

**Action Summary – 15 April 2013**

Analyst Theodore R. O'Neill *is initiating coverage of TKR with a Hold rating and a \$60 price target*

- Shares are not trading on fundamentals and near our price target prompting us to initiate coverage with a Hold rating
- Shares are being held aloft by the expectation that activist shareholders will “unlock substantial value” by spinning out the steel business which we believe is a BAD idea for long-term investors and employees
- The only value being unlocked by this action is in the hedge fund community that is long the “activist trade”
- The timing could not be worse for creating a standalone steel business: we are likely heading into an oversupply situation and economic growth is anemic. Investors won't be clamoring for small cap steel ideas under this scenario.
- While we think the stock may move lower if shareholders vote NO on the spin-out, we think in the longer term, the combined company will have greater value than two standalone businesses

Current share price: \$54.05	Market cap: \$5.3 billion	GAAP 2014 P/E: 12	2013 EV/Sales: 1.2
Shares outstanding: 97 million	Insider ownership: 22%	Avg. trading volume: 766 million	Dividend & Yield: \$0.92/1.7%

**Macroeconomic context**

- Slow growth in U.S. GDP likely to affect 2013 revenue estimates
- U.S. GDP growth is back end loaded in 2013

**Estimates (GAAP EPS in dollars – GAAP Revenue in millions)**

Period	EPS	Revenue	Net Margin
1Q12A	\$1.58	\$1,421	11.0%
2Q12A	\$1.86	\$1,343	13.7%
3Q12A	\$0.83	\$1,143	7.1%
4Q12A	<u>\$0.78</u>	<u>\$1,080</u>	<u>7.0%</u>
FY12A	<u>\$5.07</u>	<u>\$4,987</u>	<u>9.9%</u>
1Q13E	\$0.72	\$1,107	6.3%
2Q13E	\$0.71	\$1,095	6.3%
3Q13E	\$1.03	\$1,169	8.6%
4Q13E	<u>\$1.13</u>	<u>\$1,235</u>	<u>8.9%</u>
FY13E	<u>\$3.60</u>	<u>\$4,606</u>	<u>7.6%</u>
1Q14E	\$0.94	\$1,180	7.7%
2Q14E	\$1.25	\$1,260	9.6%
3Q14E	\$1.28	\$1,275	9.8%
4Q14E	<u>\$1.12</u>	<u>\$1,190</u>	<u>9.1%</u>
FY14E	<u>\$4.60</u>	<u>\$4,905</u>	<u>9.1%</u>

Note: Calculation of full year data may not add up due to rounding. See our full model in the back of this report. Excel versions available.

**Cash balance (in millions)**

• 2012A	• \$586.4
• 2013E	• \$362.2
• 2014E	• \$482.1

**Debt (in millions)**

• 2012A	• \$455
• 2013E	• \$450
• 2014E	• \$450

Debt is owed to the Department of Energy

**EBITDA (in millions)**

• 2012A	• \$991.8
• 2013E	• \$762.2
• 2014E	• \$911.4

**Risks/Valuation**

- Steel business is facing potential excess supply
- Our \$60 target is derived using a modified dividend discount model, details of which can be found in this report

**Company description**

The Timken Company, a global industrial technology company, engineers, manufactures and markets mechanical components and high-performance steel. Timken® bearings and engineered steel bars and tubes, as well as transmissions, gearboxes, chain, related products and services, support markets worldwide. HQ is in North Canton, OH.

Figure 1 – The Timken Company - Trading snapshot



Stock volume has declined significantly since the spin-off was first advocated by activist shareholders

Source: BigCharts.marketwatch.com

**ViewPoint**

- 1) We are looking for a better entry point for investing in this stock and we think we will get it
- 2) We hope the CalSTRS proposal is voted down as this will facilitate a better entry point and greater liquidity
- 3) We think there is some risk that consensus estimates will have to be trimmed post the April 24<sup>th</sup> 1Q13 conference call. Our 2013 and 2014 estimates anticipate falling consensus.
- 4) We believe the steel business will see a 12% decline in 2013 but that the Mobile segment will decline more due to declining growth in the EU, which will hurt this segments revenue or margins.
- 5) 2013 Earnings appear to be down significantly but 2012 EPS was juiced by approximately \$1.00 per share of non-operating income
- 6) Two catalyst to move the stock in our favor are the April 24<sup>th</sup> 1Q13 CC and the May 7<sup>th</sup> annual meeting
- 7) We do not see a big risk to our neutral position on the stock. Stock is not trading on fundamentals in our opinion and the activist trade has already played out. We would wait for a better entry point and greater volume.

We would wait for a better entry point

**We believe the CalSTRS Proposal is a bad idea for long-term investors and steel unit employees**

Relational Investors and the California State Teachers' Retirement System are urging investors to vote for a proposal to spin-out the Timken steel division. As evidence that the market likes this idea, it points to the \$15 rise in the price of Timken stock (since the spin-out was proposed) as proof. This is not proof the market approves. *It is* proof that hedge funds find it an easy trade to go long any stock with credible activist involvement. The activists make the point that the stock will go down if shareholders vote no to Item 6. Yes, the stock is likely to fall following a NO vote on Item 6 but a fall in stock price following a NO vote is not a statement on the merits of spinning out the steel business. It is simply the result of hedge funds unwinding the trade.

Spin-out makes sense at the top of the market, not heading into a downturn

The timing could not be worse. The majority of steel manufacturers have been adding capacity over the last few years (Timken included) which is likely to lead to excess supply. Investors are not going to be clamoring for small cap steel stocks when the industry is oversupplied and global economic growth is anemic. Under this scenario, the stock of Stand-alone steel is likely to fall. As a standalone steel business, in the situation we described above, it will have little choice but to lay off employees, cut benefits or both.



## The Timken Company

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### Financial Analysis

Company DSOs and inventory turns are reasonable. We forecast an 8% decline in revenue in 2013 and a healthy drop in earnings. According to our cash flow analysis, cash balances are likely to fall by about \$200 million by the end of 2013 before rising again in 2014. Our estimates are at the very low end of the range and we anticipate consensus to decline.

### Forecasts

We are forecasting an 8% revenue decline in 2013 followed by 6% growth in 2014. We expect to see year-over-year comps improve in 3Q13. Our forecast for 2013 growth in the Mobile segment is below management expectations.

### Price Target

Our price target is derived using a modified dividend discount model. Intellectually we assume we just bought 100% of the outstanding stock and the earnings stream flows to a single investor. What is the value of that stream? We assume all the annual earnings are dividends, we grow them as shown in the model at the back of this report and then over the course of the next 10 years we scale the growth back until earnings growth matches GDP. We then discount those "dividends" at 13%. This model probably understates the tax benefits thus could be seen as understating the price target but offsetting this is that the model never shows a decline in earnings (except in 2013) and thus we feel the two balance out.

We assume that a single investor owns all the stock. What is the discounted value of the earnings stream?

### Field Work

We have made two visits to company headquarters and visited each of the three steel plants.

### Overview

The Company was founded in 1899 by Henry Timken, who received two patents on the design of a tapered roller bearing. Timken grew to become the world's largest manufacturer of tapered roller bearings. Over the years, the Company has expanded its breadth of bearing products beyond tapered roller bearings to include cylindrical, spherical, needle and precision ball bearings. In addition to bearings, Timken further broadened its portfolio to include metallurgy, a wide array of friction management and mechanical power transmission products and maintenance services to improve the operation of customers' machinery and equipment, such as lubricants, seals, bearing maintenance tools and condition-monitoring equipment.

The Company also manufactures power transmission components and assemblies, as well as systems such as helicopter transmissions, high-quality alloy steel, bars and tubing to custom specifications to meet demanding performance requirements, and finished and semi-finished steel components. Timken's global footprint consists of 62 manufacturing facilities, 10 technology and engineering centers, 12 distribution centers and nearly 20,000 employees. Timken operates in 30 countries and territories.

**Markets**

Timken makes products for a wide range of industries.

**Figure 2 – The Timken Company – Industry map**

<u>Industry</u>	<u>Product or Application</u>
Aerospace	Products and systems for commercial and military aircraft and systems
Agriculture	Products and systems for everything from hay balers to combines
Automotive and Heavy Truck	Products and systems that improve fuel economy, reduce emissions and improve performance
Bearings manufacturers	High quality steel
Cement and Aggregate	Products and services for severe environments
Construction	Products to enhance the performance of earthmovers, bulldozers, cranes, etc.
Consumer	Products for recreational vehicles and small motors
Coal, Oil and Gas	Products that improve performance in drilling and power plant operation
Health	Precision and miniature bearings used in dental drills and surgical tools
Mining	Products to reduce maintenance costs
Paper	Products that lower maintenance costs for everything from pulp processing to printing presses
Primary Metal	Products for rolling mills
Rail	Global standard for locomotive and rail car builders and operators
Wind Energy	Products to lower maintenance costs and improve performance and uptime

Source: The Timken Company and Litchfield Hills Research, LLC

**Industry Segments**

The Company operates under two business groups and four reportable segments. The two groups are the Steel Group and the Bearings and Power Transmission Group. The Bearings and Power Transmission Group is composed of three operating segments: (1) Mobile Industries, (2) Process Industries and (3) Aerospace and Defense. These three operating segments and the Steel Group comprise the Company's four reportable segments.

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The Company's reportable segments are business units that target different industry segments or types of product. Each reportable segment is managed separately because of the need to specifically address customer needs in these different industries.

### Segment #1 – Mobile Industries

- 34 % of total revenue in 2012
- We expect a 14% decline in revenue for this segment in 2013
- We expect a larger decline than management foresees

The Mobile Industries segment provides bearings, power transmission components and related products and services and is the core historic market of the company. Customers of the Mobile Industries segment include original equipment manufacturers and suppliers for motorcycles, passenger cars, light trucks, medium and heavy-duty trucks, rail cars, locomotives and agricultural, construction and mining equipment. Customers also include aftermarket distributors of automotive products.

Figure 3 – The Timken Company – Pit Truck and European Train



Source: Getty Images

### Segment #2 Process Industries

- 27% of sales in 2012
- We expect growth of 2% for this segment in 2013

The Process Industries segment provides bearings, power transmission components and related products and services. Customers of the Process Industries segment include original equipment manufacturers of power transmission, energy and heavy industries machinery and equipment, including rolling mills, cement and aggregate processing equipment, paper mills, sawmills, printing presses, cranes, hoists, drawbridges, wind energy turbines, gear drives, coal conveyors and

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crushers, drilling equipment and food processing equipment. Customers also include aftermarket distributors of products other than those for steel and automotive applications.

Figure 4 – The Timken Company – Wind Turbine and Coal Conveyor



Source: Getty Images

### Segment #3 Aerospace and Defense

- 7% of total revenues in 2012
- We expect 8% growth for this segment in 2013

The Aerospace and Defense segment manufactures bearings, helicopter transmission systems, rotor head assemblies, turbine engine components, gears and other precision flight-critical components for commercial and military aviation applications. The Aerospace and Defense segment also provides aftermarket services, including repair and overhaul of engines, transmissions and fuel controls as well as aerospace bearing repair and component reconditioning. In addition, the Aerospace and Defense segment also manufactures bearings for original equipment manufacturers of health and positioning control equipment.

Figure 5 – The Timken Company – Rotorheads for helicopters



Source: The Timken Company

#### Segment #4 – Engineered Steel

- 33% of total revenue in 2012
- We expect a 12% decline in revenue for this segment in 2013

The Steel segment manufactures more than 300 standard types of steel and over 450 customized alloy grades of carbon and alloy steel, which are produced in both solid and tubular sections with a variety of lengths and finishes. The Steel segment also manufactures custom-made steel products for both industrial and automotive applications, including precision steel components. Its specialty steels are used in oil drilling pipe, bit and collars, hub, axles, crankshafts, connecting rods, bearing races and rolling elements, bushings, fuel injectors, wind energy drive shafts and other demanding application. Approximately 10% of the Company's steel is consumed directly in its bearing operations however, including indirect use the percentage is much larger. In addition, sales are made to other anti-friction bearing companies and to the automotive and truck, forging, construction, industrial equipment, oil and gas drilling companies and to steel service centers. This is a somewhat strategically important business line as alloyed steel is the main component of bearings and it provides valuable quality control for its bearing products.

#### Product Line P&L

The Company reports profitability by segment excluding (interest and taxes and special items such as impairment and restructuring charges, rationalization and integration costs, one-time gains or losses on sales of assets, allocated receipts received or payments made under the Continued Dumping and Subsidy Offset Act (CDSOA), gains and losses on the dissolution of a subsidiary and other items similar in nature). The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies.

Intersegment sales and transfers are recorded at values based on market prices, which creates intercompany profit on intersegment sales or transfers that is eliminated in consolidation. While interesting, we would likely disagree with the methodology used to generate this information. It is highly subjective and politically fraught. Complicating the analysis, Timken does not allocate all corporate overhead and the unallocated corporate expense is large enough that it could swing one of the segments from profit to a loss. Investors should take management self-reporting of EBIT segment margins with a large grain of salt.

Export sales from the United States and Canada are less than 10% of revenue. The Company's Bearings and Power Transmission Group has historically participated in the global bearing industry, while the Steel Group has concentrated primarily on U.S. customers.



**Products**

The Timken Company manufactures two core product lines: anti-friction bearings and steel products. Differentiation in these two product lines is achieved by either: (1) differentiation by bearing type or steel type or (2) differentiation in the applications of bearings and steel. Bearings come in four classes like bond ratings ranging from C/3 or low precision, up through B/0, A/00 and the highest precision AA/000.

***Tapered Roller Bearings***

The tapered roller bearing is Timken's principal product in the anti-friction industry segment. It consists of four components: (1) the cone or inner race, (2) the cup or outer race, (3) the tapered rollers, which roll between the cup and cone and (4) the cage, which serves as a retainer and maintains proper spacing between the rollers. Timken manufactures or purchases these four components and then sells them in a wide variety of configurations and sizes.

Figure 6 – The Timken Company – Tapered Roller Bearings



Source: The Timken Company

The tapered rollers permit ready absorption of both radial and axial load combinations. For this reason, tapered roller bearings are particularly well adapted to reducing friction where shafts, gears or wheels are used. The uses for tapered roller bearings are diverse and include applications on passenger cars, light and heavy trucks and trains, as well as a wide variety of industrial applications, ranging from very small gear drives to bearings over two meters in diameter for wind energy machines. A number of applications utilize bearings with sensors to measure parameters such as speed, load, temperature or overall bearing condition.

Matching bearings to the specific requirements of customers' applications requires engineering and, often, sophisticated analytical techniques. The design of Timken's tapered roller bearing permits distribution of unit pressures over the full length of the roller.



*Precision Cylindrical and Ball Bearing*

Figure 7 – The Timken Company - Precision Cylindrical and Ball Bearings



Source: The Timken Company

Timken's aerospace and super precision facilities produce high-performance ball and cylindrical bearings for ultra high-speed and/or high-accuracy applications in the aerospace, medical and dental, computer and other industries. These bearings utilize ball and straight rolling elements and are in the super precision end of the general ball and straight roller bearing product range in the bearing industry. A majority of Timken's aerospace and super precision bearings products are custom-designed bearings and spindle assemblies. They often involve specialized materials and coatings for use in applications that subject the bearings to extreme operating conditions of speed and temperature. These bearings are used in the newest Mars rover, the Curiosity.

*Spherical and Cylindrical Bearings*

Figure 8 –The Timken Company – Spherical Bearing



Source: The Timken Company

Timken produces spherical and cylindrical roller bearings for large gear drives, rolling mills and other process industry and infrastructure development applications. These products are sold worldwide to original equipment manufacturers and industrial distributors serving major industries, including construction and mining, natural resources, defense, pulp and paper

production, rolling mills and general industrial goods.

### *Chains and Augers*

Through the acquisition of Drives LLC (Drives) in 2011, Timken manufactures American National Standards Institute (ANSI) precision roller chain, pintle chain (go ahead and Google it), agricultural conveyor chain, engineering class chain, and oil field roller chain and auger products. These highly engineered products are used in a wide range of mobile and industrial machinery applications, including agriculture, oil and gas, aggregate and mining, primary metals, forest products and other heavy industries. They also are utilized in the food and beverage and packaged goods sectors, which often require high-end, specialty products including stainless steel and corrosion-resistant roller chains.

### *Gear-Drive Systems*

Through the acquisition of the assets of Philadelphia Gear Corp. (Gears and Services) in 2011, Timken provides aftermarket gear box repair services and gear-drive systems for the industrial, energy and military marine sectors, including refining and pipeline systems, mining, cement, pulp and paper making and water management systems.

### *Service*

Less than 5% of the business involves providing bearing reconditioning services for industrial and railroad customers, both domestically and internationally.

### *Aerospace Products and Services*

Timken provides parts, systems and services for the aerospace market, where they are used in helicopters and fixed-wing aircraft for the military and commercial aviation. Timken provides design, manufacture and testing for a wide variety of power transmission and drive train components including transmissions, gears and rotor head components. Other parts include bearings, airfoils (such as blades, vanes, rotors and diffusers), nozzles and other precision flight critical components. As an example of a specialized part, consider the demand on aircraft landing wheel bearings. When a 500-ton airplane touches down on the runway, all the load is transmitted from the airframe to the ground through the wheel bearings to the landing wheels. Under these conditions, the wheels accelerate from 0 to 170+ MPH in less than a second and experience temperature ranges from sub-zero to extreme heat at braking.

Figure 9 – The Timken Company – Aircraft Landing Gear Bearing



Source: The Timken Company

Timken also supplies comprehensive aftermarket maintenance, repair and overhaul services and parts for gas turbine engines, gearboxes and accessory systems in rotary and fixed-wing aircraft. Services range from aerospace bearing repair and component reconditioning to the complete

overhaul of engines, transmissions and fuel controls.

***Engineered Steel***

Steel products include steels of low and intermediate alloy, as well as some carbon grades. These products are available in a wide range of solid and tubular sections with a variety of lengths and finishes. These steel products are used in a wide array of applications, including bearings, automotive transmissions, engine crankshafts, oil-drilling components and other similarly demanding applications.

Timken also produces custom-made steel products, including steel components for automotive and industrial customers. The steel components business has provided the Company with the opportunity to further expand its market for tubing and higher value-added steel sales. It also enables Timken's traditional tubing customers in the automotive and bearing industries to take advantage of higher-performing components that cost less than current alternative products. Customization of products is an important component of the Company's steel business. Timken seamless tubing is used in demanding well drilling applications.

Figure 10 – The Timken Company – Specialty Steel Components



Source: The Timken Company

Timken also makes integrated bearing assemblies for a variety of applications such as the bearing shown below. It consists of a bearing, the hub, anti-locking brake and speed sensor.

Figure 11 – The Timken Company – Integrated Hub and Bearing Assembly for Automotive Applications



Source: The Timken Company

***Lubricants and lubricators***

Bearings need lubrication and Timken makes its own line of lubricants and lubrication delivery systems or lubricators. Some bearings need to be lubricated on a regular basis but are not easy to

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get to like wind turbines in the North Sea. For those applications, the company makes a special product. The Timken® wind energy lubrication system provides consistent, lubrication for wind turbine main-shaft bearings. The system is available in two configurations and features a single pump capable of working with either series-progressive or injector-based lubricant delivery methods.

Figure 12 – The Timken Company – Wind Energy Lubrication Systems



Source: The Timken Company

For other application, it makes lubricators that dispense in place as a single time use.

Figure 13 – The Timken Company – Single point lubricators



Source: The Timken Company

For bearings that experience heavy loads over long periods, such as railroad cars, Timken sell lubricants in bulk.

Figure 14 – The Timken Company – Premium Rail Grease



Source: The Timken Company

#### Sales and Distribution

Timken's products in the Bearings and Power Transmission Group are sold principally by its own internal sales organizations. A portion of the Process Industries segment's sales are made through authorized distributors.

Traditionally, a focus of the Company's sales strategy has consisted of collaborative projects with customers. For this reason, the Company's sales forces are primarily located in close proximity to its customers rather than at production sites. In some instances, the sales forces are located inside customer facilities.

The Company has a joint venture in North America focused on joint logistics and e-business services. This alliance is called CoLinX, LLC and was founded by Timken, SKF Group, INA and Rockwell Automation (ROK-NR). The current alliance members are Timken, SKF Group, the Schaeffler Group, Rockwell Automation and Gates Corporation. The e-business service is focused on information and business services for authorized distributors in the Process Industries segment.

Timken's steel products are sold principally by its own sales organization. Most orders are customized to satisfy customer-specific applications and are shipped directly to customers from Timken's steel manufacturing plants. Approximately 10% of Timken's Steel Group net sales are used internally. Sales are made to other anti-friction bearing companies and to the automotive and truck, forging, construction, industrial equipment, oil and gas drilling and aircraft industries and to steel service centers.

Timken has entered into individually negotiated contracts with some of its customers in its Bearings and Power Transmission Group and Steel Group. These contracts may extend for one or more years and, if a price is fixed for any period extending beyond current shipments, customarily include a commitment by the customer to purchase a designated percentage of its requirements from Timken.

#### Competition

The anti-friction bearing business is highly competitive in every country in which Timken sells products. Timken competes primarily based on price, quality, timeliness of delivery, product design and the ability to provide engineering support and service on a global basis. The Company competes with domestic manufacturers and many foreign manufacturers of anti-friction bearings, including SKF Group, Schaeffler Group, NTN Corporation, JTEKT Corporation and NSK Ltd.

Competition within the steel industry, both domestically and globally, is intense and is expected to remain so. Principal bar competitors include foreign-owned domestic producers Gerdau Special Steel North America (wholly owned by Brazilian steelmaker Gerdau, S.A), Republic Engineered

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Products (a unit of Mexican steel producer ICH) along with domestic steel producers Steel Dynamics (STLD-NR) and Nucor Corporation (NUE-NR). Seamless tubing competitors include foreign-owned domestic producers ArcelorMittal Tubular Products (MT-NR), V&M Star Tubes (a unit of Vallourec, S.A.), and Tenaris, S.A. Additionally, Timken competes with a wide variety of offshore producers of both bars and tubes, including Sanyo Special Steel and Ovako. Timken also provides value-added steel products to its customers in the energy, industrial and automotive sectors. Competitors within the value-added segment include Linamar, Jernberg, and Curtis Screw Company.

### Trade Law Enforcement

The U.S. government has six antidumping duty orders in effect covering ball bearings from France, Germany, Italy, Japan and the United Kingdom and tapered roller bearings from China. The Company is a producer of all of these products in the United States. The U.S. government determined in August 2006 that each of these six antidumping duty orders should remain in effect for an additional five years, after which the orders could be reviewed again. In addition to dealing with a market that is highly competitive, Timken has to deal with counterfeit Timken products.

#### *Continued Dumping and Subsidy Offset Act (CDSOA)*

The CDSOA provides for distribution of monies collected by U.S. Customs from antidumping cases to qualifying domestic producers where the domestic producers have continued to invest in their technology, equipment and people. The Company reported CDSOA receipts, net of expenses, of \$108 million in 2012.

In September 2002, the World Trade Organization (WTO) ruled that such payments are not consistent with international trade rules. In February 2006, U.S. legislation was enacted that ends CDSOA distributions for dumped imports covered by antidumping duty orders entering the United States after September 30, 2007. It is possible that court rulings might prevent the Company from receiving any CDSOA distributions in 2013 and beyond.

### Backlog

The backlog of orders of Timken's domestic and overseas operations is estimated to have been \$1.8 billion at December 31, 2012 and \$2.3 billion at December 31, 2011. Actual shipments are dependent upon ever-changing production schedules of customers. We do not believe that its backlog data are reliable indicators of future sales or shipments.

### Raw Materials

The principal raw materials used by Timken in its North American bearing plants to manufacture bearings are its own steel tubing and bars, strip steel and energy resources. Outside North America, the Company purchases raw materials from local sources with whom it has worked closely to ensure steel quality according to the Company's demanding specifications.

The principal raw materials used by Timken in steel manufacturing are scrap metal, nickel, molybdenum and other alloys. The availability and prices of raw materials and energy resources are subject to curtailment or change due to, among other things, new laws or regulations, changes in demand levels, suppliers' allocations to other purchasers, interruptions in production by suppliers, changes in exchange rates and prevailing price levels. For example, the weighted average price of scrap metal increased 14.7% from 2006 to 2007, increased 56.2% from 2007 to 2008, decreased 49.0% from 2008 to 2009, increased by 59% from 2009 to 2010, increased 23.4% in from 2010 to 2011 and decreased 6.1% from 2011 to 2012.

We expect the Company to be able to pass a significant portion of these increased costs through to customers in the form of price increases or raw material surcharges.

### Research

One of the strategic advantages Timken has over its competitors is the vast trove of data collected



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on bearings use and performance over the last 100 years. This allows it to qualify the performance of new products more rapidly than others do because it has the statistical data to prove how a change in a design will behave in a real world setting. This translates into a reduced risk of failures in the field. Timken operates a network of technology and engineering centers to support its global customers with sites in North America, Europe and Asia. This network develops and delivers innovative friction management and power transmission solutions and technical services. The largest technical center is located in North Canton, Ohio, near Timken's world headquarters. Other sites in the United States include Mesa, Arizona; Manchester, Connecticut; Keene and Lebanon, New Hampshire and King of Prussia, Pennsylvania. Within Europe, the Company has facilities in Ploiesti, Romania; and Colmar France, and in Asia, it operates a technology facility in Bangalore, India and Shanghai, China.

### Environmental Matters

The Company has invested in pollution control equipment and updated plant operational practices to meet local environmental standards. The Company is implementing a documented environmental management system worldwide and to becoming certified under the ISO 14001 standard where appropriate to meet or exceed customer requirements. By the end of 2012, 21 of the Company's plants had obtained ISO 14001 certification.

The Company and certain U.S. subsidiaries have been designated as potentially responsible parties by the EPA for site investigation and remediation at certain sites under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), known as the Superfund, or state laws similar to CERCLA. The claims for remediation have been asserted against numerous other entities, which are believed to be financially solvent and are expected to fulfill their proportionate share of the obligation. The Company believes it has adequate reserves to cover its environmental expenses and has an established environmental compliance audit program.

### Patents, Trademarks and Licenses

Timken owns a number of U.S. and foreign patents, trademarks and licenses relating to certain products. While Timken regards these as important, it does not deem its business as a whole, or any industry segment, to be materially dependent upon any one item or group of items.

### Employment

At December 31, 2012, Timken had nearly 20,000 employees. Approximately 9% of Timken's U.S. employees are covered under collective bargaining agreements.

### Management

**James W. Griffith**, 59, has served as the President and Chief Executive Officer of The Timken Company since 2002. Mr. Griffith joined the Company in 1984, and has held positions as plant manager, Vice President of Manufacturing in North America and Managing Director of the Company's business in Australia. From 1996 to 1999, he led the Company's automotive business in North America and the Company's bearing business activities in Asia and Latin America. He was elected President and Chief Operating Officer in 1999. Since that time, Mr. Griffith has led a transformation of the Company focused on creating ever-increasing levels of value for customers and shareholders. With Mr. Griffith's broad experience and deep understanding of the Company, and as Chief Executive Officer, he is a key director for the Company. He has served on the Board of Directors since 1999. He serves on the Board of Illinois Tool Works (ITW-NR) and was a director of Goodrich Corporation from 2002-2012.

**Glenn A. Eisenberg**, 51 is executive vice president – finance and administration and Chief financial officer of The Timken Company. He also is an officer of the Company. Since joining Timken in 2001, Eisenberg has been instrumental in executing Timken's global growth and financial strategies, including the billion-dollar acquisition of The Torrington Company. Prior to joining the company, Eisenberg served as president and chief operating officer of United Dominion Industries, a diversified industrial manufacturing company with \$2.5 billion in sales, prior to its acquisition by





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SPX Corporation. At UDI, he also held the positions of president – test instrument segment, executive vice president and chief financial officer and vice president – planning and development. Before joining UDI in 1990, he was a vice president at the Citizens and Southern Corporation. Eisenberg serves on the boards of directors for Family Dollar Stores Inc. (FDO-NR) and Alpha Natural Resources Inc. (ANR-NR). He holds a bachelor’s degree in economics and environmental studies from Tulane University and a master’s degree in business administration from Georgia State University

Exhibit 15 - The Timken Company - Income Statement

(\$ in thousands except per share)

December year end	2010 Year	2011 Year	2012				2012 Year	2013E				2013E Year	2014E				2014E Year
			Q1	Q2	Q3	Q4		Q1E	Q2E	Q3E	Q4E		Q1E	Q2E	Q3E	Q4E	
<b>Total revenue</b>	\$4,055,490	\$5,170,200	\$1,421,000	\$1,343,200	\$1,142,500	\$1,080,300	\$4,987,000	\$1,107,000	\$1,095,000	\$1,169,000	\$1,235,000	\$4,606,000	\$1,180,000	\$1,260,000	\$1,275,000	\$1,190,000	\$4,905,000
<i>Growth</i>	29%	27%	13%	1%	-14%	-15%	-4%	-22%	-18%	2%	14%	-8%	7%	15%	9%	-4%	6%
Cost of Goods	\$3,032,399	\$3,800,500	\$1,009,400	\$965,900	\$843,600	\$801,800	\$3,620,700	\$830,250	\$821,250	\$853,370	\$901,550	\$3,406,420	\$873,200	\$907,200	\$918,000	\$856,800	\$3,555,200
<b>Gross Profit</b>	<b>\$1,023,091</b>	<b>\$1,369,700</b>	<b>\$411,600</b>	<b>\$377,300</b>	<b>\$298,900</b>	<b>\$278,500</b>	<b>\$1,366,300</b>	<b>\$276,750</b>	<b>\$273,750</b>	<b>\$315,630</b>	<b>\$333,450</b>	<b>\$1,199,580</b>	<b>\$306,800</b>	<b>\$352,800</b>	<b>\$357,000</b>	<b>\$333,200</b>	<b>\$1,349,800</b>
<b>Gross Margin</b>	<b>25.2%</b>	<b>26.5%</b>	<b>29.0%</b>	<b>28.1%</b>	<b>26.2%</b>	<b>25.8%</b>	<b>27.4%</b>	<b>25.0%</b>	<b>25.0%</b>	<b>27.0%</b>	<b>27.0%</b>	<b>26.0%</b>	<b>26.0%</b>	<b>28.0%</b>	<b>28.0%</b>	<b>28.0%</b>	<b>27.5%</b>
SG&A and Marketing	\$563,857	\$626,200	\$164,700	\$163,000	\$152,700	\$163,500	\$643,900	\$160,000	\$159,000	\$152,000	\$155,000	\$626,000	\$157,000	\$157,000	\$156,000	\$157,000	\$627,000
% of total revenue	13.9%	12.1%	11.6%	12.1%	13.4%	15.1%	12.9%	14.5%	14.5%	13.0%	12.6%	13.6%	13.3%	12.5%	12.2%	13.2%	12.8%
Total Operating Expenses	\$563,857	\$626,200	\$164,700	\$163,000	\$152,700	\$163,500	\$643,900	\$160,000	\$159,000	\$152,000	\$155,000	\$626,000	\$157,000	\$157,000	\$156,000	\$157,000	\$627,000
<b>Operating Income</b>	<b>\$459,234</b>	<b>\$743,500</b>	<b>\$246,900</b>	<b>\$214,300</b>	<b>\$146,200</b>	<b>\$115,000</b>	<b>\$722,400</b>	<b>\$116,750</b>	<b>\$114,750</b>	<b>\$163,630</b>	<b>\$178,450</b>	<b>\$573,580</b>	<b>\$149,800</b>	<b>\$195,800</b>	<b>\$201,000</b>	<b>\$176,200</b>	<b>\$722,800</b>
<b>Operating Margin</b>	<b>11.3%</b>	<b>14.4%</b>	<b>17.4%</b>	<b>16.0%</b>	<b>12.8%</b>	<b>10.6%</b>	<b>14.5%</b>	<b>10.5%</b>	<b>10.5%</b>	<b>14.0%</b>	<b>14.4%</b>	<b>12.5%</b>	<b>12.7%</b>	<b>15.5%</b>	<b>15.8%</b>	<b>14.8%</b>	<b>14.7%</b>
Total Other Items	(\$48,463)	(\$49,000)	(\$9,700)	\$81,800	(\$18,300)	(\$10,600)	\$43,200	(\$9,200)	(\$9,200)	(\$9,200)	(\$9,200)	(\$36,800)	(\$9,200)	(\$9,200)	(\$9,200)	(\$9,200)	(\$36,800)
<b>Pre-Tax Income</b>	<b>\$410,771</b>	<b>\$694,500</b>	<b>\$237,200</b>	<b>\$296,100</b>	<b>\$127,900</b>	<b>\$104,400</b>	<b>\$765,600</b>	<b>\$107,550</b>	<b>\$105,550</b>	<b>\$154,430</b>	<b>\$169,250</b>	<b>\$536,780</b>	<b>\$140,600</b>	<b>\$186,600</b>	<b>\$191,800</b>	<b>\$167,000</b>	<b>\$686,000</b>
<b>Pre-Tax Margin</b>	<b>10.1%</b>	<b>13.4%</b>	<b>16.7%</b>	<b>22.0%</b>	<b>11.2%</b>	<b>9.7%</b>	<b>15.4%</b>	<b>9.7%</b>	<b>9.6%</b>	<b>13.2%</b>	<b>13.7%</b>	<b>11.7%</b>	<b>11.9%</b>	<b>14.8%</b>	<b>15.0%</b>	<b>14.0%</b>	<b>14.0%</b>
Taxes (benefit)	\$135,954	\$240,200	\$81,500	\$112,500	\$47,000	\$29,100	\$270,100	\$37,643	\$36,943	\$54,051	\$59,238	\$187,873	\$49,210	\$65,310	\$67,130	\$58,450	\$240,100
Tax Rate	33.1%	34.6%	34.4%	38.0%	36.7%	27.9%	35.3%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%
<b>Net Income (loss)</b>	<b>\$274,817</b>	<b>\$454,300</b>	<b>\$155,700</b>	<b>\$183,600</b>	<b>\$80,900</b>	<b>\$75,300</b>	<b>\$495,500</b>	<b>\$69,908</b>	<b>\$68,608</b>	<b>\$100,380</b>	<b>\$110,013</b>	<b>\$348,907</b>	<b>\$91,390</b>	<b>\$121,290</b>	<b>\$124,670</b>	<b>\$108,550</b>	<b>\$445,900</b>
<b>Net Margin</b>	<b>6.8%</b>	<b>8.8%</b>	<b>11.0%</b>	<b>13.7%</b>	<b>7.1%</b>	<b>7.0%</b>	<b>9.9%</b>	<b>6.3%</b>	<b>6.3%</b>	<b>8.6%</b>	<b>8.9%</b>	<b>7.6%</b>	<b>7.7%</b>	<b>9.6%</b>	<b>9.8%</b>	<b>9.1%</b>	<b>9.1%</b>
<b>EPS, as reported</b>	<b>\$2.81</b>	<b>\$4.59</b>	<b>\$1.58</b>	<b>\$1.86</b>	<b>\$0.83</b>	<b>\$0.78</b>	<b>\$5.07</b>	<b>\$0.72</b>	<b>\$0.71</b>	<b>\$1.03</b>	<b>\$1.13</b>	<b>\$3.60</b>	<b>\$0.94</b>	<b>\$1.25</b>	<b>\$1.28</b>	<b>\$1.12</b>	<b>\$4.60</b>
EPS for Thomson Reuters/FC	\$3.12	\$4.59	\$1.58	\$1.86	\$0.83	\$0.78	\$5.07	\$0.72	\$0.71	\$1.03	\$1.13	\$3.60	\$0.94	\$1.25	\$1.28	\$1.12	\$4.60
Diluted Shares Outstanding	97,516	98,656	98,588	98,204	97,123	96,553	97,602	97,000	97,010	97,020	97,030	97,015	97,000	97,010	97,020	97,030	97,015

Sources: Company reports and Litchfield Hills Research, LLC

Exhibit 16 - The Timken Company - Balance Sheet				
(\$ in thousands except per share)				
December year end	FY2014E	FY2013E	FY2012	FY2011
<b>Balance sheet</b>				
Current Assets				
Cash and S.T.I.	\$482,088	\$362,188	\$586,381	\$464,781
Accounts receivable	700,000	600,000	546,700	645,500
Inventories	900,000	850,000	862,100	964,400
Other assets	200,000	200,000	178,900	218,200
<b>Total Current Assets</b>	<b>2,282,088</b>	<b>2,012,188</b>	<b>2,174,081</b>	<b>2,292,881</b>
Net PP&E	1,550,000	1,500,000	1,405,300	1,308,900
Other non-current assets	680,000	675,000	665,300	725,600
<b>Total Assets</b>	<b>\$4,512,088</b>	<b>\$4,187,188</b>	<b>\$4,244,681</b>	<b>\$4,327,381</b>
Current Liabilities				
Accounts payable	\$210,000	\$190,000	\$216,200	\$287,300
Other payables and accrued exp.	350,000	300,000	437,400	510,600
Short-term debt	10,000	10,000	14,300	22,000
<b>Total current liabilities</b>	<b>570,000</b>	<b>500,000</b>	<b>667,900</b>	<b>819,900</b>
Long Term Debt	450,000	450,000	455,100	478,800
Consists of varying maturities and interest rates				
Other non-current assets	775,000	800,000	875,100	986,200
<b>Total Liabilities</b>	<b>1,795,000</b>	<b>1,750,000</b>	<b>1,998,100</b>	<b>2,284,900</b>
Minority interest				
Stockholders Equity				
Preferred stock				
Total stockholders equity	2,717,088	2,437,188	2,246,581	2,042,481
<b>Total Liabilities and equity</b>	<b>\$4,512,088</b>	<b>\$4,187,188</b>	<b>\$4,244,681</b>	<b>\$4,327,381</b>
<i>Sources: Company reports and Litchfield Hills Research, LLC</i>				



**Disclosures:**

**Analyst Certification**

I Theodore R. O'Neill, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company and the underlying securities. I further certify that I have not and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this research report.

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