

Manufacturing Barometer™

Business outlook 2Q 2007

In cooperation with
BSI Global Research, Inc.

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Quarterly highlights

In 2Q 2007, PricewaterhouseCoopers interviewed 61 US-based industrial manufacturing executives about their current business performance, the state of the economy and their expectations for business growth over the next 12 months. We then compared their responses to the prior quarter's results to see how the 12-month outlook has changed. The final step was to compare their views to a wider panel to show how the industry differs from the broader population.

The second quarter 2007 Manufacturing Barometer™ results show that industrial manufacturers have once again lowered their 12-month growth projections, citing oil/energy costs and competition from foreign markets among their top concerns. Despite this, they remain optimistic that both the US and world economies will grow and expect international sales to increase to 35 percent of total revenue over the next 12 months. The majority plan to increase capital investments and add new workers, but are also becoming more concerned about the potential for higher interest rates and unfavorable exchange rates in the months to come.

Key findings:

- Consistent with the last several quarters, revenue projections are continuing to edge downward. Revenue projections now average 5.7 percent for the next 12 months. This is a 16 percent drop from the prior quarter and a 30 percent drop from a high of a year ago. Rising top-of-mind concerns that impact growth include oil/energy costs, competition from foreign markets, the strength of the US dollar and higher interest rates.
- Lower revenue projections are set against an optimistic economic outlook. Seventy-eight percent of industrial manufacturers are optimistic that the world economy will grow over the next 12 months—well above the 62 percent who expect the US economy to grow.

- Sixty-seven percent of those marketing abroad reported an increase in international sales this quarter. Looking ahead, this group expects 35 percent of total revenues to come from international sales, up from 27 percent a year ago.
- Fifty-seven percent of industrial manufacturers are planning new investments of capital over the next 12 months. The mean investment as a percent of revenue is expected to be 9.4 percent, the highest projection for this number in the last five quarters, partly due to strong M&A plans.
- Although the majority of US-based industrial manufacturers we interviewed plan to increase their workforce, the companies that plan to reduce are doing so in larger numbers. As a result, new workers as a percent of the total workforce is slightly on the downside compared to prior estimates.
- Costs continue to rise for a large number of industrial manufacturers. Forty-six percent said that costs increased in the second quarter, and only 13 percent reported a decrease. Thirty-eight percent said that, in turn, their prices rose. Overall, gross margins appeared to fare well, with 31 percent citing higher gross margins while only 16 percent reported lower gross margins.

A quarter-by-quarter comparison of the key indicators shows the business outlook for the next 12 months and how the views of the panel have changed each quarter, see Chart 1.1. The pages that follow provide a detailed look at each survey question for the past five quarters of the survey.

Key indicators for the business outlook

Chart 1.1 Key indicators for the business outlook

A quarter-over-quarter comparison of the key indicators shows how the 12-month outlook has changed each quarter. The change column indicates the movement of opinion from the last two quarters.

| Business outlook, next 12 months among industrial manufacturers | 2006 | | | 2007 | | Change | Page |
|---|--------|--------|--------|--------|--------|-----------|------|
| | 2Q '06 | 3Q '06 | 4Q '06 | 1Q '07 | 2Q '07 | 1Q-2Q '07 | |
| Optimistic about US economy | 63% | 45% | 64% | 57% | 62% | ↑ | 7 |
| Optimistic about world economy | 64% | 58% | 69% | 83% | 78% | ↓ | 9 |
| Expect positive revenue growth | 89% | 85% | 85% | 85% | 84% | = | 19 |
| Average growth rate expected | 8.1% | 7.3% | 6.2% | 6.8% | 5.7% | ↓ | 19 |
| Planning major new investments | 60% | 47% | 51% | 56% | 57% | = | 23 |
| New investments as a % of sales | 8.7% | 6.6% | 6.5% | 7.4% | 9.4% | ↑ | 23 |
| Planning to hire | 58% | 37% | 33% | 46% | 51% | ↑ | 21 |
| New workers as a % of workforce (net) | -0.1% | +0.3% | +1.0% | +0.7% | -0.4% | ↓ | 21 |
| Expected barriers to growth | | | | | | | |
| • Oil/energy prices | 65% | 48% | 62% | 51% | 59% | ↑ | 25 |
| • Competition from foreign markets | 45% | 38% | 28% | 39% | 53% | ↑ | 25 |
| • Legislative/ Regulatory pressures | 23% | 25% | 34% | 36% | 36% | = | 25 |
| • Lack of demand | 32% | 48% | 39% | 36% | 34% | = | 25 |
| • Lack of qualified workers | 44% | 25% | 30% | 41% | 30% | ↓ | 25 |
| • Monetary exchange rate | 26% | 20% | 20% | 21% | 30% | ↑ | 25 |
| • Higher interest rates | 32% | 32% | 18% | 20% | 28% | ↑ | 25 |

Economic views

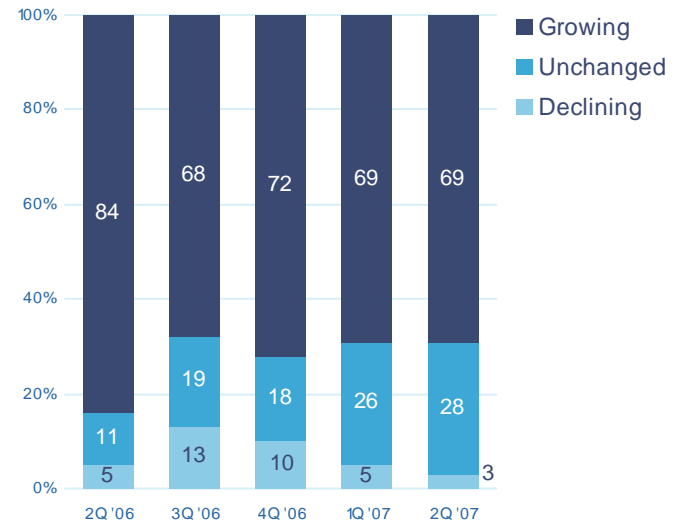
View of the US economy, this quarter

Which best describes your view of the US economy this quarter?

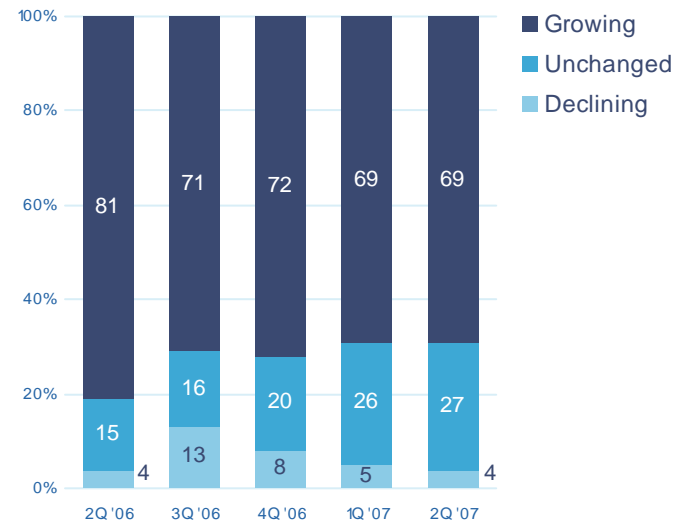
Sixty-nine percent of US-based industrial manufacturing executives believe the US economy continues to grow. This view is consistent with last quarter's 69 percent, but well below last year's 84 percent.

Chart 2.1 View of the US economy, this quarter

Industrial manufacturers



All respondents



Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

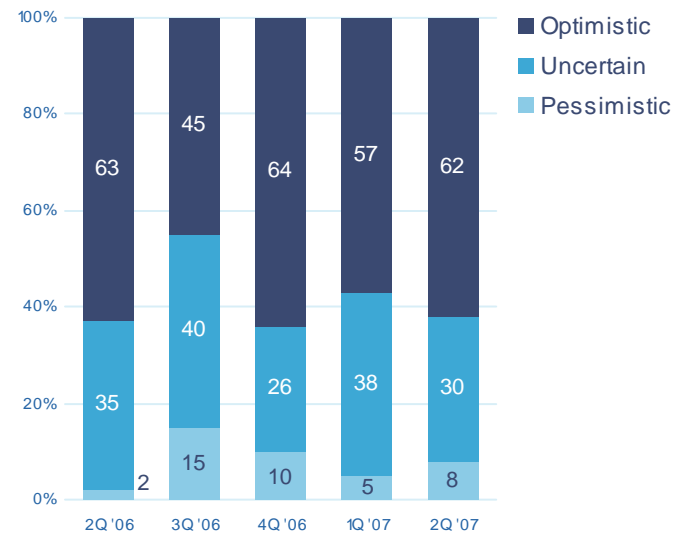
View of the US economy, next 12 months

Looking ahead over the next 12 months, how do you feel about the prospects for the US economy?

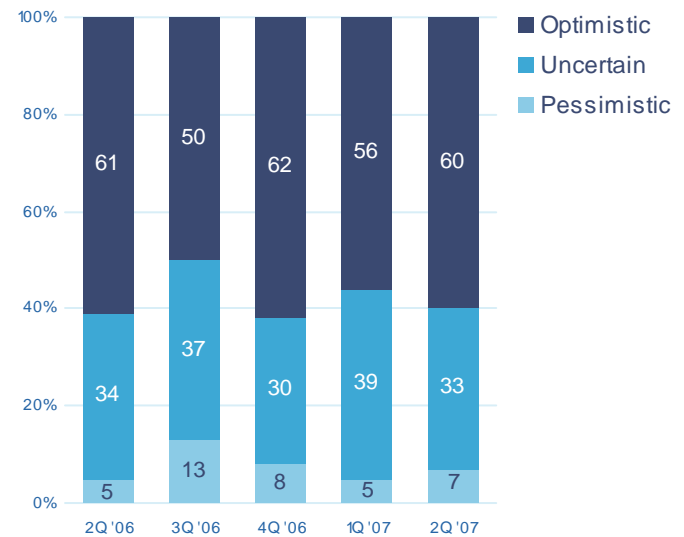
Sixty-two percent of US-based industrial manufacturers are optimistic about the prospects for the US economy, up from the 57 percent level of the prior quarter and comparable to the 63 percent a year ago. Their views have been consistent with the broader consensus over the past three quarters.

Chart 2.2 View of the US economy, next 12 months

Industrial manufacturers



All respondents



Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

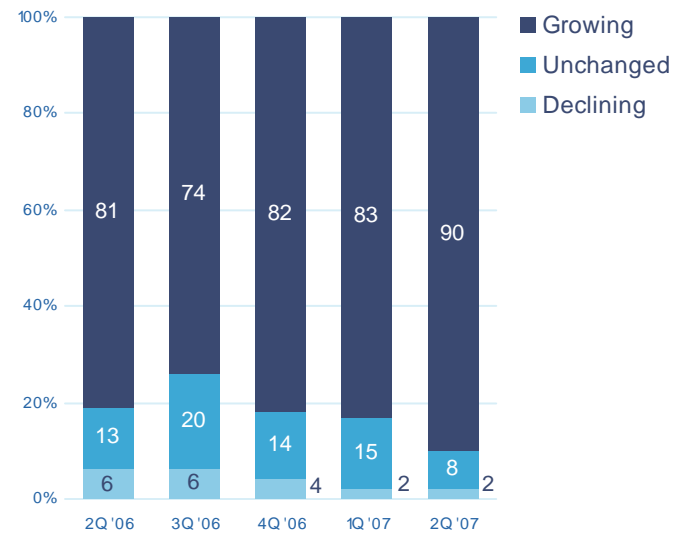
View of the world economy, this quarter

Which best describes your view of the world economy this quarter? (international marketers only)

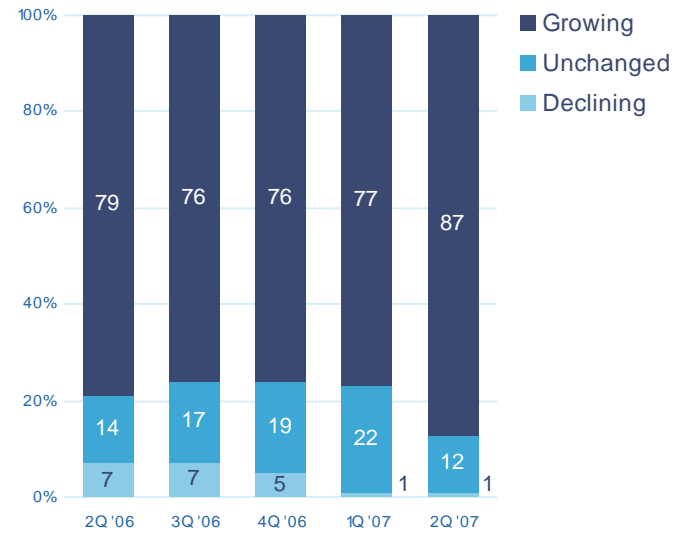
Of those marketing abroad, 90 percent view the world economy as growing, up 7 points from 83 percent in the prior quarter. For the past three quarters, industrial manufacturers have been more optimistic about the world economy than the broader consensus.

Chart 2.3 View of the world economy, this quarter

Industrial manufacturers



All respondents



Note: In 2Q 2007 those marketing abroad, Industrial manufacturers n = 51, All respondents, n= 93

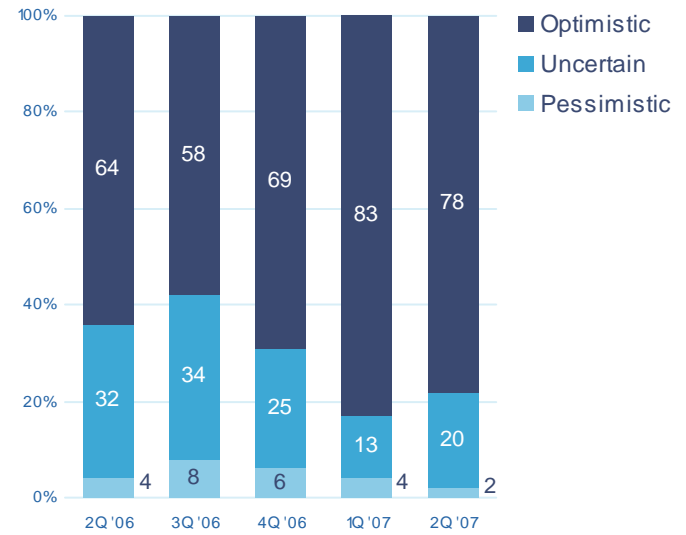
View of the world economy, next 12 months

Looking ahead over the next 12 months, how do you feel about the prospects for the world economy? (international marketers only)

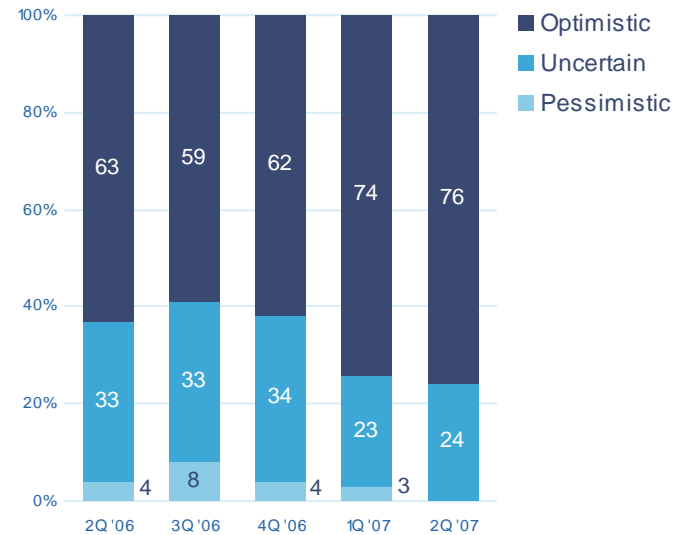
Seventy-eight percent of US-based industrial manufacturers who market abroad are optimistic about the prospects for the world economy, only 5 points below the prior quarter's 83 percent, and well above the 64 percent level of a year ago. The bullish views of those marketing abroad have been higher than the broader consensus over the past three quarters, but have narrowed to within 2 points in the current quarter.

Chart 2.4 View of the world economy, next 12 months

Industrial manufacturers



All respondents



Note: In 2Q 2007 those marketing abroad, Industrial manufacturers n = 51, All respondents, n= 93

Company performance

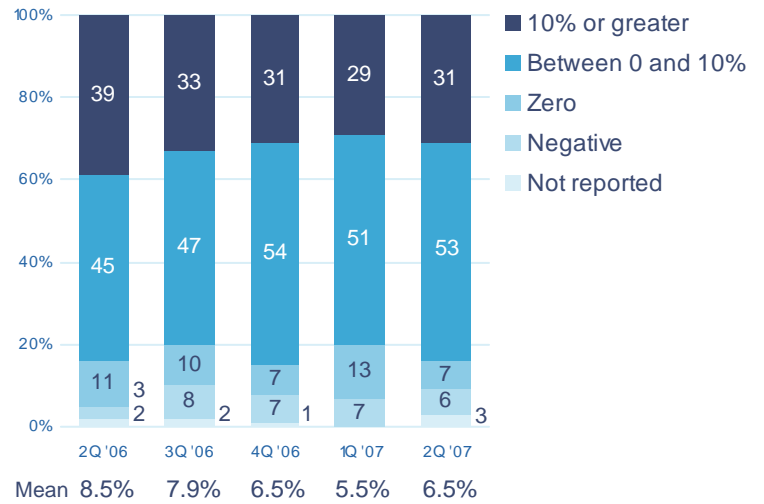
Company revenue growth, calendar year

What is your company's estimated revenue growth rate for the calendar year?

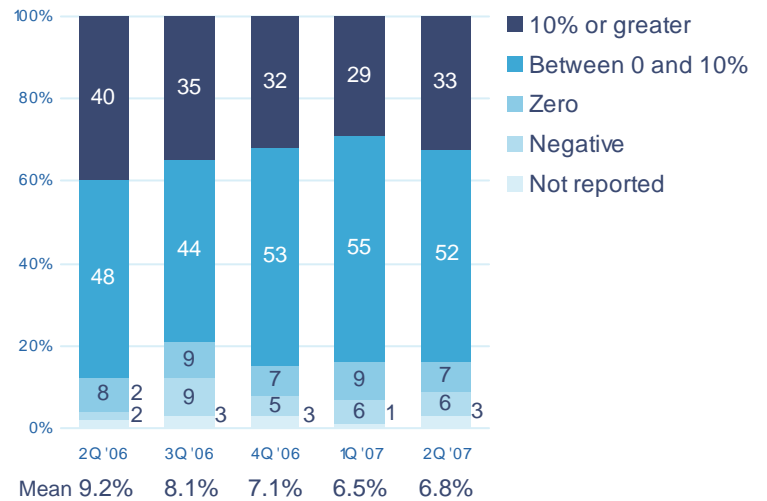
Currently, 84 percent of US-based industrial manufacturers expect revenue growth in 2007, with 31 percent expecting double-digit growth and 53 percent expecting single-digit growth. Overall, the composite average growth estimate has risen to 6.5 percent from 5.5 percent the previous quarter. The pace of revenue growth expected in 2007 among US-based industrial manufacturers is now comparable to the broader consensus 6.8 percent average. For more information on revenue expectations, see Chart 4.1, revenue expectations, next 12 months.

Chart 3.1 Company revenue growth, calendar year

Industrial manufacturers



All respondents



Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

Industry growth, calendar year

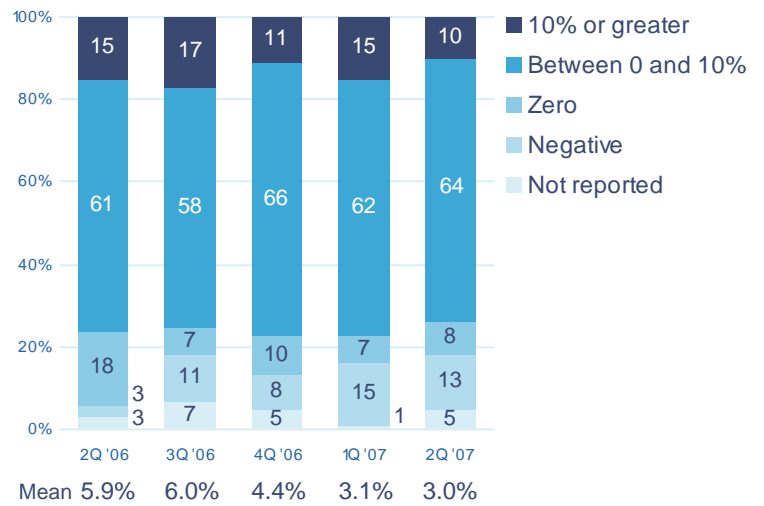
What is your industry's estimated growth rate for the calendar year?

Industry growth now averages 3.0 percent—well below the 5.9 percent level a year ago.

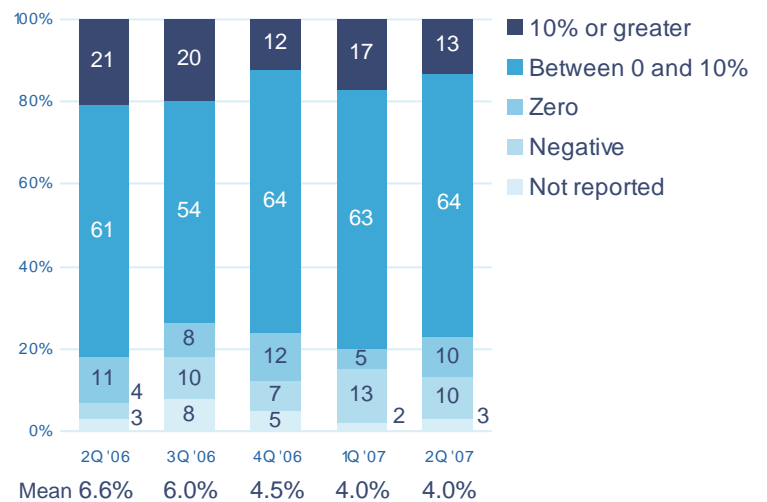
Note that the industry growth estimate is typically lower than the average company growth rate. US-based industrial manufacturers anticipate an average growth rate of 6.5 percent for their own companies in 2007, more than two times greater than the estimated growth rate of 3.0 percent for their industry.

Chart 3.2 Industry growth, calendar year

Industrial manufacturers



All respondents



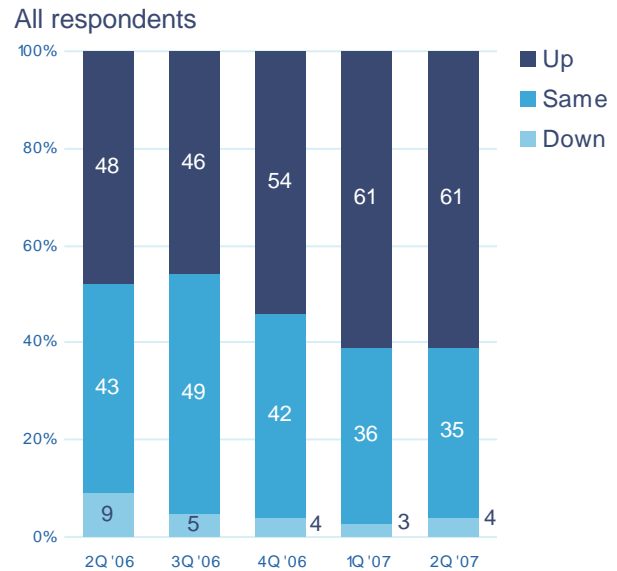
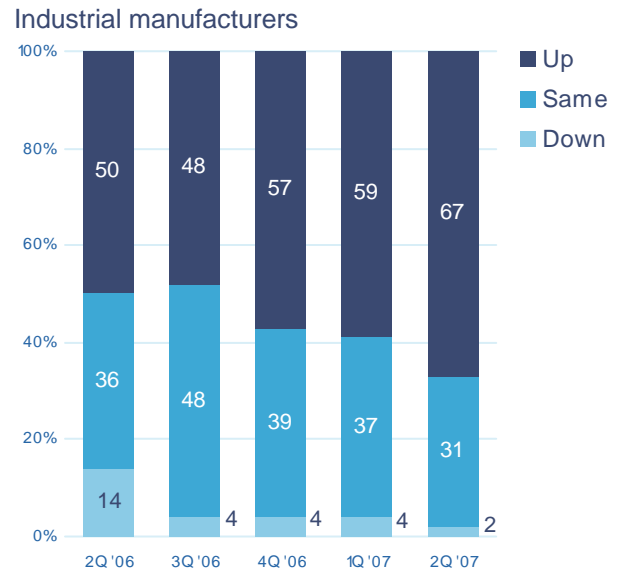
Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

International sales

Are international sales up, down or the same compared to three months ago?

International markets continue to strengthen for US-based industrial manufacturers who sell abroad. The strongest quarterly performance was reported in 2Q 2007, as 67 percent of international marketers increased sales abroad, up 8 points from the prior quarter and 17 points higher than a year ago. Companies showing a quarterly decrease dropped to 2 percent in 2Q 2007, a notable reduction from last year's 14 percent.

Chart 3.3 International sales



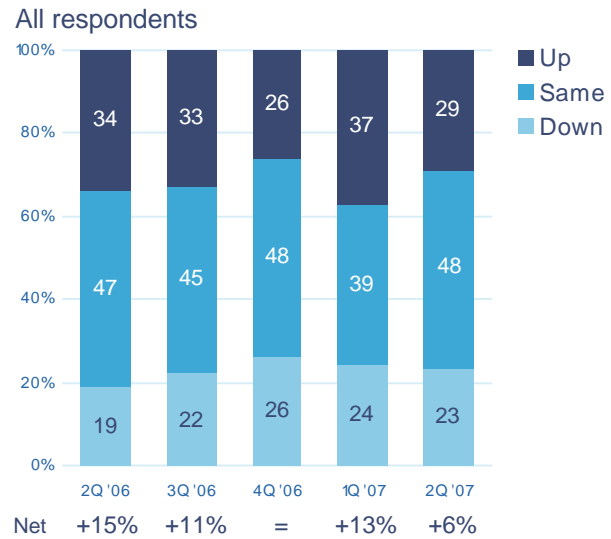
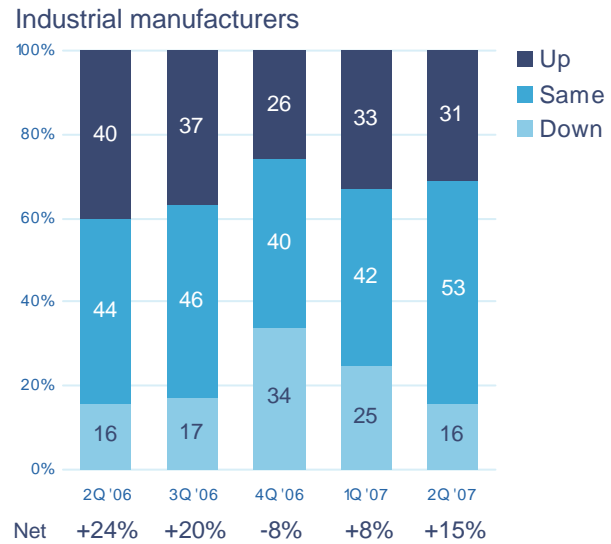
Note: In 2Q 2007 those marketing abroad, Industrial manufacturers n = 51, All respondents, n= 93

Changes in gross margins

Are gross margins up, down or the same compared to three months ago?

In 2Q 2007, gross margins were higher for 31 percent of US-based industrial manufacturers and lower for 16 percent. Gross margins in 2Q 2007 were a net positive 15 percent, 7 points higher than the prior quarter. As a result, more US-based industrial manufacturers saw an increase in gross margins than the broader peer group.

Chart 3.4 Changes in gross margins



Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

Changes in costs and prices

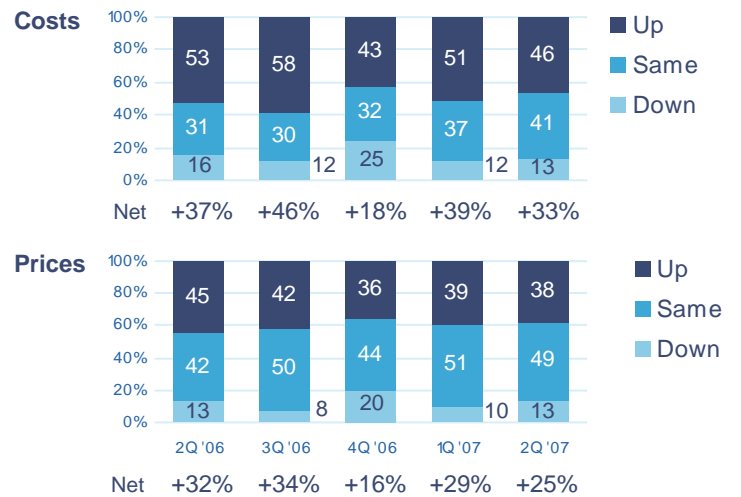
Are costs up, down or the same compared to three months ago? Prices?

Costs, in 2Q 2007, increased for 46 percent of US-based industrial manufacturers and decreased for only 13 percent—a net of 33 percent with higher costs. While this figure is directionally on the high side, net costs are 6 points below the previous quarter.

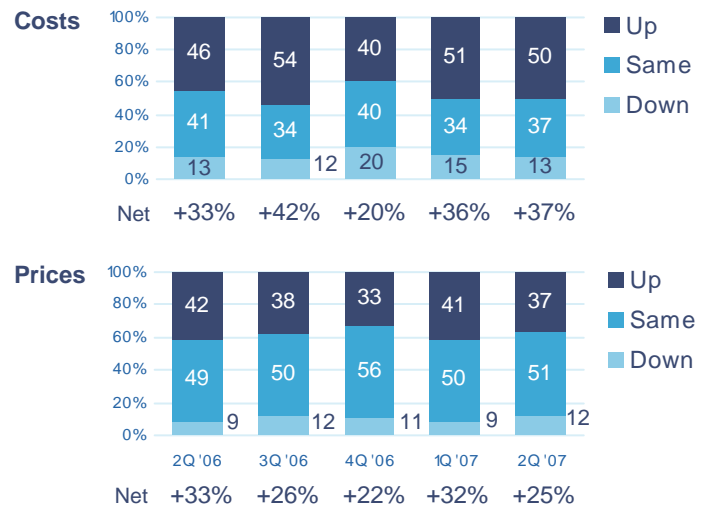
The 2Q 2007 prices followed suit at a slightly lower level, with 38 percent raising prices and 13 percent lowering them—a net of 25 percent with higher prices. Net prices were 4 points below the prior quarter, but directionally high. The upward changes in costs and prices were quite similar to the broader consensus.

Chart 3.5 Changes in costs and prices

Industrial manufacturers



All respondents



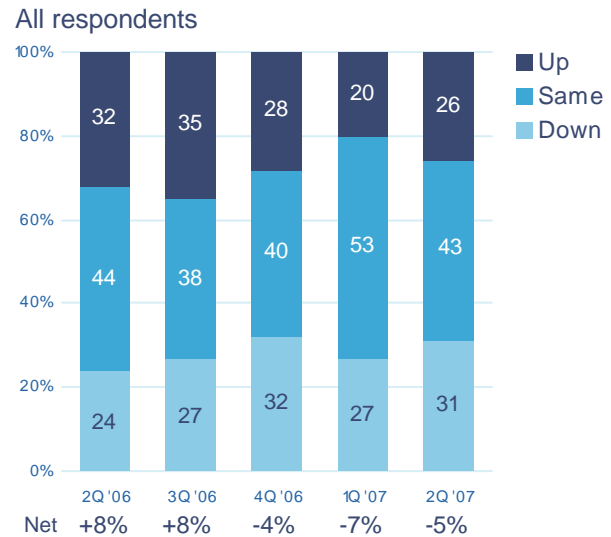
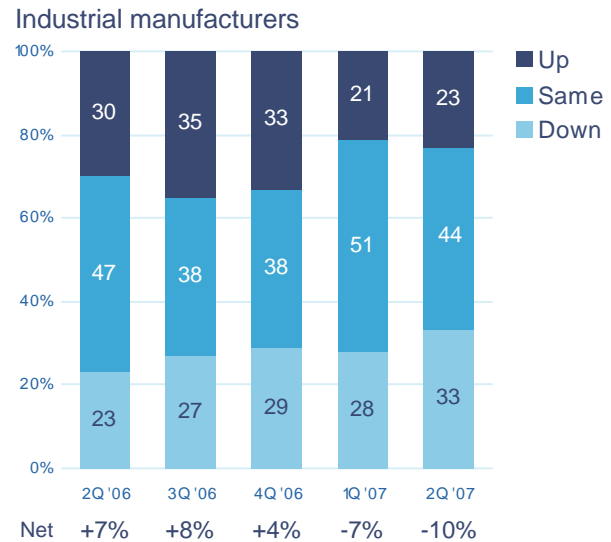
Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

Inventory movement

Are finished inventories as a percent of sales up, down or the same compared to three months ago? (product companies only)

Overall, net inventories were down for 10 percent of US-based industrial manufacturers: 23 percent reported higher inventories, 33 percent lower and 44 percent about the same. This is similar to the prior quarter, but directionally different from a year ago. The broader peer group shows a similar pattern.

Chart 3.6 Inventory movement



Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

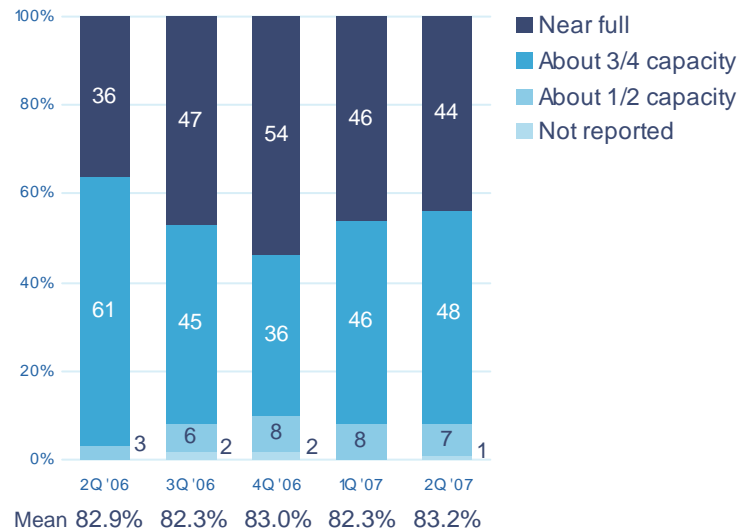
Level of operating capacity

What is your organization's current operating capacity?

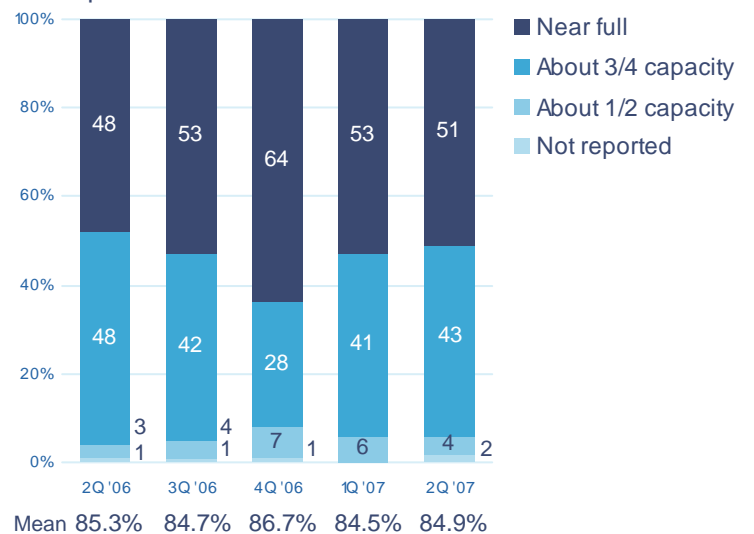
Operating capacity is an estimate of the current level of permanent staffing compared to what is needed for full-capacity output. In 2Q 2007, the average level of operating capacity for US-based industrial manufacturers was an estimated 83.2 percent of capacity—slightly above the prior quarter, but consistent over the past year. This quarter, 44 percent of industrial manufacturers claimed to be at or near full capacity. It is common for the broader consensus—51 percent reportedly at or near full capacity in 2Q 2007—to report a higher operating capacity compared to the industry group.

Chart 3.7 Level of operating capacity

Industrial manufacturers



All respondents



Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

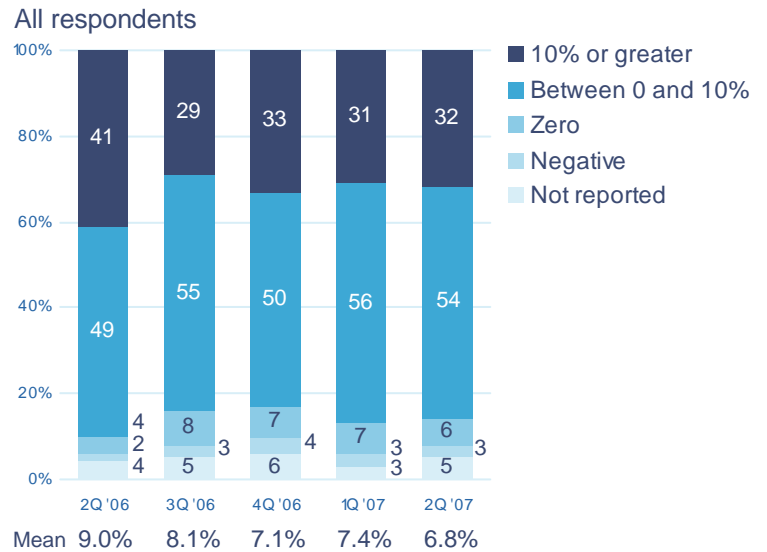
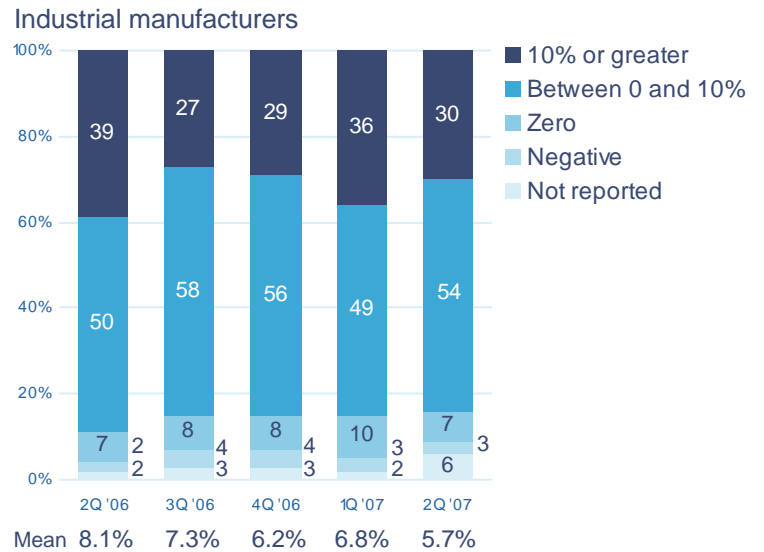
Business outlook, next 12 months

Revenue growth, next 12 months

What is your organization's estimated revenue growth rate for the next 12 months?

US-based industrial manufacturers project a lower revenue growth rate for their own companies over the next 12 months. The 5.7 percent average is below the prior quarter's projected 6.8 percent, and well below the 8.1 percent projection a year ago. Currently, 84 percent plan for growth over the next 12 months—30 percent expect double-digit revenue growth and 54 percent expect single-digit growth. Compared to last quarter's results, the pace of revenue growth over the next 12 months now lags the broader consensus by a wider margin—5.7 percent for the industry versus 6.8 percent for the consensus group.

Chart 4.1 Revenue growth, next 12 months



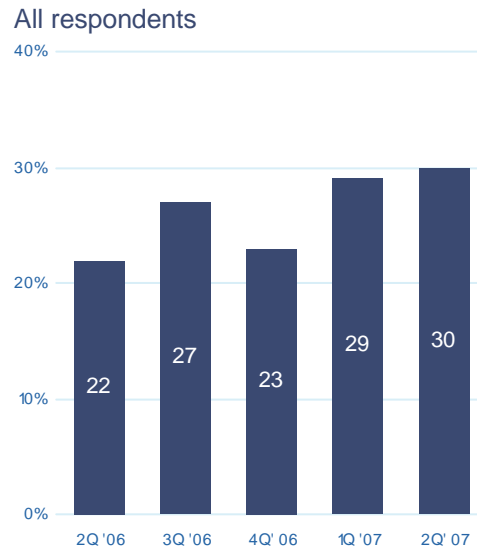
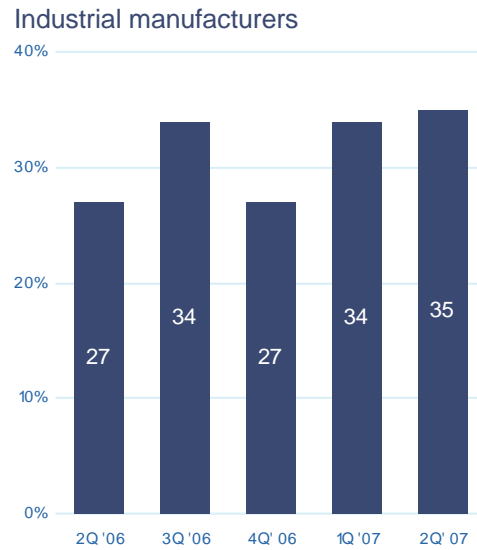
Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

International sales, next 12 months

What percent of your business' total revenues over the next 12 months do you expect to be derived from international sales?

Of those selling abroad, the contribution of international sales to total revenue is projected at 35 percent over the next 12 months, comparable to 34 percent in the prior quarter and notably higher than the 27 percent a year ago. Industrial manufacturers selling abroad have consistently outpaced the broader consensus in projected revenue contributions from international sales.

Chart 4.2 International sales, next 12 months



Note: In 2Q 2007 those marketing abroad, Industrial manufacturers n = 51, All respondents, n= 93

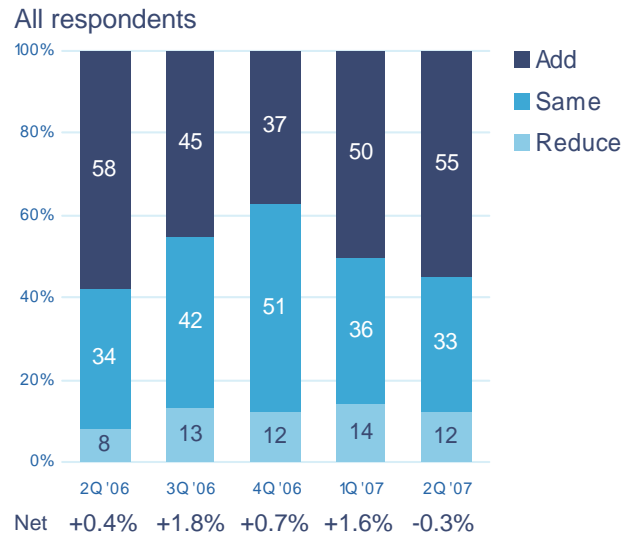
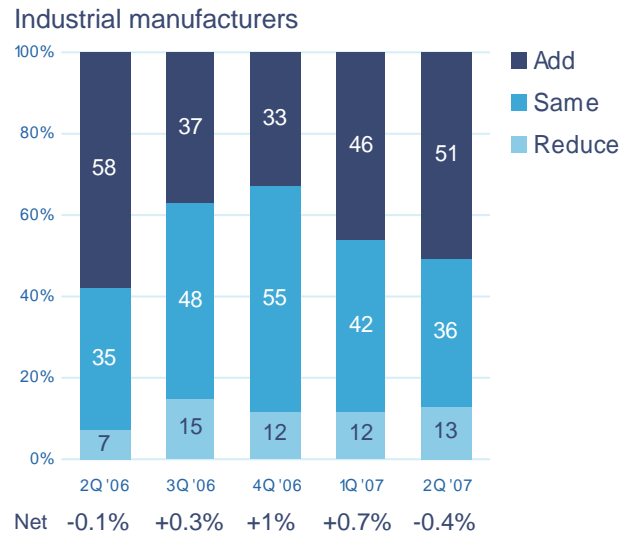
Percent planning to hire

Do you plan to add or reduce the number of full-time equivalent employees over the next 12 months?

More US-based industrial manufacturers—51 percent, up 5 points from the prior quarter—are planning to add employees to their workforce over the next 12 months. While fewer are planning to reduce the number of full time-equivalent employees, the total number of planned reductions is higher than the total number of additions. As a result, the net projection is at negative 0.4 percent. In the prior quarter, the net projection was at plus 0.7 percent, so composite workforce projections for the next 12 months are lower. The broader consensus projections have also turned slightly negative, with an average net projection of negative 0.3 percent—a major change from the prior quarter’s plus 1.6 percent.

Industrial manufacturers planning to add employees to their workforce project a much higher revenue growth rate over the next 12 months—7.8 percent versus 3.6 percent for those staying the same or reducing.

Chart 4.3 Percent planning to hire



Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

Percent planning to hire by type of employee

What types of employees do you plan to add or reduce over the next 12 months?

Over the next 12 months, industrial manufacturers will primarily be looking for production workers and white-collar management support to hire.

More interest in the professionals/technicians category was found in the broader consensus—32 percent versus 26 percent for industrial manufacturers. The broader consensus is also more interested in sales/marketing executives—24 percent versus 18 percent.

Chart 4.4 Percent planning to hire by type of employee

Industrial manufacturers

| | 2Q '06 | 3Q '06 | 4Q '06 | 1Q '07 | 2Q '07 |
|-----------------------------|--------|--------|--------|--------|--------|
| Planning to hire (net) | 58% | 37% | 33% | 46% | 51% |
| • Production workers | 37% | 18% | 17% | 33% | 33% |
| • White collar support | 29% | 15% | 20% | 26% | 30% |
| • Professionals/technicians | 32% | 23% | 26% | 25% | 26% |
| • Skilled labor | 29% | 20% | 18% | 25% | 26% |
| • Sales/marketing | 26% | 17% | 18% | 25% | 18% |

All respondents

| | 2Q '06 | 3Q '06 | 4Q '06 | 1Q '07 | 2Q '07 |
|-----------------------------|--------|--------|--------|--------|--------|
| Planning to hire (net) | 58% | 45% | 37% | 50% | 55% |
| • Production workers | 27% | 16% | 15% | 22% | 28% |
| • White collar support | 28% | 19% | 18% | 28% | 28% |
| • Professionals/technicians | 36% | 28% | 23% | 26% | 32% |
| • Skilled labor | 24% | 16% | 17% | 24% | 23% |
| • Sales/marketing | 27% | 21% | 22% | 28% | 24% |

Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

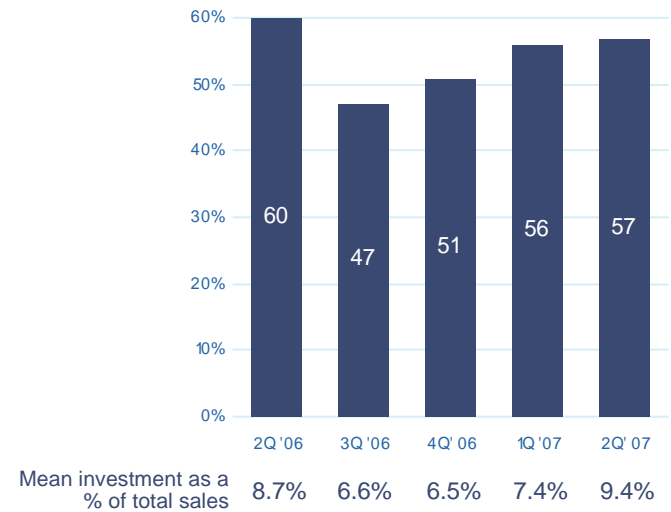
Percent planning major new investments of capital

Are you actively planning any major new investments of capital over the next 12 months? If so, what percent of total sales to you expect to invest?

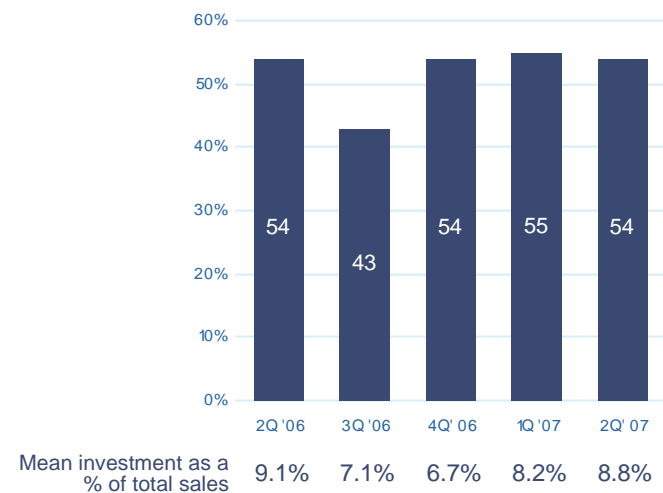
More than half of US-based industrial manufacturers plan for major new investments in business growth over the next 12 months. The mean investment is also high at 9.4 percent of total sales (including an M&A component). Overall, plans for major new investments among industrial manufacturers have been consistently strong over the past five quarters.

Chart 4.5 Percent planning major new investments of capital

Industrial manufacturers



All respondents



Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

Percent planning to increase operational spending

Over the next 12 months, where do you expect to increase spending?

Looking ahead over the next 12 months, three types of increased expenditures lead the way among US-based industrial manufacturers: new product or service introductions, information technology, and research and development. Plans for business acquisitions are also notably higher this quarter. The broader consensus was equally high on two of these three types of expenditures, lower only in R&D. On the down side, fewer industrial manufacturers are now planning increased expenditures in geographic expansion and facilities expansion.

Chart 4.6 Percent planning to increase operational spending

| Industrial manufacturers | | | | | |
|---|--------|--------|--------|--------|--------|
| | 2Q '06 | 3Q '06 | 4Q '06 | 1Q '07 | 2Q '07 |
| Percent planning to increase spending (net) | 88% | 80% | 84% | 92% | 89% |
| • New product or service introduction | 57% | 47% | 43% | 46% | 48% |
| • Information technology | 49% | 43% | 39% | 38% | 48% |
| • Research and development | 47% | 33% | 30% | 30% | 43% |
| • Business acquisition | 37% | 40% | 34% | 31% | 38% |
| • Geographic expansion | 34% | 35% | 43% | 44% | 36% |
| • Facilities expansion | 40% | 38% | 41% | 41% | 34% |
| • Marketing & sales promotion | 24% | 28% | 25% | 33% | 21% |
| • Internet commerce | 11% | 12% | 16% | 18% | 15% |
| • Advertising | 18% | 18% | 13% | 18% | 13% |
| All respondents | | | | | |
| | 2Q '06 | 3Q '06 | 4Q '06 | 1Q '07 | 2Q '07 |
| Percent planning to increase spending (net) | 84% | 82% | 84% | 91% | 87% |
| • New product or service introduction | 50% | 44% | 40% | 45% | 49% |
| • Information technology | 48% | 48% | 47% | 46% | 49% |
| • Research and development | 34% | 27% | 25% | 30% | 36% |
| • Business acquisition | 39% | 39% | 37% | 37% | 40% |
| • Geographic expansion | 33% | 34% | 37% | 38% | 39% |
| • Facilities expansion | 39% | 32% | 40% | 37% | 38% |
| • Marketing & sales promotion | 27% | 26% | 30% | 32% | 28% |
| • Internet commerce | 12% | 15% | 22% | 23% | 24% |
| • Advertising | 23% | 17% | 23% | 23% | 22% |

Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

Expected barriers to business growth

Over the next 12 months, will any of the following represent barriers to business growth?

The impact of oil/energy prices and competition from foreign markets top the list of concerns for the next 12 months among US-based industrial manufacturers. While the oil/energy barrier was also high in the broader consensus, competition from foreign markets was rated much lower among this group. Compared to last quarter's results, two fiscal barriers also increased notably among US-based industrial manufacturers: the dollar's lower monetary exchange rate and concern about higher interest rates.

Those who are concerned about oil/energy costs (59 percent of total) have above-average concerns for five other potential barriers: competition from foreign markets (69 percent); legislative/regulatory pressure (47 percent); demand (44 percent); monetary exchange rates (39 percent); and taxation (33 percent). As noted earlier, those concerned about the cost of oil/energy reported higher costs and lower revenue projections for the next 12 months.

Chart 4.7 Expected barriers to business growth



Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

Plans for M&A and other business initiatives

Over the next 12 months, do you expect to participate in any of the following new business initiatives?

Plans for M&A activity among US-based industrial manufacturers over the next 12 months rose 18 points to the 56 percent level in 2Q 2007, even higher than a year ago. Forty-eight percent plan to purchase another business, while 16 percent might divest part of their own business and 8 percent plan an equity carve-out or spin-off.

Other business initiatives planned include new strategic alliances, expansion to new markets abroad, new joint ventures and development of manufacturing or distribution facilities abroad. Of these initiatives, the greatest increase is seen for new strategic alliances, up 13 points from 33 percent in the prior quarter to 46 percent. Compared to the all-industry consensus, significantly more industrial manufacturers plan involvement in expansion to new markets abroad, new joint ventures and new manufacturing/distribution facilities abroad.

Chart 4.8 Plans for M&A and other business initiatives

Industrial manufacturers

| | 2Q '06 | 3Q '06 | 4Q '06 | 1Q '07 | 2Q '07 |
|-------------------------------------|-----------|-----------|-----------|-----------|-----------|
| New business initiatives (net) | 73% | 67% | 66% | 67% | 79% |
| • M&A activity (net) | 50% | 48% | 46% | 38% | 56% |
| - Purchase another business | 45% | 38% | 41% | 31% | 48% |
| - Sale part/all own business | 10% | 12% | 8% | 13% | 16% |
| - Equity carve-out/spin-off | 3% | 2% | 2% | 5% | 8% |
| • New strategic alliance | 32% | 25% | 26% | 33% | 46% |
| • Expand to new markets abroad | 37% | 27% | 33% | 39% | 43% |
| • New joint venture | 24% | 22% | 18% | 28% | 30% |
| • New facilities abroad | 23% | 25% | 23% | 26% | 23% |
| • Close/reduce facilities abroad | 11% | 13% | 8% | 10% | 12% |
| • Reduce activity in markets abroad | 8% | 5% | 5% | 7% | 10% |

All respondents

| | 2Q '06 | 3Q '06 | 4Q '06 | 1Q '07 | 2Q '07 |
|-------------------------------------|-----------|-----------|-----------|-----------|-----------|
| New business initiatives (net) | 67% | 66% | 68% | 71% | 79% |
| • M&A activity (net) | 47% | 47% | 45% | 45% | 56% |
| - Purchase another business | 43% | 41% | 38% | 37% | 49% |
| - Sale part/all own business | 12% | 9% | 13% | 16% | 17% |
| - Equity carve-out/spin-off | 4% | 2% | 2% | 7% | 8% |
| • New strategic alliance | 32% | 29% | 30% | 38% | 45% |
| • Expand to new markets abroad | 31% | 24% | 27% | 36% | 36% |
| • New joint venture | 24% | 22% | 16% | 25% | 26% |
| • New facilities abroad | 14% | 17% | 18% | 16% | 18% |
| • Close/reduce facilities abroad | 7% | 9% | 6% | 8% | 9% |
| • Reduce activity in markets abroad | 4% | 4% | 4% | 8% | 7% |

Note: In 2Q 2007 Industrial manufacturers n = 61, All respondents, n= 105

Survey demographics and research methodology

Demographics

| | | |
|--------------------------------|--|--|
| Who | Senior executives of US-based, publicly held organizations | |
| Interview dates | May 5, 2007 to July 12, 2007 | |
| | Industrial manufacturers (61) | All respondents (105) |
| Average number of employees | 5,763 | 9,136 |
| Average business unit revenues | \$2.99 billion | \$2.93 billion |
| Average enterprise revenues | \$7.45 billion | \$7.27 billion |
| Market capitalization | \$10.61 billion | \$13.42 billion |
| Industry sectors | Products 100% Manufacturing 100% Trade/Distribution --- All other --- Services --- | Products 80% Manufacturing 72% Trade/Distribution 3% All other 5% Services 20% |

Methodology

PricewaterhouseCoopers' Manufacturing Barometer is a quarterly telephone survey conducted by the independent research firm BSI Global Research Inc. The survey panel consists of senior executives from a geographically balanced sample of large, publicly held companies in the United States. Ninety-five percent of the panelists hold titles such as president, CEO, CFO, VP of finance, treasurer, controller, internal audit director or related. The remaining hold executive titles such as President,

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About the research:

The Manufacturing Barometer is one in a series of quarterly business outlook surveys from PricewaterhouseCoopers. The survey provides a view on the 12-month outlook for revenue growth, new investments, new hiring plans, emerging business barriers and more. In addition to the business outlook, we hear from our panelists about special issues they face as the business climate changes. Results of the quarterly business outlook surveys and special issue surveys are available from www.barometersurveys.com.

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