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

# FORM 10-Q

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

**For the quarterly period ended July 2, 2011**

**Commission file number 0-21835**

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

| | |
|---|---|
| **FLORIDA**<br>(State or Other Jurisdiction of Incorporation or Organization) | **59-2754337**<br>(I.R.S. Employer Identification No.) |
| **1500 WEST UNIVERSITY PARKWAY**<br>**SARASOTA, FLORIDA**<br>(Address of Principal Executive Offices) | **34243**<br>(Zip Code) |

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

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 whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

| | |
|---|---|
| Large accelerated filer ☐ | Accelerated filer ☒ |
| Non-accelerated filer ☐ | Smaller Reporting Company ☐ |

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

The Registrant had 25,651,422 shares of common stock, par value $.001, outstanding as of July 22, 2011.

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For the quarter ended July 2, 2011

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PART I: FINANCIAL INFORMATION

Item 1.

**Sun Hydraulics Corporation**
**Consolidated Balance Sheets**
**(in thousands, except share data)**

| | July 2, 2011 (unaudited) | January 1, 2011 |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 49,720 | $ 33,206 |
| Restricted cash | 139 | 131 |
| Accounts receivable, net of allowance for doubtful accounts of $83 and $82 | 23,352 | 16,399 |
| Inventories | 12,049 | 10,773 |
| Income taxes receivable | 483 | 1,154 |
| Deferred income taxes | 446 | 446 |
| Marketable securities | 12,866 | 11,614 |
| Other current assets | 2,907 | 2,556 |
| Total current assets | 101,962 | 76,279 |
| Property, plant and equipment, net | 53,031 | 53,127 |
| Other assets | 1,481 | 2,628 |
| **Total assets** | **$156,474** | **$ 132,034** |
| **Liabilities and shareholders' equity** | | |
| Current liabilities: | | |
| Accounts payable | $ 5,175 | $ 3,348 |
| Accrued expenses and other liabilities | 6,364 | 5,250 |
| Dividends payable | 2,307 | 1,531 |
| Total current liabilities | 13,846 | 10,129 |
| Deferred income taxes | 5,690 | 5,684 |
| Other noncurrent liabilities | 1,562 | 1,197 |
| Total liabilities | 21,098 | 17,010 |
| Commitments and contingencies | — | — |
| Shareholders' equity: | | |
| Preferred stock, 2,000,000 shares authorized, par value $0.001, no shares outstanding | — | — |
| Common stock, 40,000,000 shares authorized, par value $0.001, 25,646,862 and 25,522,568 shares outstanding | 26 | 26 |
| Capital in excess of par value | 47,583 | 44,001 |
| Retained earnings | 85,610 | 71,132 |
| Accumulated other comprehensive income | 2,157 | (135) |
| Total shareholders' equity | 135,376 | 115,024 |
| **Total liabilities and shareholders' equity** | **$156,474** | **$ 132,034** |

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

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

| | Three months ended July 2, 2011 (unaudited) | Three months ended July 3, 2010 (unaudited) |
|---|---|---|
| **Net sales** | **$ 54,770** | **$ 39,246** |
| Cost of sales | 33,096 | 25,262 |
| **Gross profit** | **21,674** | **13,984** |
| Selling, engineering and administrative expenses | 6,290 | 4,845 |
| **Operating income** | **15,384** | **9,139** |
| Interest income, net | (186) | (144) |
| Foreign currency transaction (gain) loss, net | (33) | 69 |
| Miscellaneous expense (income), net | 32 | (109) |
| **Income before income taxes** | **15,571** | **9,323** |
| Income tax provision | 5,134 | 3,210 |
| **Net income** | **$ 10,437** | **$ 6,113** |
| **Basic net income per common share** | **$ 0.41** | **$ 0.24** |
| **Weighted average basic shares outstanding** | 25,638 | 25,429 |
| **Diluted net income per common share** | **$ 0.41** | **$ 0.24** |
| **Weighted average diluted shares outstanding** | 25,674 | 25,477 |
| **Dividends declared per share** | **$ 0.090** | **$ 0.060** |

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

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

| | Six months ended | |
|---|---|---|
| | **July 2, 2011 (unaudited)** | **July 3, 2010 (unaudited)** |
| **Net sales** | **$105,473** | **$ 70,850** |
| Cost of sales | 63,857 | 46,747 |
| **Gross profit** | **41,616** | **24,103** |
| Selling, engineering and administrative expenses | 12,322 | 10,001 |
| **Operating income** | **29,294** | **14,102** |
| Interest income, net | (349) | (281) |
| Foreign currency transaction (gain) loss, net | (87) | 41 |
| Miscellaneous income, net | (258) | (128) |
| **Income before income taxes** | **29,988** | **14,470** |
| Income tax provision | 9,781 | 5,047 |
| **Net income** | **$ 20,207** | **$ 9,423** |
| **Basic net income per common share** | **$ 0.79** | **$ 0.37** |
| **Weighted average basic shares outstanding** | 25,593 | 25,421 |
| **Diluted net income per common share** | **$ 0.79** | **$ 0.37** |
| **Weighted average diluted shares outstanding** | 25,629 | 25,471 |
| **Dividends declared per share** | **$ 0.223** | **$ 0.120** |

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

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

| | Preferred shares | Preferred stock | Common shares | Common stock | Capital in excess of par value | Retained earnings | Accumulated other comprehensive income | Total |
|---|---|---|---|---|---|---|---|---|
| Balance, January 1, 2011 | — | $ — | 25,523 | $ 26 | $44,001 | $71,132 | $ (135) | $115,024 |
| Shares issued, other comp | | | 8 | | | | | — |
| Shares issued, stock options | | | 9 | | 61 | | | 61 |
| Shares issued, ESPP | | | 14 | | 280 | | | 280 |
| Shares issued, shared distribution | | | 93 | | 2,412 | | | 2,412 |
| Stock-based compensation | | | | | 829 | | | 829 |
| Dividends declared | | | | | | (5,729) | | (5,729) |
| Comprehensive income: | | | | | | | | |
| Net income | | | | | | 20,207 | | 20,207 |
| Foreign currency translation adjustments | | | | | | | 2,307 | 2,307 |
| Unrealized loss on available-for-sale securities | | | | | | | (15) | (15) |
| Comprehensive income | | | | | | | | 22,499 |
| Balance, July 2, 2011 | — | $ — | 25,647 | $ 26 | $47,583 | $85,610 | $ 2,157 | $135,376 |

The accompanying Notes to the Consolidated, Unaudited Financial Statements are an integral part of this financial statement.

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

| | Six months ended July 2, 2011 (unaudited) | Six months ended July 3, 2010 (unaudited) |
|---|---|---|
| **Cash flows from operating activities:** | | |
| Net income | $ 20,207 | $ 9,423 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 3,368 | 3,460 |
| Loss on disposal of assets | 69 | 21 |
| Provision for deferred income taxes | 6 | (18) |
| Allowance for doubtful accounts | 1 | (13) |
| Stock-based compensation expense | 829 | 540 |
| Stock options income tax benefit | — | (29) |
| (Increase) decrease in: | | |
| Accounts receivable | (6,954) | (6,634) |
| Inventories | (1,276) | (1,501) |
| Income taxes receivable | 671 | 1,485 |
| Other current assets | (352) | (936) |
| Other assets | (318) | 549 |
| Increase (decrease) in: | | |
| Accounts payable | 1,827 | 2,301 |
| Accrued expenses and other liabilities | 3,526 | 752 |
| Income taxes payable | — | 203 |
| Other noncurrent liabilities | 365 | (37) |
| Net cash provided by operating activities | 21,969 | 9,566 |
| **Cash flows from investing activities:** | | |
| Proceeds from sale of joint venture | 1,451 | — |
| Capital expenditures | (2,811) | (1,325) |
| Proceeds from dispositions | 30 | — |
| Purchases of marketable securities | (5,500) | (11,126) |
| Proceeds from sale of marketable securities | 4,190 | 5,390 |
| Net cash used in investing activities | (2,640) | (7,061) |
| **Cash flows from financing activities:** | | |
| Proceeds from exercise of stock options | 61 | 39 |
| Proceeds from stock issued | 281 | 176 |
| Dividends to shareholders | (4,952) | (3,051) |
| Stock options income tax benefit | — | 29 |
| Net cash used in financing activities | (4,610) | (2,807) |
| Effect of exchange rate changes on cash and cash equivalents | 1,803 | (2,160) |
| Net increase (decrease) in cash and cash equivalents | 16,522 | (2,462) |
| Cash and cash equivalents, beginning of period | **33,337** | **30,446** |
| Cash and cash equivalents, end of period | **$ 49,859** | **$ 27,984** |
| Supplemental disclosure of cash flow information: | | |
| Cash paid: | | |
| Income taxes | $ 9,104 | $ 3,406 |
| Supplemental disclosure of noncash transactions: | | |
| Common stock issued for shared distribution through accrued expenses and other liabilities | $ 2,412 | $ — |

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

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

## 1. BASIS OF PRESENTATION AND SUMMARY OF BUSINESS

Sun Hydraulics Corporation, and its wholly-owned subsidiaries and joint ventures, design, manufacture, and sell screw-in cartridge valves and manifolds used in hydraulic systems. The Company has facilities in the United States, the United Kingdom, Germany, Korea, France, China, and India. Sun Hydraulics Corporation ("Sun Hydraulics"), with its main offices located in Sarasota, Florida, designs, manufactures, and sells its products primarily through distributors. Sun Hydraulik Holdings Limited ("Sun Holdings"), a wholly-owned subsidiary of Sun Hydraulics, was formed to provide a holding company for the European market operations; its wholly-owned subsidiaries are Sun Hydraulics Limited (a British corporation, "Sun Ltd.") and Sun Hydraulik GmbH (a German corporation, "Sun GmbH"). Sun Ltd. operates a manufacturing and distribution facility located in Coventry, England, and Sun GmbH operates a manufacturing and distribution facility located in Erkelenz, Germany. Sun Hydraulics Korea Corporation ("Sun Korea"), a wholly-owned subsidiary of Sun Hydraulics, located in Inchon, South Korea, operates a manufacturing and distribution facility. Sun Hydraulics, SARL ("Sun France"), a wholly-owned subsidiary of Sun Hydraulics, located in Bordeaux, France, operates a sales and engineering support facility. WhiteOak Controls, Inc. ("WhiteOak"), a 40% equity method investment, is located in Mediapolis, Iowa, and designs and produces complementary electronic control products. High Country Tek, Inc. ("HCT"), a 48% equity method investment, is located in Nevada City, California, and designs and manufacturers ruggedized electronic/hydraulic control solutions for mobile equipment markets. Sun Hydraulics also has a representative office in Shanghai, China, and a sales office in Bangalore, India, to develop new business opportunities in the Chinese and Indian markets.

The accompanying unaudited interim consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission for reporting on Form 10-Q. Accordingly, certain information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements are not included herein. The financial statements are prepared on a consistent basis (including normal recurring adjustments) and should be read in conjunction with the consolidated financial statements and related notes contained in the Annual Report on Form 10-K for the fiscal year ended January 1, 2011, filed by Sun Hydraulics Corporation (together with its subsidiaries, the "Company") with the Securities and Exchange Commission on March 11, 2011. In Management's opinion, all adjustments necessary for a fair presentation of the Company's financial statements are reflected in the interim periods presented. Operating results for the three and six month periods ended July 2, 2011, are not necessarily indicative of the results that may be expected for the period ending December 31, 2011.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Earnings per share

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

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | July 2, 2011 | July 3, 2010 | July 2, 2011 | July 3, 2010 |
| **Net income** | **$ 10,437** | **$ 6,113** | **$ 20,207** | **$ 9,423** |
| Weighted average basic shares outstanding | 25,638 | 25,429 | 25,593 | 25,421 |
| **Basic net income per common share** | **$ 0.41** | **$ 0.24** | **$ 0.79** | **$ 0.37** |
| Effect of dilutive stock options | 36 | 48 | 36 | 50 |
| Weighted average diluted shares outstanding | 25,674 | 25,477 | 25,629 | 25,471 |
| **Diluted net income per common share** | **$ 0.41** | **$ 0.24** | **$ 0.79** | **$ 0.37** |

Stock Split

On June 9, 2011, the Company declared a three-for-two stock split, effected in the form of a 50% stock dividend, to shareholders of record on June 30, 2011, payable on July 15, 2011. The Company issued approximately 8,500,000 shares of common stock as a result of the stock split. The effect of the stock split on outstanding shares and earnings per share was retroactively applied to all periods presented.

3. STOCK-BASED COMPENSATION

During 1996, the Company adopted the 1996 Stock Option Plan ("1996 Plan"), which provides for the grant of incentive stock options and nonqualified stock options for the purchase of up to an aggregate of 3,375,000 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 activity under the 1996 Plan for the six months ended July 2, 2011, is as follows:

| | Number of shares | Weighted average exercise price | Weighted average remaining contractual term (in years) | Aggregate intrinsic value |
|---|---|---|---|---|
| Options outstanding as of January 1, 2011 | 9 | $ 6.67 | | |
| Granted | — | | | |
| Exercised | (9) | $ 6.67 | | |
| Forfeitures | — | | | |
| Options outstanding as of July 2, 2011 | — | $ — | 0.00 | $ — |
| Options exercisable as of July 2, 2011 | — | $ — | 0.00 | $ — |

As of July 2, 2011, all options under the 1996 Plan have been exercised and the Plan is no longer active.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model using weighted average assumptions. Stock option compensation expense for the six month periods ended July 2, 2011, and July 3, 2010, was zero and $3 respectively. There were no options granted during these periods.

In September 2006, the Company adopted the 2006 Stock Option Plan ("2006 Plan"), which provides for the grant of incentive stock options and nonqualified stock options for the purchase of up to an aggregate of 1,125,000 shares of the Company's common stock by officers, employees and directors of the Company. The Company adopted the 2006 Plan due to the expiration of the Company's 1996 Stock Option Plan in 2006. Under the terms of the plan, incentive stock options may be granted to employees at an exercise price per share of not less than the fair value per common share on the date of the grant (not less than 110% of the fair value in the case of holders of more than 10% of the Company's voting stock). Nonqualified stock options may be granted at the discretion of the Company's Board of Directors. The maximum term of an option may not exceed 10 years, and options become exercisable at such times and in such installments as determined by the Board of Directors. No awards have been granted under the 2006 Plan.

During 2001, the Company adopted the 2001 Restricted Stock Plan, which provides for the grant of restricted stock of up to an aggregate of 928,125 shares of the Company's common stock to officers, employees, consultants and directors of the Company. Under the terms of the plan, the minimum period before any shares become non-forfeitable may not be less than six months. Compensation cost is measured at the date of the grant and is recognized in earnings over the period in which the shares vest. Restricted stock expense for the six months ended July 2, 2011, and July 3, 2010, totaled $518 and $408 respectively.

The following table summarizes restricted stock activity from January 1, 2011, through July 2, 2011:

| | Number of shares | Weighted average grant-date fair value |
|---|---|---|
| Nonvested balance at January 1, 2011 | 129 | 17.41 |
| Granted | — | — |
| Vested | — | — |
| Forfeitures | — | — |
| Nonvested balance at July 2, 2011 | 129 | 17.41 |

The Company has $1,382 of total unrecognized compensation cost related to restricted stock awards granted under the Plan as of July 2, 2011. That cost is expected to be recognized over a weighted average period of 1.23 years.

The Company maintains an Employee Stock Purchase Plan ("ESPP"), in which most employees are eligible to participate. Employees in the United States who choose to participate are granted an opportunity to purchase common stock at 85 percent of market value on the first or last day of the quarterly purchase period, whichever is lower. Employees in the United Kingdom, under a separate plan, are granted an opportunity to purchase common stock at market value, on the first or last day of the quarterly purchase period, whichever is lower, with the Company issuing one additional free share of common stock for each six shares purchased by the employee under the ESPP. The ESPP authorizes the issuance, and the purchase by employees, of up to 1,096,875 shares of common stock through payroll deductions. No U.S. employee is allowed to buy more than $25 of common stock in any year, based on the market value of the common stock at the beginning of the purchase period, and no U.K. employee is allowed to buy more than the lesser of £1.5 or 10% of their annual salary in any year. Employees purchased 14,405 shares at a weighted average price of $19.05, and 14,226 shares at a weighted average price of $12.98, under the ESPP during the six months ended July 2, 2011, and July 3, 2010, respectively. The Company recognized $105 and $61 of compensation expense during the six months ended July 2, 2011, and July 3, 2010, respectively. At July 2, 2011, 763,199 shares remained available to be issued through the ESPP.

The Company has a Nonemployee Director Equity and Deferred Compensation Plan (the "Plan"), which originally was adopted by the Board of Directors and approved by the shareholders in 2004. The Plan was amended on March 1, 2008, and was approved by the shareholders at the 2008 Annual Meeting. Under the Plan, Directors who are not officers of the Company are paid 250 shares of Company common stock and $3 in cash fees for attendance at each meeting of the Board of Directors, as well as each meeting of each Board Committee on which they serve when the committee meeting is not held within one day of a meeting of the Board of Directors. Additionally, the Board of Directors has the authority to increase from time to time, as it deems desirable or appropriate, the number of shares of stock awarded to all or any one or more of the Nonemployee Directors. No more than 25,000 shares of stock, in the aggregate, may be issued under the Plan during any single calendar year. Committee Chairmen currently receive additional fees equal to 25% of normal compensation and the Chairman of the Board is paid twice the amount of normal compensation, with such additional compensation payable in Company common stock.

Directors may elect under the Plan to receive all or part of their cash fees in Company stock and to defer receipt of their fees until a subsequent year. When so deferred, the shares of stock are converted to deferred stock units. Deferred stock units are treated as liabilities. At July 2, 2011, there were 48,640 deferred stock units outstanding. The Plan has been amended to eliminate deferral of cash fees or fees paid in stock subsequent to June 7, 2011.

Directors were granted 7,468 and 7,918 shares for the six months ended July 2, 2011, and July 3, 2010, respectively. The Company recognized director stock compensation expense of $512 and $36 for the six months ended July 2, 2011, and July 3, 2010, respectively. The Plan authorizes the issuance of up to 270,000 shares of common stock. At July 2, 2011, 190,768 shares remained available to be issued through the Plan.

## 4. RESTRICTED CASH

The restricted cash balance at July 2, 2011, consisted of $48 in reserves as a required deferment for customs in the U.K. operation. The restricted amount was calculated as an estimate of two months of customs for items coming into the Company's U.K. operations and is held with Lloyd's TSB in the U.K. The remaining amount of $91 relates to a guarantee of VAT in our France operation. The guarantee is held with Crédit Agricole Bank in France.

## 5. INVENTORIES

| | July 2, 2011 | January 1, 2011 |
|---|---|---|
| Raw materials | $ 5,569 | $ 4,315 |
| Work in process | 3,761 | 3,628 |
| Finished goods | 3,246 | 3,379 |
| Provision for slow moving inventory | (527) | (549) |
| Total | $ 12,049 | $ 10,773 |

## 6. GOODWILL

On July 2, 2011, the Company had $715 of goodwill, related to its acquisition of Sun Korea. Goodwill is held in other assets on the balance sheet. Valuation models reflecting the expected future cash flow projections were used to value Sun Korea at January 1, 2011. The analysis indicated that there was no impairment of the carrying value of the goodwill. As of July 2, 2011, no factors were identified that indicated impairment of the carrying value of the goodwill.

## 7. INVESTMENTS

On January 5, 2011, Sun Hydraulics completed the sale of its Chinese joint venture company, Sun Hydraulics Systems (Shanghai) Co, Ltd., to the joint venture partner, Links Lin, for the amount of $1,451, and recognized a gain on the sale of $366. The former joint venture company has become Sun's first authorized distributor in China. Concurrently, Sun established Sun Hydraulics China Co. Ltd, a representative office in Shanghai which now is the Company's primary operation in the country.

8. LONG-TERM DEBT

The Company has a $35,000 revolving line of credit with a commercial bank, collateralized by U.S. assets, with an interest rate of Libor plus 1.5% (1.69% at July 2, 2011), that comes due August 1, 2011. The Company did not have any debt outstanding for the periods ending July 2, 2011 and January 1, 2011.

The revolving line of credit is subject to debt covenants (capitalized terms are defined therein) including: 1) Debt to Tangible Net Worth ratio of not more than 1.5:1.0, 2) Funded Debt to EBITDA ratio of not more than 2.5:1.0, and 3) EBIT to Interest Expense ratio of not less than 1.1:1.0; and requires the Company to maintain its primary domestic deposit accounts with the bank. As of July 2, 2011, the Company was in compliance with all debt covenants.

The Company refinanced its debt effective August 1, 2011. See footnote 14. Subsequent Events.

9. INCOME TAXES

At July 2, 2011, the Company had an unrecognized tax benefit of $169 including accrued interest for uncertain tax positions related to previous years. If recognized, the unrecognized tax benefit would have a favorable effect on the effective tax rate in future periods. The Company recognizes interest and penalties related to income tax matters in income tax expense. Interest accrued as of July 2, 2011, is not considered material to the Company's Consolidated Financial Statements.

The Company files U.S. federal income tax returns as well as income tax returns in various states and foreign jurisdictions. The Company is no longer subject to income tax examinations by tax authorities for years prior to 2004 for the majority of tax jurisdictions.

The Company's federal returns are currently under examination by the Internal Revenue Service (IRS) in the United States for the periods 2004 through 2009. The IRS proposed a significant adjustment to the Company's research and development tax credit position. Management has disagreed with the proposed adjustment and believes sufficient evidence is available to defend the position. To date, there have not been any other significant proposed adjustments that have not been accounted for in the Company's financial statements.

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

10. SEGMENT REPORTING

The individual subsidiaries comprising the Company operate predominantly in a single industry as manufacturers and distributors of hydraulic components. The Company is multinational with operations in the United States, and subsidiaries in the United Kingdom, Germany, Korea, and France. Amounts for France, due to their immateriality, are included with the U.S. In computing operating profit for the foreign subsidiaries, no allocations of general corporate expenses have been made. Management bases its financial decisions by the geographical location of its operations.

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.

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Segment information is as follows:

| | United States | Korea | Germany | United Kingdom | Elimination | Consolidated |
|---|---|---|---|---|---|---|
| **Three Months Ended July 2, 2011** | | | | | | |
| Sales to unaffiliated customers | $35,152 | $ 5,674 | $ 7,308 | $ 6,636 | $ — | $ 54,770 |
| Intercompany sales | 8,470 | — | 63 | 407 | (8,940) | — |
| Operating income | 11,383 | 659 | 1,922 | 1,281 | 139 | 15,384 |
| Depreciation | 1,292 | 29 | 88 | 246 | — | 1,655 |
| Capital expenditures | 1,615 | 23 | 5 | 56 | — | 1,699 |
| **Three Months Ended July 3, 2010** | | | | | | |
| Sales to unaffiliated customers | $25,259 | $ 4,644 | $ 4,669 | $ 4,674 | $ — | $ 39,246 |
| Intercompany sales | 6,785 | — | 28 | 287 | (7,100) | — |
| Operating income (loss) | 7,005 | 651 | 911 | 759 | (187) | 9,139 |
| Depreciation | 1,320 | 22 | 102 | 234 | — | 1,678 |
| Capital expenditures | 515 | 48 | 1 | 92 | — | 656 |
| **Six Months Ended July 2, 2011** | | | | | | |
| Sales to unaffiliated customers | $65,618 | $11,697 | $14,496 | $13,662 | $ — | $ 105,473 |
| Intercompany sales | 17,959 | — | 116 | 783 | (18,858) | — |
| Operating income | 21,359 | 1,599 | 3,662 | 2,487 | 187 | 29,294 |
| Depreciation | 2,585 | 54 | 188 | 486 | — | 3,313 |
| Capital expenditures | 2,510 | 146 | 50 | 104 | — | 2,810 |
| **Six Months Ended July 3, 2010** | | | | | | |
| Sales to unaffiliated customers | $44,228 | $ 8,836 | $ 9,368 | $ 8,418 | $ — | $ 70,850 |
| Intercompany sales | 11,882 | — | 81 | 625 | (12,588) | — |
| Operating income (loss) | 9,875 | 1,277 | 2,028 | 1,095 | (173) | 14,102 |
| Depreciation | 2,648 | 44 | 214 | 484 | — | 3,390 |
| Capital expenditures | 1,081 | 113 | 5 | 125 | — | 1,324 |

Sales to unaffiliated customers represent sales from each of the individual subsidiaries. For information on sales to geographic locations, see the Comparison of the Six Month Periods Ended July 2, 2011, and July 3, 2010, in Management's Discussion and Analysis of Financial Condition and Results of Operations. Operating income is total sales and other operating income less operating expenses. Segment operating income does not include interest income/expense, foreign currency transaction gain/loss, and net miscellaneous income/expense.

11. FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company uses the three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value as follows:

*Level 1.* Observable inputs such as quoted prices in active markets;

*Level 2*. Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly; and

*Level 3*. Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

The Company held available-for-sale securities with an aggregate fair value of $12,866 and $13,352 at July 2, 2011, and July 3, 2010, respectively. The Company, on a recurring basis, measures available-for-sale securities at fair value using quoted prices in active markets. The net unrealized holding gain amounted to $81 at July 2, 2011, and a net unrealized holding loss of $54 at July 3, 2010. In addition, the Company reports deferred director stock units and phantom stock units as a liability. These liabilities, on a recurring basis, are measured at fair value using quoted prices in the active market. The Company's liability was $1,635 and $676, at July 2, 2011, and July 3, 2010, respectively. The Company recognized expense related to those liabilities of $101 for the period ended July 2, 2011, and a net gain related to those expenses of $50 for the period ended July 3, 2010.

The Company did not have any fair value adjustments for assets and liabilities measured at fair value on a nonrecurring basis during the six months ended July 2, 2011, and July 3, 2010.

Assets measured at fair value on a recurring basis include the following as of July 2, 2011:

| | | Fair Value Measurements at Reporting Date Using | | |
|---|---|---|---|---|
| **Description** | **July 2, 2011** | **Quoted Prices in Active Markets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Unobservable Inputs (Level 3)** |
| Available-for-sale securities | $ 12,866 | $ 12,866 | $ — | $ — |

| | | Fair Value Measurements at Reporting Date Using | | |
|---|---|---|---|---|
| **Description** | **July 2, 2011** | **Quoted Prices in Active Markets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Unobservable Inputs (Level 3)** |
| Deferred director stock units | $ 1,562 | $ 1,562 | $ — | $ — |
| Phantom stock units | 73 | 73 | — | — |
| Total | $ 1,635 | $ 1,635 | $ — | $ — |

The carrying amounts of cash and cash equivalents, restricted cash, accounts receivable, other current assets, accounts payable, accrued expenses and other liabilities approximate fair value based on their short-term status.

12. NEW ACCOUNTING PRONOUNCEMENTS

In May 2011, the Financial Accounting Standards Board ("FASB") issued guidance amending certain fair value measurement and disclosure requirements in U.S. GAAP and IFRS. The amendments change the wording used to describe many of the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. The amendments are intended to create comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with U.S. Generally Accepted Accounting Principles and International Financial Reporting Standards. This guidance is effective for interim and annual periods beginning after December 15, 2011. The Company does not expect material financial statement implications relating to the adoption of this guidance.

In June 2011, the FASB issued guidance amending the presentation of comprehensive income. This amends existing guidance by allowing only two options for presenting the components of net income and other comprehensive income: (1) in a single continuous financial statement, statement of comprehensive income or (2) in two separate but consecutive financial statements, consisting of an income statement followed by a separate statement of other comprehensive income. Also, items that are reclassified from other comprehensive income to net income must be presented on the face of the financial statements. The guidance requires retrospective application, and it is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. We believe the adoption of this update will change the order in which certain financial statements are presented and provide additional detail on those financial statements when applicable, but will not have any other material impact on our consolidated financial statements.

13. 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.

14. SUBSEQUENT EVENTS

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

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

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

Facility C is a $15,000 construction and term loan. Facility C requires monthly payments of interest for the first 24 months and monthly payments of principal plus accrued interest for 60 months based upon a 15 year amortization schedule. The Construction Loan bears interest at the 30-day LIBOR Rate or the Bank's Base Rate, at the Company's discretion, plus a margin based on the Borrower's Funded Debt to EBITDA Leverage Ratio. The LIBOR Margin ranges from 1.65% to 2.45% and the Bank's Base Rate ranges from -0.05% to 0.20%.

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

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

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

## Item 2. 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 through wholly-owned subsidiaries and independent distributors. Sales outside the United States for the year ended January 1, 2011, were approximately 61% of total net sales.

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

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

*Industry conditions*

Demand for the Company's products is dependent on demand for the capital goods into which the products are incorporated. The capital goods industries in general, and the fluid power industry specifically, are subject to economic cycles. According to the National Fluid Power Association (the fluid power industry's trade association in the United States), the United States index of twelve-month shipments of hydraulic products increased 42% in 2010, after a decrease of 40% in 2009. The index of shipments of hydraulic products increased 26% for the three-month period ending June 30, 2011, compared to the same period of the prior year.

The Company's order trend has historically tracked closely to the United States Purchasing Managers Index (PMI). When PMI is over 50, it indicates economic expansion in the manufacturing sector; when it is below 50, it indicates contraction in the economy. The index decreased to 55.3 in June 2011 compared to 56.2 in June 2010. In July 2011, the index was 50.9, which represents twenty-four consecutive months of expansion in the manufacturing sector, although at a slower rate than in June 2011. Production and employment continued to grow in July, while new orders showed contraction.

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***Results for the second quarter***
(Dollars in millions except net income per share)

| | July 2, 2011 | July 3, 2010 | Increase |
|---|---|---|---|
| Three Months Ended | | | |
| Net Sales | $ 54.8 | $39.2 | 40% |
| Net Income | $ 10.4 | $ 6.1 | 70% |
| Net Income per share: | | | |
| Basic | $ 0.41 | $0.24 | 71% |
| Diluted | $ 0.41 | $0.24 | 71% |
| Six Months Ended | | | |
| Net Sales | $105.5 | $70.9 | 49% |
| Net Income | $ 20.2 | $ 9.4 | 115% |
| Net Income per share: | | | |
| Basic | $ 0.79 | $0.37 | 114% |
| Fully Diluted | $ 0.79 | $0.37 | 114% |

The global capital goods expansion is strong and Sun's second quarter activity reflects that. Sales were higher than Q2 estimates and all regions contributed to the top line growth. Earnings were consistent with strong first quarter results. Gross margin remains high, at 39.6%, as manufacturing assets continue to be leveraged. The US PMI, Sun's primary leading indicator, demonstrates that further expansion is at hand.

Product development continues to yield interesting additions to the product line. New products, which account for approximately 10% – 12% of sales, provide new and efficient innovative solution possibilities. Sun's brand is built on developing products that help customers' create unique solutions for their motion control needs and management believes the Company continues to meet that challenge."

***Outlook***

Third quarter 2011 revenues are expected to be approximately $53 million, reflecting what the Company believes is its normal seasonal business pattern. This represents a 39% increase over 2010 third quarter revenue of $38 million. Earnings per share for the third quarter are estimated to be $0.38 to $0.41, commensurate with sales levels, and compared with $0.23 cents in the same quarter last year.

**COMPARISON OF THE THREE MONTHS ENDED JULY 2, 2011 AND JULY 3, 2010**

***Net Sales***

Net sales were $54.8 million, an increase of $15.5 million, or 39.6%, compared to $39.2 million in 2010. The increase in net sales was primarily driven by increased demand in our end markets, which primarily include capital goods equipment. A price increase, effective July 1, 2010, contributed approximately 3% to sales. The change in exchange rates had a positive impact on sales of approximately $1.4 million. New product sales (defined as products introduced within the last five years) continue to make up 10 - 12% of total sales.

North American sales increased 38.0% or $6.7 million, to $24.3 million, Asian sales increased 28.5% or $2.5 million, to $11.3 million, and European sales increased 50.6% or $5.7 million, to $17.0 million.

The U.S. reporting segment had sales of $35.2 million in the second quarter of 2011, up $9.9 million or 39.2%, compared to sales of $25.3 million during the second quarter last year. The increase was driven by demand in our end markets and the general upturn in the global economy. International sales out of the U.S. were $14.0 million during the second quarter of 2011, up 44.1% or $4.3 million, compared to $9.7 million during the second quarter last year. Significant increases in sales were noted in almost all geographic regions.

The Korean reporting segment had sales of $5.7 million during the second quarter of 2011, up $1.0 million or 22.2%, compared to sales of $4.6 million during the second quarter last year. The increase was related to demand in almost all market segments. Currency effect increased 2011 second quarter sales by approximately $0.4 million.

The German reporting segment had sales of $7.3 million during the second quarter of 2011, up $2.6 million or 56.5%, compared to sales of $4.7 million during the second quarter last year. Currency effect increased 2011 second quarter sales by approximately $0.8 million. The increase in sales was primarily related to demand within Germany and from Austria and Italy.

The U.K. reporting segment had sales of $6.6 million during the second quarter of 2011, up $1.9 million or 42.0%, compared to sales of $4.7 million during the second quarter last year. Currency effect increased 2011 second quarter sales by approximately $0.2 million. The increase in sales was primarily related to demand within the U.K. and from Sweden, Norway, and France.

***Gross Profit***

Gross profit increased $7.7 million or 55.0% to $21.7 million in the second quarter of 2011, compared to $14.0 million in the second quarter last year. Gross profit as a percentage of net sales increased to 39.6% in the second quarter of 2011, compared to 35.6% in the second quarter last year. As sales increased across all segments, the Company was able to leverage its overhead costs to generate higher gross profit and also achieved productivity improvements.

Higher sales volume in the second quarter of 2011 contributed $4.9 million of the increase. Decreases in fixed overhead expenses as a percentage of sales added approximately $1.1 million to gross profit, which occurred primarily in the U.S. The remaining increase in gross profit was attributed to a price increase in July 2010, of approximately $1.8 million and productivity improvements of approximately $0.5 million. The increase in gross profit was partially offset by additional retirement benefit costs of approximately $1.0 million and material costs of $0.5 million.

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

Selling, engineering and administrative expenses increased 29.8%, or $1.4 million, to $6.3 million in 2011, compared to $4.8 million last year. The change for the second quarter of 2011 was related to additional retirement benefits of approximately $0.4 million, which were primarily in the U.S., and compensation, including variable stock compensation, totaling $0.6 million.

***Operating Income***

Operating income increased $6.2 million or 68.3% to $15.4 million in the second quarter of 2011, compared to $9.1 million in the second quarter last year, with operating margins of 28.1% and 23.3% for the second quarters of 2011 and 2010, respectively. As sales increased during the second quarter across all segments, the Company was able to respond to the increase in demand. Through productivity improvements and by leveraging its overhead costs, the Company generated higher operating income.

The U.S. reporting segment contributed $11.4 million to our consolidated operating income during the second quarter of 2011, compared to $7.0 million during the second quarter of 2010. This increase of $4.4 million in the U.S. operating segment was primarily related to the increase in sales volume, which resulted in $2.7 million of additional operating income. The remaining increase was primarily related to leverage of overhead costs. Decreases, as a percent of sales, in variable and fixed overhead costs added $0.9 million and absorption of selling, engineering, and administrative expenses added $0.3 million to operating income. The remaining increases in operating income were from productivity improvements of $0.5 million.

The Korean reporting segment contributed $0.7 million to our consolidated operating income during the second quarter of 2011 compared to $0.7 million during the second quarter last year. Operating income from additional sales volume was offset primarily by increased material costs.

The German reporting segment contributed $1.9 million to our consolidated operating income during the second quarter of 2011 compared to $0.9 million during the second quarter last year, an increase of $1.0 million. Increased sales volume contributed $0.5 million to additional operating income. The remaining increase was related to decreases, as a percent of sales, in material costs of $0.3 million and fixed costs of $0.2 million.

The U.K. reporting segment contributed $1.3 million to our consolidated operating income during the second quarter of 2011 compared to $0.8 million during the second quarter last year, an increase of $0.5 million. Increased sales volume contributed $0.3 million to additional operating income. The remaining increase was primarily related to absorption of fixed costs adding $0.2 million to operating income, and productivity improvements of $0.1 million. These amounts were partially offset by increased material costs of $0.1 million.

***Interest Income, Net***

Net interest income was $0.2 million and $0.1 million for the quarters ended July 2, 2011, and July 3, 2010, respectively. The Company currently has no outstanding debt. Total average cash and investments for the quarter ended July 2, 2011, was $52.0 million compared to $39.5 million for the quarter ended July 3, 2010.

***Foreign Currency Transaction Loss (Gain), Net***

There was minimal impact from foreign currency transaction gain or loss for the quarters ended July 2, 2011, and July 3, 2010.

***Miscellaneous (Income) Expense, Net***

There was minimal net miscellaneous expense for the quarter ended July 2, 2011, compared to net miscellaneous income of $0.1 for the quarter ended July 3, 2010.

***Income Taxes***

The provision for income taxes for the quarter ended July 2, 2011, was 33.0 % of pretax income compared to 34.4% for the quarter ended July 3, 2010. The change was primarily due to the relative levels of income and different tax rates in effect among the countries in which the Company sells its products. The prior period provision was affected by discrete items related to a reserve for uncertain tax positions from previous years. Excluding these discrete items, the effective rate would have been approximately 33%.

**COMPARISON OF THE SIX MONTHS ENDED JULY 2, 2011 AND JULY 3, 2010**

***Net Sales***

Net sales were $105.5 million in 2011, an increase of $34.6 million, or 48.9%, compared to $70.9 million in 2010. Net sales increased 46.1% excluding the effect of exchange rates. The increase in net sales was primarily driven by increased demand in our end markets, which primarily include capital goods equipment. A price increase, effective July 1, 2010, contributed approximately 3% to sales. New product sales (defined as products introduced within the last five years) generally make up 10 - 12% of total sales.

North American sales increased 46.5% or $14.6 million, to $46.0 million, Asian sales increased 41.9% or $6.5 million, to $22.1 million, and European sales increased 58.6% or $12.5 million, to $33.8 million.

The U.S. reporting segment had sales of $65.6 million in 2011, up $21.4 million or 48.4%, compared to sales of $44.2 million last year. The increase was driven by demand in our end markets and the general upturn in the global economy. International sales out of the U.S. were $25.7 million in 2011, up 54.8% or $9.1 million, compared to $16.6 million last year. Significant increases in sales were noted in almost all geographic regions.

The Korean reporting segment had sales of $11.7 million in 2011, up $2.9 million or 32.4%, compared to sales of $8.8 million last year. The increase was related to demand in almost all market segments. Currency effect increased 2011 second quarter sales by approximately $0.5 million.

The German reporting segment had sales of $14.5 million in 2011, up $5.1 million or 54.7%, compared to sales of $9.4 million last year. The increase was primarily related to demand within Germany. Currency effect increased 2011 sales by approximately $0.7 million.

The U.K. reporting segment had sales of $13.7 million in 2011, up $5.2 million or 62.3%, compared to sales of $8.4 million last year. The increase was primarily related to demand within the U.K. Currency effect increased 2011 sales by approximately $0.3 million

***Gross Profit***

Gross profit increased $17.5 million or 72.7% to $41.6 million, compared to $24.1 million last year. Gross profit as a percentage of net sales increased to 39.5% in 2011, compared to 34.0% last year. As sales increased across all segments, the Company achieved productivity improvements and was able to leverage its overhead costs to generate higher gross profit.

Higher sales volume in 2011 contributed $10.6 million of the increase. The remaining increase in gross profit was attributed to productivity improvements of approximately $0.9 million, decreases in overhead expenses as a percentage of sales of approximately $3.4 million, both of which occurred primarily in the U.S., and a price increase in July 2010, of approximately $3.5 million. The increase in gross profit was partially offset by higher material costs as a percent of sales of approximately $0.9 million and additional retirement benefit costs of approximately $2.0 million.

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

Selling, engineering and administrative expenses increased 23.2%, or $2.3 million, to $12.3 million in 2011, compared to $10.0 million last year. The change was related to additional retirement benefits of approximately $0.7 million, which were primarily in the U.S., and compensation, including variable stock compensation totaling $1.1 million.

***Operating Income***

Operating income increased $15.2 million or 107.8% to $29.3 million in 2011, compared to $14.1 million last year, with operating margins of 27.8% and 19.9% for 2011 and 2010, respectively. The increase in sales during 2011 has improved operating margins across almost all segments. The Company has been able to respond to the increasing demand in 2011. As sales increase across all segments, the Company achieved productivity improvements and was able to leverage its overhead costs to generate higher operating income.

The U.S. reporting segment contributed $21.4 million to our consolidated operating income during 2011, compared to $9.9 million during 2010, an increase of $11.5 million. The increase in the U.S. operating segments was primarily related to productivity gains and leverage of its overhead costs. Productivity gains contributed $1.0 million and decreases in variable and fixed overhead costs, as a percent of sales, added $3.6 million to operating income. Absorption of selling, engineering, and administrative expenses added $1.8 million of additional operating income. The remaining increase was primarily from increased sales volume which added $4.8 million of additional operating income.

The Korean reporting segment contributed $1.6 million to our consolidated operating income during 2011 compared to $1.3 million last year, an increase of $0.3 million. The increase in operating income was primarily related to increased sales volume.

The German reporting segment contributed $3.7 million to our consolidated operating income during 2011 compared to $2.0 million last year, an increase of $1.6 million. The increase was primarily related to increased sales volume, which contributed $1.1 million of additional operating income. The remaining increase was related to the absorption of fixed overhead costs.

The U.K. reporting segment contributed $2.5 million to our consolidated operating income during 2011 compared to $1.1 million last year, an increase of $1.4 million. Increased sales volume contributed $0.7 million of additional operating income. The remaining increase was primarily related to productivity improvement of $0.3 million and decreased variable and fixed costs of $0.9 million. These amounts were partially offset by increased material costs of $0.5 million.

***Interest Income, Net***

Net interest income was $0.3 million in 2011 and 2010. The Company currently has no outstanding debt. Total average cash and investments for the six months ended July 2, 2011, was $53.8 million compared to $39.8 million for the six months ended July 3, 2010. Although average cash increased, interest income remained flat due to lower interest rates compared to the prior year.

***Foreign Currency Transaction (Gain) Loss, Net***

There was a foreign currency transaction gain of $0.1 million during the six months ended July 2, 2011, compared to minimal impact to net expense from foreign currency during the six months ended July 3, 2010. During the current period, the British Pound, Euro, and Korean Won all made gains against the U.S. Dollar.

***Miscellaneous Income, Net***

There was net miscellaneous income of $0.3 million in 2011, compared to net miscellaneous income of $0.1 for 2010. The 2011 income was related primarily to the gain on the sale of the Chinese joint venture company.

***Income Taxes***

The provision for income taxes for the six months ended July 2, 2011, was 32.6% of pretax income compared to 34.9% for the six months ended July 3, 2010. The change was primarily due to the relative levels of income and different tax rates in effect among the countries in which the Company sells its products. The prior year provision was affected by discrete items related to a reserve for uncertain tax positions from previous years. Excluding these discrete items, the effective rate would have been approximately 32.5%.

## LIQUIDITY AND CAPITAL RESOURCES

Historically, the Company's primary source of capital has been cash generated from operations, although fluctuations in working capital requirements have from time to time been met through borrowings under revolving lines of credit. The Company's principal uses of cash have been to pay operating expenses, make capital expenditures, pay dividends to shareholders, repurchase Company common stock and service debt.

Cash from operations for the six months ended July 2, 2011, was $22.0 million, compared to $9.6 million for the six months ended July 3, 2010. The $12.4 million increase in the Company's net cash flow from operations during the period was due primarily to the increase in net income of $10.8 million and from increases in accounts payable and accruals totaling $5.4 million, compared to an increase of $3.1 million during 2010. Cash on hand increased $21.9 million from $28.0 million in 2010 to $49.9 million in 2011. Days sales outstanding (DSO) were 39 and 38 at July 2, 2011, and July 3, 2010, respectively. Inventory turns were 11.0 as of July 2, 2011 and 10.9 as of July 3, 2010.

Capital expenditures, consisting primarily of purchases of machinery and equipment, were $2.8 million for the six months ended July 2, 2011, compared to $1.3 million for the six months ended July 3, 2010. Capital expenditures for the year are projected to be approximately $10.0 million.

The Company continues to be watchful of both its capability and capacity. The current capacity is sufficient for the business levels expected throughout 2011. The Company recognizes that additional capacity may be required as the expansion of this business cycle and its market share gains continue.

The Company declared a 50% stock dividend and quarterly cash dividend of $0.09 per share during the quarter ended June 30, 2011; both were payable on July 15, 2011, to shareholders of record as of June 30, 2011. The cash dividend was payable on the new total shares outstanding after the stock dividend. This represents a 50% increase in the cash dividend. The new share amounts enhance the trading activity in the marketplace and provide Sun a flexible platform for future financing activities. 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 line of credit will be sufficient to satisfy the Company's operating expenses and capital expenditures for the foreseeable future. In the event that economic conditions were to severely worsen for a protracted period of time, the Company would have several options available to ensure liquidity in addition to increased borrowing. Capital expenditures could be postponed since they primarily pertain to long-term improvements in operations. Additional operating expense reductions also could be made. Finally, the dividend to shareholders could be reduced or suspended.

### *Off Balance Sheet Arrangements*

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

The Company uses the equity method of accounting to account for its investments in WhiteOak and High Country Tek. The Company does not have a majority ownership in or exercise control over either of the entities. These investments were not material to the financial statements of the Company at July 2, 2011.

### *Seasonality*

The Company generally has experienced increased sales during the second quarter of the year, largely as a result of the order patterns of our customers. The Company's second quarter net sales, income from operations and net income historically are the highest of any quarter during the year. However, due to the economic conditions prevailing last year, this pattern was not evident in 2010.

***Inflation***

The impact of inflation on the Company’s operating results has been moderate in recent years. 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.

***Critical Accounting Policies and Estimates***

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

*Revenue Recognition*

The Company reports revenues, net of sales incentives, when title passes and risk of loss transfers to the customer. The effect of material non-recurring events is provided for when they become known. Shipping and handling costs billed to distributors and customers are recorded in revenue. Shipping costs incurred by the Company are recorded in cost of goods sold.

*Impairment of Long-Lived Assets*

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

*Accounts Receivable*

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

*Inventory*

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

*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 January 1, 2011. It was determined that the value of the goodwill was not impaired. There is no assurance that the value of the acquired company will not decrease in the future due to changing business conditions. See Note 6 for goodwill amounts.

*Accruals*

The Company makes estimates related to certain employee benefits and miscellaneous accruals. Estimates for employee benefit accruals are based on information received from plan administrators in conjunction with management’s assessments of estimated liabilities related to workers’ compensation, health care benefits and annual contributions to an employee stock ownership plan, established in 2004 as part of the Company’s retirement plan. Estimates for miscellaneous accruals are based on management’s assessment of estimated liabilities for costs incurred.

**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 cyclicality 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 costs, 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 Item 1. "Business," and Item 1A. "Risk Factors" in the Company's Form 10-K for the year ended January 1, 2011, and "Management's Discussion and Analysis of Financial Conditions and Results of Operations" in this Form 10-Q for the quarter ended July 2, 2011. 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 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company is exposed to market risk from changes in interest rates on borrowed funds, which could affect its results of operations and financial condition. The Company's interest rate on its debt financing remains variable based upon the Company's leverage ratio. The Company had no variable-rate debt outstanding at July 2, 2011.

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

**Item 4. CONTROLS AND PROCEDURES**

As of July 2, 2011, the Company's management, under the direction of its Chief Executive Officer and the Chief Financial Officer, carried out an evaluation of the effectiveness of the design and operation of the disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Our disclosure controls and procedures are designed to provide reasonable assurance that the information required to be disclosed in our SEC reports is recorded, processed, summarized and reported within the time periods specified by the SEC's rules and forms, and is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Based upon that evaluation, the Company's Chief Executive Officer and the Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective at the reasonable assurance level as of July 2, 2011, in timely alerting them to material information required to be included in the Company's periodic SEC filings.

There were no changes in the Company's internal controls over financial reporting during the period ended July 2, 2011, that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II
OTHER INFORMATION

Item 1. Legal Proceedings.

None.

Item 1A. Risk Factors.

For information regarding risk factors, please refer to Part I, Item 1A in the Company's Annual Report on Form 10-K for the year ended January 1, 2011.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Reserved.

Item 5. Other Information.

None.

Item 6. Exhibits.

Exhibits:

| Exhibit Number | Exhibit Description |
|---|---|
| 10.1† | Amendment to Sun Hydraulics Corporation Amended and Restated 2004 Nonemployee Director Equity and Deferred Compensation Plan. |
| 10.2† | Fifth Amendment to Sun Hydraulics Corporation 401(k) and ESOP Retirement Plan. |
| 31.1 | CEO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | CFO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | CEO Certification pursuant to 18 U.S.C. § 1350. |
| 32.2 | CFO Certification pursuant to 18 U.S.C. § 1350. |

Exhibit 101.1 Interactive Data File

| | |
|---|---|
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Schema Document |
| 101.CAL | XBRL Calculation Linkbase Document |
| 101.DEF | XBRL Definition Linkbase Document |
| 101.LAB | XBRL Label Linkbase Document |
| 101.PRE | XBRL Presentation Linkbase Document |

† Executive management contract or compensatory plan or arrangement.

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 August 10, 2011.

SUN HYDRAULICS CORPORATION

By: /s/ Tricia L. Fulton
Tricia L. Fulton
Chief Financial Officer (Principal Financial and Accounting Officer)

Exhibit 10.1

AMENDMENT TO
SUN HYDRAULICS CORPORATION
2004 NONEMPLOYEE DIRECTOR EQUITY AND DEFERRED COMPENSATION PLAN
(AS AMENDED AND RESTATED EFFECTIVE MARCH 1, 2008)

(i) New Section 4.6:

4.6 TERMINATION OF DEFERRALS. Notwithstanding any other provision of this Article IV or any Deferral Election, no deferral of Share Compensation and/or Fees shall be made on or after June 7, 2011.

(ii) New Section 7.8:

7.8 PAYMENT OF DEFERRED ACCOUNTS. Notwithstanding any other provision of this Article VII, all Deferred Account Balances in Deferred Accounts for Nonemployee Directors, and any additions or earnings thereon accrued through the date of distribution, shall be distributed in accordance with the Plan to the respective Nonemployee Directors at their direction; provided that no payment shall be made prior to June 7, 2012, and all distributions must be completed no later than June 7, 2013, and otherwise in accordance with applicable regulations under the Internal Revenue Code.

Adopted and effective June 7, 2011

Exhibit 10.2

**FIFTH AMENDMENT TO**
**SUN HYDRAULICS CORPORATION 401(k) AND ESOP RETIREMENT PLAN**

The Sun Hydraulics Corporation 401(k) and ESOP Retirement Plan (hereinafter referred to as the “Plan”) provides in Section 8.1 for subsequent plan amendments. Sun Hydraulics Corporation (“Company”) now wishes to amend the Plan in the manner described below to make certain changes to the Plan requested by the Internal Revenue Service as conditions to the issuance of a favorable IRS determination letter on the Plan. The Plan is therefore, amended as follows:

1. Section 1.33 of the Plan, defining the term “Section 414(s) Compensation,” is hereby amended to read as follows:

1.33 “414(s) Compensation” means the Participant’s wages and other compensation paid by the Employer for which the Employer is required to furnish the Participant a written statement under Sections 6041(d), 6051(a)(3) and 6052 of the Code. The period for determining 414(s) Compensation must be the calendar year ending with or within the Plan Year. An Employer shall further limit the period taken into account to that part of the calendar year in which an Employee was a Participant in the component of the Plan being tested. The period used to determine 414(s) Compensation must be applied uniformly to all Participants for the Plan Year.

For Plan Years beginning after December 31, 1996, for purposes of this Section, the family member aggregation rules of Code Section 4l4(q)(6) (as in effect prior to the Small Business Job Protection Act of 1996) are eliminated.

2. Section 4.5 of the Plan, entitled “Allocation of Contributions and Earnings”, is amended by revising subsection 4.5(j) to read as follows:

“For the purposes of this Section, “415 Compensation” in excess of $150,000 (or such other amount provided in the Code) shall be disregarded. Such amount shall be adjusted for increases in the cost of living in accordance with Code Section 401(a)(17)(B), except that the dollar increase in effect on January 1 of any calendar year shall be effective for the Plan Year beginning with or within such calendar year. If “415 Compensation” for any prior determination period is taken into account in determining a Participant’s minimum benefit for the current Plan Year, the “415 Compensation” for such determination period is subject to the applicable annual “415 Compensation” limit in effect for that prior period. Notwithstanding the foregoing, the 415 Compensation of each Participant taken into account for any Plan Year beginning after December 31, 2001, shall not exceed $200,000, as adjusted for cost-of-living increases in accordance with Code Section 401(a)(17)(B). For this purpose, in determining the minimum benefit in Plan Years beginning on or after January 1, 1989, the annual “415 Compensation” limit in effect for determination periods beginning before that date is $200,000 (or such other amount as adjusted for increases in the cost of living in accordance with Code Section 415(d) for determination periods beginning on or after January 1, 1989, and in accordance with Code Section 401(a)(17)(B) for determination periods beginning on or after January 1, 1994). For determination periods beginning prior to January 1, 1989, the $200,000 limit shall apply only for Top Heavy Plan Years and shall not be adjusted. For any short Plan Year the "415 Compensation" limit shall be an amount equal to the "415 Compensation" limit for the calendar year in which the Plan Year begins multiplied by the ratio obtained by dividing the number of full months in the short Plan Year by twelve (12)."

3. Section 4.6 of the Plan, entitled "Actual Deferral Percentage Tests," is revised by deleting the last paragraph of Subsection 4.6(a), effective for Plan Years beginning on or after January 1, 2002.

4. Section 4.7 of the Plan, entitled "Adjustment to Actual Deferral Percentage Tests," is revised by deleting subparagraphs 4.7(b)(2) and (4), and renumbering the other subparagraphs of Subsection 4.7(b) accordingly.

5. Section 4.9 of the Plan, entitled "Adjustment to Actual Contribution Percentage Tests," is revised by deleting subparagraphs 4.9(f)(2) and (4), and renumbering the other subparagraphs of Subsection 4.9(f) accordingly.

6. Section 4.11 of the Plan, entitled "Adjustment for Excess Annual Additions" is revised by replacing the words "…the annual additions under this Plan would cause…" in the first sentence of Subsection 4.11(a) with the words "…the annual additions under this Plan for any limitation year beginning prior to July 1, 2007 would cause…"

7. Article IV of the Plan, entitled "Contributions and Allocations" is amended by adding the following new Section 4.18 at the end thereof:

"4.18 Income Adjustment. Any excess deferred compensation distributed under Section 4.2(f), any excess contributions distributed pursuant to Section 4.7(a) and excess aggregate contributions distributed pursuant to Section 4.9(b) shall be adjusted for any investment income or loss up to the date of the distribution. The investment income or loss attributable to such distributable contributions shall be the sum of (i) the income or loss on such contributions for the Plan Year, plus (ii) the income or loss on such contributions for the gap period, determined under any reasonable method selected by the Plan Administrator. If no other method has been specified by the Plan Administrator, the investment income or loss allocable to such excess contributions shall be the sum of: (1) income or loss allocable to the Participant's Elective Account (or, for purposes of Section 4.9(b), Account) for the Plan Year multiplied by a fraction, the numerator of which is such Participant's excess contributions for the Plan Year and the denominator is the Participant's account balance attributable to elective deferrals (or, for purposes of Section 4.9(b), matching contributions) without regard to any income or loss occurring during such Plan Year; and (2) ten percent of the amount determined under (1) multiplied by the number of whole calendar months between the end of the Plan Year and the date of distribution, counting the month of distribution if distribution occurs after the 15th of such month. Any method used to determine income or loss hereunder shall be used consistently for all Participants in determining the income or loss allocable to distributable contributions hereunder and shall be the same method that is used by the Plan in allocating income or loss to Participants' Accounts. For purposes of this paragraph, the "gap period" means the period between the end of the Plan Year and the date of distribution; provided, however, that income or loss for the gap period may be determined as of a date that is no more than seven days before the date of distribution.

For Plan Years beginning after December 31, 2007, notwithstanding anything in the preceding paragraph or elsewhere in this Section 4.18 to the contrary, the requirement that gap period income be allocated pursuant to Treasury Regulations Section 1.401(k)-2(b)(2) shall no longer apply to excess aggregate contributions, excess contributions, and excess deferred compensation returned to a Participant. Thus, with respect to such items, the Plan Administrator may exclude gap period income that is allocated to Participants' accounts prior to distribution."

8. Section 5.2 of the Plan, entitled "Acquisition Loans" is amended by revising Subsection 5.2(c) to read as follows:

"(c) Loan Payment. Repayment of principal and interest on any Acquisition Loan shall be made by the Trustee from contributions made pursuant to Article IV which are designated to be used for the repayment of the Acquisition Loan and may be made pursuant to the provisions of Section 5.10(b) from (i) to the extent permitted by law, cash dividends on Employer Stock acquired with the proceeds of an Acquisition Loan, which are allocated to Participant's ESOP Accounts and earnings, if any, thereon; and (ii) cash dividends on Employer Stock held in the Loan Suspense Account and earnings, if any, thereon. The payments made with respect to an Acquisition Loan by the Trustee during any Plan Year shall not exceed an amount equal to the sum of such contributions and dividends received during the Plan Year or in prior Plan Years less the amount of such loan payments made in prior Plan Years."

Section 5.2 is further amended by adding the following as additional Subsections 5.2(f) and 52(g):

"(f) Exclusive Benefit. An Acquisition Loan must be primarily for the benefit of Participants in the Plan.

(g) Notwithstanding any other provision of this Plan to the contrary, the ESOP Trust may not enter in any arrangement granting any other person a put option with respect to Employer Stock except as described in Section 5.6 below, and may not obligate itself to acquire Employer Stock or other securities from a particular stockholder at an indefinite time determined upon the happening of a future event such as the death of the stockholder."

9. Section 5.10, entitled "Distribution of Dividends on Employer Stock" is revised by adding the following as a new Subsection 5.10(c):

"(c) Dividends paid with respect to the shares of Company Stock allocated to a Participant's Company Stock Account may be reinvested in shares of Company Stock in accordance with Section 5.10(a)(ii) or (iii) above only if the portion of the affected Participants' Accounts attributable to the reinvested dividends is 100 percent vested and non-forfeitable."

10. Section 5.11 of the Plan, entitled "Prohibited Allocations of Securities in an S Corporation," is deleted from the Plan.

11. Section 6.3 of the Plan, entitled "Valuation of Employer Stock," is amended by adding the following new sentence to the end thereof:

"Notwithstanding the foregoing, in the case of a transaction between the Trust Fund and a disqualified person (within the meaning of Section 4975 of the Code), the value of the Employer Company Stock shall be determined as of the date of the transaction, whether or not this date is a Valuation Date."

12. Section 7.4 of the Plan, entitled "Determination of Benefits Upon Termination," is amended by adding the following as a new subsection 7.4(f):

"(f) The amount of any Forfeiture from a Participant's Accounts shall first be taken from the unvested portion of the Participant's Accounts other than his ESOP Account. If the Forfeiture of such other Accounts is not sufficient to reduce the fair market value of his unvested interest in his or her Accounts to the percentage of the total balance of his Accounts determined under Subsection (b) above, the remainder of the Forfeiture shall be deducted from the Participant's ESOP Account."

13. Section 8.2 of the Plan, entitled "Termination," is amended by adding the following new Subsection 8.2(c):

"(c) Notwithstanding anything in the preceding paragraph to the contrary, amounts held in the Participant's Elective Deferral Account may not be distributed as a result of the termination of the Plan if a successor defined contribution plan is established by the Employer within the period ending twelve months after distribution of all assets from the Plan. For this purpose, a defined contribution plan is not treated as a successor defined contribution plan if the plan is an employee stock ownership plan (as defined in Code Section 4975(e)(7) or 409(a)), a simplified employee pension plan (as defined in Code Section 408(k)), a SIMPLE IRA plan (as defined in Code Section 408(p)), a plan or contract that satisfies the requirements of Code Section 403(b), or a plan that is described in Code Sections 457(b) or 457(f). Furthermore, if at all times during the 24-month period beginning 12 months before the date of the Plan's termination, fewer than 2% of the Participants in the Plan as of the date of Plan termination are eligible under the other defined contribution plan, then the other defined contribution plan is not a successor defined contribution plan."

14. Section 9.3 of the Plan, entitled "Determination of Top Heavy Status for Plan Years Beginning After December 31, 2001" is amended by revising Subsection 9.3(b)(1) to read as follows:

"Distributions during year ending on the determination date. The present values of accrued benefits and the amounts of account balances of an Employee as of the determination date shall be increased by the distributions made with respect to the Employee under the Plan and any plan aggregated with the Plan under Code Section 416(g)(2) during the 1-year period ending on the determination date. The preceding sentence shall also apply to distributions under a terminated plan which, had it not been terminated, would have been aggregated with the Plan under Code Section 416(g)(2)(A)(i). In the case of a distribution made for a reason other than severance from employment, death, or disability, this provision shall be applied by substituting "5-year period" for "1-year period."

15. In all other respects, the terms of the Plan, as amended to date, are hereby ratified and confirmed.

**IN WITNESS WHEREOF**, Sun Hydraulics Corporation has caused this Fifth Amendment to the Plan to be executed by its duly authorized representative this 7th day of June, 2011.

**SUN HYDRAULICS CORPORATION**

**Attest:**

| | |
|---|---|
| /s/ Gregory C. Yadley | By: /s/ Tricia L. Fulton |
| Gregory C. Yadley, Secretary | Tricia L. Fulton, Chief Financial Officer |

**EXHIBIT 31.1**

CERTIFICATION

I, Allen J. Carlson, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the quarter ended July 2, 2011, of Sun Hydraulics Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 10, 2011

/s/ Allen J. Carlson

Allen J. Carlson
President, Chief Executive Officer

**EXHIBIT 31.2**

CERTIFICATION

I, Tricia L. Fulton, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the quarter ended July 2, 2011, of Sun Hydraulics Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 10, 2011

/s/ Tricia L. Fulton

Tricia L. Fulton
Chief Financial Officer

**EXHIBIT 32.1**

**CERTIFICATION PURSUANT TO 18 U.S.C. § 1350**

I, Allen J. Carlson, the Chief Executive Officer of Sun Hydraulics Corporation (the "Company"), certify that (i) the Quarterly Report on Form 10-Q for the Company for the quarter ended July 2, 2011 (the "Report"), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Allen J. Carlson
Chief Executive Officer
August 10, 2011

**EXHIBIT 32.2**

**CERTIFICATION PURSUANT TO 18 U.S.C. § 1350**

I, Tricia L. Fulton, the Chief Financial Officer of Sun Hydraulics Corporation (the "Company"), certify that (i) the Quarterly Report on Form 10-Q for the Company for the quarter ended July 2, 2011 (the "Report"), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Tricia L. Fulton
Chief Financial Officer
August 10, 2011