent public accountants of the Company, to discuss and review the scope of and the fees for the prospective annual audit with the independent public accountants, to review the results thereof with the independent public accountants, to review and approve non-audit services of the independent public accountants, to review compliance with existing major accounting and financial policies of the Company, to review the adequacy of the financial organization of the Company, to review management's procedures and policies relative to the adequacy of the Company's internal accounting controls, to review compliance with federal and state laws relating to accounting practices and to review and approve (with the concurrence of a majority of the disinterested Directors of the Company) transactions, if any, with affiliated parties.

A Compensation Committee was formed in December 1996 to review, approve and recommend to the Board of Directors the terms and conditions of all employee benefit plans or changes thereto, to administer the Company's stock option plans and carry out the responsibilities required by the rules of the Securities and Exchange Commission. The Committee met four times during 2001.

The Board of Directors held four meetings during 2001. Each Director attended all of the meetings of the Board and of each committee of which he was a member in 2001.

## Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934 requires the Company's Directors, officers and holders of more than 10% of the Company's Common Stock to file with the Securities and Exchange Commission initial reports of ownership and reports of changes in ownership of Common Stock and any other equity securities of the Company. To the Company's knowledge, based solely upon a review of the forms, reports and certificates filed with the Company by such persons, all of them complied with the Section 16(a) filing requirements in 2001.

### ITEM 11. EXECUTIVE COMPENSATION

#### Summary Compensation

The following table is a summary of the compensation paid or accrued by the Company for the last three fiscal years for services in all capacities to the Company's Chief Executive Officer and each of its four most highly compensated executive officers who earned more than \$100,000 from the Company in 2001 under the rules of the Securities and Exchange Commission (the "Named Executive Officers").

Summary Compensation Table

Name and Principal Position	Year	Salary	Long Term Compensation Awards		Other Annual Compensation (1)
			Restricted Stock	Securities Underlying Options/SARs (#)	
Clyde G. Nixon, Chairman of the Board of Directors	2001	\$197,500	—	—	\$ 15,060(2)
	2000	205,200	—	—	19,816
	1999	205,200	—	—	11,703
Allen J. Carlson President and Chief Executive Officer	2001	\$177,975	—	—	\$ 9,305
	2000	157,500	—	—	10,230
	1999	122,000	—	—	2,850
Jeffrey Cooper Engineering Manager	2001	\$141,570	—	—	\$ 10,325
	2000	138,100	—	—	14,677
	1999	133,100	—	—	7,246
Richard J. Dobbyn Chief Financial Officer	2001	\$138,600	\$29,200	—	\$ 7,326
	2000	130,000	—	—	9,560
	1999	118,000	—	—	4,228
Peter G. Robson General Manager, Sun Hydraulics Limited	2001	\$103,752	—	—	\$ 20,652
	2000	98,709	—	—	17,647
	1999	95,106	—	—	17,469

(1) Except as otherwise noted, reflects primarily contributions made by the Company on behalf of the employee to the Company's 401(k) plan and excess life insurance premiums.

(2) Includes dues of \$750.

There were no Option/SAR grants in 2001 to the Company's Chief Executive Officer and each of its four most highly compensated executive officers who earned more than \$100,000 from the Company in 2001 under the rules of the Securities and Exchange Commission (the "Named Executive Officers").

**Aggregated Option/SAR Exercises in Last Fiscal Year  
and Fiscal Year End Option Values**

Name	Shares Acquired on Exercise (#)	Value Realized (\$)	Number of Securities Underlying Unexercised Options/SARs at Fiscal Year-End (#) Exercisable/ Unexercisable	Value of Unexercised in-the-Money Options/SARs at Fiscal Year-End (\$) Exercisable/ Unexercisable (1)
(a)	(b)	(c)	(d)	(e)
Clyde G. Nixon	—	—	157,546/16,000	\$ 724,952/0
Allen J. Carlson	—	—	31,200/28,800	\$ 76,500/0
Jeffrey Cooper	—	—	87,189/9,600	\$337,281/12,240
Richard J. Dobbyn	—	—	43,400/5,600	\$ 3,060/12,240
Peter G. Robson	—	—	98,995/4,000	\$435,178/30,600

(1) Based upon the December 29, 2001, closing stock price of \$7.65 per share, as reported on the Nasdaq National Market.

**Compensation Committee Interlocks and Insider Participation**

The members of the Committee in 2001 were John Kahler, Robert E. Koski, Ferdinand E. Megerlin, and David N. Wormley. Mr. Koski is an employee of the Company and formerly was an officer. See "Item 10. Directors and Executive Officers of the Company."

**Director Compensation**

Directors who are not officers of the Company are paid \$2,500 for attendance at each meeting of the Board of Directors, as well as each meeting of each Board Committee on which they serve when the committee meeting is not held within one day of a meeting of the Board of Directors. Directors also are reimbursed for their expenses incurred in connection with their attendance at such meetings.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN  
BENEFICIAL OWNERS AND MANAGEMENT**

The following table sets forth as of February 27, 2002, information as to the beneficial ownership of the Company's Common Stock by (i) each person or entity known by the Company to be the beneficial owner of more than 5% of the outstanding shares of Common Stock, (ii) each Director, (iii) Each Named Executive Officer of the Company, and (iv) all Directors and executive officers of the Company as a group.

Name and Address of Beneficial Owner (1)	Amount and Nature of Beneficial Ownership (2)	Percent of Class
Robert E. Koski (3)(4)(5)	2,608,921	40.6%
Beverly Koski (3)(4)(5)	2,608,921	40.6%
Christine L. Koski (3) 3525 Turtle Creek Boulevard #19B Dallas, Texas 75219	2,424,838	37.8%
Robert C. Koski (3)(5) 315 Sycamore Street Decatur, Georgia 30030	2,369,543	36.9%
Koski Family Limited Partnership 3525 Turtle Creek Boulevard #19B Dallas, Texas 75219	2,360,543	36.8%
Thomas L. Koski (3) Six New Street East Norwalk, Connecticut 06855	2,360,543	36.8%
Royce & Associates, Inc. (6) Royce Management Company Charles M. Royce 1414 Avenue of the Americas New York, NY 10019	625,600	9.7%
Bradley S. Ferrell (7) 5924 Cranbrook Way, #101 Naples, Florida 34112	471,142	7.3%
Robert S. and Ann R. Ferrell (8) 5924 Cranbrook Way, #101 Naples, Florida 34112	322,537	5.0%
Clyde G. Nixon (9)	249,295	3.9%
Peter G. Robson (10)	98,995	1.5%
Jeffrey Cooper (10)	87,189	1.4%
Richard J. Dobbyn (11)	48,900	*
Allen J. Carlson (12)	31,700	*
Taco van Tijn (13)	23,920	*
David N. Wormley (14)	3,940	*
John S. Kahler (15)	3,345	*
Ferdinand E. Megerlin	0	—
Marc Bertoneche	0	—
<b>All Directors and Executive Officers as a Group (12 persons)</b>	<b>3,220,500</b>	<b>50.2%</b>

\* Less than 1%.

- (1) Unless otherwise indicated, the address of each of the persons listed who own more than 5% of the Company's Common Stock is 1500 West University Parkway, Sarasota, Florida 34243.
- (2) This column sets forth shares of the Company's Common Stock which are deemed to be "beneficially owned" by the persons named in the table under Rule 13d-3 of the Securities and Exchange Commission. Except as otherwise indicated, the persons listed have sole voting and investment power with respect to all shares of Common Stock owned by them, except to the extent such power may be shared with a spouse.
- (3) Includes 2,333,543 shares owned by the Koski Family Limited Partnership, over which Christine L. Koski, Robert C. Koski, Thomas L. Koski, Robert E. Koski and Beverly Koski share voting and investment power as the general partners in the Partnership. Christine L. Koski, Robert C. Koski and Thomas L. Koski are the adult children of Robert E. Koski and Beverly Koski.
- (4) Includes 141,216 shares owned by Beverly Koski and 107,162 shares owned by Robert E. Koski. Beverly Koski is the spouse of Robert E. Koski.
- (5) Includes 27,000 shares owned by the Koski Family Foundation, Inc., over which Robert E. Koski, Beverly Koski and Robert C. Koski share voting and investment power.
- (6) According the Schedule 13G, filed February 12, 2002, by Royce & Associates, Inc. ("Royce"), Royce has sole voting and investment power with respect to the 625,600 shares.
- (7) Includes 38,205 shares owned by Mr. Ferrell, over which Mr. Ferrell has sole voting and investment power, and 432,937 shares beneficially owned by Mr. Ferrell in his capacity as trustee of various trusts, over which Mr. Ferrell has shared voting and investment power.
- (8) Includes 196,625 shares owned by Bradley S. Ferrell, Trustee of Robert S. Ferrell Flint Trust, dated 06/16/98, 125,312 shares owned by Bradley S. Ferrell, Trustee of Ann R. Ferrell Flint Trust dated 06/16/98, and 600 shares owned individually by Ann R. Ferrell. Robert S. Ferrell is the spouse of Ann R. Ferrell.
- (9) Includes 157,546 shares subject to currently exercisable options and 49,522 shares in the Joan Nixon Trust.
- (10) Represents shares subject to currently exercisable options.
- (11) Includes 43,400 shares subject to currently exercisable options.
- (12) Includes 35,200 shares subject to currently exercisable options.
- (13) Includes 3,920 shares subject to currently exercisable options, 2,500 shares owned by Mr. van Tijn's spouse, and 15,000 shares owned by Taco van Tijn Settlement, of which Mr. van Tijn and his spouse have a life interest.
- (14) Includes 2,940 shares subject to currently exercisable options.
- (15) Includes 500 shares owned by Mr. Kahler's spouse and 2,345 shares owned in trust, of which Mrs. Kahler is the trustee and beneficiary.

#### **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

None.

**PART IV**

**ITEM 14. EXHIBITS, FINANCIAL STATEMENT  
SCHEDULES AND REPORTS ON FORM 8-K**

- (a) 1. The following financial statements are included in Part II, Item 8:
- |   |    |
|---|----|
| Report of Independent Certified Public Accountants  | 23 |
| Consolidated Balance Sheets as of December 29, 2001, and December 30, 2000  | 24 |
| Consolidated Statements of Income for the years ended December 29, 2001, December 30, 2000, and January 1, 2000               | 25 |
| Consolidated Statements of Shareholders' Equity for the years ended December 29, 2001, December 30, 2000, and January 1, 2000 | 26 |
| Consolidated Statements of Cash Flows for the years ended December 29, 2001, December 30, 2000, and January 1, 2000           | 27 |
| Notes to Consolidated Financial Statements  | 28 |
- All other schedules are omitted as the required information is inapplicable or the information is presented in the consolidated financial statements and notes thereto in Item 8 above.
2. Exhibits:

Exhibit Number	Exhibit Description
3.1	Amended and Restated Articles of Incorporation of the Company (previously filed as Exhibit 3.1 in the Pre-Effective Amendment No. 4 to the Company's Registration Statement on Form S-1 filed on December 19, 1996 (File No. 333-14183) and incorporated herein by reference).
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4.2	Loan Agreement, dated March 29, 1996, between Suninco, Inc., Sun Hydraulics Corporation, and Northern Trust Bank of Florida, N.A. (previously filed as Exhibit 4.6 in the Company's Registration Statement on Form S-1 filed on October 15, 1996 (File No. 333-14183) and incorporated herein by reference).

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4.3	Security Agreement, dated March 29, 1996, between Suninco, Inc., Sun Hydraulics Corporation, and Northern Trust Bank of Florida, N.A. (previously filed as Exhibit 4.7 in the Company's Registration Statement on Form S-1 filed on October 15, 1996 (File No. 333-14183) and incorporated herein by reference).
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4.18	Renewal Master Note, dated February 3, 1998, in the amount of \$10,000,000.00, made by the Company to evidence a line of credit granted to the Company by Northern Trust Bank of Florida, N.A. (previously filed as Exhibit 4.22 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 1998 and incorporated herein by reference).
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4.20	Renewal Master Note, dated as of February 3, 1998, in the amount of \$4,965,524.51, between the Company and Northern Trust Bank of Florida, N.A. (previously filed as Exhibit 4.24 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 1998 and incorporated herein by reference).
4.21	Renewal Master Note, dated of February 3, 1999, in the amount of \$4,965,524.51, between the Company and Northern Trust Bank of Florida, N.A. (previously filed as Exhibit 4.25 to the Company's Quarterly Report on Form 10-Q for the quarter ended April 3, 1999 and incorporated herein by reference).

Exhibit Number	Exhibit Description
4.22	Renewal Master Note, dated July 23, 1999, in the amount of \$5,000,000.00 between the Company and Northern Trust Bank of Florida, N.A. (previously filed as Exhibit 4.26 to the Company's Quarterly Report on Form 10-Q for the quarter ended July 3, 1999 and incorporated herein by reference).
4.23	Loan Agreement, dated July 23, 1999, in the amount of \$7,500,000.00, between the Company and Northern Trust Bank of Florida, N.A. (previously filed as Exhibit 4.27 to the Company's Quarterly Report on Form 10-Q for the quarter ended July 3, 1999 and incorporated herein by reference).
4.24	Security Agreement, dated July 23, 1999, between the Company and Northern Trust Bank of Florida, N.A. (previously filed as Exhibit 4.28 to the Company's Quarterly Report on Form 10-Q for the quarter ended July 3, 1999 and incorporated herein by reference).
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4.30	Second Amended and Restated Loan Agreement (Line of Credit) by and among Northern Trust Bank of Florida, N.A., Sun Hydraulics Corporation, Sun Hydraulik Holdings Limited, Sun Hydraulics Limited and Sun Hydraulik GmbH dated December 1, 2001.
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23.1	Consent of Independent Certified Public Accountants.

+ Executive management contract or compensatory plan or arrangement.

(b) Reports on Form 8-K

1. Report on Form 8-K (dated October 10, 2001) filed October 12, 2001, announcing the appointment of Marc Bertoneche to the Company's Board of Directors.
2. Report on Form 8-K (dated November 7, 2001) filed November 9, 2001, announcing the Company's third quarter financial results.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Sarasota, State of Florida on March 15, 2002.

SUN HYDRAULICS CORPORATION

By: /s/ Allen J. Carlson

Allen J. Carlson, President and  
Chief Executive Officer

Pursuant to requirements of the Securities Exchange Act of 1934, this Report has been signed by the following persons on behalf of the Registrant and in the capacities indicated on March 15, 2002.

Signature	Title
<u>/s/ Allen J. Carlson</u> Allen J. Carlson	President, Chief Executive Officer and Director
<u>/s/ Richard J. Dobbyn</u> Richard J. Dobbyn	Chief Financial Officer (Principal Financial and Accounting Officer)
<u>/s/ John S. Kahler</u> John S. Kahler	Director
<u>/s/ Christine L. Koski</u> Christine L. Koski	Director
<u>/s/ Robert E. Koski</u> Robert E. Koski	Director
<u>/s/ Ferdinand E. Megerlin</u> Ferdinand E. Megerlin	Director
<u>/s/ Clyde G. Nixon</u> Clyde G. Nixon	Chairman of the Board of Directors
<u>/s/ Taco van Tijn</u> Taco van Tijn	Director

/s/ David N. Wormley

Director

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David N. Wormley

/s/ Marc Bertoneche

Director

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Marc Bertoneche

## EXHIBIT INDEX

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23.1	Consent of Independent Certified Public Accountants.

+ Executive management contract or compensatory plan or arrangement.

**CONSENT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS**

We hereby consent to the incorporation by reference in the Registration Statement on Form S-8 (No. 333-30801, 333-83269, 333-62816, and 333-66008) of Sun Hydraulics Corporation of our report dated March 1, 2002 relating to the financial statements, which appears in this Form 10-K.

PricewaterhouseCoopers LLP  
Tampa, Florida  
March 1, 2002

EXHIBIT 4.30

SECOND AMENDED AND RESTATED LOAN AGREEMENT  
[Revolving Line of Credit]

THIS SECOND AMENDED AND RESTATED LOAN AGREEMENT made on this day of January, 2002, by and among NORTHERN TRUST BANK OF FLORIDA, N.A. ("Lender"), SUN HYDRAULICS CORPORATION, a Florida corporation ("Borrower"), and SUN HYDRAULIK HOLDINGS LIMITED, a corporation organized and existing under the laws of the United Kingdom, SUN HYDRAULICS LIMITED, a corporation organized and existing under the laws of the United Kingdom, and SUN HYDRAULIK GMBH, a corporation organized and existing under the laws of Germany (collectively referred to herein as "Guarantors").

WITNESSETH:

WHEREAS, Lender has made a revolving line of credit loan to Borrower in the maximum principal amount of \$7,500,000.00 ("Loan"), which loan is evidenced by a modification renewal master note of even date herewith in the principal amount of \$7,500,000.00 ("Note"), and

WHEREAS, in connection with making the Loan, Borrower, Guarantors, and Lender entered into a loan agreement dated July 23, 2000, which was amended by an amended and restated loan agreement dated November 1, 2000 ("Original Loan Agreement"), and

WHEREAS, Borrower has requested Lender to modify certain terms of the Original Loan Agreement and other loan documents, and Lender has agreed to do so provided that Borrower modify the terms of the Original Loan Agreement by entering into this Second Amended and Restated Loan Agreement ("Loan Agreement"),

NOW, THEREFORE, in consideration of the premises and of the covenants and agreements herein contained, the parties hereto agree that the Original Loan Agreement is amended and restated in its entirety as follows:

1. LOAN TO BORROWER; EXECUTION OF LOAN DOCUMENTS. Lender agrees, in accordance with the terms of this Agreement, to make the Loan to Borrower. Concurrently herewith, Borrower has executed the Note, and other documents related to the Loan. Guarantors have each executed separate guaranties of the Loan ("Guaranties"). The Note, Guaranties, this Loan Agreement and other documents executed in connection with the Loan are collectively referred to herein as the "Loan Documents."

2. COSTS AND EXPENSES. Borrower shall pay all costs and expenses incurred in connection with preparation for, closing, and servicing the Loan including, without limitation, any legal fees, including the fees of Lender's counsel, intangible taxes, documentary taxes, recording costs, and document preparation fees.

3. REPRESENTATIONS AND WARRANTIES. To induce Lender to make the Loan, Borrower makes the following representations and warranties:

A. The financial information for Borrower and each Guarantor furnished to Lender in connection with Borrower's application for the Loan is complete and accurate. There has been no material nor adverse change in the financial condition of either Borrower or any guarantor or other obligor of the Loan from that reflected on such financial information.

B. Borrower is a duly organized corporation, existing and in good standing under the laws of the State of Florida, has corporate power to carry on the business in which it is engaged, and the obtaining and performing of the Loan has been duly authorized by all necessary actions of the board of directors and shareholders of the corporation under applicable law, and do not and will not violate any provisions of applicable law or any of its organizational documents.

C. The obtaining and performing of the Loan does not and will not result in a breach of, constitute a default under, require any consent under, or result in the creation of any lien, charge, or encumbrance upon any

property of Borrower pursuant to any instrument, order, or other agreement to which Borrower is a party or by which Borrower, any of its officers as such, or any of its property is bound.

D. There are no judgments, liens, encumbrances, or other security interests outstanding against Borrower or any of its subsidiaries, or any of their properties other than those disclosed to Lender in connection with Borrower's request for the Loan, nor is there any pending or, to Borrower's knowledge, threatened litigation that is reasonably likely to give rise to any such judgment, lien or encumbrance.

E. Neither Borrower nor any Guarantor, or any of their respective subsidiaries have incurred any debts, liabilities, or obligations (whether direct or contingent) nor committed themselves to incur any debts, liabilities, or obligations other than those disclosed to Lender in connection with Borrower's request for the Loan or shown on the financial statements submitted to Lender.

F. Neither Borrower nor any Guarantor, or any of their respective subsidiaries have made any assignment for the benefit of their creditors, admitted in writing their inability to pay their debts as they become due, filed a petition of bankruptcy or been adjudicated bankrupt or insolvent, or filed a petition seeking any reorganization, arrangement, composition, readjustment, liquidation, dissolution, receivership or similar relief under any statute, law or regulation.

G. There are no actions, suits or proceedings pending or, to Borrower's knowledge, threatened against or affecting Borrower or any Guarantor, or any of their respective subsidiaries, at law or in equity, or before or by any governmental authorities, and neither Borrower nor any Guarantor, or any of their respective subsidiaries is in default with respect to any order, writ, injunction, decree or demand of any court or any governmental authority.

H. The obtaining of the Loan and the consummation of all other transactions contemplated by the Loan Documents, and performance under the Loan Documents, will not result in any breach of, or constitute a default under, any mortgage, indenture, lease, loan, credit

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agreement or any other contract or instrument to which the Borrower or any of its subsidiaries is a party or by which their properties may be bound or affected.

4. GUARANTORS' REPRESENTATIONS AND WARRANTIES. To induce Lender to make the Loan, each Guarantor makes the following representations and warranties:

A. The financial information for each Guarantor furnished to Lender in connection with Borrower's application for the Loan is complete and accurate. There has been no material nor adverse change in the financial condition of any Guarantor from that reflected on such financial information.

B. The obtaining and performing of the Loan does not and will not result in a breach of, constitute a default under, require any consent under, or result in the creation of any lien, charge, or encumbrance upon any property of any Guarantor pursuant to any instrument, order, or other agreement to which a Guarantor is a party or by which a Guarantor or any of its property is bound, other than those created by the Loan Documents.

C. There are no judgments, liens, encumbrances, or other security interests outstanding against a Guarantor or any of its property other than those disclosed to Lender in connection with Borrower's request for the Loan, nor is there any pending or, to Guarantor's knowledge, threatened litigation that could or will give rise to any such judgment, lien or encumbrance.

D. No Guarantor has incurred any debts, liabilities, or obligations (whether direct or contingent) and has not committed to incur any

debts, liabilities, or obligations other than those disclosed to Lender in connection with Borrower's request for the Loan or shown on the financial statements submitted to Lender.

E. No Guarantor has made any assignment for the benefit of his creditors, admitted in writing its inability to pay its debts as they become due, filed a petition of bankruptcy or been adjudicated bankrupt or insolvent, or filed a petition seeking any reorganization, arrangement, composition, readjustment, liquidation, dissolution, receivership or similar relief under any statute, law or regulation.

F. There are no actions, suits or proceedings pending or, to Guarantor's knowledge, threatened against or affecting any Guarantor, at law or in equity, or before or by any governmental authorities, and Guarantor is not in default with respect to any order, writ, injunction, decree or demand of any court or any governmental authority.

G. The obtaining of the Loan and the consummation of all other transactions contemplated by the Loan Documents, and performance under the Loan Documents, will not result in any breach of, or constitute a default under, any mortgage, indenture, lease, loan, credit agreement or any other contract or instrument to which any Guarantor is a party or by which its property may be bound or affected.

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5. AFFIRMATIVE COVENANTS. Borrower will:

A. Preserve and keep in force all licenses, permits, and franchises necessary for the proper conduct of its business and duly pay and discharge all taxes, assessments, and governmental charges upon Borrower or against Borrower's property before the date on which penalties attach thereto, unless and to the extent only that the same shall be contested in good faith and by appropriate proceedings.

B. Furnish to Lender (i) within 90 days after the close of each fiscal year a consolidated annual profit and loss statement and balance sheet on Borrower and its subsidiaries reviewed by an independent certified public accountant who is satisfactory to Lender; (ii) within 30 days after filing each year, an executed copy of Borrower's Federal income tax return, and if any extensions have been filed, copies of each Extension Notice shall be furnished to Lender within 30 days of filing; and (iii) such other information reflecting the financial condition of Borrower and/or its subsidiaries as Lender may request from time to time.

C. Permit any representative or agent of Lender to examine and audit any or all of Borrower's books and records when requested by Lender.

D. Inform Lender immediately of any material adverse change in the financial condition of Borrower or any of its subsidiaries. Borrower will also promptly inform Lender of any litigation or threatened litigation which might substantially affect Borrower's financial condition.

E. Maintain Borrower's property and equipment in a state of good repair.

F. Maintain Borrower's net working capital, on a consolidated basis ("Net Working Capital") in an amount not less than \$2,000,000.00 and a current ratio ("Current Ratio") of not less than 1.2:1.0 at all times during the term of this Agreement. For the purposes of this Agreement, Net Working Capital shall mean the excess of Borrower's current assets over current liabilities, on a consolidated basis with its subsidiaries, which shall be determined in accordance with generally accepted accounting principles as consistently applied in the preparation of Borrower's previous financial statements, and Current Ratio shall mean the quotient of current assets divided by current liabilities, on a consolidated basis with its subsidiaries.

G. Maintain Borrower's Tangible Net Worth at a minimum of \$35,000,000.00 ("Minimum Tangible Net Worth") for the fiscal year 2001. Borrower's Minimum Tangible Net Worth as of each fiscal year-end thereafter

shall increase by at least 50% of Borrower's reported net income for the immediately preceding fiscal year. For the purposes of this Agreement, Tangible Net Worth shall mean (i) the aggregate amount of assets shown on the balance sheet of Borrower at any particular date (but excluding from such assets capitalized organization and development costs, capitalized interest, debt discount and expense, goodwill, patents, trademarks, copyrights, franchises, licenses, amounts due from officers, directors, stockholders and affiliates, and such other assets as are properly classified "intangible assets" under generally

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accepted accounting principles) less (ii) liabilities at such date, all computed in accordance with generally accepted accounting principles applied on a consistent basis.

H. Maintain Borrower's Total Liabilities to Tangible Net Worth ratio, on a consolidated basis with its subsidiaries throughout the term of the Loan at a minimum of 1.5:1.0 at all times during the term of this Agreement. For purposes of this Agreement, the term "Liabilities" shall mean Borrower's liabilities as computed in accordance with generally accepted accounting principles.

I. Maintain Borrower's debt service coverage ratio, on a consolidated basis with its subsidiaries ("Debt Service Coverage Ratio") throughout the term of the Loan at a minimum of 1.25:1.0 on a calendar year basis for all operations of the Borrower and its subsidiaries, computed as follows: net profits plus interest, plus depreciation, all divided by interest plus current maturities of long term debt and capitalized leases, plus unfunded capital expenditures and advances/withdrawals made to shareholders of Borrower and/or its subsidiaries.

6. GUARANTORS' AFFIRMATIVE COVENANTS. Each Guarantor will:

A. Furnish to Lender (i) within 90 days after the close of each calendar year, a financial statement, including income information and contingent liabilities, certified to Lender; (ii) within 30 days after filing each year, an executed copy of Guarantor's Federal income tax return; and (iii) such other information reflecting the financial condition of Guarantor as Lender may request from time to time. In the event such financial statements disclose a material, adverse change in the financial condition of Guarantor from the conditions set forth in any prior financial statement of Guarantor theretofore furnished to Lender, same shall constitute a default which shall entitle Lender to all of the rights and remedies provided for in the Note, or other Loan Documents.

B. Permit any representative or agent of Lender to examine and audit any or all of Guarantor's books and records when requested by Lender.

C. Inform Lender immediately of any material adverse change in the financial condition of Guarantor. Each Guarantor will also promptly inform Lender of any litigation or threatened litigation which might substantially affect such Guarantor's financial condition.

7. NEGATIVE COVENANTS. Neither Borrower nor any of its subsidiaries will, without prior written consent of Lender:

A. Collaterally assign, mortgage, pledge, encumber, or grant any security interest in any of its assets, whether now owned or hereafter acquired.

B. Enter into any merger or consolidation, or sell, lease, transfer, or otherwise dispose of all or any substantial part of its assets, whether now owned or hereafter acquired.

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C. Change the name in which it does business without providing Lender prior written notice thereof.

D. Move its principal place of business without giving written notice thereof to Lender at least 30 days prior thereto.

E. Incur any new debt whether secured or unsecured, except trade debt for the purchase of equipment which does not exceed \$100,000.00 for any item of equipment, and trade debt for the purchase of inventory.

F. Execute any guarantees or assumptions of any debt, or endorse any obligations, except that Borrower may guaranty any trade debt for the purchase of equipment which does not exceed \$100,000.00 for any item of equipment, and trade debt for the purchase of inventory which is incurred by a subsidiary of Borrower.

G. Enter into any asset sale/leaseback arrangement.

8. EVENTS OF DEFAULT. The Lender shall have the option to declare the entire unpaid balance due on the Loan without notice of any kind, if any of the following events occur:

A. Failure or omission to pay, within fifteen (15) days after payment is due, the Note (or any installment of principal or interest thereunder).

B. Default in the payment (other than payment of principal and interest) or performance of any obligation, covenant, agreement or liability contained or referred to in the Loan Agreement, Note, Guaranties, or any other Loan Document, or upon the existence or occurrence of any circumstance or event deemed a default under the Note or any other Loan Document, where such default is not cured within 30 days.

C. Any warranty, representation or statement made or furnished by Borrower or Guarantors for the purpose of inducing Lender to make the Loan proves to have been false in any material respect when made or furnished.

D. The default by Borrower or any party obligated under the Note or any guaranty thereof in the payment or performance of any obligation, covenant, agreement, or liability contained in any other mortgage, note, obligation or agreement held by Lender, including but not limited to that certain loan in the amount of \$3,871,754.35 made by Lender to Borrower, evidenced by a modification note of even date hereof, and that certain mortgage loan in the current principal amount of \$4,425,219.37, evidenced by a modification note of even date herewith.

E. The death, dissolution, termination of existence, insolvency, or business failure of Borrower, or any party obligated under the Note or Guaranties.

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F. The assignment for the benefit of creditors or the commencement of any proceedings in bankruptcy or insolvency by or against Borrower or by or against any person obligated under the Note or Guaranties.

G. The determination by Lender that a material adverse change has occurred in the financial condition of Borrower or any person obligated under the Note or any guaranty thereof, from the conditions set forth in the most recent financial statement of such person heretofore furnished to Lender or from the condition of such person as heretofore most recently disclosed to Lender in any manner.

H. The failure by Borrower or any party obligated under the Note or Guaranties thereof to make any payment of principal or interest when due under any obligation to any other creditor, if such failure continues beyond any applicable grace period; provided, however, that the aggregate outstanding obligation is in excess of \$100,000.00, and is not being contested in good faith.

I. Any substantial part of the inventory, equipment, or



other property of Borrower, real or personal, is damaged or destroyed and the damage or destruction is not covered by collectible insurance.

J. Borrower suffers or permits any lien, encumbrance, or security interest to arise or attach to any of Borrower's property, which is not satisfied within 30 days.

K. Any judgment is entered against Borrower that is not satisfied or appealed within 30 days.

L. Falsity in any material respect of, or any material omission in, any representation or statement made to Lender by or on behalf of Borrower or any person obligated under the Note or any guaranty thereof, in connection with the Loan.

9. REMEDIES UPON DEFAULT. Upon the occurrence, or the discovery by Lender of the occurrence, of any of the foregoing events, circumstances, or conditions of default, Lender shall have, in addition to its option to accelerate to maturity the full unpaid balance of the Loan, all of the rights and remedies under applicable law, and in addition shall have the following specific rights and remedies:

A. To exercise Lender's right of set-off against any account, fund, or property of any kind, tangible or intangible, belonging to Borrower which shall be in Lender's possession or under its control.

B. To cure such defaults, with the result that all costs and expenses incurred or paid by Lender in effecting such cure shall be additional charges on the Loan, shall bear interest at the highest rate permitted by law, and shall be payable upon demand.

10. ATTORNEYS' FEES AND COSTS. Borrower promises and agrees to pay all costs of collection and attorneys' fees, including fees for appellate proceedings, bankruptcy proceedings

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or otherwise, incurred or paid by Lender in enforcing this Agreement or preserving any right or interest of Lender hereunder.

11. WAIVER. No failure or delay on the part of Lender in exercising any power or right hereunder, and no failure of Lender to give Borrower notice of a default hereunder, shall operate as a waiver thereof, nor shall any single or partial exercise of any such right or power preclude any other or further exercise thereof or the exercise of any other right or power hereunder. No modification or waiver of any provision of this Agreement or any instrument executed pursuant hereto or consent to any departure by Borrower from this Agreement or such instrument shall in any event be effective unless the same shall be in writing, and such waiver or consent shall be effective only in the specific instance and for the particular purpose for which given.

12. BENEFIT. This Agreement shall be binding upon and inure to the benefit of Borrower and Lender and their respective successors and assigns. Lender may assign this Agreement in whole or in part. Borrower may not assign this Agreement or its obligations hereunder without Lender's written consent.

13. GOVERNING LAW. This Agreement shall be governed and construed in accordance with the laws of the State of Florida, and any litigation arising out of or relating to this Agreement or the Loan shall be commenced and conducted in the courts of the State of Florida or in the federal courts of the State of Florida.

IN WITNESS WHEREOF, the parties hereto have executed this Loan Agreement on the day and year first above written.

SUN HYDRAULICS CORPORATION,  
a Florida corporation

By: /s/ Allen Carlson

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Allen Carlson  
As its President

BORROWER

NORTHERN TRUST BANK OF FLORIDA, N.A.

By: /s/ Terence E. McGannon

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Terence E. McGannon  
As its Vice President

LENDER

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SUN HYDRAULIK HOLDINGS LIMITED,  
a corporation organized under the laws  
of the United Kingdom

By: /s/ Clyde G. Nixon

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Clyde G. Nixon  
As its Deputy Chairman

SUN HYDRAULIKS LIMITED,  
a corporation organized under the laws  
of the United Kingdom

By: /s/ Clyde G. Nixon

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Clyde G. Nixon  
As its Director

SUN HYDRAULIK GmbH,  
a corporation organized under the laws  
of Germany

By: /s/ Wulf Stegelmann

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Wulf Stegelmann  
As its Geschäftsführer

GUARANTORS

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EXHIBIT 4.31

MODIFICATION NOTE  
[Revolving Line of Credit]

\$7,500,000.00

Effective Date: December 1, 2001  
Execution Date: January 18, 2002

FOR VALUE RECEIVED, SUN HYDRAULICS CORPORATION ("Maker"), hereby promises, jointly and severally, to pay to the order of NORTHERN TRUST BANK OF FLORIDA, N.A. ("Lender") at 1515 Ringling Blvd., Sarasota, FL 34236 or at such other place as the holder hereof may from time to time designate in writing, the principal sum of Seven Million Five Hundred Thousand Dollars (\$7,500,000.00), or so much thereof as may be disbursed by Lender to Maker or for Maker's account from time to time, together with interest at the rate hereinafter specified on such indebtedness as shall from time to time remain unpaid, until paid in full, such principal and interest being payable in lawful money of the United States which shall be legal tender in payment of all debts at the time of payment. Interest will be calculated on the basis of a 365/360 method, which computes a daily amount of interest for a hypothetical year of 360 days, then multiplies such amount by the actual number of days elapsed in an interest calculating period.

Interest on the unpaid principal sum outstanding from time to time shall accrue at one of the following rates, as selected from time to time by Maker in accordance with this Note:

A. A variable rate of one percent (1.00%) per annum below the prime rate announced by Lender from time to time ("Prime Rate"). The interest rate will be adjusted accordingly on each date of change in the Prime Rate. The Prime Rate is not necessarily the lowest interest rate charged by Lender for monies loaned, and is intended solely as an index reference. If Maker does not affirmatively select an interest rate pursuant to subparagraph B below, the interest under this Note shall accrue pursuant to this subparagraph A.

B. A variable rate of two percent (2.00%) per annum above the Adjusted LIBOR Rate for either one month, two months, or three months (each an "Interest Period"), as selected by Maker, from time to time. The Adjusted LIBOR Rate means, with respect to any Interest Period, (i) the rate of interest per annum (rounded upward, if necessary, to the next higher 1/16th of one percent) determined by the Lender, in accordance with its customary general practice from time to time, to be the rate equal to the London InterBank Offered Rate (expressed as a percentage) for dollar deposits as would be quoted by the Lender for 11:00 a.m. London time, or as soon thereafter as practicable, on the second business day immediately preceding the first day of such Interest Period, for a term comparable to such Interest Period and (ii) as adjusted from time to time in the Lender's sole discretion for then applicable reserve requirements, deposit insurance assessment rates and other regulatory costs. In the event the London InterBank Offered Rate ceases to be available, Lender shall have the right to substitute another comparable index selected in Lender's discretion. Maker shall give to Lender five business days notice, in writing, if Maker desires to select the interest rate option based on the Adjusted LIBOR Rate pursuant to this subparagraph B, and such notice shall specify the Interest Period selected by Maker. The interest rate shall adjust five business days after Lender's receipt of such notice (which date shall be deemed the first day of the Interest Period) to equal a fixed rate computed in accordance with this subparagraph B, which fixed interest rate shall remain in effect for the Interest Period. At the end of

the Interest Period, and at the end of each successive Interest Period thereafter, the interest rate shall be adjusted and computed in accordance with this subparagraph B for the same Interest Period unless, at least five business days prior to the end of any Interest Period, Maker gives Lender written notice that Maker has selected a different interest rate in accordance with the terms of either subparagraph A above or this subparagraph B.

Interest shall be due and payable in arrears on the first day of each calendar month. The entire unpaid principal balance, together with accrued interest shall be due and payable August 15, 2004.

All payments made hereunder shall be applied first to accrued interest then due and owing; next to amounts expended by Lender to cure any default under this Note, (as hereinafter defined), or any other loan documents executed in connection herewith; next to charges, costs, expenses, or attorneys' fees then due and payable to Lender under this Note, or any other loan documents; and the balance, if any, to principal.

This Note may be prepaid, in whole or in part, at any time without penalty. All prepayments made hereunder shall be applied in the same manner as other payments made hereunder, as set forth above. The making of any prepayment shall not relieve Maker from the obligation to make the payments next due hereunder on a timely basis.

If any payment is more than fifteen (15) days late, Maker agrees to pay to Lender a late charge equal to five percent (5%) of the payment. Notwithstanding the foregoing, however, all payments shall be due and payable as of the dates set forth above, and the failure to make all payments when due shall constitute a default under this Note. The terms of this paragraph are not intended and shall not be deemed to create a grace period for payment.

This Note evidences a loan in the original principal amount of \$7,500,000.00; however, the actual indebtedness from time to time evidenced hereby shall be the sum of all advances made by Lender to Maker, less the aggregate amount of all principal repayments made under this Note by Maker to Lender. It is the intention hereof and the purpose of this Note to evidence a revolving line of credit against which Maker may draw and from which Lender will advance from time to time. Maker may repay the principal amount outstanding, in whole or in part, from time to time, and again draw against the line of credit, so that the principal amount outstanding hereunder may fluctuate in accordance with such advances and repayments, but the aggregate principal amount outstanding under this Note shall not at any time exceed the principal sum of \$7,500,000.00. Maker's right to draw principal amounts under this Note is conditioned upon Maker not being in default under this Note, or any other loan document executed in connection herewith.

Each and every party to this Note, whether as Maker, endorser, surety, guarantor, or otherwise ("Obligor"), hereby waives all rights of homestead and other exemptions granted by the constitution or laws of Florida, and further waives presentment, demand, protest, notice of dishonor, notice of nonpayment, notice of protest, and diligence in collection, and assents to the terms hereof and to any extension or postponement of the time for payment or any other indulgence. It is further specifically agreed that this Note or any part of the principal or interest due hereon may be renewed, modified or extended, in whole or in part, such modification to include but not be limited to changes

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in payment schedules and interest rates, from time to time by the holder of this Note, at the request of the then owners of all or part of any collateral for this Note, or at the request of any party bound hereon or who has assumed or may hereafter assume payment hereof, without the consent of or notice to other parties bound hereon and without releasing them from any liabilities then existing.

Each and every Obligor hereby consents that any real or personal property now or hereafter securing this Note, or any part of such security, may be released, exchanged, added to or substituted for by Lender, without in any way modifying, altering, releasing, affecting or limiting their respective liabilities or the lien of any mortgage or security agreement, and further agrees that Lender shall not be required first to institute any suit, or to exhaust any of its remedies against Maker or any other person or party liable or to become liable hereunder, in order to enforce payment of this Note, and further agrees that Maker or any other party liable hereunder may be released by Lender from any or all liability under this Note and such release shall in no way affect or modify the liability of the remaining parties hereto.

Each and every Obligor hereby consents and agrees that he is bound, jointly and severally, under the terms hereof and is subject to all of the provisions set forth herein as fully as though each was an undersigned hereof, and further consents and agrees that any Obligor may be sued by Lender without joining any other Obligor, whether primarily or secondarily liable.

Notwithstanding anything contained herein to the contrary or in other loan documents executed in connection herewith, no payee or holder of this Note shall ever be entitled to receive, collect or apply as interest on the obligation evidenced hereby any amount in excess of the maximum rate of interest permitted to be charged by applicable law and, in the event Lender or any holder hereof ever receives, collects or applies as interest any such excess, such amount which would be excessive interest shall be applied to the reduction of the principal sum; and, if the principal sum is paid in full, any remaining excess shall forthwith be paid to Maker. In determining whether or not the interest paid or payable under any specific contingency exceeds the highest lawful rate, Maker and Lender shall, to the maximum extent permitted under applicable law: (a) characterize any non-principal payment as an expense, fee or premium rather than as interest; (b) exclude voluntary prepayments and the effects thereof; and (c) spread the total amount of interest, or charges in the nature of interest, pursuant to applicable law.

As used herein, "Event of Default" shall mean the occurrence of any of the following events or conditions: (a) failure or omission to pay when due this Note (or any installment of principal or interest hereunder); (b) default in the payment (other than payment of principal and interest) or performance of any obligation, covenant, agreement or liability contained or referred to in this Note, or any other loan document executed in connection herewith, or upon the existence or occurrence of any circumstance or event deemed a default under this Note or any other loan document executed in connection herewith; (c) any warranty, representation or statement made or furnished by any Obligor to Lender for the purpose of inducing Lender to make the loan evidenced by this Note, proves to have been false in any material respect when made or furnished; (d) the default by Maker or any party obligated under this Note or any guaranty hereof or any affiliate of any of the foregoing ("Affiliated Companies") in the payment or performance of any obligation, covenant, agreement, or liability contained in any other mortgage, note, obligation or agreement held by Lender including but not limited to those certain loans in the current principal amounts of

\$3,871,754.35 and \$4,425,219.37 evidenced by notes executed by Maker on even date herewith; (e) the death, dissolution, termination of existence, insolvency, or business failure of any Obligor; (f) the appointment of a receiver of any property of an obligor; (g) the assignment for the benefit of creditors or the commencement of any proceedings in bankruptcy or insolvency by or against any Obligor; (h) the determination by Lender that a material adverse change has occurred in the financial condition of any Obligor from the conditions set forth in the most recent financial statement of such Obligor heretofore furnished to Lender or from the condition of such Obligor as heretofore most recently disclosed to Lender in any manner; (i) the failure by Maker or any party obligated under this Note or any guaranty hereof to make any payment of principal or interest when due under any obligation to any other creditor; (j) any substantial part of the inventory, equipment, or other property of Maker, real or personal, is damaged or destroyed and the damage or destruction is not covered by collectible insurance; (k) Maker suffers or permits any lien, encumbrance, or security interest to arise or attach to any of Maker's property, which is not satisfied within 30 days; (l) any judgment is entered against Maker that is not satisfied or appealed within 30 days; or (m) falsity in any material respect of, or any material omission in, any representation or statement made to Lender by or on behalf of any Obligor in connection with the loan evidenced by this Note. Upon the occurrence of any such default or at any time thereafter, subject to the grace period, if any, provided in this Note, Lender may, at its option, declare the whole amount of principal and interest provided for in and by this Note, and any and all other secured indebtedness, immediately due and payable without demand or notice of any kind to any person, and the same thereupon shall become immediately due, payable and collectible (by foreclosure or otherwise) at once and without notice to Maker. Any default hereunder shall constitute a default under any other mortgage, note, obligation or agreement of Maker or any Affiliated Company held by Lender. The agreements contained in this paragraph to create cross-defaults under all mortgages, notes, obligations and agreements between Maker, and any Affiliated Company, and Lender, whether currently existing or hereafter created, in the event of default under one or more of such mortgages, notes, obligations or agreements are a material and specific inducement and consideration for the making by Lender of the loan

evidenced by this Note.

Notwithstanding the provisions of the foregoing paragraph to the contrary, in the event of a non-monetary default of the type set forth in subsections (b), (d), (h) or (j) of the foregoing paragraph, then prior to Lender precipitating to maturity the full unpaid balance of this Note or otherwise exercising any rights available to Lender under the terms of this Note or any other loan document executed in connection herewith, Lender shall give written notice to Maker and Maker shall have a period of thirty (30) days from the date such notice is given in which to cure such default; provided, however, if such default cannot, with due diligence, be cured within said 30 day period, and such default does not threaten to impair Lender's security for this Note, then the 30 day period shall be extended for such period as may be reasonably necessary to complete the curing of same, provided that Maker proceeds with all due diligence and continuity to cure the default. Notice required hereunder may, at the option of Lender, be given by either certified mail, registered mail, regular mail, facsimile transmission, Federal Express or other express courier, or by personal delivery, and shall be deemed given when mailed, transmitted, placed with the courier or delivered to Maker, whichever is first. In the event the default is not cured within the time provided, then Lender shall have the right to accelerate this Note and proceed to enforce this Note and the loan documents, without further notice to Maker.

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It is expressly agreed that upon the occurrence of an Event of Default, or if Lender shall deem itself insecure (because the prospect of timely payments is impaired, because the value of Lender's security is impaired, because the prospect of performance of any covenant or agreement under this Note, or any other loan document is impaired, because of any change of circumstance which adversely affects any matters originally considered by Lender in making the loan, or otherwise), then or at any time thereafter at the option of Lender, the whole of the principal sum remaining unpaid hereunder, together with all accrued and unpaid interest thereon, shall become due and payable immediately without notice, anything contained herein to the contrary in any way notwithstanding, and in any such event Lender shall have the right to set-off against this Note all money owed by Lender in any capacity to any Obligor, whether or not due, and Lender shall be deemed to have exercised such right of set-off and to have made a charge against any such money immediately upon the occurrence of an Event of Default although made or entered on the books subsequent thereto. From and after an Event of Default, the interest rate on the entire outstanding principal balance hereunder shall accrue at the highest rate permitted to be charged by applicable law ("Default Rate"). In the event the Default Rate shall be applicable and Lender has not accelerated this Note, the amount of each payment otherwise due hereunder shall be increased to an amount equal to the regular amount of the principal installment due hereunder, plus accrued interest at the Default Rate. Any judgment rendered on this Note shall bear interest at the Default Rate.

Each Obligor shall be obligated to pay as part of the indebtedness evidenced by this Note all costs of collection, whether or not a suit is brought, including any reasonable attorneys' fees that may be incurred in the collection or enforcement hereof. The term "attorneys' fees" shall include but not be limited to any such fees incurred in any appellate or related ancillary or supplementary proceedings, whether before or after final judgment related to the enforcement or defense of this Note.

If at any time any federal, state, county or municipal government or agency thereof shall impose any documentary stamp tax, intangible tax, or any other type of tax upon this Note, or upon the indebtedness evidenced hereby (other than any federal, state or local income tax imposed upon Lender), then Maker shall pay same within fifteen (15) days after demand by Lender, together with any interest and penalties thereon.

Time is of the essence of this Note. The remedies of Lender as provided herein, or any other loan document executed in connection herewith, shall be cumulative and concurrent, and may be pursued singularly, successively or together, at the sole discretion of Lender, and may be exercised as often as occasion therefor shall arise. No act or omission of Lender, including specifically any failure to exercise any right, remedy or recourse, shall be deemed to be a waiver or release of such right, remedy or recourse, and any

waiver or release may be effected only through a written document executed by Lender and then only to the extent specifically recited therein. A waiver or release with respect to any one event shall not be construed as continuing as a bar to, or as a waiver or release of, any subsequent right, remedy or recourse as to any subsequent event.

The term "Lender" where used herein shall include Lender's successors and assigns. The term "Maker" shall include each person signing this Note, jointly and severally, and their respective heirs, successors and assigns. The term "Obligor" shall include Maker and every person who is an endorser, guarantor, or surety of this Note, or who is otherwise a party hereto, and their respective

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heirs, successors and assigns. The terms "person" and "party" shall include individuals, firms, associations, joint ventures, partnerships, estates, trusts, business trusts, syndicates, fiduciaries, corporations, and all other groups or combinations. Whenever used herein, the singular number shall include the plural, the plural the singular, and the use of any gender shall include all genders. This Note shall be construed under Florida law.

This note amends and replaces that certain promissory note dated July 23, 2000 ("Original Note").

IN WITNESS WHEREOF, Maker has caused this Note to be duly executed and delivered as of the date first above written.

Maker's Address:

1500 University Parkway                      SUN HYDRAULICS CORPORATION  
Sarasota, FL 34243                      a Florida Corporation

By:    /s/ Tricia Fulton  
-----  
Tricia Fulton  
As its Corporate Controller

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EXHIBIT 4.32

AMENDED AND RESTATED LOAN AGREEMENT  
[Mortgage Loan]

THIS AMENDED AND RESTATED LOAN AGREEMENT executed on this \_\_\_\_ day of January, 2002, and effective December 1, 2001, by and among NORTHERN TRUST BANK OF FLORIDA, N.A. ("Lender"), SUN HYDRAULICS CORPORATION, a Florida corporation ("Borrower").

WITNESSETH:

WHEREAS, Lender has made a loan to Borrower ("Loan"), which loan is evidenced by a modification note of even date herewith in the principal amount of \$4,425,219.37 ("Note"), and

WHEREAS, the Loan is secured by a certain real estate mortgage recorded in Official Records Book 1494, page 6860, Public Records of Manatee County, Florida, as modified ("Mortgage"), and

WHEREAS, in connection with making the Loan, Borrower and Lender entered into a loan agreement dated June 14, 1996 ("Original Loan Agreement"), and

WHEREAS, Borrower has requested Lender to modify certain terms of the Original Loan Agreement and other loan documents, and Lender has agreed to do so provided that Borrower modify the terms of the Original Loan Agreement by entering into this Amended and Restated Loan Agreement ("Loan Agreement"),

NOW, THEREFORE, in consideration of the premises and of the covenants and agreements herein contained, the parties hereto agree that the Original Loan Agreement is amended and restated in its entirety as follows:

1. LOAN TO BORROWER; EXECUTION OF LOAN DOCUMENTS. Lender agrees, in accordance with the terms of this Agreement, to make the Loan to Borrower. Concurrently herewith, Borrower has executed the Note, and a Modification Agreement ("Modification Agreement"), and other documents related to the Loan. The Note, The Mortgage (as amended), this Loan Agreement and other documents executed in connection with the Loan are collectively referred to herein as the "Loan Documents."

2. COSTS AND EXPENSES. Borrower shall pay all costs and expenses incurred in connection with preparation for, closing, and servicing the Loan including, without limitation, any legal fees, including the fees of Lender's counsel, intangible taxes, documentary taxes, recording costs, and document preparation fees.

3. REPRESENTATIONS AND WARRANTIES. To induce Lender to make the Loan, Borrower makes the following representations and warranties:

A. The financial information for Borrower and each guarantor or other obligor furnished to Lender in connection with Borrower's application for the Loan is complete

and accurate. There has been no material nor adverse change in the financial condition of either Borrower or any guarantor or other obligor of the Loan from that reflected on such financial information.

B. Borrower is a duly organized corporation, existing and in good standing under the laws of the State of Florida, has corporate power to carry on the business in which it is engaged, and the obtaining and performing of the Loan has been duly authorized by all necessary actions of the board of directors and shareholders of the corporation under applicable law, and do not and will not violate any provisions of law or any of its organizational documents.

C. The obtaining and performing of the Loan does not and will not result in a breach of, constitute a default under, require any consent under, or result in the creation of any lien, charge, or encumbrance upon any property of Borrower pursuant to any instrument, order, or other agreement to which Borrower is a party or by which Borrower, any of its officers as such, or

any of its property is bound.

D. There are no judgments, liens, encumbrances, or other security interests outstanding against Borrower or any of its subsidiaries, or any of their properties other than those disclosed to Lender in connection with Borrower's request for the Loan, nor is there any pending or threatened litigation that could or will give rise to any such judgment, lien or encumbrance.

E. Neither Borrower nor any of its subsidiaries have incurred any debts, liabilities, or obligations (whether direct or contingent) nor committed themselves to incur any debts, liabilities, or obligations other than those disclosed to Lender in connection with Borrower's request for the Loan or shown on the financial statements submitted to Lender.

F. Neither Borrower nor any of its subsidiaries have made any assignment for the benefit of their creditors, admitted in writing their inability to pay their debts as they become due, filed a petition of bankruptcy or been adjudicated bankrupt or insolvent, or filed a petition seeking any reorganization, arrangement, composition, readjustment, liquidation, dissolution, receivership or similar relief under any statute, law or regulation.

G. There are no actions, suits or proceedings pending or, threatened against or affecting Borrower or any of its subsidiaries, the Collateral or any guarantor or obligor on the Loan, or involving the validity or enforceability of the Mortgage or the priority of the lien thereof, at law or in equity, or before or by any governmental authorities, and neither Borrower nor any of its subsidiaries is in default with respect to any order, writ, injunction, decree or demand of any court or any governmental authority.

H. The obtaining of the Loan and the consummation of all other transactions contemplated by the Loan Documents, and performance under the Loan Documents, will not result in any breach of, or constitute a default under, any mortgage, indenture, security agreement, lease, loan, credit agreement or any other contract or instrument to which the Borrower or any of its subsidiaries is a party or by which their properties may be bound or affected.

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4. AFFIRMATIVE COVENANTS. Borrower will:

A. Preserve and keep in force all licenses, permits, and franchises necessary for the proper conduct of its business and duly pay and discharge all taxes, assessments, and governmental charges upon Borrower or against Borrower's property before the date on which penalties attach thereto, unless and to the extent only that the same shall be contested in good faith and by appropriate proceedings.

B. Furnish to Lender (i) within 90 days after the close of each fiscal year a consolidated annual profit and loss statement and balance sheet on Borrower and its subsidiaries reviewed by an independent certified public accountant who is satisfactory to Lender; (ii) within 30 days after filing each year, an executed copy of Borrower's Federal income tax return, and if any extensions have been filed, copies of each Extension Notice shall be furnished to Lender within 30 days of filing; and (iii) such other information reflecting the financial condition of Borrower and/or its subsidiaries as Lender may request from time to time.

C. Permit any representative or agent of Lender to examine and audit any or all of Borrower's books and records when requested by Lender.

D. Inform Lender immediately of any material adverse change in the financial condition of Borrower or any of its subsidiaries. Borrower will also promptly inform Lender of any litigation or threatened litigation which might substantially affect Borrower's financial condition.

E. Maintain Borrower's property and equipment in a state of good repair.

F. Maintain Borrower's net working capital, on a

consolidated basis ("Net Working Capital") in an amount not less than \$2,000,000.00 and a current ratio ("Current Ratio") of not less than 1.2:1.0 at all times during the term of this Agreement. For the purposes of this Agreement, Net Working Capital shall mean the excess of Borrower's current assets over current liabilities, on a consolidated basis with its subsidiaries, which shall be determined in accordance with generally accepted accounting principles as consistently applied in the preparation of Borrower's previous financial statements, and Current Ratio shall mean the quotient of current assets divided by current liabilities, on a consolidated basis with its subsidiaries.

G. Maintain Borrower's Tangible Net Worth at a minimum of \$35,000,000.00 ("Minimum Tangible Net Worth") for the fiscal year 2001. Borrower's Minimum Tangible Net Worth as of each fiscal year-end thereafter shall increase by at least 50% of Borrower's reported net income for the immediately preceding fiscal year. For the purposes of this Agreement, Tangible Net Worth shall mean (i) the aggregate amount of assets shown on the balance sheet of Borrower at any particular date (but excluding from such assets capitalized organization and development costs, capitalized interest, debt discount and expense, goodwill, patents, trademarks, copyrights, franchises, licenses, amounts due from officers, directors, stockholders and affiliates, and such other assets as are properly classified "intangible assets" under generally

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accepted accounting principles) less (ii) liabilities at such date, all computed in accordance with generally accepted accounting principles applied on a consistent basis.

H. Maintain Borrower's Total Liabilities to Tangible Net Worth ratio, on a consolidated basis with its subsidiaries throughout the term of the Loan at a minimum of 1.5:1.0 at all times during the term of this Agreement. For purposes of this Agreement, the term "Liabilities" shall mean Borrower's liabilities as computed in accordance with generally accepted accounting principles.

I. Maintain Borrower's debt service coverage ratio, on a consolidated basis with its subsidiaries ("Debt Service Coverage Ratio") throughout the term of the Loan at a minimum of 1.25:1.0 on a calendar year basis for all operations of the Borrower and its subsidiaries, computed as follows: net profits plus interest, plus depreciation, all divided by interest plus current maturities of long term debt and capitalized leases, plus unfunded capital expenditures and advances/withdrawals made to shareholders of Borrower and/or its subsidiaries.

5. NEGATIVE COVENANTS. Neither Borrower nor any of its subsidiaries will, without prior written consent of Lender:

A. Collaterally assign, mortgage, pledge, encumber or grant any security interest in any of its assets, whether now owned or hereafter acquired.

B. Enter into any merger or consolidation, or sell, lease, transfer, or otherwise dispose of all or any substantial part of its assets, whether now owned or hereafter acquired.

C. Change the name in which it does business.

D. Move its principal place of business without giving written notice thereof to Lender at least 30 days prior thereto.

E. Incur any new debt whether secured or unsecured, except trade debt for the purchase of equipment which does not exceed \$100,000.00 for any item of equipment, and trade debt for the purchase of inventory.

F. Execute any guarantees or assumptions of any debt, or endorse any obligations, except that Borrower may guaranty any trade debt for the purchase of equipment which does not exceed \$100,000.00 for any item of equipment, and trade debt for the purchase of inventory which is incurred by a subsidiary of Borrower.

G. Enter into any asset sale/leaseback arrangement.

6. EVENTS OF DEFAULT. The Lender shall have the option to declare the entire unpaid balance due on the Loan without notice of any kind, if any of the following events occur:

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A. Failure or omission to pay, within fifteen (15) days after payment is due, the Note (or any installment of principal or interest thereunder).

B. Default in the payment (other than payment of principal and interest) or performance of any obligation, covenant, agreement or liability contained or referred to in the Mortgage, Note, this Loan Agreement, or any other Loan Document, or upon the existence or occurrence of any circumstance or event deemed a default under the Note or any other Loan Document.

C. Any warranty, representation or statement made or furnished by Borrower for the purpose of inducing Lender to make the Loan proves to have been false in any material respect when made or furnished.

D. A default under any other mortgage on the Collateral (whether such other mortgage be held by Lender or by a third party).

E. The institution of foreclosure proceedings of another mortgage or lien of any kind on the Collateral (whether such other mortgage or lien be held by Lender or by a third party).

F. The default by Borrower or any party obligated under the Note or any guaranty thereof in the payment or performance of any obligation, covenant, agreement, or liability contained in any other mortgage, note, obligation or agreement held by Lender, including but not limited to that certain revolving line of credit loan in the amount of \$7,500,000.00 made by Lender to Borrower, evidenced by a modification note of even date hereof, and that certain loan in the current principal amount of \$3,871,754.35, evidenced by a modification note of even date herewith.

G. The death, dissolution, termination of existence, insolvency, or business failure of Borrower or any party obligated under the Note or any guaranty thereof.

H. The appointment of a receiver of any part of the Collateral.

I. The assignment for the benefit of creditors or the commencement of any proceedings in bankruptcy or insolvency by or against Borrower or by or against any person obligated under the Note or any guaranty thereof.

J. The determination by Lender that a material adverse change has occurred in the financial condition of Borrower or any person obligated under the Note or any guaranty thereof, from the conditions set forth in the most recent financial statement of such person heretofore furnished to Lender or from the condition of such person as heretofore most recently disclosed to Lender in any manner.

K. The failure by Borrower or any party obligated under the Note or any guaranty thereof to make any payment of principal or interest when due under any obligation to any other creditor, if such failure continues beyond any applicable grace period.

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L. Any substantial part of the inventory, equipment, or other property of Borrower, real or personal, is damaged or destroyed and the damage or destruction is not covered by collectible insurance.

M. Borrower suffers or permits any lien, encumbrance, or security interest to arise or attach to any of Borrower's property, which is not satisfied within 30 days.

N. Any judgment is entered against Borrower that is not satisfied or appealed within 30 days.

O. Falsity in any material respect of, or any material omission in, any representation or statement made to Lender by or on behalf of Borrower or any person obligated under the Note or any guaranty thereof, in connection with the Loan.

7. REMEDIES UPON DEFAULT. Upon the occurrence, or the discovery by Lender of the occurrence, of any of the foregoing events, circumstances, or conditions of default, Lender shall have, in addition to its option to accelerate to maturity the full unpaid balance of the Loan, all of the rights and remedies under applicable law, and in addition shall have the following specific rights and remedies:

A. To exercise Lender's right of set-off against any account, fund, or property of any kind, tangible or intangible, belonging to Borrower which shall be in Lender's possession or under its control.

B. To cure such defaults, with the result that all costs and expenses incurred or paid by Lender in effecting such cure shall be additional charges on the Loan, shall bear interest at the highest rate permitted by law, and shall be payable upon demand, and shall be secured by the Mortgage and other Loan Documents.

8. ATTORNEYS' FEES AND COSTS. Borrower promises and agrees to pay all costs of collection and attorneys' fees, including fees for appellate proceedings, bankruptcy proceedings or otherwise, incurred or paid by Lender in enforcing this Agreement or preserving any right or interest of Lender hereunder.

9. WAIVER. No failure or delay on the part of Lender in exercising any power or right hereunder, and no failure of Lender to give Borrower notice of a default hereunder, shall operate as a waiver thereof, nor shall any single or partial exercise of any such right or power preclude any other or further exercise thereof or the exercise of any other right or power hereunder. No modification or waiver of any provision of this Agreement or any instrument executed pursuant hereto or consent to any departure by Borrower from this Agreement or such instrument shall in any event be effective unless the same shall be in writing, and such waiver or consent shall be effective only in the specific instance and for the particular purpose for which given.

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10. BENEFIT. This Agreement shall be binding upon and inure to the benefit of Borrower and Lender and their respective successors and assigns. Lender may assign this Agreement in whole or in part. Borrower may not assign this Agreement or its obligations hereunder without Lender's written consent.

11. GOVERNING LAW. This Agreement shall be governed and construed in accordance with the laws of the State of Florida, and any litigation arising out of or relating to this Agreement or the Loan shall be commenced and conducted in the courts of the State of Florida or in the federal courts of the State of Florida.

IN WITNESS WHEREOF, the parties hereto have executed this Loan Agreement on the day and year first above written.

SUN HYDRAULICS CORPORATION,  
a Florida corporation

By: /s/ Allen Carlson

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Allen Carlson  
As its President

BORROWER

NORTHERN TRUST BANK OF FLORIDA, N.A.

By: /s/ Terence E. McGannon

-----  
Terence E. McGannon  
As its Vice President

LENDER

EXHIBIT 4.33

MODIFICATION NOTE  
[Mortgage Loan]

\$4,425,219.37

Effective Date: December 1, 2001

Execution Date: January \_\_, 2002

FOR VALUE RECEIVED, SUN HYDRAULICS CORPORATION, a Florida corporation ("Maker"), hereby promises, jointly and severally, to pay to the order of NORTHERN TRUST BANK OF FLORIDA, N.A. ("Lender") at 1515 Ringling Boulevard, Sarasota, FL 34236, or at such other place as the holder hereof may from time to time designate in writing, the principal sum of Four Million Four Hundred Twenty Five Thousand Two Hundred Nineteen and 37/100 Dollars (\$4,425,219.37), or so much thereof as may be disbursed by Lender to Maker or for Maker's account from time to time, together with interest at the rate hereinafter specified on such indebtedness as shall from time to time remain unpaid, until paid in full, such principal and interest being payable in lawful money of the United States which shall be legal tender in payment of all debts at the time of payment. Interest will be calculated on the basis of a 365/360 method, which computes a daily amount of interest for a hypothetical year of 360 days, then multiplies such amount by the actual number of days elapsed in an interest calculating period.

Interest on the unpaid principal sum outstanding from time to time shall accrue from the Effective Date through November 30, 2006, at six and one-half percent (6.50%) per annum. The interest rate shall be adjusted on December 1, 2006, (being an "Interest Adjustment Date"), to equal the weekly average yield on United States Treasury securities, adjusted to a constant maturity of five years, as made available by the Federal Reserve Board, plus two percent (2.0%). The figures so used to compute the change in interest rate shall be those figures made most recently available prior to the Interest Adjustment Date. In the event said index ceases to be available, Lender shall have the right to substitute another comparable index selected in Lender's discretion.

Beginning January 1, 2002, principal and interest on the loan shall be due and payable in consecutive monthly installments. Until the Interest Adjustment Date, the monthly installments hereunder shall equal \$33,239.02. On the Interest Adjustment Date, the amount of the monthly installments shall be increased or decreased so as to maintain an amortization of the loan evidenced by this Note over a twenty year period, which period shall be deemed to have commenced on December 1, 2001. The entire unpaid principal balance, together with accrued interest, shall be due and payable December 1, 2011.

All payments made hereunder shall be applied first to accrued interest then due and owing; next to amounts expended by Lender to cure any default under this Note, the Mortgage (as hereinafter defined), or any other loan documents executed in connection herewith; next to charges, costs, expenses, or attorneys' fees then due and payable to Lender under this Note, the Mortgage, or any other loan documents; and the balance, if any, to principal.

This Note may be prepaid, in whole or in part, at any time without penalty. All prepayments made hereunder shall be applied in the same manner as other payments made hereunder, as set forth above. The making of any prepayment shall not relieve Maker from the obligation to make the payments next due hereunder on a timely basis.

If any payment is more than fifteen (15) days late, Maker agrees to pay to Lender a late charge equal to five percent (5%) of the payment.

This Note is secured by a mortgage and security agreement (the "Mortgage") dated June 14, 1996, as amended, made by Maker in favor of Lender encumbering real property and personal property described therein (the "Mortgaged Property") located in Manatee County, Florida.

The entire unpaid principal balance hereof together with all accrued interest due shall, at Lender's sole option, become immediately due and payable in the event of the sale or transfer of all or any part of the Mortgaged Property, or any interest therein.

Each and every party to this Note, whether as Maker, endorser, surety,

guarantor, or otherwise ("Obligor"), hereby waives all rights of homestead and other exemptions granted by the constitution or laws of Florida, and further waives presentment, demand, protest, notice of dishonor, notice of nonpayment, notice of protest, and diligence in collection, and assents to the terms hereof and to any extension or postponement of the time for payment or any other indulgence. It is further specifically agreed that this Note or any part of the principal or interest due hereon may be renewed, modified or extended, in whole or in part, such modification to include but not be limited to changes in payment schedules and interest rates, from time to time by the holder of this Note, at the request of the then owners of all or part of the Mortgaged Property, or at the request of any party bound hereon or who has assumed or may hereafter assume payment hereof, without the consent of or notice to other parties bound hereon and without releasing them from any liabilities then existing.

Each and every Obligor hereby consents that the real or personal property securing this Note, or any part of such security, may be released, exchanged, added to or substituted for by Lender, without in any way modifying, altering, releasing, affecting or limiting their respective liabilities or the lien of the Mortgage, and further agrees that Lender shall not be required first to institute any suit, or to exhaust any of its remedies against Maker or any other person or party liable or to become liable hereunder, in order to enforce payment of this Note, and further agrees that Maker or any other party liable hereunder may be released by Lender from any or all liability under this Note and such release shall in no way affect or modify the liability of the remaining parties hereto.

Each and every Obligor hereby consents and agrees that he is bound, jointly and severally, under the terms hereof and is subject to all of the provisions set forth herein as fully as though each was an undersigned hereof, and further consents and agrees that any Obligor may be sued by Lender without joining any other Obligor, whether primarily or secondarily liable.

Notwithstanding anything contained herein to the contrary or in the Mortgage, or other loan documents executed in connection herewith, no payee or holder of this Note shall ever be entitled to receive, collect or apply as interest on the obligation evidenced hereby any amount in excess of the maximum rate of interest permitted to be charged by applicable law and, in the event Lender or any holder hereof ever receives, collects or applies as interest any such excess, such amount which would be excessive interest shall be applied to the reduction of the principal sum; and, if the principal sum is paid in full, any remaining excess shall forthwith be paid to Maker. In determining whether or not the interest paid or payable under any specific contingency exceeds the highest lawful rate, Maker and Lender shall, to the maximum extent permitted under applicable law: (a) characterize any non-principal payment as an expense, fee or premium rather than as interest; (b)

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exclude voluntary prepayments and the effects thereof; and (c) spread the total amount of interest, or charges in the nature of interest, pursuant to applicable law.

As used herein, "Event of Default" shall mean the occurrence of any of the following events or conditions: (a) failure or omission to pay when due this Note (or any installment of principal or interest hereunder) within fifteen (15) days after payment is due; (b) default in the payment (other than payment of principal and interest) or performance of any obligation, covenant, agreement or liability contained or referred to in the Mortgage, this Note, or any other loan document executed in connection herewith, or upon the existence or occurrence of any circumstance or event deemed a default under this Note or any other loan document executed in connection herewith; (c) any warranty, representation or statement made or furnished by any Obligor to Lender for the purpose of inducing Lender to make the loan evidenced by this Note, proves to have been false in any material respect when made or furnished; (d) a default under any other mortgage on the Mortgaged Property (whether such other mortgage be held by Lender or by a third party); (e) the institution of the foreclosure proceedings of another mortgage or lien of any kind on the Mortgaged Property (whether such other mortgage or lien be held by lender or by a third party); (f) the default by Maker or any party obligated under this Note or any guaranty hereof or any affiliate of any of the foregoing ("Affiliated Companies") in the payment or performance of any obligation, covenant, agreement, or liability contained in



any other mortgage, note, obligation or agreement held by Lender including but not limited to those certain loans in the current principal amounts of \$4,094,669.00 and \$7,500,000.00 evidenced by notes executed by Maker on even date herewith; (g) the death, dissolution, termination of existence, insolvency, or business failure of any Obligor; (h) the appointment of a receiver of any property of an obligor; (i) the assignment for the benefit of creditors or the commencement of any proceedings in bankruptcy or insolvency by or against any Obligor; (j) the determination by Lender that a material adverse change has occurred in the financial condition of any Obligor from the conditions set forth in the most recent financial statement of such Obligor heretofore furnished to Lender or from the condition of such Obligor as heretofore most recently disclosed to Lender in any manner; (k) the failure by Maker or any party obligated under this Note or any guaranty hereof to make any payment of principal or interest when due under any obligation to any other creditor; (l) any substantial part of the inventory, equipment, or other property of Maker, real or personal, is damaged or destroyed and the damage or destruction is not covered by collectible insurance; (m) Maker suffers or permits any lien, encumbrance, or security interest to arise or attach to any of Maker's property, which is not satisfied within 30 days; (n) any judgment is entered against Maker that is not satisfied or appealed within 30 days; or (o) falsity in any material respect of, or any material omission in, any representation or statement made to Lender by or on behalf of any Obligor in connection with the loan evidenced by this Note. Upon the occurrence of any such default or at any time thereafter, subject to the grace period, if any, provided in this Note, Lender may, at its option, declare the whole amount of principal and interest provided for in and by this Note, and any and all other secured indebtedness, immediately due and payable without demand or notice of any kind to any person, and the same thereupon shall become immediately due, payable and collectible (by foreclosure or otherwise) at once and without notice to Maker. Any default hereunder shall constitute a default under any other mortgage, note, obligation or agreement of Maker or any Affiliated Company held by Lender. The agreements contained in this paragraph to create cross-defaults under all mortgages, notes, obligations and agreements between Maker, and any Affiliated Company, and Lender, whether currently existing or hereafter created, in the event of default under one or more of such mortgages, notes, obligations or agreements are a material and specific inducement and consideration for the making by Lender of the loan evidenced by this Note.

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Notwithstanding the provisions of the foregoing paragraph to the contrary, in the event of a non-monetary default of the type set forth in subsections (b), (d), (f), (j) or (l) of the foregoing paragraph, then prior to Lender precipitating to maturity the full unpaid balance of this Note or otherwise exercising any rights available to Lender under the terms of this Note or any other loan document executed in connection herewith, Lender shall give written notice to Maker and Maker shall have a period of thirty (30) days from the date such notice is given in which to cure such default; provided, however, if such default cannot, with due diligence, be cured within said 30 day period, and such default does not threaten to impair Lender's security for this Note, then the 30 day period shall be extended for such period as may be reasonably necessary to complete the curing of same, provided that Maker proceeds with all due diligence and continuity to cure the default. Notice required hereunder may, at the option of Lender, be given by either certified mail, registered mail, regular mail, facsimile transmission, Federal Express or other express courier, or by personal delivery, and shall be deemed given when mailed, transmitted, placed with the courier or delivered to Maker, whichever is first. In the event the default is not cured within the time provided, then Lender shall have the right to accelerate this Note and proceed to enforce this Note and the loan documents, without further notice to Maker.

It is expressly agreed that upon the occurrence of an Event of Default, or if Lender shall deem itself insecure (because the prospect of timely payments is impaired, because the value of Lender's security is impaired, because the prospect of performance of any covenant or agreement under this Note, the Mortgage, or any other loan document is impaired, because of any change of circumstance which adversely affects any matters originally considered by Lender in making the loan, or otherwise), then or at any time thereafter at the option of Lender, the whole of the principal sum remaining unpaid hereunder, together with all accrued and unpaid interest thereon, shall become due and payable immediately without notice, anything contained herein to the contrary in any way notwithstanding, and in any such event Lender shall have the right to set-off

against this Note all money owed by Lender in any capacity to any Obligor, whether or not due, and Lender shall be deemed to have exercised such right of set-off and to have made a charge against any such money immediately upon the occurrence of an Event of Default although made or entered on the books subsequent thereto. From and after an Event of Default, the interest rate on the entire outstanding principal balance hereunder shall accrue at the highest rate permitted to be charged by applicable law ("Default Rate"). In the event the Default Rate shall be applicable and Lender has not accelerated this Note, the amount of each payment otherwise due hereunder shall be increased to an amount equal to the regular amount of the principal installment due hereunder, plus accrued interest at the Default Rate.

Each Obligor shall be obligated to pay as part of the indebtedness evidenced by this Note all costs of collection, whether or not a suit is brought, including any reasonable attorneys' fees that may be incurred in the collection or enforcement hereof. The term "attorneys' fees" shall include but not be limited to any such fees incurred in any appellate or related ancillary or supplementary proceedings, whether before or after final judgment related to the enforcement or defense of this Note.

If at any time any federal, state, county or municipal government or agency thereof shall impose any documentary stamp tax, intangible tax, or any other type of tax upon this Note or the Mortgage, or upon the indebtedness evidenced hereby (other than any federal, state or local income

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tax imposed upon Lender), then Maker shall pay same within fifteen (15) days after demand by Lender, together with any interest and penalties thereon.

Time is of the essence of this Note. The remedies of Lender as provided herein or in the Mortgage, or any other loan document executed in connection herewith, shall be cumulative and concurrent, and may be pursued singularly, successively or together, at the sole discretion of Lender, and may be exercised as often as occasion therefor shall arise. No act or omission of Lender, including specifically any failure to exercise any right, remedy or recourse, shall be deemed to be a waiver or release of such right, remedy or recourse, and any waiver or release may be effected only through a written document executed by Lender and then only to the extent specifically recited therein. A waiver or release with respect to any one event shall not be construed as continuing as a bar to, or as a waiver or release of, any subsequent right, remedy or recourse as to any subsequent event.

The term "Lender" where used herein shall include Lender's successors and assigns. The term "Maker" shall include each person signing this Note, jointly and severally, and their respective heirs, successors and assigns. The term "Obligor" shall include Maker and every person who is an endorser, guarantor, or surety of this Note, or who is otherwise a party hereto, and their respective heirs, successors and assigns. The terms "person" and "party" shall include individuals, firms, associations, joint ventures, partnerships, estates, trusts, business trusts, syndicates, fiduciaries, corporations, and all other groups or combinations. Whenever used herein, the singular number shall include the plural, the plural the singular, and the use of any gender shall include all genders. This Note shall be construed under Florida law.

This is a modification of that certain note dated March 1, 1999 in the principal amount of \$4,840,738.63. State of Florida documentary stamps in the amount required by law were paid on the mortgage securing the note which this Note modifies. No further State documentary stamps are required.

IN WITNESS WHEREOF, Maker has caused this Note to be duly executed and delivered as of the date first above written.

Maker's Address:

1500 University Parkway                      SUN HYDRAULICS CORPORATION,  
Sarasota, FL 34243                              a Florida corporation

By: /s/ Allen Carlson

-----  
Allen Carlson

As its President

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EXHIBIT 4.34

AMENDED AND RESTATED LOAN AGREEMENT  
(Equipment Loan)

THIS AMENDED AND RESTATED AGREEMENT made on this \_\_\_\_ day of January, 2002, and effective December 1, 2001, by and between SUN HYDRAULICS CORPORATION, a Florida corporation ("Borrower"), and NORTHERN TRUST BANK OF FLORIDA, N.A. ("Lender").

WITNESSETH:

WHEREAS, Lender has made a loan to Borrower ("Loan"), which is evidenced by a modification note of even date herewith in the principal amount of \$3,871,754.35 ("Note") and

WHEREAS, the Loan is secured by certain property described in the security agreement ("Security Agreement") entered into between Borrower and Lender dated July 23, 1999, to secure the Loan, encumbering certain personal property owned by Borrower ("Collateral"), and

WHEREAS, in connection with making the Loan, Borrower and Lender entered into a loan agreement dated July 23, 1999, which was amended by First Amendment to Loan Agreement dated July 23, 2000, ("Original Loan Agreement"), and

WHEREAS, Borrower has requested Lender to modify certain terms of the Original Loan Agreement and other loan documents, and Lender has agreed to do so provided that Borrower modify the terms of the Original Loan Agreement by entering into this Amended and Restated Loan Agreement ("Loan Agreement"),

NOW, THEREFORE, in consideration of the premises and of the covenants and agreements herein contained and the agreement by Lender to make the Loan, the parties hereto agree that the Original Loan Agreement is amended and restated in its entirety as follows:

1. LOAN TO BORROWER; EXECUTION OF LOAN DOCUMENTS. Lender agrees, in accordance with the terms of this Agreement, to make the Loan to Borrower. Concurrently herewith, Borrower has executed a note in the amount of the Loan ("Note"), and other documents related to the Loan. The Note, Security Agreement, this Loan Agreement and other documents executed in connection with the Loan are collectively referred to herein as the "Loan Documents".

2. COSTS AND EXPENSES. Borrower shall pay all costs and expenses incurred in connection with preparation for, closing, and servicing the Loan including, without limitation, any legal fees, including the fees of Lender's counsel, intangible taxes, documentary taxes, recording costs, and document preparation fees.

3. REPRESENTATIONS AND WARRANTIES. To induce Lender to make the Loan, Borrower makes the following representations and warranties:

A. The financial information for Borrower and each guarantor or other obligor furnished to Lender in connection with Borrower's application for the Loan is complete and accurate. There has been no material nor adverse change in the financial condition of either Borrower or any guarantor or other obligor of the Loan from that reflected on such financial information.

B. Borrower is a duly organized corporation, existing and in good standing under the laws of the State of Florida, has corporate power to carry on the business in which it is engaged, and the obtaining and performing of the Loan has been duly authorized by all necessary actions of the board of directors and shareholders of the corporation under applicable law, and do not and will not violate any provisions of law or any of its organizational documents.

C. The obtaining and performing of the Loan does not and will not result in a breach of, constitute a default under, require any consent under, or result in the creation of any lien, charge, or encumbrance upon any property of Borrower pursuant to any instrument, order, or other agreement to

which Borrower is a party or by which Borrower, any of its officers as such, or any of its property is bound.

D. There are no judgments, liens, encumbrances, or other security interests outstanding against Borrower or any of its subsidiaries, or any of their properties other than those disclosed to Lender in connection with Borrower's request for the Loan, nor is there any pending or threatened litigation that could or will give rise to any such judgment, lien or encumbrance.

E. Neither Borrower nor any of its subsidiaries have incurred any debts, liabilities, or obligations (whether direct or contingent) nor committed themselves to incur any debts, liabilities, or obligations other than those disclosed to Lender in connection with Borrower's request for the Loan or shown on the financial statements submitted to Lender.

F. Neither Borrower nor any of its subsidiaries have made any assignment for the benefit of their creditors, admitted in writing their inability to pay their debts as they become due, filed a petition of bankruptcy or been adjudicated bankrupt or insolvent, or filed a petition seeking any reorganization, arrangement, composition, readjustment, liquidation, dissolution, receivership or similar relief under any statute, law or regulation.

G. There are no actions, suits or proceedings pending or, threatened against or affecting Borrower or any of its subsidiaries, the Collateral or any guarantor or obligor on the Loan, or involving the validity or enforceability of the Security Agreement or the priority of the lien thereof, at law or in equity, or before or by any governmental authorities, and neither Borrower nor any of its subsidiaries is in default with respect to any order, writ, injunction, decree or demand of any court or any governmental authority.

H. The obtaining of the Loan and the consummation of all other transactions contemplated by the Loan Documents, and performance under the Loan Documents, will not result in any breach of, or constitute a default under, any mortgage, indenture, security agreement, lease, loan, credit agreement or any other contract or instrument to which the

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Borrower or any of its subsidiaries is a party or by which their properties may be bound or affected.

4. AFFIRMATIVE COVENANTS. Borrower will:

A. Preserve and keep in force all licenses, permits, and franchises necessary for the proper conduct of its business and duly pay and discharge all taxes, assessments, and governmental charges upon Borrower or against Borrower's property before the date on which penalties attach thereto, unless and to the extent only that the same shall be contested in good faith and by appropriate proceedings.

B. Furnish to Lender (i) within 90 days after the close of each fiscal year a consolidated annual profit and loss statement and balance sheet on Borrower and its subsidiaries reviewed by an independent certified public accountant who is satisfactory to Lender; (ii) within 30 days after filing each year, an executed copy of Borrower's Federal income tax return, and if any extensions have been filed, copies of each Extension Notice shall be furnished to Lender within 30 days of filing; and (iii) such other information reflecting the financial condition of Borrower and/or its subsidiaries as Lender may request from time to time.

C. Permit any representative or agent of Lender to examine and audit any or all of Borrower's books and records when requested by Lender.

D. Inform Lender immediately of any material adverse change in the financial condition of Borrower or any of its subsidiaries. Borrower will also promptly inform Lender of any litigation or threatened litigation which might substantially affect Borrower's financial condition.

E. Maintain Borrower's property and equipment in a state

of good repair.

F. Maintain Borrower's net working capital, on a consolidated basis ("Net Working Capital") in an amount not less than \$2,000,000.00 and a current ratio ("Current Ratio") of not less than 1.2:1.0 at all times during the term of this Agreement. For the purposes of this Agreement, Net Working Capital shall mean the excess of Borrower's current assets over current liabilities, on a consolidated basis with its subsidiaries, which shall be determined in accordance with generally accepted accounting principles as consistently applied in the preparation of Borrower's previous financial statements, and Current Ratio shall mean the quotient of current assets divided by current liabilities, on a consolidated basis with its subsidiaries.

G. Maintain Borrower's Tangible Net Worth at a minimum of \$35,000,000.00 ("Minimum Tangible Net Worth") for the fiscal year 2001. Borrower's Minimum Tangible Net Worth as of each fiscal year-end thereafter shall increase by at least 50% of Borrower's reported net income for the immediately preceding fiscal year. For the purposes of this Agreement, Tangible Net Worth shall mean (i) the aggregate amount of assets shown on the balance sheet of Borrower at any particular date (but excluding from such assets capitalized organization and development costs, capitalized interest, debt discount and expense, goodwill, patents,

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trademarks, copyrights, franchises, licenses, amounts due from officers, directors, stockholders and affiliates, and such other assets as are properly classified "intangible assets" under generally accepted accounting principles) less (ii) liabilities at such date, all computed in accordance with generally accepted accounting principles applied on a consistent basis.

H. Maintain Borrower's Total Liabilities to Tangible Net Worth ratio, on a consolidated basis with its subsidiaries throughout the term of the Loan at a minimum of 1.5:1.0 at all times during the term of this Agreement. For purposes of this Agreement, the term "Liabilities" shall mean Borrower's liabilities as computed in accordance with generally accepted accounting principles.

I. Maintain Borrower's debt service coverage ratio, on a consolidated basis with its subsidiaries ("Debt Service Coverage Ratio") throughout the term of the Loan at a minimum of 1.25:1.0 on a calendar year basis for all operations of the Borrower and its subsidiaries, computed as follows: net profits plus interest, plus depreciation, all divided by interest plus current maturities of long term debt and capitalized leases, plus unfunded capital expenditures and advances/withdrawals made to shareholders of Borrower and/or its subsidiaries.

5. NEGATIVE COVENANTS. Neither Borrower nor any of its subsidiaries will, without prior written consent of Lender:

A. Collaterally assign, mortgage, pledge, encumber or grant any security interest in any of its assets, whether now owned or hereafter acquired.

B. Enter into any merger or consolidation, or sell, lease, transfer, or otherwise dispose of all or any substantial part of its assets, whether now owned or hereafter acquired.

C. Change the name in which it does business.

D. Move its principal place of business without giving written notice thereof to Lender at least 30 days prior thereto.

E. Incur any new debt whether secured or unsecured, except trade debt for the purchase of equipment which does not exceed \$100,000.00 for any item of equipment, and trade debt for the purchase of inventory.

F. Execute any guarantees or assumptions of any debt, or endorse any obligations, except that Borrower may guaranty any trade debt for the purchase of equipment which does not exceed \$100,000.00 for any item of equipment, and trade debt for the purchase of inventory which is incurred by a

subsidiary of Borrower.

G. Enter into any asset sale/leaseback arrangement.

6. EVENTS OF DEFAULT. The Lender shall have the option to declare the entire unpaid balance due on the Loan without notice of any kind, if any of the following events occur:

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A. Failure or omission to pay, within fifteen (15) days after payment is due, the Note (or any installment of principal or interest thereunder).

B. Default in the payment (other than payment of principal and interest) or performance of any obligation, covenant, agreement or liability contained or referred to in the Security Agreement, Note, this Loan Agreement or any other Loan Document, or upon the existence or occurrence of any circumstance or event deemed a default under the Note or any other Loan Document.

C. Any warranty, representation or statement made or furnished by Borrower for the purpose of inducing Lender to make the Loan proves to have been false in any material respect when made or furnished.

D. A default under any other mortgage on the Collateral (whether such other mortgage be held by Lender or by a third party).

E. The institution of foreclosure proceedings of another mortgage or lien of any kind on the Collateral (whether such other mortgage or lien be held by Lender or by a third party).

F. The default by Borrower or any party obligated under the Note or any guaranty thereof in the payment or performance of any obligation, covenant, agreement, or liability contained in any other mortgage, note, obligation or agreement held by Lender, including but not limited to that certain revolving line of credit loan in the amount of \$7,500,000.00 made by Lender to Borrower, evidenced by modification note of even date hereof, and that certain mortgage loan in the current principal amount of \$4,425,219.37, evidenced by a modification note of even date herewith.

G. The death, dissolution, termination of existence, insolvency, or business failure of Borrower or any party obligated under the Note or any guaranty thereof.

H. The appointment of a receiver of any part of the Collateral.

I. The assignment for the benefit of creditors or the commencement of any proceedings in bankruptcy or insolvency by or against Borrower or by or against any person obligated under the Note or any guaranty thereof.

J. The determination by Lender that a material adverse change has occurred in the financial condition of Borrower or any person obligated under the Note or any guaranty thereof, from the conditions set forth in the most recent financial statement of such person heretofore furnished to Lender or from the condition of such person as heretofore most recently disclosed to Lender in any manner.

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K. The failure by Borrower or any party obligated under the Note or any guaranty thereof to make any payment of principal or interest when due under any obligation to any other creditor, if such failure continues beyond any applicable grace period.

L. Any substantial part of the inventory, equipment, or other property of Borrower, real or personal, is damaged or destroyed and the damage or destruction is not covered by collectible insurance.

M. Borrower suffers or permits any lien, encumbrance, or security interest to arise or attach to any of Borrower's property, which is not satisfied within 30 days.

N. Any judgment is entered against Borrower that is not satisfied or appealed within 30 days.

O. Falsity in any material respect of, or any material omission in, any representation or statement made to Lender by or on behalf of Borrower or any person obligated under the Note or any guaranty thereof, in connection with the Loan.

7. REMEDIES UPON DEFAULT. Upon the occurrence, or the discovery by Lender of the occurrence, of any of the foregoing events, circumstances, or conditions of default, Lender shall have, in addition to its option to accelerate to maturity the full unpaid balance of the Loan, all of the rights and remedies under applicable law, and in addition shall have the following specific rights and remedies:

A. To exercise Lender's right of set-off against any account, fund, or property of any kind, tangible or intangible, belonging to Borrower which shall be in Lender's possession or under its control.

B. To cure such defaults, with the result that all costs and expenses incurred or paid by Lender in effecting such cure shall be additional charges on the Loan, shall bear interest at the highest rate permitted by law, and shall be payable upon demand, and shall be secured by the Security Agreement and other Loan Documents.

8. ATTORNEYS' FEES AND COSTS. Borrower promises and agrees to pay all costs of collection and attorneys' fees, including fees for appellate proceedings, bankruptcy proceedings or otherwise, incurred or paid by Lender in enforcing this Agreement or preserving any right or interest of Lender hereunder.

9. WAIVER. No failure or delay on the part of Lender in exercising any power or right hereunder, and no failure of Lender to give Borrower notice of a default hereunder, shall operate as a waiver thereof, nor shall any single or partial exercise of any such right or power preclude any other or further exercise thereof or the exercise of any other right or power hereunder. No modification or waiver of any provision of this Agreement or any instrument executed pursuant hereto or consent to any departure by Borrower from this Agreement or such instrument shall in any event be effective unless the same shall be in writing, and such waiver or

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consent shall be effective only in the specific instance and for the particular purpose for which given.

10. BENEFIT. This Agreement shall be binding upon and inure to the benefit of Borrower and Lender and their respective successors and assigns. Lender may assign this Agreement in whole or in part. Borrower may not assign this Agreement or its obligations hereunder without Lender's written consent.

11. GOVERNING LAW. This Agreement shall be governed and construed in accordance with the laws of the State of Florida, and any litigation arising out of or relating to this Agreement or the Loan shall be commenced and conducted in the courts of the State of Florida or in the federal courts of the State of Florida.

IN WITNESS WHEREOF, the parties hereto have executed this Loan Agreement on the day and year first above written.

SUN HYDRAULICS CORPORATION,  
a Florida corporation

By: /s/ Allen Carlson  
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Allen Carlson  
As its President

BORROWER

NORTHERN TRUST BANK OF FLORIDA, N.A.

By: /s/ Terence E. McGannon

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Terence E. McGannon  
As its Vice President

LENDER

EXHIBIT 4.35

MODIFICATION NOTE  
[Equipment Loan]

\$3,871,754.35

Effective Date: December 23, 2001

Execution Date: January 18, 2002

FOR VALUE RECEIVED, SUN HYDRAULICS CORPORATION, a Florida corporation ("Maker"), hereby promises, jointly and severally, to pay to the order of NORTHERN TRUST BANK OF FLORIDA, N.A. ("Lender") at 1515 Ringling Boulevard, Sarasota, FL 34236, or at such other place as the holder hereof may from time to time designate in writing, the principal sum of Three Million Eight Hundred Seventy One Thousand Seven Hundred Fifty Four and 35/100 Dollars (\$3,871,754.35), or so much thereof as may be disbursed by Lender to Maker or for Maker's account from time to time, together with interest at the rate hereinafter specified on such indebtedness as shall from time to time remain unpaid, until paid in full, such principal and interest being payable in lawful money of the United States which shall be legal tender in payment of all debts at the time of payment. Interest will be calculated on the basis of a 365/360 method, which computes a daily amount of interest for a hypothetical year of 360 days, then multiplies such amount by the actual number of days elapsed in an interest calculating period.

Interest on the unpaid principal sum outstanding from time to time shall accrue at a fixed rate of 5.3% per annum.

Principal and interest on the loan shall be due and payable in equal monthly installments of principal and interest in the amount of \$89,823.44, the first such installment to be due and payable on January 23, 2002, with subsequent installments to be due and payable on the same day of every month thereafter until December 23, 2005, on which date the then remaining unpaid principal balance, together with all accrued but unpaid interest, shall be due and payable.

All payments made hereunder shall be applied first to accrued interest then due and owing; next to amounts expended by Lender to cure any default under this Note, the Security Agreement (as hereinafter defined), or any other loan documents executed in connection herewith; next to charges, costs, expenses, or attorneys' fees then due and payable to Lender under this Note, the Security Agreement, or any other loan documents; and the balance, if any, to principal.

This Note may be prepaid, in whole or in part, at any time without penalty. All prepayments made hereunder shall be applied in the same manner as other payments made hereunder, as set forth above. The making of any prepayment shall not relieve Maker from the obligation to make the payments next due hereunder on a timely basis.

If any payment is more than fifteen (15) days late, Maker agrees to pay to Lender a late charge equal to five percent (5%) of the payment. Notwithstanding the foregoing, however, all payments shall be due and payable as of the dates set forth above, and the failure to make all payments when due shall constitute a default under this Note.

This Note is secured by a security agreement (the "Security Agreement") dated July 23, 1999 herewith made by Maker in favor of Lender encumbering personal property described therein (the "Collateral") owned by Maker.

The entire unpaid principal balance hereof together with all accrued interest due shall, at Lender's sole option, become immediately due and payable in the event of the sale or transfer of (i) all or any part of the Collateral, or any interest therein.

Each and every party to this Note, whether as Maker, endorser, surety, guarantor, or otherwise ("Obligor"), hereby waives all rights of homestead and other exemptions granted by the constitution or laws of Florida, and further waives presentment, demand, protest, notice of dishonor, notice of nonpayment, notice of protest, and diligence in collection, and assents to the terms hereof and to any extension or postponement of the time for payment or any other indulgence. It is further specifically agreed that this Note or any part of the principal or interest due hereon may be renewed, modified or extended, in whole

or in part, such modification to include but not be limited to changes in payment schedules and interest rates, from time to time by the holder of this Note, at the request of the then owners of all or part of the Collateral, or at the request of any party bound hereon or who has assumed or may hereafter assume payment hereof, without the consent of or notice to other parties bound hereon and without releasing them from any liabilities then existing.

Each and every Obligor hereby consents that the real or personal property securing this Note, or any part of such security, may be released, exchanged, added to or substituted for by Lender, without in any way modifying, altering, releasing, affecting or limiting their respective liabilities or the lien of the Security Agreement, and further agrees that Lender shall not be required first to institute any suit, or to exhaust any of its remedies against Maker or any other person or party liable or to become liable hereunder, in order to enforce payment of this Note, and further agrees that Maker or any other party liable hereunder may be released by Lender from any or all liability under this Note and such release shall in no way affect or modify the liability of the remaining parties hereto.

Each and every Obligor hereby consents and agrees that he is bound, jointly and severally, under the terms hereof and is subject to all of the provisions set forth herein as fully as though each was an undersigned hereof, and further consents and agrees that any Obligor may be sued by Lender without joining any other Obligor, whether primarily or secondarily liable.

Notwithstanding anything contained herein to the contrary or in the Security Agreement, or other loan documents executed in connection herewith, no payee or holder of this Note shall ever be entitled to receive, collect or apply as interest on the obligation evidenced hereby any amount in excess of the maximum rate of interest permitted to be charged by applicable law and, in the event Lender or any holder hereof ever receives, collects or applies as interest any such excess, such amount which would be excessive interest shall be applied to the reduction of the principal sum; and, if the principal sum is paid in full, any remaining excess shall forthwith be paid to Maker. In determining whether or not the interest paid or payable under any specific contingency exceeds the highest lawful rate, Maker and Lender shall, to the maximum extent permitted under applicable law: (a) characterize any non-principal payment as an expense, fee or premium rather than as interest; (b)

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exclude voluntary prepayments and the effects thereof; and (c) spread the total amount of interest, or charges in the nature of interest, pursuant to applicable law.

As used herein, "Event of Default" shall mean the occurrence of any of the following events or conditions: (a) failure or omission to pay, within fifteen (15) days after payment is due, this Note (or any installment of principal or interest hereunder); (b) default in the payment (other than payment of principal and interest) or performance of any obligation, covenant, agreement or liability contained or referred to in the Security Agreement, this Note, or any other loan document executed in connection herewith, or upon the existence or occurrence of any circumstance or event deemed a default under this Note or any other loan document executed in connection herewith; (c) any warranty, representation or statement made or furnished by any Obligor to Lender for the purpose of inducing Lender to make the loan evidenced by this Note, proves to have been false in any material respect when made or furnished; (d) the default by Maker or any party obligated under this Note or any guaranty hereof or any affiliate of any of the foregoing ("Affiliated Companies") in the payment or performance of any obligation, covenant, agreement, or liability contained in any other mortgage, note, obligation or agreement held by Lender including but not limited to those certain loans in the current principal amounts of \$7,500,000.00 and \$4,425,219.37 evidenced by notes executed by Maker on even date herewith; (e) the death, dissolution, termination of existence, insolvency, or business failure of any Obligor; (f) the appointment of a receiver of any part of the Mortgaged Property; (g) the assignment for the benefit of creditors or the commencement of any proceedings in bankruptcy or insolvency by or against any Obligor; (h) the determination by Lender that a material adverse change has occurred in the financial condition of any Obligor from the conditions set forth in the most recent financial statement of such Obligor heretofore furnished to Lender or from the condition of such Obligor as heretofore most recently disclosed to Lender in any manner; (i) the failure by Maker or any party

obligated under this Note or any guaranty hereof to make any payment of principal or interest when due under any obligation to any other creditor; (j) any substantial part of the inventory, equipment, or other property of Maker, real or personal, is damaged or destroyed and the damage or destruction is not covered by collectible insurance; (k) Maker suffers or permits any lien, encumbrance, or security interest to arise or attach to any of Maker's property, which is not satisfied within 30 days; (l) any judgment is entered against Maker that is not satisfied or appealed within 30 days; or (m) falsity in any material respect of, or any material omission in, any representation or statement made to Lender by or on behalf of any Obligor in connection with the loan evidenced by this Note. Upon the occurrence of any such default or at any time thereafter, subject to the grace period, if any, provided in this Note, Lender may, at its option, declare the whole amount of principal and interest provided for in and by this Note, and any and all other secured indebtedness, immediately due and payable without demand or notice of any kind to any person, and the same thereupon shall become immediately due, payable and collectible (by foreclosure or otherwise) at once and without notice to Maker. Any default hereunder shall constitute a default under any other mortgage, note, obligation or agreement of Maker or any Affiliated Company held by Lender. The agreements contained in this paragraph to create cross-defaults under all mortgages, notes, obligations and agreements between Maker, and any Affiliated Company and Lender, whether currently existing or hereafter created, in the event of default under one or more of such mortgages, notes, obligations or agreements are a material and specific inducement and consideration for the making by Lender of the loan evidenced by this Note.

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Notwithstanding the provisions of the foregoing paragraph to the contrary, in the event of a non-monetary default of the type set forth in subsections (b), (d) or (e) of the foregoing paragraph, then prior to Lender precipitating to maturity the full unpaid balance of this Note or otherwise exercising any rights available to Lender under the terms of this Note or any other loan document executed in connection herewith, Lender shall give written notice to Maker and Maker shall have a period of thirty (30) days from the date such notice is given in which to cure such default; provided, however, if such default cannot, with due diligence, be cured within said 30 day period, and such default does not threaten to impair Lender's security for this Note, then the 30 day period shall be extended for such period as may be reasonably necessary to complete the curing of same, provided that Maker proceeds with all due diligence and continuity to cure the default. Notice required hereunder may, at the option of Lender, be given by either certified mail, registered mail, regular mail, facsimile transmission, Federal Express or other express courier, or by personal delivery, and shall be deemed given when mailed, transmitted, placed with the courier or delivered to Maker, whichever is first. In the event the default is not cured within the time provided, then Lender shall have the right to accelerate this Note and proceed to enforce this Note and the loan documents, without further notice to Maker.

It is expressly agreed that upon the occurrence of an Event of Default, or if Lender shall deem itself insecure (because the prospect of timely payments is impaired, because the value of Lender's security is impaired, because the prospect of performance of any covenant or agreement under this Note, the Security Agreement, or any other loan document is impaired, because of any change of circumstance which adversely affects any matters originally considered by Lender in making the loan, or otherwise), then or at any time thereafter at the option of Lender, the whole of the principal sum remaining unpaid hereunder, together with all accrued and unpaid interest thereon, shall become due and payable immediately without notice, anything contained herein to the contrary in any way notwithstanding, and in any such event Lender shall have the right to set-off against this Note all money owed by Lender in any capacity to any Obligor, whether or not due, and Lender shall be deemed to have exercised such right of set-off and to have made a charge against any such money immediately upon the occurrence of an Event of Default although made or entered on the books subsequent thereto. From and after an Event of Default, the interest rate on the entire outstanding principal balance hereunder shall accrue at the highest rate permitted to be charged by applicable law ("Default Rate"). In the event the Default Rate shall be applicable and Lender has not accelerated this Note, the amount of each payment otherwise due hereunder shall be increased to an amount equal to the regular amount of the principal installment due hereunder, plus accrued interest at the Default Rate. Any judgment rendered on this Note shall bear interest at the Default Rate.

Each Obligor shall be obligated to pay as part of the indebtedness evidenced by this Note all costs of collection, whether or not a suit is brought, including any reasonable attorneys' fees that may be incurred in the collection or enforcement hereof. The term "attorneys' fees" shall include but not be limited to any such fees incurred in any appellate or related ancillary or supplementary proceedings, whether before or after final judgment related to the enforcement or defense of this Note.

If at any time any federal, state, county or municipal government or agency thereof shall impose any documentary stamp tax, intangible tax, or any other type of tax upon this Note or the

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Security Agreement, or upon the indebtedness evidenced hereby (other than any federal, state or local income tax imposed upon Lender), then Maker shall pay same within fifteen (15) days after demand by Lender, together with any interest and penalties thereon.

Time is of the essence of this Note. The remedies of Lender as provided herein or in the Security Agreement, or any other loan document executed in connection herewith, shall be cumulative and concurrent, and may be pursued singularly, successively or together, at the sole discretion of Lender, and may be exercised as often as occasion therefor shall arise. No act or omission of Lender, including specifically any failure to exercise any right, remedy or recourse, shall be deemed to be a waiver or release of such right, remedy or recourse, and any waiver or release may be effected only through a written document executed by Lender and then only to the extent specifically recited therein. A waiver or release with respect to any one event shall not be construed as continuing as a bar to, or as a waiver or release of, any subsequent right, remedy or recourse as to any subsequent event.

The term "Lender" where used herein shall include Lender's successors and assigns. The term "Maker" shall include each person signing this Note, jointly and severally, and their respective heirs, successors and assigns. The term "Obligor" shall include Maker and every person who is an endorser, guarantor, or surety of this Note, or who is otherwise a party hereto, and their respective heirs, successors and assigns. The terms "person" and "party" shall include individuals, firms, associations, joint ventures, partnerships, estates, trusts, business trusts, syndicates, fiduciaries, corporations, and all other groups or combinations. Whenever used herein, the singular number shall include the plural, the plural the singular, and the use of any gender shall include all genders. This Note shall be construed under Florida law.

This Note amends and replaces that certain note dated July 23, 1999 in the original principal amount of \$7,500,000.00

IN WITNESS WHEREOF, Maker has caused this Note to be duly executed and delivered as of the date first above written.

Maker's Address:

1500 University Parkway                      SUN HYDRAULICS CORPORATION,  
Sarasota, FL 34243                              a Florida corporation

By:    /s/ Tricia Fulton  
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Tricia Fulton  
As its Corporate Controller

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