

**Harley-Davidson, Inc.**  
**HOG - \$60.50 – NYSE**

**Recommendation: Sell Short**

**Reasons For Short Sale Recommendation**

- **Stock price up 60% in last 52 weeks.**
- Worldwide revenue **down 4.5%** in 3Q16.
- Worldwide motorcycle revenue **up 1%** in three years.
- Motorcycle shipments **down 9.1%** in 3Q16.
- Parts & Accessories revenue **down 8.3%** in 3Q16.
- Motorcycle gross margin **down 100 bps** in 3Q16, 33.6% vs 34.6%.
- Motorcycle operating income **down 23.9%** in 3Q16.
- Motorcycle operating margin **down 250 bps** in 3Q16, 10.0% vs 12.5%.
- Gross profit **down 6.9%** in 3Q16, \$367.0 million vs \$394.0 million.
- Total operating income **down 17.4%** in 3Q16, \$178.4 million vs \$215.8 million.
- EPS **down 7.2%** in 3Q16, \$0.64 vs \$0.69.

**Financials**

Market Capitalization	\$10.54B	Revenue/Shr (TTM)	\$33.18
Enterprise Value	\$17.06B	EBITDA (TTM)	\$1.26B
Trailing P/E	15.97	Diluted Earnings/Shr mrq)	\$3.73
Forward P/E	14.14	Total Cash (MRQ)	\$795.3M
PEG ratio (5 Yr Expected)	1.55	Total Cash/Shr (mrq)	\$4.44
Price/Sales (TTM)	1.74	Total Debt (MRQ)	<b>\$7.421B</b>
Price/ Book (MRQ)	5.34	Current Ratio (MRQ)	1.61
Enterprise Value/Revenue	<b>2.81</b>	Book Value/Share (MRQ)	\$11.17
Enterprise Value/ EBITDA	13.51%	Operating cash Flow (TTM)	\$1.01B
Profit Margin %	11.33%	Levered Free Cash Flow(TTM)	\$532.11M
Operating Margin (TTM)	17.34%	52 Week Change	<b>47.80%</b>
Return on Assets (TTM)	6.28%	<b>Shares Short</b>	<b>17.22M</b>
Return on Equity (TTM)	30.19%	<b>% of Float Short</b>	<b>9.40%</b>
Revenue (TTM)	\$6.07B	Short Ratio	8.75

(TTM) = Trailing 12 months, (MRQ) = Most recent quarter, M = Millions, B = Billions, m = Thousands

## Business Overview

Harley-Davidson, Inc. is the parent company for the groups of companies doing business as **Harley-Davidson Motor Company (HDMC)** and **Harley-Davidson Financial Services (HDFS)**.

The Company **operates in two segments**: the **Motorcycles & Related Products** (Motorcycles) and the **Financial Services**. The Motorcycles segment has three parts, which consists of:

- 1). **HDMC**, which designs, manufactures and sells at wholesale on-road Harley-Davidson **motorcycles**,
- 2). **Motorcycle parts and accessories**,
- 3). **General merchandise and related services**.

The Company offers its products to retail customers through a network of independent dealers.

The Company operates across the world in three main operating regions:

1. The Americas (**71% of sales**): U.S., Canada and Latin America
2. Europe/Middle East/Africa (EMEA, 18% of sales)
3. Asia-Pacific (11% of sales).

The United States comprises 63.4 percent of worldwide motorcycle sales for HOG. In the most recent quarter, 3Q16, **the United States was 66 percent or two thirds of total worldwide sales.**

Harley-Davidson, Inc.				
Condensed Consolidated Statements of Income				
(In thousands, except per share amounts)				
	(Unaudited)		(Unaudited)	
	Three months ended		Nine months ended	
	September 25, 2016	September 27, 2015	September 25, 2016	September 27, 2015
Motorcycles and related products revenue	\$ 1,091,630	\$ 1,140,321	\$ 4,338,353	\$ 4,301,674
Gross profit	367,019	394,039	1,564,857	1,631,528
Selling, administrative and engineering expense	258,090	250,974	800,722	762,406
Operating income from motorcycles & related products	108,929	143,065	764,135	869,122
Financial services revenue	183,183	177,109	547,505	513,093
Financial services expense	113,736	104,338	332,114	293,745
Operating income from financial services	69,447	72,771	215,391	219,348
Operating income	178,376	215,836	979,526	1,088,470
Investment income	2,300	3,211	3,754	5,983
Interest expense	7,706	4,879	21,968	4,897
Income before income taxes	172,970	214,168	961,312	1,089,556
Provision for income taxes	58,905	73,821	316,327	379,545
Net income	\$ 114,065	\$ 140,347	\$ 644,985	\$ 710,011
Earnings per common share:				
Basic	\$ 0.64	\$ 0.69	\$ 3.57	\$ 3.43
Diluted	\$ 0.64	\$ 0.69	\$ 3.55	\$ 3.41
Weighted-average common shares:				
Basic	178,438	203,598	180,779	207,255
Diluted	179,320	204,580	181,582	208,282
Cash dividends per common share	\$ 0.35	\$ 0.31	\$ 1.05	\$ 0.93

In the 3Q16, Motorcycle revenue was down 4.3%, gross profit was down 6.9%, SG&A expense up 2.8%, **operating income from motorcycles was down 23.9%**, financial service revenue up 3.4%, financial services expenses up 9.0%, **operating income from financial services down 4.6%**, **total operating income down 17.4%**, interest expense up 57.9%, **net income down 18.7%**, **EPS down 7.2%**.

Harley-Davidson, Inc.  
Condensed Consolidated Balance Sheets<sup>(1)</sup>  
(In thousands)

	(Unaudited) September 25, 2016	December 31, 2015	(Unaudited) September 27, 2015
<b>ASSETS</b>			
<b>Current assets:</b>			
Cash and cash equivalents	\$ 790,284	\$ 722,209	\$ 1,368,554
Marketable securities	5,038	45,192	47,358
Accounts receivable, net	346,176	247,405	294,054
Finance receivables, net	2,205,644	2,053,582	2,068,873
Inventories	426,547	585,907	466,657
Restricted cash	65,088	88,267	113,499
Other current assets	263,567	235,321	251,225
<b>Total current assets</b>	<b>4,102,344</b>	<b>3,977,883</b>	<b>4,610,220</b>
Finance receivables, net	4,944,322	4,814,571	5,009,473
Other long-term assets	1,165,560	1,180,523	1,092,341
	<b>\$ 10,212,226</b>	<b>\$ 9,972,977</b>	<b>\$ 10,712,034</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>			
<b>Current liabilities:</b>			
Accounts payable & accrued liabilities	\$ 798,127	\$ 707,578	\$ 781,246
Short-term debt	1,055,428	1,201,380	990,049
Current portion of long-term debt, net	700,152	838,349	885,889
<b>Total current liabilities</b>	<b>2,553,707</b>	<b>2,747,307</b>	<b>2,657,184</b>
Long-term debt, net	5,170,609	4,832,469	5,040,644
Pension and postretirement healthcare liabilities	303,319	358,547	254,864
Other long-term liabilities	192,223	195,000	199,669
<b>Total shareholders' equity</b>	<b>1,992,368</b>	<b>1,839,654</b>	<b>2,559,673</b>
	<b>\$ 10,212,226</b>	<b>\$ 9,972,977</b>	<b>\$ 10,712,034</b>

Harley-Davidson, Inc.		
Condensed Consolidated Statements of Cash Flows		
(In thousands)		
	(Unaudited)	(Unaudited)
	Nine months ended	
	September 25, 2016	September 27, 2015
Net cash provided by operating activities	\$ 927,809	\$ 1,020,957
Cash flows from investing activities:		
Capital expenditures	(162,726)	(139,054)
Finance receivables, net	(569,013)	(719,472)
Proceeds from sale of finance receivables	312,571	-
Net change in marketable securities	40,014	9,500
Acquisition of business	-	(59,910)
Other	251	5,172
Net cash used by investing activities	(378,903)	(903,764)
Cash flows from financing activities:		
Proceeds from issuance of senior unsecured notes	-	740,949
Proceeds from issuance of medium-term notes	1,193,396	595,386
Repayments of medium-term notes	(451,336)	(600,000)
Proceeds from securitization debt	-	1,195,668
Repayments of securitization debt	(535,616)	(764,909)
Net (decrease) increase in credit facilities and unsecured commercial paper	(146,328)	258,734
Borrowings of asset-backed commercial paper	33,428	69,191
Repayments of asset-backed commercial paper	(55,170)	(55,124)
Net change in restricted cash	30,981	(15,165)
Dividends paid	(190,387)	(191,451)
Purchase of common stock for treasury	(374,234)	(894,565)
Excess tax benefits from share-based payments	1,291	2,878
Issuance of common stock under employee stock option plans	6,444	16,755
Net cash (used by) provided by financing activities	(487,531)	358,347
Effect of exchange rate changes on cash and cash equivalents	6,700	(13,666)
Net increase in cash and cash equivalents	\$ 68,075	\$ 461,874
Cash and cash equivalents:		
Cash and cash equivalents - beginning of period	\$ 722,209	\$ 906,680
Net increase in cash and cash equivalents	68,075	461,874
Cash and cash equivalents - end of period	\$ 790,284	\$ 1,368,554

Motorcycles and Related Products Revenue and  
Motorcycle Shipment Data

	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
	Three months ended		Nine months ended	
	September 25, 2016	September 27, 2015	September 25, 2016	September 27, 2015
<b>MOTORCYCLES AND RELATED PRODUCTS REVENUE (in thousands)</b>				
Motorcycles	\$ 788,856	\$ 812,398	\$ 3,437,066	\$ 3,376,356
Parts & Accessories	231,279	252,226	673,192	692,938
General Merchandise	65,289	69,008	211,664	212,954
Other	6,206	6,689	16,431	19,426
	<u>\$ 1,091,630</u>	<u>\$ 1,140,321</u>	<u>\$ 4,338,353</u>	<u>\$ 4,301,674</u>
<b>MOTORCYCLE SHIPMENTS:</b>				
United States	26,269	30,092	141,708	141,884
International	22,342	23,380	78,099	76,349
Total	<u>48,611</u>	<u>53,472</u>	<u>219,807</u>	<u>218,233</u>
<b>MOTORCYCLE PRODUCT MIX:</b>				
Touring	23,295	21,994	89,467	95,354
Cruiser	13,986	18,405	78,570	71,753
Sportster® / Street	11,330	13,073	51,770	51,126
Total	<u>48,611</u>	<u>53,472</u>	<u>219,807</u>	<u>218,233</u>

In the 3Q16 Motorcycle revenue was **down 2.9%**, Parts and Accessories were **down 8.3%**, General Merchandise was **down 7.2%**, Total motorcycle and related products revenue was **down 4.3%**.

Total motorcycle shipments were **down 9.1%**, **U.S. Shipments were down 12.7%**, International shipments were **down 4.4%**.

Worldwide Retail Sales of Harley-Davidson Motorcycles<sup>(1)</sup>

	Three months ended		Nine months ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
<b>Americas Region</b>				
United States	45,469	48,918	135,581	142,196
Canada	2,663	2,554	8,946	8,414
Latin America	2,605	2,818	7,064	8,091
<b>Total Americas Region</b>	<b>50,737</b>	<b>54,290</b>	<b>151,591</b>	<b>158,701</b>
<b>Europe, Middle East and Africa Region (EMEA)</b>				
Europe <sup>(2)</sup>	8,807	8,441	32,590	30,720
Other	1,417	1,590	5,357	4,878
<b>Total EMEA Region</b>	<b>10,224</b>	<b>10,031</b>	<b>37,947</b>	<b>35,598</b>
<b>Asia Pacific Region</b>				
Japan	2,762	2,642	7,631	7,194
Other	5,232	5,215	16,510	16,277
<b>Total Asia Pacific Region</b>	<b>7,994</b>	<b>7,857</b>	<b>24,141</b>	<b>23,471</b>
<b>Total Worldwide Retail Sales</b>	<b>68,955</b>	<b>72,178</b>	<b>213,679</b>	<b>217,770</b>
<b>Total International Retail Sales</b>	<b>23,486</b>	<b>23,260</b>	<b>78,098</b>	<b>75,574</b>

**Total Americas revenue was down 6.5%, the U.S. was down 7.1%.**

Total EMEA revenue was up 1.9%.

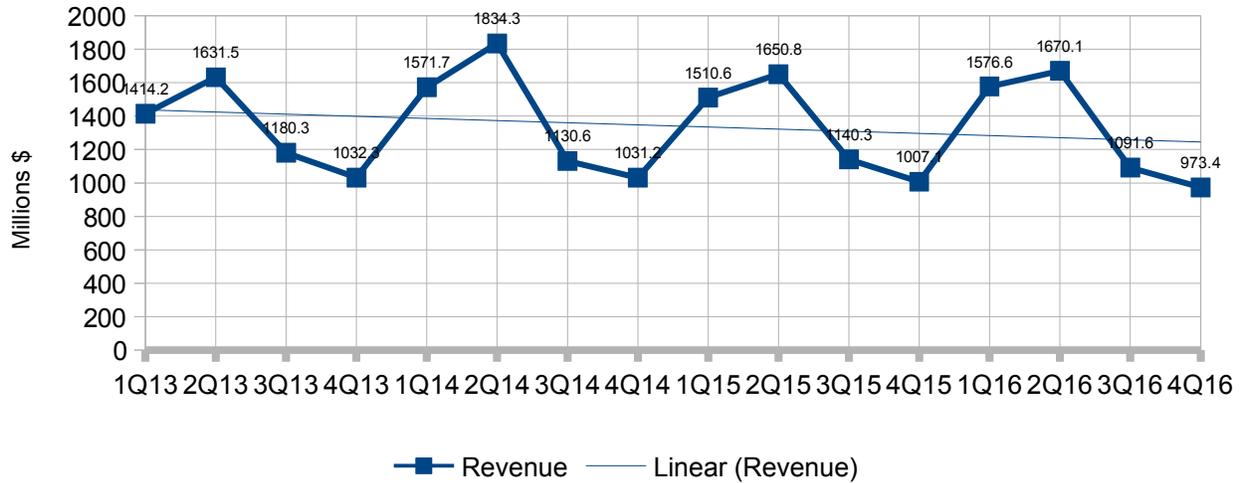
Total Asia Pacific region revenue was up 1.7%.

**Total worldwide revenue was down 4.5%.**

Total International revenue was up 0.9%.

### HOG Motorcycle Revenue

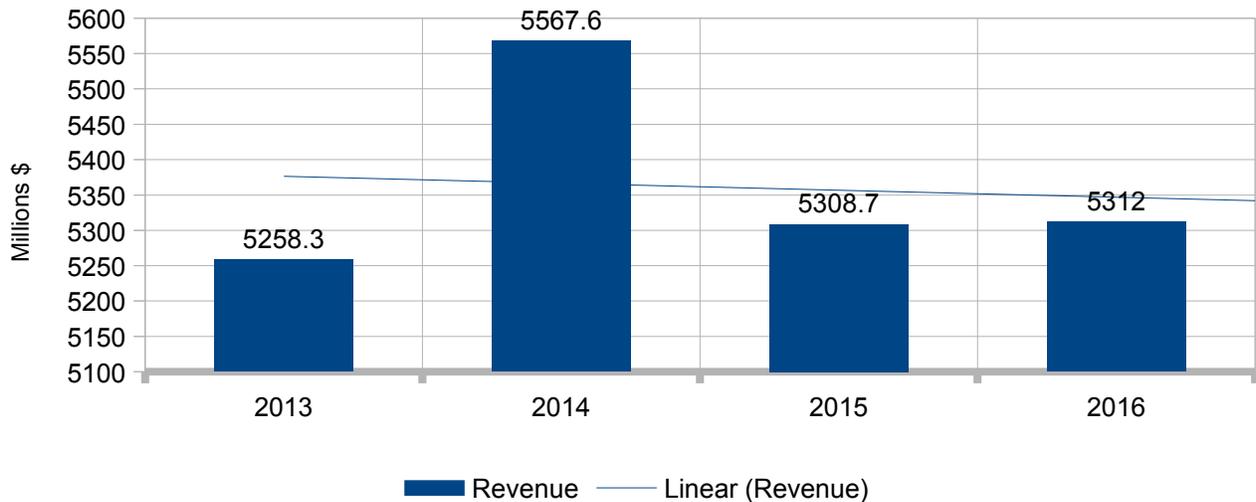
March 2013 To December 2016 Est.



**Motorcycle revenue has been trending down for three years!**

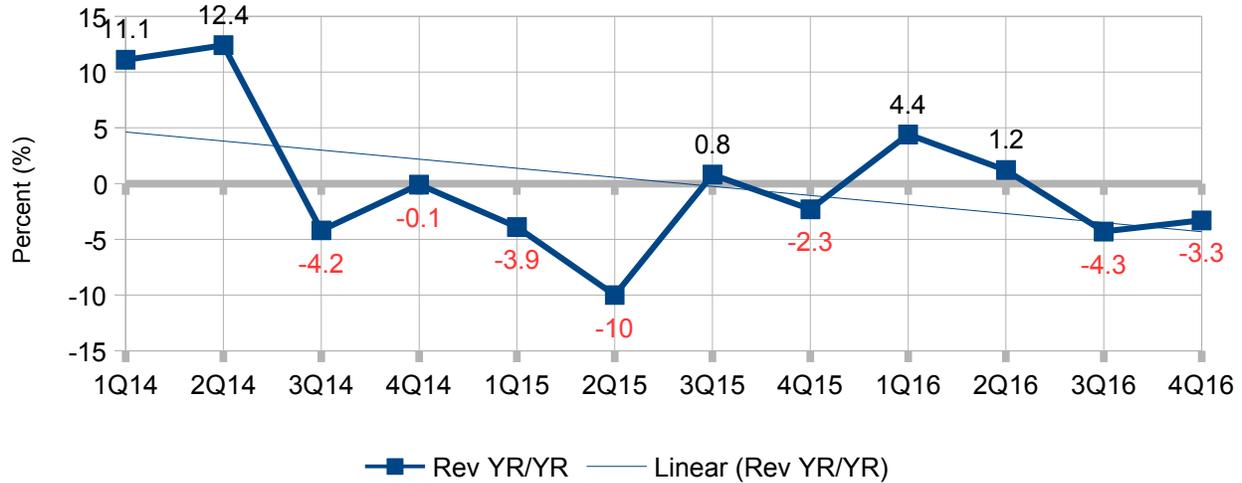
### Hog Motorcycle Revenue

2013 To 2016 Est.



### HOG YR/YR Revenue Growth

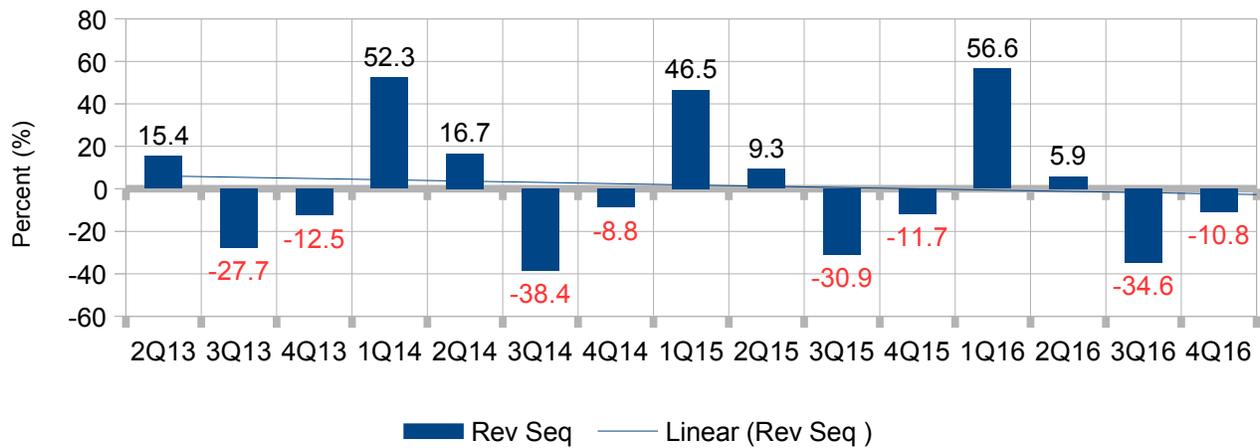
March 2014 To December 2016 Est.



**Year over year revenue growth has gone from an average of plus five percent to negative five percent in the past three years.**

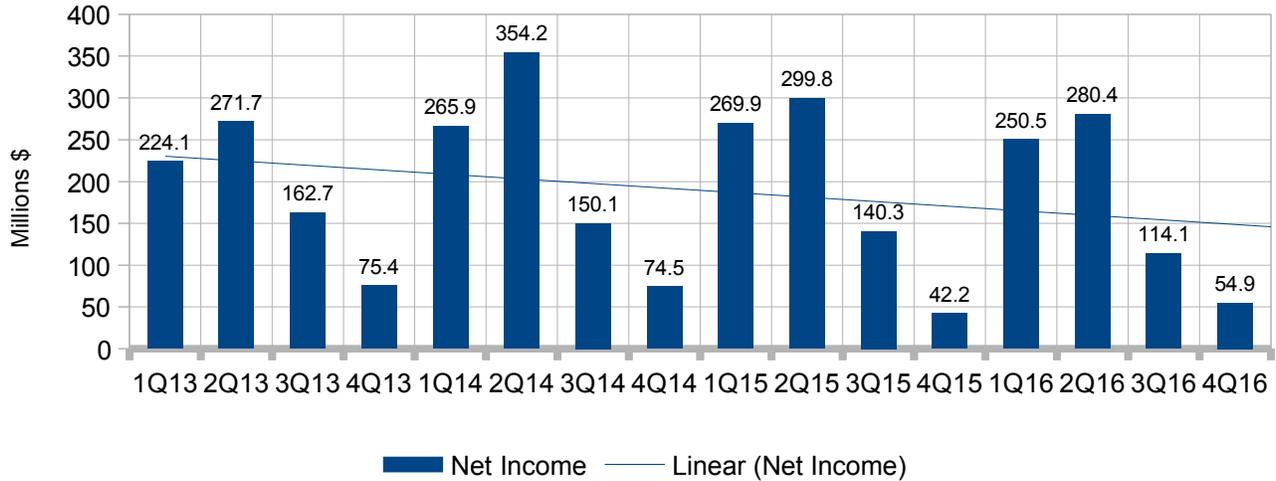
### HOG Sequential Revenue Growth

June 2013 To December 2016 Est.



### HOG Net Income

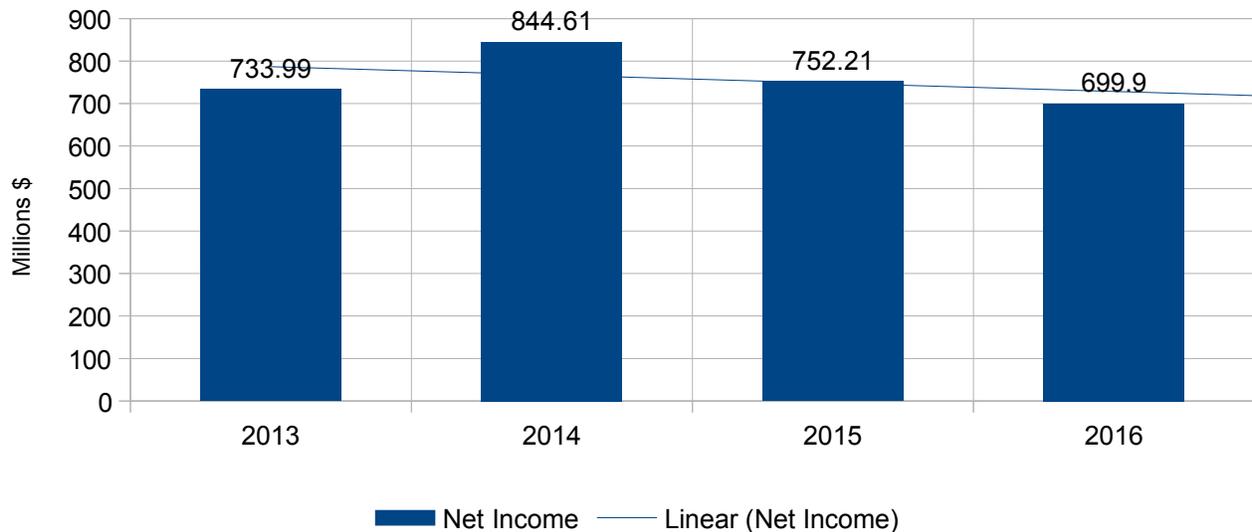
March 2013 To December 2016 Est.



**Net income is also trending down during the past four years.**

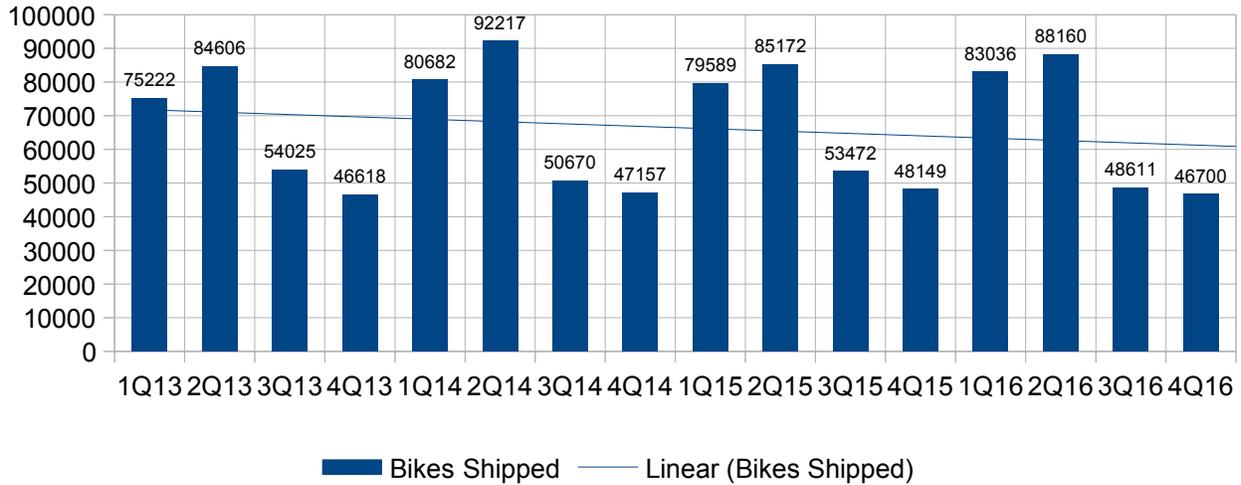
### HOG Net Income

2013 To 2016 Est.



### HOG Worldwide Motorcycle Shipments

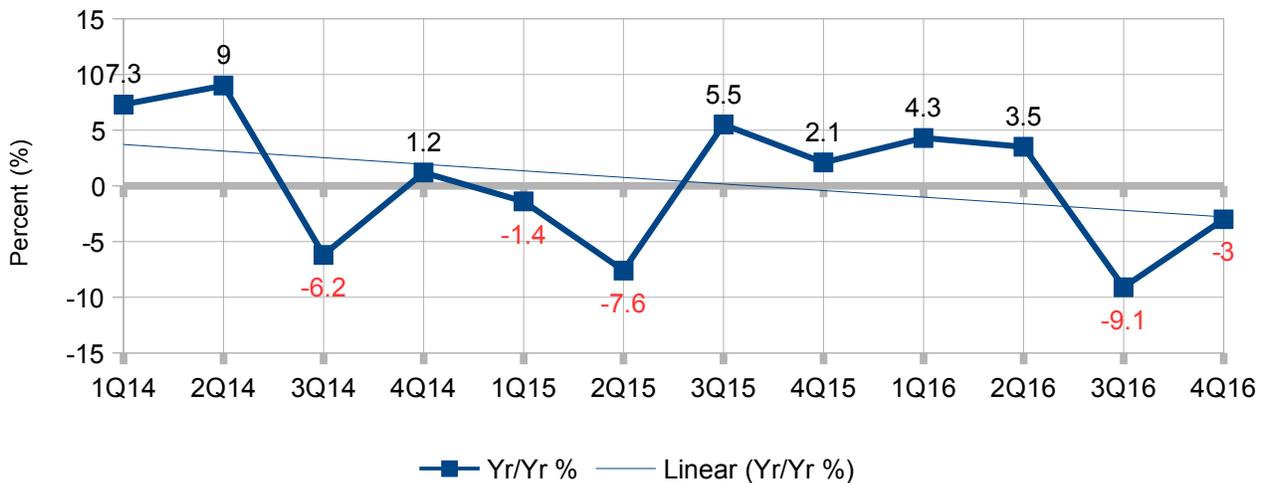
March 2013 To December 2016 Est.



**Worldwide motorcycle shipments have been declining for the past four years.**

### HOG YR/YR Worldwide Motorcycle Shipment Growth

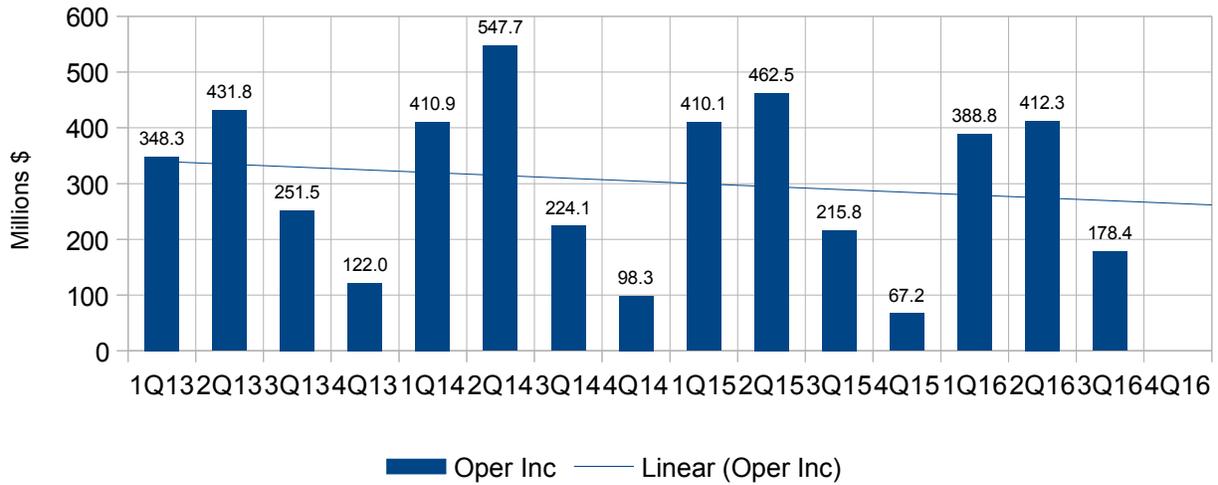
March 2014 To December 2016 Est.



**Year over year growth in motorcycle shipments has gone from an average of plus four percent to negative three percent, despite new product introductions.**

### HOG Operating Income

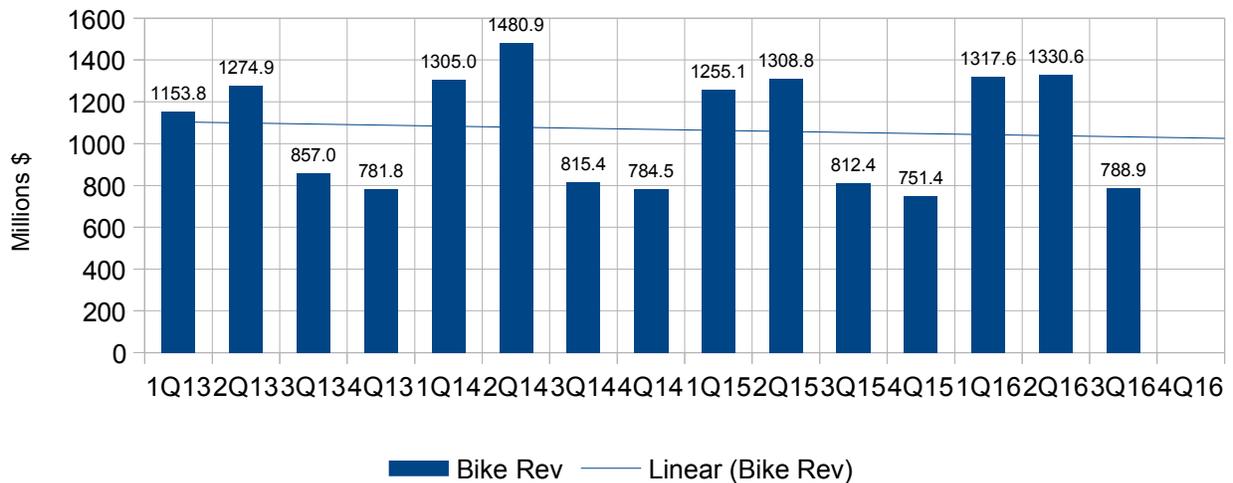
March 2013 To December 2016 Est.



**Operating income is also trending down for the past four years.**

### HOG Motorcycle Revenue

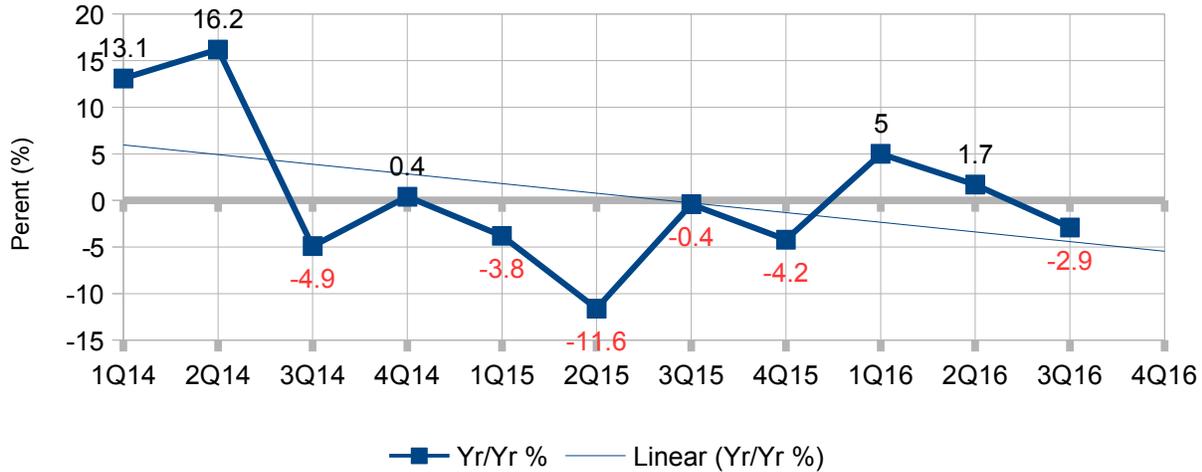
March 2013 To December 2016 Est.



**Motorcycle only revenue.**

## HOG YR/YR Motorcycle Revenue Growth

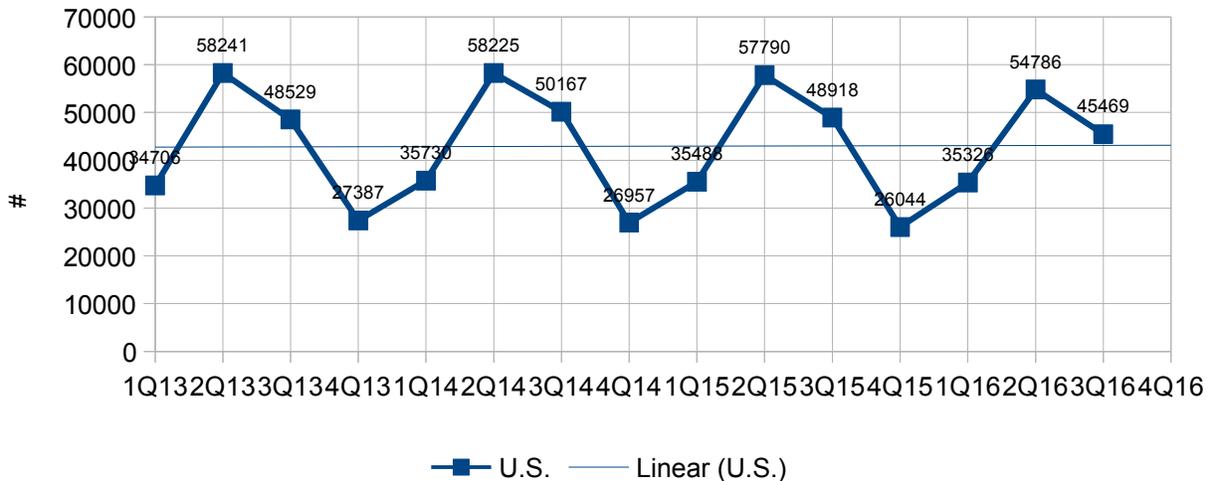
March 2014 To December 2016 Est.



**Motorcycle only revenue is trending down even faster than total revenue.**

## HOG Domestic Motorcycle Units

2013 To 2016

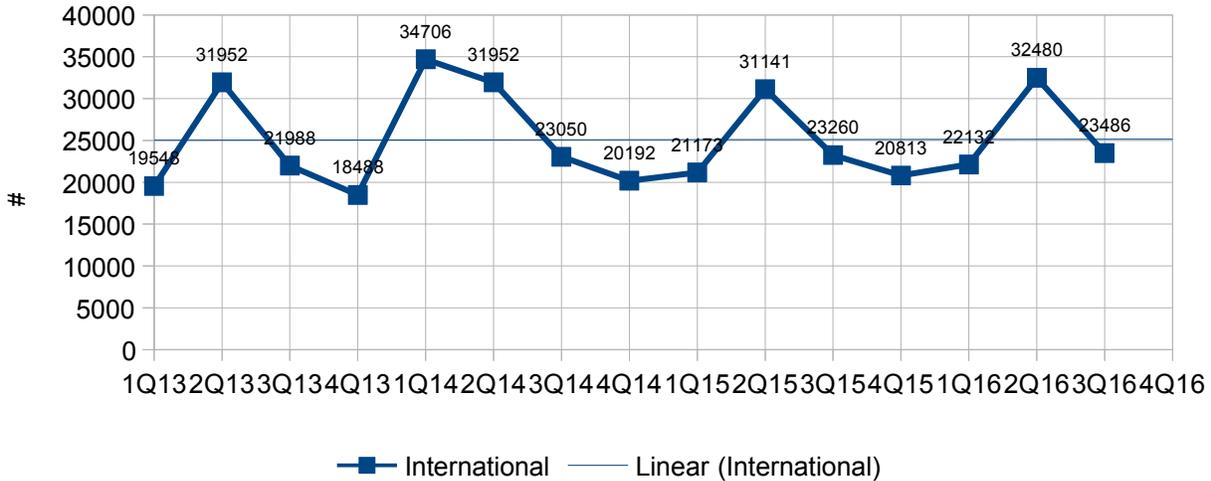


**Two thirds of their revenue shows no growth in the past four years!**

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### HOG International Motorcycle Units

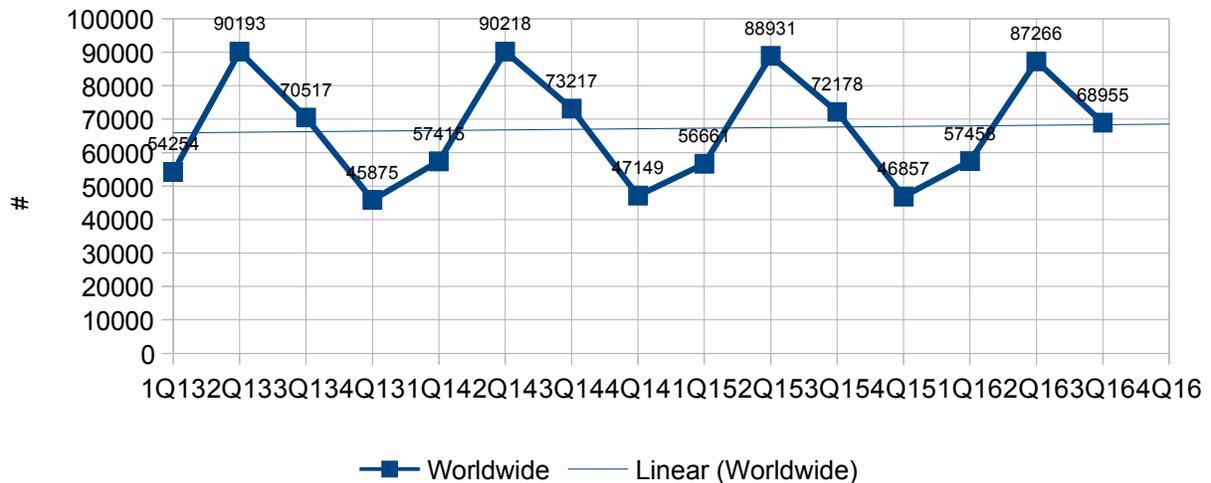
2013 To 2016



**International motorcycle units, which is one third of revenue is flatter than a pancake!**

### HOG Worldwide Motorcycle Units

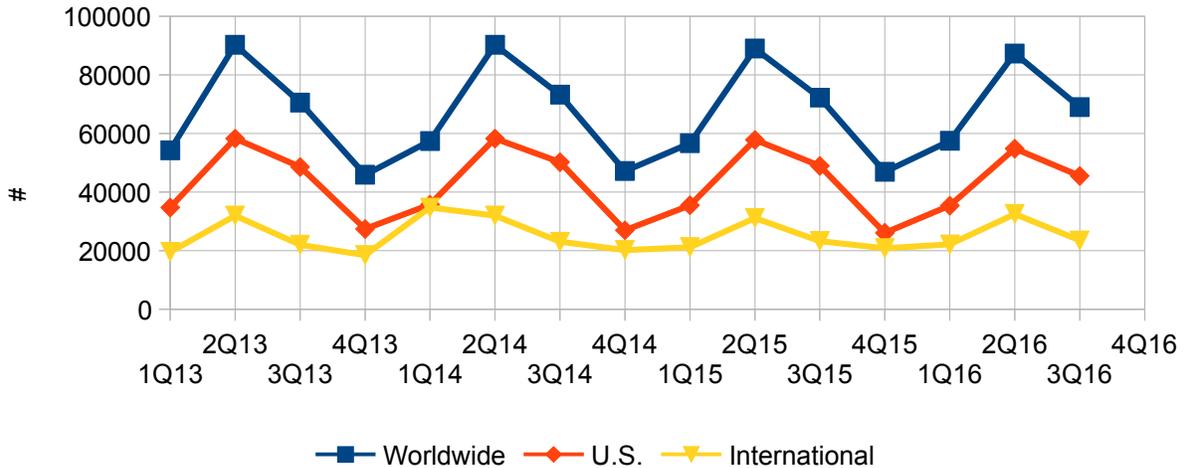
2013 To 2016



**Domestic and International together are barely growing in four years.**

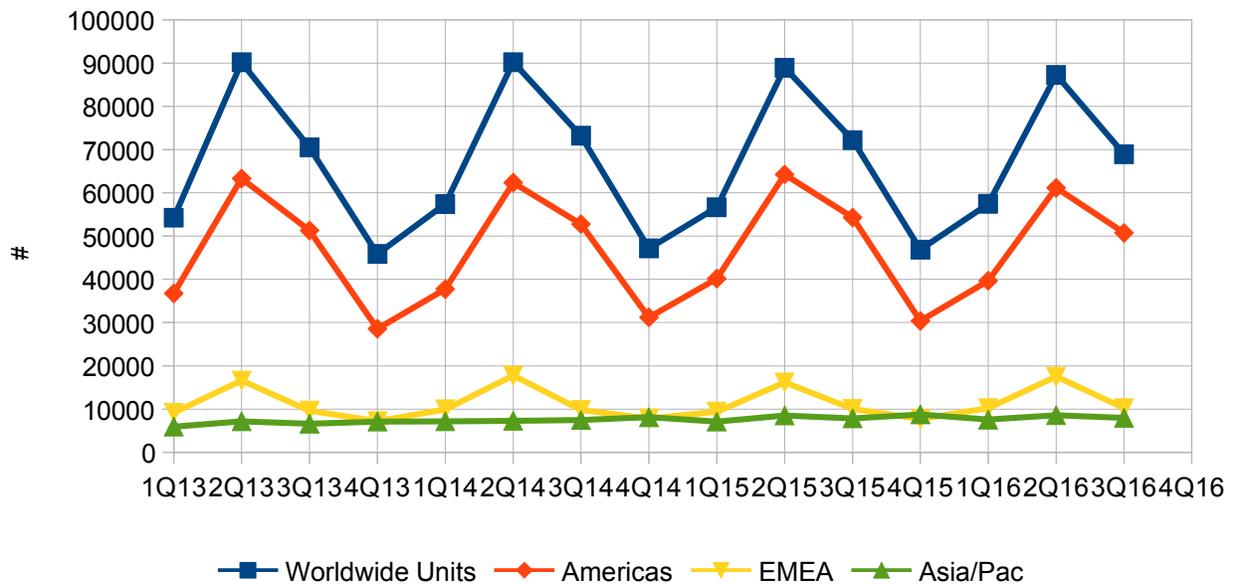
### HOG Worldwide Motorcycle Units

Domestic and International 2013 To 2016



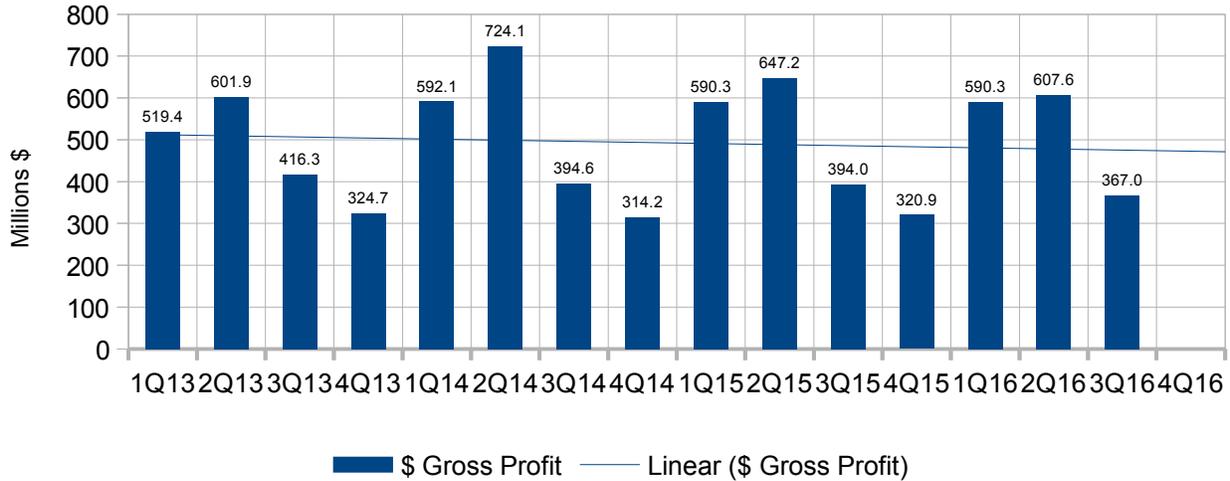
### HOG Worldwide Motorcycle Units By Region

2013 To 2016



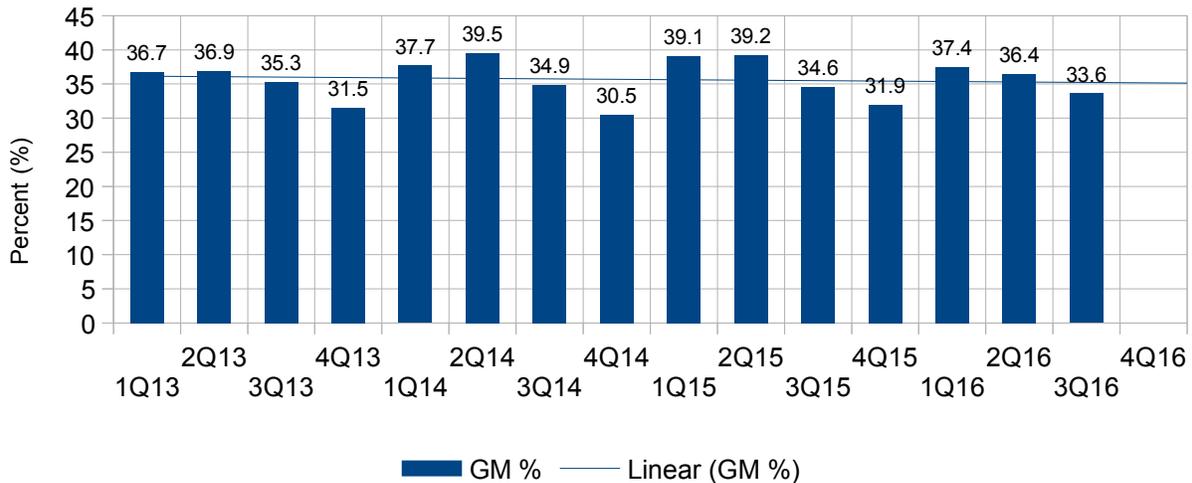
### HOG Motorcycle Gross Profit

March 2013 To December 2016 Est.



### Hog Motorcycle Gross Margin

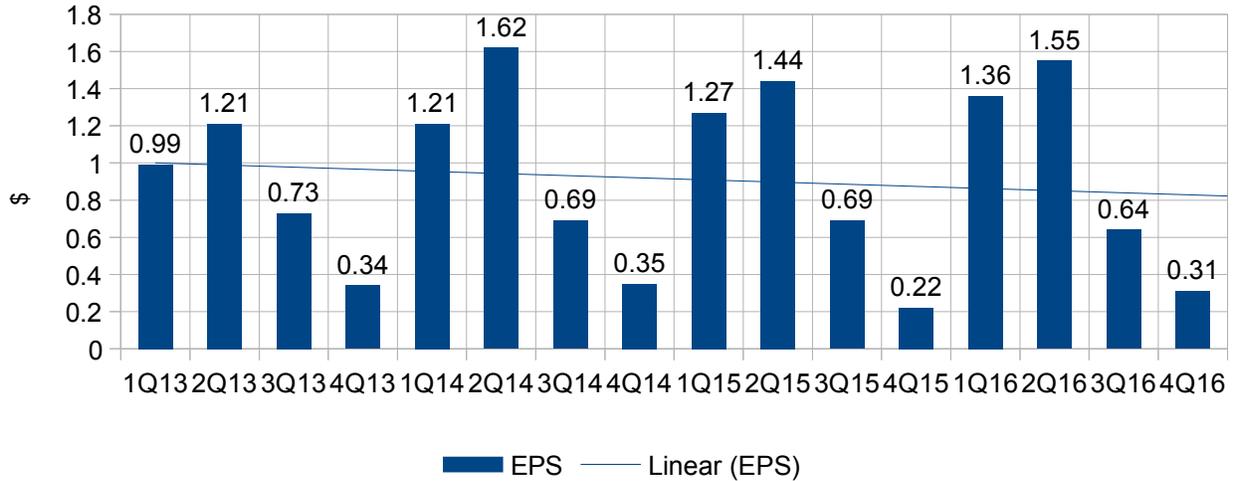
March 2013 To December 2016 Est.



**Gross profit and Gross Margin are both flat to trending down a little.**

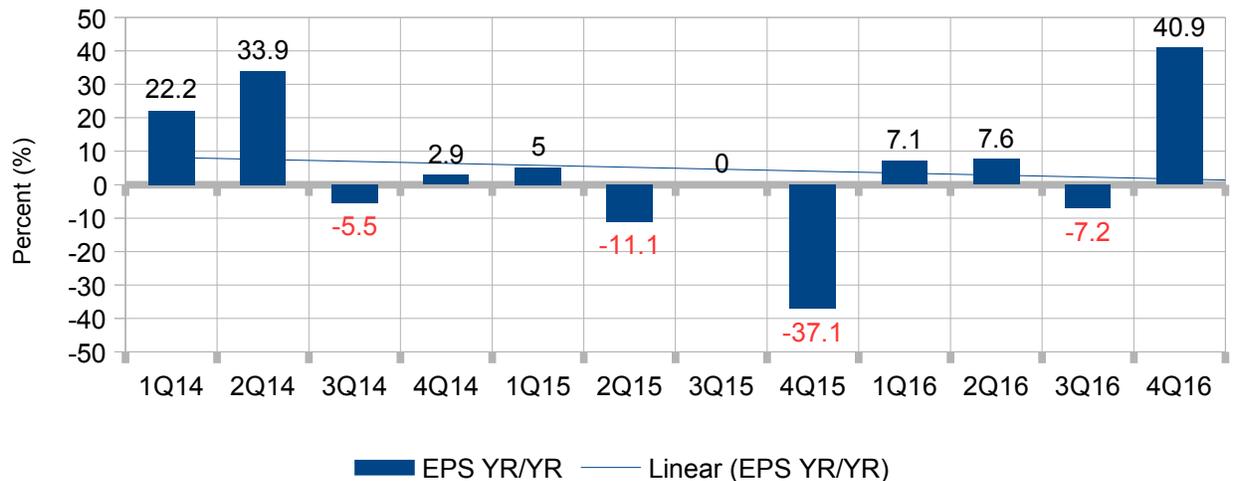
### HOG Earnings Per Share

March 2013 To December 2016 Est.



### HOG YR/YR Earnings Per Share Growth

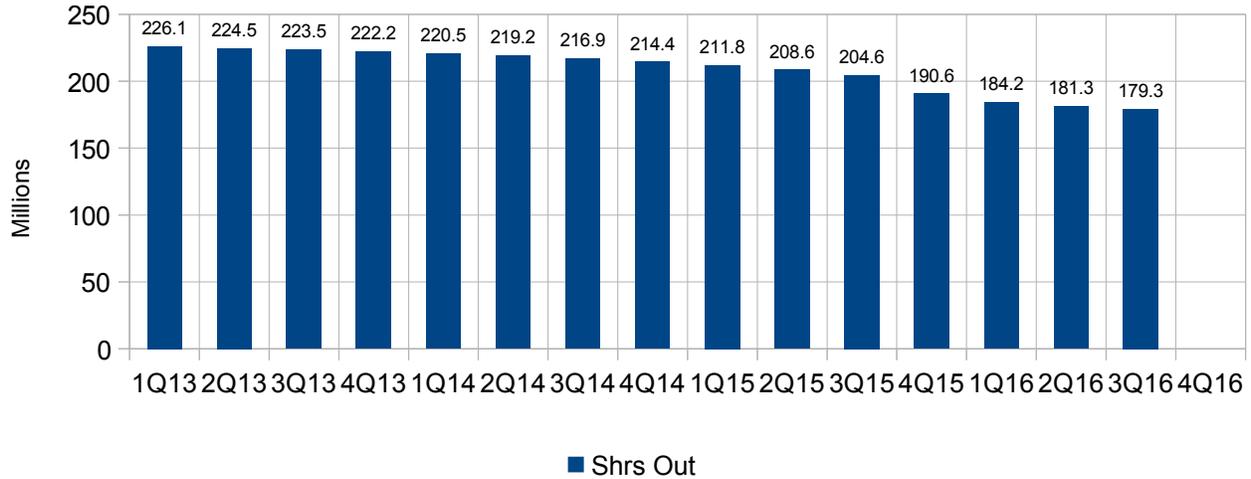
March 2014 To December 2016 Est.



**Earnings per share has also been trending down despite HOG aggressively buying back stock. 4Q16 EPS growth will look good only because 4Q15 was so terrible. 4Q16 EPS estimate of \$031, while 40% higher than 2015 is still 11.4% below 2014's \$035.**

### HOG Shares Outstanding FD

March 2013 To December 2016 Est.



HOG has shrunk shares outstanding by 12.4 percent in the last year. This is the only way that they can show any earnings per share growth. The business is in slow decline as aging baby boomers start dying off or get too old to ride big heavy motorcycles.

Competitor Polaris (PII) just lowered 2017 EPS guidance below expectations off its view the power sports market will be weak this year.

Harley-Davidson, Inc. (HOG) 60.02 0.32 (0.54%) As of 4:00PM EST. Market closed.



HOG hit a low of \$37.49 on January 27, 2016. Today the stock is \$60, **60 percent higher than one year ago.** The business has not improved by sixty percent, in fact the business is shrinking. **We look at stocks to short where the stock price is going straight up while the fundamentals are going down.** HOG fits this bill. Earnings declined 7 percent last quarter and the stock is going up.

Out of 22 analysts, 3 rate it a sell, 14 rate it a hold, 5 rate it a buy. The average price target is \$57, \$3 below where it is today. Talk about all the good news already priced in! Perhaps most of the analysts see the declining sales, gross profit and margins.

In the third quarter of 2016, revenue declined 3.2% from a year earlier, from \$1.31 billion to \$1.27 billion, but it was “better than expectations” of \$1.1 billion, so off to the races? For the fourth quarter of 2016, analyst estimates for revenue are \$0.97 billion, **another 3 percent decline from the year before.**

For the full year 2016 the revenue estimate is \$5.31 billion, essentially flat with 2015's \$5.30 billion. And the stock is up 60%?

In 3Q16, HOG's US retail motorcycles sales were 45,469 units compared to 48,918 units in 3Q15. **It was a year over year fall of about 7.1%**. Similarly, in 2Q16, the company's sales volume in the United States **fell 5.2%** to 54,786 units, from 57,790 in 2Q15.

**So, in the last two quarters, in the all important domestic market, motorcycle sales declined 5.2% and 7.1%. And the stock is up 60%?**

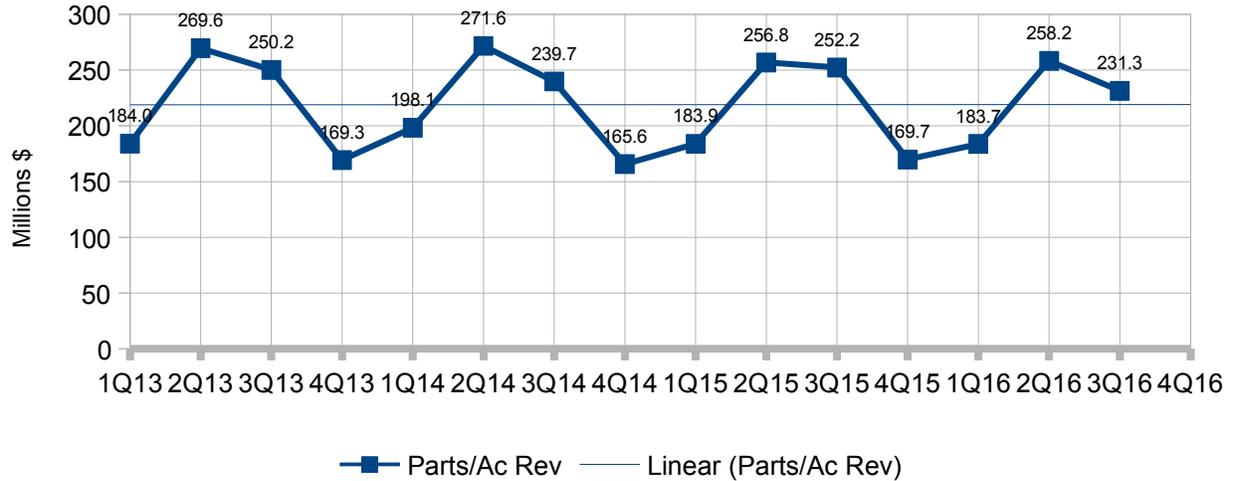
In 3Q16, Harley-Davidson's consolidated **gross profits were \$436.0 million, a 13.2% decline** from \$503.0 million in 3Q15. Its **gross margin came in at 34.2% compared to 38.1% in 3Q15, a decline of 390 bps! That is a 10.2% decline in margins in one year.** The gross margin for its motorcycles and related products was 33.6% in 3Q16 compared to 34.6% in 3Q15.

Analysts are estimating that Harley-Davidson's **gross margin have declined to 32.8% in 4Q16 from 37.9% a year before, a whopping 510 bps, or 13.5% decline in one year!** For fiscal 2016, analysts estimate HOG's **gross margins to fall to 35.5% from 42.1% in the previous year, a huge decline of 660 bps, or 15.7%!** And the stock is up 60% on this?

The reason for the margin shrinkage is two fold. Expenses are rising and they are selling more, less expensive motorcycles outside of the slowing U.S. market.

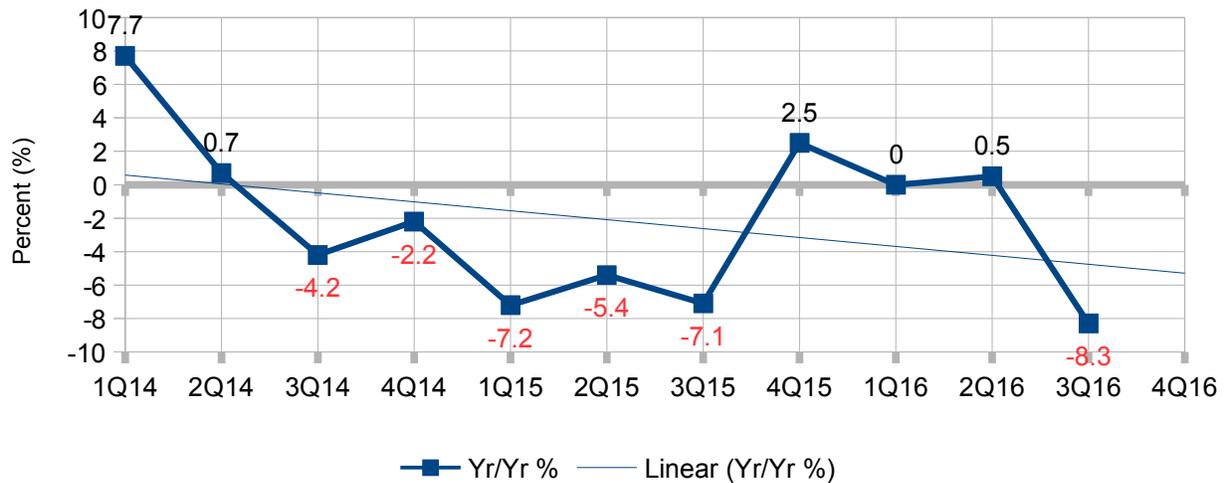
### HOG Parts & Accessories Revenue

2013 To 2016



### HOG Parts & Accessories YR/YR Revenue Growth

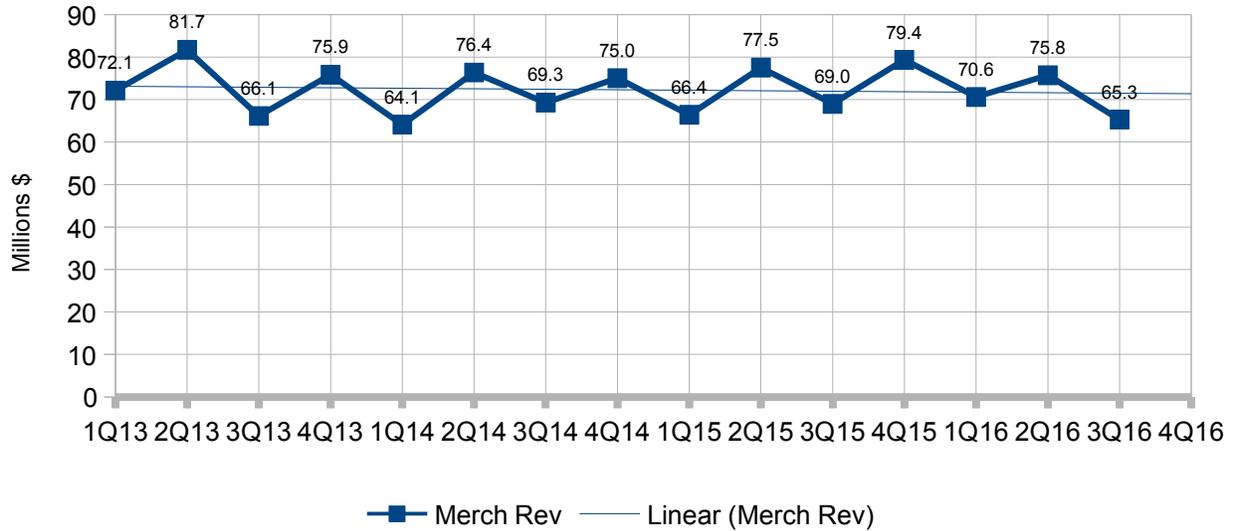
2014 To 2016



**Parts & accessories revenue is trending lower.**

### HOG Merchandise Revenue

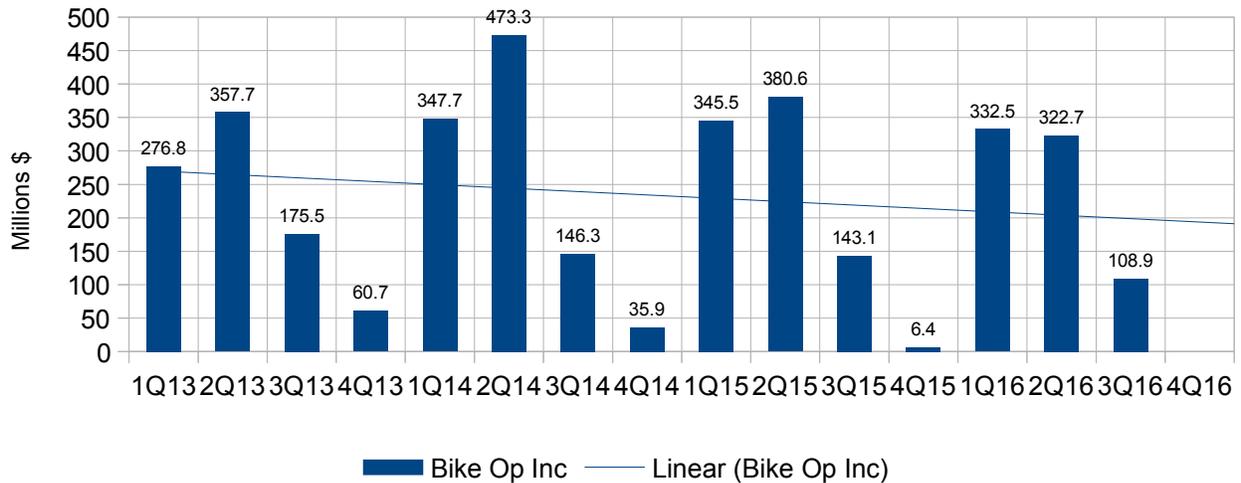
2013 To 2016



**Merchandise revenue is flat to trending down.**

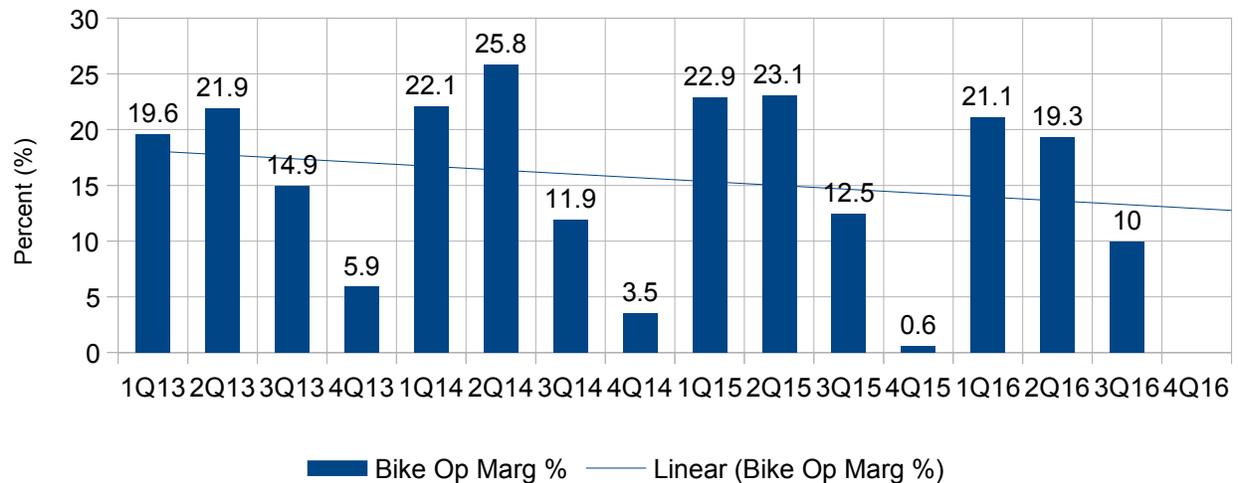
### HOG Motorcycle Operating Income

2013 To 2016



### HOG Motorcycle Operating Margin

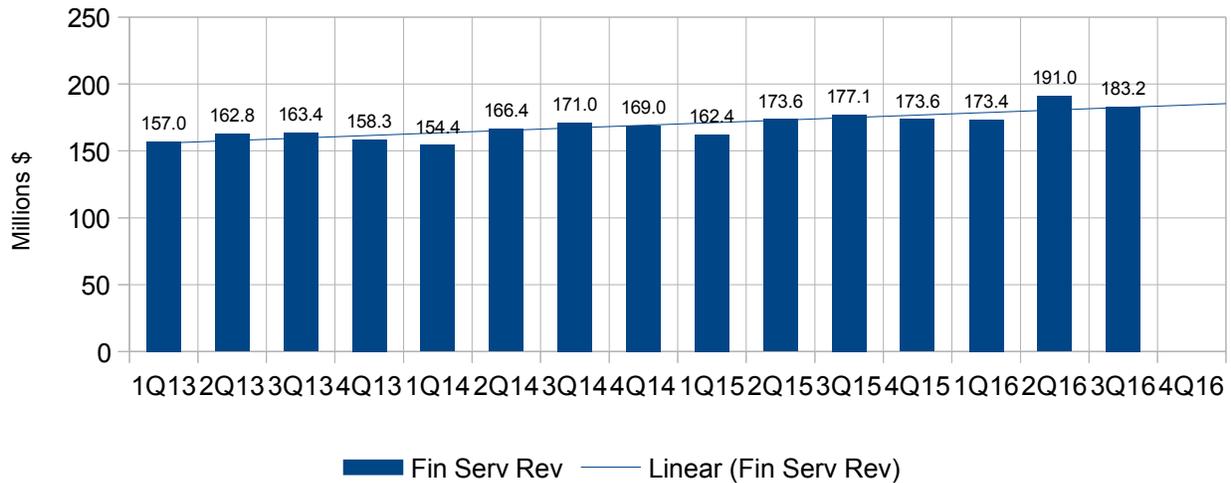
2013 To 2016



**Motorcycle operating income and operating margin are both trending down.**

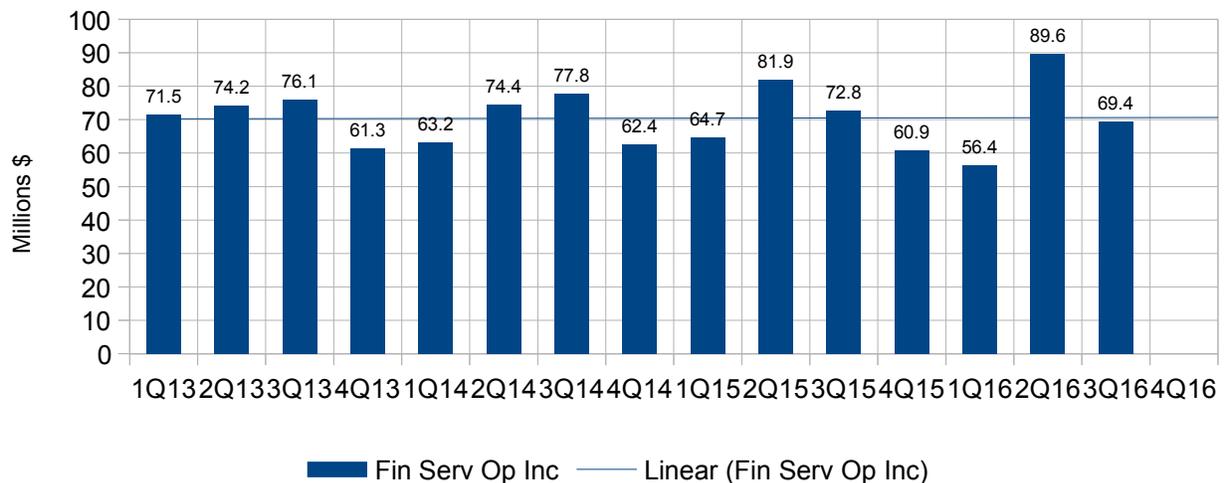
### HOG Financial Services Revenue

2013 To 2016



### Financial Services Operating Income

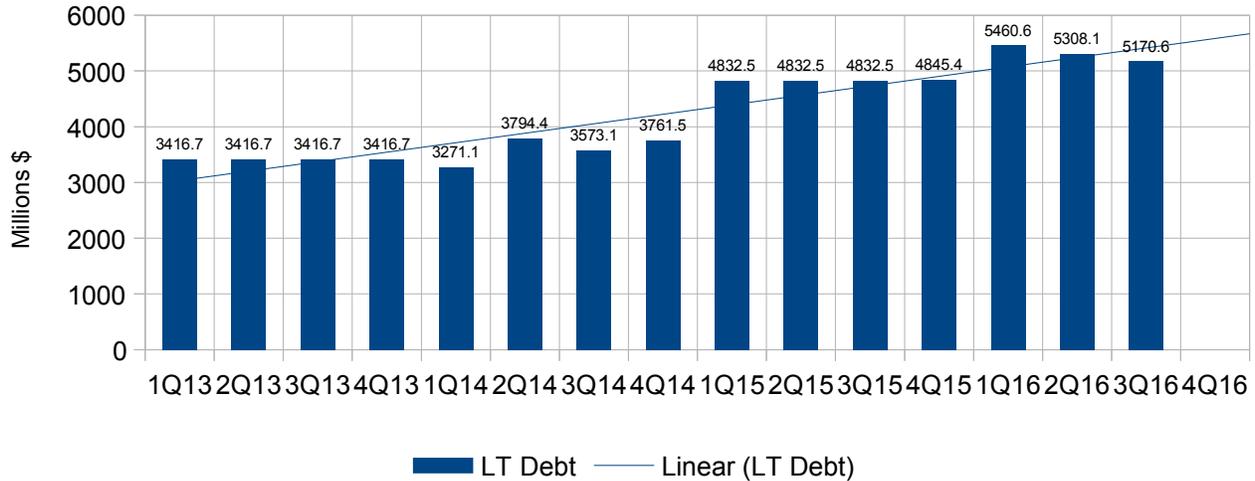
2013 To 2016



**Financial services revenue is growing a little but financial services operating income has been flat for years.**

### HOG Long Term Debt

2013 To 2016



### Valuation

As of January 23, 2017, Harley-Davidson’s **forward EV-to-EBITDA** (enterprise value to earnings before interest, tax, depreciation, and amortization) **multiple is 12.0x**. This is **almost double their Japanese competitors**. The multiple is significantly higher than the EV-to-EBITDA multiple of Japanese motorcycle makers Honda (HMC) 6.5x and Kawasaki 7.1x.

Harley-Davidson’s forward PE multiple, based on its earnings forecast for the next 12 months, is 13.8x. That’s higher than Honda’s 10.6x and Kawasaki’s 11.8x.

HOG is struggling to protect its margins and faces strong competition from its Japanese competitors.

## Conclusion

- Revenue **trending down**.
- YR/YR Revenue growth **trending down**.
- Sequential revenue growth **trending down**.
- EPS **trending down**, despite share buybacks.
- YR/YR EPS growth **trending down**.
- Gross margin **trending down huge**.
- Gross profit **trending down**.
- Total operating income **trending down**.
- Motorcycle shipments **trending down**.
- YR/YR Motorcycle shipment growth **trending down**.
- Motorcycle revenue **trending down**.
- YR/YR motorcycle revenue **trending down**.
- Parts & Accessories revenue **flat**.
- YR/YR Parts & Accessories revenue growth **trending down**.
- Merchandise revenue **trending down**.
- Motorcycle gross margin **trending down**.
- Motorcycle operating income **trending down**.
- Motorcycle operating margin **trending down**.
- Long term debt increasing.
- Interest expense increasing.
- Financial services revenue growing a little.
- Financial services operating income **flat**.
- Worldwide motorcycle shipments **flat**.
- **Stock price UP 60 percent!**

### What is trending up besides the stock price?

We have a short term price target of \$54 and a long term price target of \$50. With continued deterioration of the business these targets could/will be lowered.

Fourth quarter 2016 earnings are to be released on January 31, 2017. While EPS growth should be up about 40% because of the disaster one year ago. The fundamentals are still in decline. If the stock moves up on this report we would add to the position.

Sell.