

HARLEY DAVIDSON INC
Form 10-Q
August 03, 2007

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 1, 2007**

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from _____ to _____

Commission File Number 1-9183

Harley-Davidson, Inc.

(Exact name of registrant as specified in its Charter)

Wisconsin

39-1382325

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

3700 West Juneau Avenue, Milwaukee, Wisconsin

53208

(Address of principal executive offices)

(Zip Code)

(Registrant's telephone number, including area code) (414) 342-4680

None

(Former name, former address and former fiscal year, if changed since last report)

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock Outstanding as of July 30, 2007: 257,533,007 shares

HARLEY-DAVIDSON, INC.

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For the Quarter Ended July 1, 2007

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PART I FINANCIAL INFORMATION**Item 1. Consolidated Financial Statements**

Harley-Davidson, Inc.
Condensed Consolidated Statements of Income
(Unaudited)
(In thousands, except per share amounts)

Three Months Ended		Six Months Ended	
July 1, 2007	June 25, 2006	July 1, 2007	June 25, 2006
_____	_____	_____	_____

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Net revenue	\$ 1,620,218	\$ 1,377,047	\$ 2,799,093	\$ 2,662,137
Cost of goods sold	1,015,051	860,721	1,770,880	1,652,597
Gross profit	605,167	516,326	1,028,213	1,009,540
Financial services income	112,330	98,567	221,493	194,468
Financial services expense	47,121	42,310	97,347	86,580
Operating income from financial services	65,209	56,257	124,146	107,888
Selling, administrative and engineering expense	225,344	198,109	417,915	383,768
Income from operations	445,032	374,474	734,444	733,660
Investment income and other, net	5,335	5,885	14,079	13,202
Income before provision for income taxes	450,367	380,359	748,523	746,862
Provision for income taxes	159,877	136,929	265,723	268,869
Net income	\$ 290,490	\$ 243,430	\$ 482,800	\$ 477,993
Earnings per common share:				
Basic	\$ 1.15	\$ 0.91	\$ 1.89	\$ 1.77
Diluted	\$ 1.14	\$ 0.91	\$ 1.89	\$ 1.77
Cash dividends per common share	\$ 0.25	\$ 0.21	\$ 0.46	\$ 0.39

The accompanying notes are an integral part of the consolidated financial statements.

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Harley-Davidson, Inc.
Condensed Consolidated Balance Sheets
(In thousands)

	(Unaudited) July 1, 2007	December 31, 2006	(Unaudited) June 25, 2006
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 416,084	\$ 238,397	\$ 391,967
Marketable securities	307,347	658,133	612,508
Accounts receivable, net	163,369	143,049	150,526
Finance receivables held for sale	381,927	547,106	233,167
Finance receivables held for investment, net	1,318,025	1,554,260	1,101,587
Inventories	344,969	287,798	292,757
Prepaid expenses and other current assets	122,342	121,890	114,613
Total current assets	3,054,063	3,550,633	2,897,125
Finance receivables held for investment, net	817,027	725,957	678,938

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	(Unaudited) July 1, 2007	December 31, 2006	(Unaudited) June 25, 2006
Property, plant and equipment, net	1,004,863	1,024,469	992,271
Prepaid pension costs	47,714	55,351	345,418
Goodwill	59,372	58,800	57,687
Other assets	138,555	116,940	71,890
	<u>\$ 5,121,594</u>	<u>\$ 5,532,150</u>	<u>\$ 5,043,329</u>
 <u>LIABILITIES AND SHAREHOLDERS' EQUITY</u>			
Current liabilities:			
Accounts payable	\$ 414,031	\$ 283,477	\$ 305,740
Accrued liabilities	458,252	479,709	433,770
Current portion of finance debt	204,817	832,491	34,605
	<u>1,077,100</u>	<u>1,595,677</u>	<u>774,115</u>
Total current liabilities	1,077,100	1,595,677	774,115
Finance debt	975,000	870,000	1,000,000
Pension liability	55,032	47,916	34,325
Postretirement healthcare benefits	205,767	201,126	67,801
Other long-term liabilities	150,851	60,694	199,255
Commitments and contingencies (Note 11)			
Total shareholders' equity	<u>2,657,844</u>	<u>2,756,737</u>	<u>2,967,833</u>
	<u>\$ 5,121,594</u>	<u>\$ 5,532,150</u>	<u>\$ 5,043,329</u>

The accompanying notes are an integral part of the consolidated financial statements.

Harley-Davidson, Inc.
Condensed Consolidated Statements of Cash Flows
(Unaudited)
(In thousands)

	Six Months Ended	
	July 1, 2007	June 25, 2006
Net cash provided by operating activities (Note 3)	\$ 1,062,455	\$ 825,619
Cash flows from investing activities:		
Capital expenditures	(86,016)	(89,124)
Origination of finance receivables held for investment	(272,784)	(189,929)
Collections on finance receivables held for investment	202,656	135,444
Collection of retained securitization interests	43,241	26,227
Purchase of marketable securities	(317,270)	(426,182)
Sales and redemptions of marketable securities	669,747	719,805

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	Six Months Ended	
	3,582	1,719
	<u> </u>	<u> </u>
Other, net		
Net cash provided by investing activities	243,156	177,960
Cash flows from financing activities:		
Net decrease in finance-credit facilities and commercial paper	(535,990)	(161,437)
Dividends	(116,650)	(104,494)
Purchase of common stock for treasury	(491,103)	(499,543)
Excess tax benefits from share-based payments	2,932	1,547
Issuance of common stock under employee stock option plans	20,621	8,176
	<u> </u>	<u> </u>
Net cash used by financing activities	(1,120,190)	(755,751)
Effect of exchange rate changes on cash and cash equivalents	(7,734)	3,164
Net increase in cash and cash equivalents	177,687	250,992
Cash and cash equivalents:		
At beginning of period	238,397	140,975
	<u> </u>	<u> </u>
At end of period	\$ 416,084	\$ 391,967
	<u> </u>	<u> </u>

The accompanying notes are an integral part of the consolidated financial statements.

HARLEY-DAVIDSON, INC.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Note 1 Basis of Presentation and Use of Estimates

The condensed interim consolidated financial statements included in this quarterly report on Form 10-Q have been prepared by Harley-Davidson, Inc. (the Company) without audit. Certain information and footnote disclosures normally included in complete financial statements have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission and U.S. generally accepted accounting principles for interim financial information. However, the foregoing statements contain all adjustments (consisting only of normal recurring adjustments) which are, in the opinion of Company management, necessary to present fairly the condensed consolidated balance sheets as of July 1, 2007 and June 25, 2006, the condensed consolidated statements of income for the three and six month periods then ended and the condensed consolidated statements of cash flows for the six month periods then ended. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2006.

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Certain prior year amounts have been reclassified to conform to the current year presentation.

Note 2 New Accounting Standards

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In September 2006, the Financial Accounting Standards Board issued SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R). SFAS No. 158 requires employers that sponsor defined benefit pension and postretirement benefit plans to recognize previously unrecognized actuarial losses and prior service costs in the statement of financial position and to recognize future changes in these amounts in the year in which changes occur through comprehensive income. Additionally, employers are required to measure the funded status of a plan as of the date of their year-end statements of financial position. The Company adopted SFAS No. 158, as it relates to recognizing the funded status of its defined benefit pension and postretirement benefit plans, and the related disclosure requirements, as of December 31, 2006. The requirement to measure the funded status as of the date of the year-end statement of financial position is required by December 31, 2008. The Company will adopt the funded status measurement date requirement in 2008 and is currently evaluating the impact the change in the measurement date will have on its consolidated financial statements and notes thereto.

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Note 3 Additional Balance Sheet and Cash Flow Information

The Company values its inventories at the lower of cost or market. Substantially all inventories located in the United States are valued using the last-in, first-out (LIFO) method. Other inventories are valued at the lower of cost or market using the first-in, first-out (FIFO) method. Inventories consist of the following (in thousands):

	July 1, 2007	December 31, 2006	June 25, 2006
	<u> </u>	<u> </u>	<u> </u>
Components at the lower of FIFO cost or market			
Raw materials and work in process	\$ 136,006	\$ 123,376	\$ 95,356
Motorcycle finished goods	123,262	94,399	137,282
Parts and accessories and general merchandise	116,799	98,749	84,409
	<u> </u>	<u> </u>	<u> </u>
Inventory at lower of FIFO cost or market	376,067	316,524	317,047
Excess of FIFO over LIFO cost	31,098	28,726	24,290
	<u> </u>	<u> </u>	<u> </u>
	<u>\$ 344,969</u>	<u>\$ 287,798</u>	<u>\$ 292,757</u>

The reconciliation of net income to net cash provided by operating activities is as follows (in thousands):

	Six Months Ended	
	July 1, 2007	June 25, 2006
	<u> </u>	<u> </u>
Cash flows from operating activities:		
Net income	\$ 482,800	\$ 477,993
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	105,809	108,017
Provision for employee long-term benefits	37,692	43,811
Stock compensation expense	10,946	11,540
Gain on current year securitizations	(32,494)	(19,518)
Net change in wholesale finance receivables	247,222	257,545
Origination of retail finance receivables held for sale	(1,650,053)	(1,560,469)
Collections on retail finance receivables held for sale	34,062	47,512
Proceeds from securitization of retail finance receivables	1,742,408	1,514,602
Contributions to pension and postretirement plans	(6,539)	(5,822)
Foreign currency adjustments	1,706	(4,176)
Other, net	18,411	7,128

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	Six Months Ended	
Changes in current assets and liabilities:		
Accounts receivable, net	(18,242)	(25,881)
Finance receivables - accrued interest and other	(5,954)	(14,192)
Inventories	(53,352)	(67,629)
Accounts payable and accrued liabilities	147,073	60,182
Other	960	(5,024)
	<hr/>	<hr/>
Total adjustments	579,655	347,626
	<hr/>	<hr/>
Net cash provided by operating activities	\$ 1,062,455	\$ 825,619
	<hr/>	<hr/>

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Note 4 Impairment of Investment in Retained Securitization Interests

During the six months ended July 1, 2007, the Company recorded an impairment charge of \$3.5 million on its retained securitization interests. Retained securitization interests are recorded at fair value, which is based on the present value of future expected cash flows using the Company's best estimate of key assumptions for credit losses, prepayments and discount rates commensurate with the risks involved. During the six months ended July 1, 2007, the fair value of certain retained securitization interests were lower than the amortized cost, which indicated impairment. This impairment was considered permanent and as a result the investment in retained securitization interests has been appropriately written down to fair value. The decline in fair value was due to higher actual and anticipated credit losses on certain securitization portfolios, partially offset by a slowing in actual and expected prepayment speeds. This charge was recorded as a reduction of financial services income.

Note 5 Income Taxes

The Company or one of its subsidiaries files income tax returns in the United States federal and Wisconsin state jurisdictions and various other state and foreign jurisdictions. The Company is no longer subject to income tax examinations for any significant tax jurisdictions for years before 1998.

The Company adopted the provisions of FASB Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes, on January 1, 2007. As a result of the implementation of FIN 48, the Company recognized a \$16.1 million increase in the liability for unrecognized tax benefits, which was accounted for as a reduction to January 1, 2007 retained earnings. The total gross liability for unrecognized tax benefits was \$84.9 million as of January 1, 2007. Included in this amount were approximately \$11.4 million of accrued interest and \$2.5 million of accrued penalties. The amount of unrecognized tax benefits as of January 1, 2007 that, if recognized, would affect the effective tax rate was approximately \$56.6 million. The Company recognizes interest and penalties related to unrecognized tax benefits in the provision for income taxes. The Company does not expect a significant increase or decrease to the total amounts of unrecognized tax benefits within the next 12 months. There was no material change to the liability for unrecognized tax benefits or its components during the six months ended July 1, 2007.

Note 6 Product Warranty and Recall Campaigns

The Company currently provides a standard two-year limited warranty on all new motorcycles sold. The warranty coverage for the retail customer includes parts and labor and begins when the motorcycle is sold to a retail customer. The Company maintains reserves for future warranty claims using an estimated cost per unit sold which is based primarily on historical Company claim information. Additionally, the Company has from time to time initiated certain voluntary recall campaigns. The Company reserves for all estimated costs associated with recalls in the period that the recalls are announced. Changes in the Company's warranty and product recall liability were as follows (in thousands):

	Three months ended		Six months ended	
	July 1, 2007	June 25, 2006	July 1, 2007	June 25, 2006
	<hr/>	<hr/>	<hr/>	<hr/>
Balance, beginning of period	\$ 66,163	\$ 49,717	\$ 66,385	\$ 43,073
Warranties issued during the period	14,759	10,382	26,295	20,983
Settlements made during the period	(16,724)	(12,172)	(31,029)	(24,246)

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	Three months ended		Six months ended	
Recalls and changes to pre-existing warranty liabilities	9,819	4,988	12,366	13,105
Balance, end of period	\$ 74,017	\$ 52,915	\$ 74,017	\$ 52,915

The liability for product recall campaigns was \$4.3 million and \$5.5 million as of July 1, 2007 and June 25, 2006, respectively.

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Note 7 Business Segments

The Company operates in two business segments: Motorcycles & Related Products (Motorcycles) and Financial Services (Financial Services). The Company's reportable segments are strategic business units that offer different products and services. They are managed separately based on the fundamental differences in their operations. Selected segment information is set forth below (in thousands):

	Three months ended		Six months ended	
	July 1, 2007	June 25, 2006	July 1, 2007	June 25, 2006
Motorcycles net revenue	\$ 1,620,218	\$ 1,377,047	\$ 2,799,093	\$ 2,662,137
Gross profit	605,167	516,326	1,028,213	1,009,540
Operating expenses	218,812	191,358	406,444	372,260
Operating income from Motorcycles	386,355	324,968	621,769	637,280
Financial Services income	112,330	98,567	221,493	194,468
Financial Services expense				