

Case 7 Harley-Davidson, Inc., May 2015

For us and for our loyal customers, the motorcycles we build aren't just motorcycles. They are living pieces of American history, mystique on two wheels. They are the vehicle with which our riders discover the power, the passion, and the people that define the Harley-Davidson Experience.

—HARLEY-DAVIDSON, INC.¹

On May 1, 2015, Matt Levatich took over as CEO of Harley-Davidson, Inc.. Levatich was 48 years old and had joined Harley as a management trainee in 1994. He held an engineering degree from Rensselaer Polytechnic Institute and an MBA from Northwestern. The company he was taking charge of was not among the world's biggest motorcycle companies—it shipped 270,726 bikes in 2014 compared to Honda's 17 million. However, it was the world's most financially successful motorcycle manufacturer: it earned a higher sales margin and a higher return on equity than any of its rivals.

Levatich's predecessor was Keith Wandell, who had stabilized Harley after the financial crisis of 2008–2009 and returned the company to its growth path. During Wandell's six-year tenure, Harley's cumulative total return to shareholders was 280%, compared to 172% for the S&P 500 as a whole.

The road ahead, however, looked distinctly bumpy. On Levatich's first day as CEO, investment advisor James Berman published a newsletter that asked the question: "Is the long, classic American love affair with Harleys a thing of the past?"² Harley's profit growth depended on its ability to keep expanding the sales of its high-priced, heavyweight motorcycles. While no other company could replicate the emotional attachment of riders to the "Harley Experience," there was always the risk that motorcycle riders might seek a different type of experience and become more attracted to the highly engineered models produced by European and Japanese manufacturers. Equally worrying was the fear that motorcycles might lose their appeal both as a leisure activity and as a male status symbol. Such concerns were fueled by demographic trends. Harley's core market was the baby-boomer generation—and this cohort was moving more toward retirement homes than outdoor sports. Would the next cohorts—Generation X and Generation Y—have the same affinity for noisy, heavyweight motorcycles and the cultural values that Harley-Davidson

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represented? Moreover, with consumer spending weak in both North America and Europe—Harley's two biggest markets—the demand for luxury leisure products costing between \$7000 and \$38,000 was likely to be subdued.

The History of Harley-Davidson

From Birth to Maturity, 1903–1981

Harley-Davidson, Inc. was founded in 1903 by William Harley and the three Davidson brothers: William, Arthur, and Walter. In 1909, Harley introduced its two-cylinder, V-twin engine with its deep, rumbling sound: this engine type would be the characteristic feature of Harley-Davidson motorcycles for the next hundred years. At that time there were about 150 US motorcycle producers in the US; by 1953, Harley-Davidson was the sole survivor.

The postwar affluence and the rise of youth culture created a growing demand for motorcycles. This was satisfied primarily by imports: first the British (BSA, Triumph, and Norton) and then the Japanese (led by Honda). Harley benefitted from the rebirth of motorcycling as a leisure activity. However, its acquisition by the leisure conglomerate AMF in 1969 was followed by quality problems and financial losses.

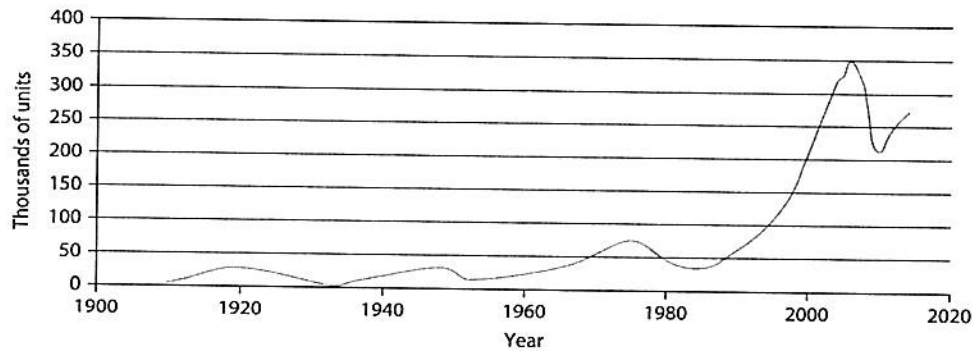
Rebirth, 1981–2008

In 1981, Harley's senior managers led a leveraged buyout of the company. Despite a perilous financial condition, the management team embarked upon rebuilding production methods and working practices. Managers visited Japanese automobile plants and introduced their own version of Toyota's just-in-time (JIT) system called "MAN" (materials-as-needed). Harley's manufacturing plants adopted collaborative processes of quality management.

The 1986 initial public offering of Harley-Davidson's shares fueled investment in new models, plants, and dealerships. Harley's share of the market for heavyweight motorcycles (over 500cc) grew steadily. During the 1990s, Harley's biggest challenge was satisfying the surging demand for its products. In 1996, Harley announced its Plan 2003 to dramatically increase production capacity in the period preceding its 100th anniversary in 2003. In 2004, Harley sold more than 300,000 motorcycles, a tenfold increase on 1983. From 1984 to 2008, Harley's output and revenue had grown in every single year (Figure 1).

Downturn and Readjustment, 2008–2014

The financial crisis of 2008 put an abrupt end to growth. After decades of customer waiting lists and a shortage of production capacity, Harley faced plummeting sales, excess inventory, and problems of bad debts as customers defaulted on their loan repayments. In the shrinking motorcycle markets of North America and Europe, Harley—with the highest average retail price of any major manufacturer—suffered disproportionately. Amidst the credit crunch, Harley-Davidson Financial Services (HDFS), which supplied credit, insurance, and extended warranties to Harley dealers and customers, was unable to securitize its customer loans and was forced to retain them on its own books.

FIGURE 1 Annual shipments of motorcycles by Harley-Davidson

Sources: Harley Davidson annual reports and Harley-Davidson archives.

When Keith Wandell took over as Harley's CEO in May 2009, his priorities were to restore funding for Harley's consumer lending, align production and employment with lower demand, and refocus on the core Harley-Davidson brand—which involved closing Buell Motorcycles³ and selling Italian subsidiary MV Augusta.⁴ In 2009, Harley posted a net loss for the year—its first as a public company. (Appendix Table A1 provides details of Harley-Davidson's financial performance.)

During 2010–2014, Wandell established “a bold, clear strategic direction that would maximize our opportunities going forward and restore the company as a strong business that could consistently grow over the long haul.”⁵ The resulting transformation of Harley included:

- Rethinking and restructuring of manufacturing operations including reducing capacity and increasing flexibility to allow a wider range of models to be produced and to match production to seasonal fluctuations in demand—what Harley called its “surge production system.”
- Expanding international sales. The primary focus for Harley's overseas sales had been Europe—the world's biggest market for heavyweight motorcycles. With Europe mired in recession, emphasis shifted to building distribution and growing sales in the emerging markets of Asia and Latin America. In 2011, Harley opened an Asia-Pacific regional headquarters in Singapore, and an assembly plant in India.⁶
- Expanding the customer base. To reestablish growth in North America, Harley needed to broaden its customer base from its core demographic of white males of 45 years or more. Targeted groups included: women riders, “Harlistas” (Latino riders), “Iron Elite” (African-American riders), “Harley's Heroes” (military and veteran riders), and, most of all, younger riders through new models. The result was a major investment in new product development. During 2013, Harley launched its “Project Rushmore” motorcycles: “The first to come through our new, world-class product development pipeline and introduce major innovation and design improvements. They were developed with

a level of consumer input that brought the voice of the customer to product design in an unparalleled way for us.”⁷ They were followed by the “Street” models—lighter, sports motorcycles featuring new, liquid-cooled 500cc and 750cc engines.

The Heavyweight Motorcycle Market

Until the financial crisis of 2008–2009, the heavyweight segment had been the most rapidly growing part of the world motorcycle market, with the US accounting for a major portion of this growth. Worldwide sales of heavyweight motorcycles trebled between 1990 and 2008. However, during 2008–2010, sales dropped sharply in North America and Europe and the subsequent recovery has been slow.

In North America, Harley was the leader in heavyweight bikes, with over half the market (Table 1). Overseas, Harley had been unable to replicate this market dominance, despite strong sales in a few markets. Harley achieved the remarkable feat of becoming heavyweight market leader in Japan. It held similar leadership in Australia and Brazil. The European market was more fragmented, with Harley one among a leading group that included Honda, BMW, Suzuki, Yamaha, Kawasaki, and Triumph, each with market shares in heavyweight motorcycles of between 8 and 15%.

The heavyweight motorcycle market comprised three segments:

- *Cruiser motorcycles*: These were “big, noisy, low riding, unapologetically macho cycles,”⁸ typically with V-twin, large displacement engines and an

TABLE 1 Retail sales (registrations) of heavyweight motorcycles (601+ cc), 2005–2014 (thousands of units)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
North America										
Total market	554	579	555	477	304	260	271 ^a	299 ^a	306 ^a	316 ^a
Harley-Davidson	265	282	267	235	174	154	152 ^a	161 ^a	168 ^a	167 ^a
Market share (%)	47.8	48.6	48.7	49.3	53.2	54.9	55.7	53.8	54.9	52.8
Europe										
Total market	351	377	372	384	314	301	293	300	282	320
Harley-Davidson ^b	30	34	42	45	40	41	44	36	36	39
Market share (%)	8.5	9.1	11.3	11.7	12.0	12.7	13.7	12.1	12.8	12.0
Asia-Pacific										
Harley-Davidson	11	13	23	25	23	21	21 ^c	25 ^c	27 ^c	30 ^c
Latin America										
Harley Davidson	n.a.	n.a.	3	8	6	6	7	9	11	12

Notes:

^aUS only.

^bIncludes Middle East and Africa for 2005–2011.

^cIn each year, sales in Japan were between 10,000 and 11,000.

n.a. = not available.

Source: Harley-Davidson 10-K reports.

upright riding position. Their design reflected the dominance of styling over either comfort or speed. For the urban males (and some females) in congested cities such as Los Angeles, New York, Paris, and Tokyo, the cruiser motorcycle, while a practical mode of transportation, was primarily a statement of style. The cruiser segment was practically created by Harley and represented over two-thirds of the heavyweight market in the US. Most of Harley's competitors in this segment had imitated the main features of the traditional Harley design.

- *Touring motorcycles*: These included cruisers especially equipped for longer-distance riding and bikes especially designed for comfort over long distances (including the Honda Goldwing and the bigger BMWs). These tourers featured luxuries such as audio systems, two-way intercoms, and heaters. While Harley led this segment on the basis of style and image, Honda and BMW had engineered their motorcycles for greater smoothness and comfort over long distances through the use of multi-cylinder, shaft-drive engines and advanced suspension systems.
- *Performance motorcycles*: These were based on racing bikes, with high-technology, high-revving engines offering speed, acceleration, race-track styling, and minimal concessions to rider comfort. The segment was the most important in the European and Asia-Pacific markets, representing 62 and 65% of total heavyweight bike sales respectively. The segment was dominated by Japanese motorcycle companies, with a strong representation of European specialists, such as Ducati and Triumph. Harley had competed in this segment during 1993–2010 through Buell Motorcycles.

Unlike its Japanese competitors, Harley was highly market focused: its Harley's models were concentrated on the "super-heavyweight" segment (over 850cc) and within this on cruiser and touring motorcycles.

Harley-Davidson in 2015

The Brand

Harley-Davidson's image and the loyalty the company engendered among its customers were seen as its greatest assets. The famed spread eagle signified not just the brand of one of the world's oldest motorcycle companies but also an entire lifestyle with which it was associated. Harley has been described as "the ultimate biker status symbol ... a quasi religion, an institution, a way of life."⁹ Harley had a unique relationship with American culture. The values that Harley represented—individuality, freedom, and adventure—could be traced back to the cowboy and frontiersman of yesteryear, and before that to the quest that brought people to America in the first place. As the sole surviving indigenous motorcycle company, Harley-Davidson represented a once-great tradition of American engineering and manufacturing.

The Harley brand was central not just to the company's marketing but also to its strategy as a whole. The central thrust of the strategy was reinforcing and extending the relationship between the company and its consumers. Harley-Davidson had long

recognized that it was not selling motorcycles: it was selling the Harley Experience, which formed the central theme in almost all its external communications:

A chill sweeps through your body, created by a spontaneous outburst of pure, unadulterated joy. You are surrounded by people from all walks of life and every corner of the globe. They are complete strangers, but you know them like your own family. They were drawn to this place by the same passion—the same dream. And they came here on the same machine. This is one place you can truly be yourself. Because you don't just fit in. You belong.¹⁰

Customers and Customer Relations

If the appeal of the Harley motorcycle was the image it conveyed and the lifestyle it represented, the company's challenge was to ensure that the experience matched the image. Harley's involvement in its consumers' riding experience was through the Harley Owners' Group (HOG), which organized social and charity events. Employees, from the CEO down, were encouraged to take an active role in attending HOG shows, rallies, and rides. "The feeling of being out there on a Harley-Davidson motorcycle links us like no other experience can. It's made HOG like no other organization in the world ... more family reunion than organized meeting."¹¹ Customer loyalty led to their continuing reinvesting in Harley products: Harley-branded accessories and apparel, customizing their bikes, and eventually trading them in for a new (typically more expensive) model. About half of bike sales were to repeat customers.

Financial success involved Harley's repositioning from blue-collar youngsters to middle-aged and upper-income buyers, many of whom had never ridden a motorcycle before. Harley's core demographic was Caucasian males aged 35 and over. The average age of Harley's customers was believed to be 47.¹² In his final letter to shareholders, retiring CEO Keith Wandell reported success in expanding Harley's customer base:

For the third straight year, Harley-Davidson grew U.S. retail sales to outreach customers, which includes young adults, women, African Americans and Hispanics, at more than twice the rate of the growth in sales to core customers. International retail sales of new Harley-Davidson motorcycles grew more than 5 percent and accounted for more than 36 percent of total retail Harley-Davidson motorcycle sales, with dealers in the Asia Pacific, EMEA and Latin America regions posting their highest new retail motorcycle sales on record for each region.¹³

The Products

Broadening Harley's market appeal had major implications for product policy and design. Ever since its disastrous foray into small bikes during the AMF years, Harley had recognized that its competitive advantage lay with super-heavyweight bikes. Here it stuck resolutely to the classic styling that had characterized Harleys since the company's early years. At the heart of the Harley motorcycle was the air-cooled V-twin engine that had been Harley's distinctive feature since 1909. Harley's frames, handlebars, fuel tanks, and seats also reflected traditional designs.

Harley's commitment to traditional design features may be seen as making a virtue out of necessity. Its smaller corporate size and inability to share R & D across cars

and bikes (unlike Honda and BMW) limited its ability to invest in technology and new products. As a result, Harley lagged far behind its competitors in the application of automotive technologies: not only did its motorcycles look old-style, much of their technology was old-style. Since the Evolution engine launched in 1984, Harley has introduced just four entirely new engines.

Yet, even in its 2015 models, Harley's commitment to tradition was clear. Long after other manufacturers had moved to multiple valves per cylinder, overhead camshafts, liquid cooling, and electronic ignition, most Harley bikes featured air-cooled push-rod engines with two valves per cylinder. In suspension systems, braking systems, and transmissions, Harley was also a laggard.

Nevertheless, Harley was engaged in constant upgrading—principally incremental refinements to its engines, frames, and gearboxes—aimed at improving power delivery and reliability, increasing braking power, and reducing vibration. Harley automotive technology alliance partners included Porsche, Ford, and Gemini Racing.

Although technological innovation was limited, Harley was very active in new product development. By 2015, Harley offered 38 different models. Its Product Development Center and Prototyping Lab were among the most important units within the company. Most of Harley's product development efforts were limited to style changes, new paint designs, and engineering improvements; however, after 2000, Harley accelerated technological development. Milestones included the V-Rod model introduced in October 2001, which featured innovative styling and an all-new liquid-cooled engine; the Twin Cam 96 engine in 2006, which featured electronic ignition and a six-speed gearbox; the Street models in 2015; and Harley's prototype all-electric motorcycle. Among the 218 US patents awarded to Harley during 2000–2014, a large proportion related to the design of peripheral items: saddlebag mounting systems, footpegs, seats, backrests, electrical assemblies, and motorcycle music systems. Over the same period Honda was awarded 10,982 US patents, Kawasaki 2002, and Suzuki 625.

Central to Harley's product strategy was the belief that every Harley rider should own a unique, personalized motorcycle—hence the offer of a wide range of pre-sale and post-sale customization opportunities. New bikes offered multiple options for seats, bars, pegs, controls, and paint jobs, with over 7000 accessories, and special services such as “Chrome Consulting.”

TABLE 2 Harley-Davidson shipments of motorcycles, 2003–2014

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
US ^a	237.7	260.6	266.5	273.2	241.5	206.3	144.4	131.6	152.2	160.5	167.0	174.0
International ^b	53.5	56.7	62.5	76.0	89.1	97.2	78.5	78.8	80.9	87.1	93.4	96.7
Product mix^b												
Sportster ^c	19.7	22.0	21.3	18.5	21.8	20.0	21.4	19.5	21.3	20.5	19.3	21.0
Custom	52.0	48.6	45.2	46.2	43.7	46.4	40.9	41.4	39.2	39.1	39.5	33.8
Touring	28.4	29.4	33.5	35.4	34.5	33.6	37.7	39.0	39.5	40.4	41.2	45.2
Buell	10.0	9.9	11.2	12.5	11.5	13.1	9.5	2.6	0.2	—	—	—
Company total^a	301.2	327.2	340.2	361.6	342.1	316.4	232.4	213.0	233.2	247.6	260.5	270.7

Note:

^aThousands of units.

^bPercentage of total shipments.

^cIncludes sales of Street motorcycles for 2014.

Source: Harley-Davidson 10-K reports.

Reconciling product differentiation with scale economies was a continuing challenge for Harley. The solution was to offer a wide range of customization options while standardizing key components. Thus, Harley's broad model range involved "permutations of four": four engine types, four basic frames, four styles of gas tank, and so on.

The Harley product line also covered a wide price range. The Street 500 model was priced as an entry-level bike, beginning at \$6799, less than one-fifth of the price of the CVO Limited, at \$39,349. Table 2 shows Harley's motorcycle output by product type.

Distribution

Upgrading Harley's distribution network was central to its resurgence during the 1980s and 1990s. At the time of the buyout, many of Harley's 620 US dealerships were operated by enthusiasts, with erratic opening hours, a poor stock of bikes and spares, and indifferent customer service. If Harley was in the business of selling a lifestyle and an experience, then dealers played a pivotal role in delivering that experience. Moreover, if Harley's target market had shifted toward mature, upper-income individuals, Harley needed to provide a retail experience commensurate with the expectations of this group.

Harley's dealer development program increased support for dealers while imposing higher standards of pre- and after-sales service, and requiring better dealer facilities. Dealers were obliged to carry a full line of Harley replacement parts and accessories and to offer an expanding range of services: in addition to traditional services such as service and repair and financing, dealers offered test ride facilities, rider instruction classes, motorcycle rental, consulting services for customizing bikes through dealer-based design centers and Chrome Consultants, and insurance services. Harley-Davidson Authorized Tours offered vacation packages with bikes supplied by Harley dealers. Over 90% of Harley dealerships in the US were exclusive: most other motorcycle manufacturers sold through multi-brand dealerships.

Dealer relations were a continuing strategic priority for Harley. Its Retail Environments Group established a meticulous set of performance standards and guidelines for dealers that covered every aspect of managing the showroom and interacting with actual and potential customers. Harley-Davidson University was established to "enhance dealer competencies in every area, from customer satisfaction to inventory management, service proficiency, and front-line sales."¹⁴

Expanding international sales required Harley to extend its dealer network into countries where it had little or no distribution presence. As Table 3 shows, emerging

TABLE 3 Harley-Davidson's dealership network, 2008–2014

	US		Canada		EMEA		Asia-Pacific		Latin America	
	2008	2014	2008	2014	2008	2014	2008	2014	2008	2014
Full-service dealerships	686	669	71	69	383	369	201	273	32	55

Note:

In addition, there were 152 non-traditional dealerships in 2014: US 96, Canada 4, EMEA 11, Asia-Pacific 12, and Latin America 29.

Source: Harley Davidson 10-K reports.

TABLE 4 Harley-Davidson's non-motorcycle sales, 2005–2014 (\$million)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Parts and accessories	815.7	862.3	868.3	858.7	767.2	749.2	816.5	836.7	873.1	875.0
General merchandise	247.9	277.5	305.4	313.8	282.2	259.1	274.1	282.5	295.9	284.8
Financial services	331.6	384.9	416.2	377.0	494.7	682.7	649.4	650.1	641.6	660.8

Source: Harley Davidson 10-K reports.

markets accounted for the whole of the increase in Harley's dealerships between 2008 and 2014.

Other Products and Services

Sales of parts, accessories, "general merchandise" (clothing and collectibles), and financial services represented 28% of Harley's total revenue in 2014 (Table 4)—much higher than for other motorcycle companies. Clothing sales included not just traditional riding apparel but also a wide range of men's, women's, and children's leisure apparel.

Most of the "general merchandising" business represented licensing of the Harley-Davidson name and trademarks to third-party manufacturers of clothing, giftware, jewelry, toys, and other products. Most of these were sold through channels other than the Harley dealership network. To expand sales of licensed products, Harley opened "non-traditional" dealerships: retail outlets selling clothing, accessories, and giftware but not motorcycles.

Manufacturing

As already noted, Harley-Davidson's development during the 1980s and 1990s focused heavily on upgrading its manufacturing operations: capacity expansion permitted investment in new plants and equipment and the introduction of more advanced process technologies. Particular emphasis was placed on developing manufacturing capabilities through total quality management, JIT scheduling, CAD/CAM, and the devolution of responsibility and decision making to the shop floor.

Despite the constant development of its manufacturing facilities and operational capabilities, Harley's low production volume relative to Honda and the other Japanese manufacturers imposed significant cost disadvantages, especially in the purchase of components. Despite this lack of bargaining muscle, Harley sought close, collaborative relations with key suppliers. Its Supplier Advisory Council (SAC) served "not only to improve purchasing efficiency, but also to provide a forum to share information, ideas, and strategy."¹⁵

Harley's capacity for efficiency was also limited by its dispersed manufacturing operations: engine manufacture in Milwaukee, Wisconsin and assembly in York, Pennsylvania and Kansas City, Missouri. During 2009–2014, Harley reorganized its manufacturing plants and manufacturing systems. A program of plant consolidation involved combining the two Milwaukee-area powertrain plants into a single facility and merging the separate paint and frame operations at York, Pennsylvania.

New agreements negotiated with unions allowed for more flexible employment arrangements and working practices, which supported the introduction of a new enterprise resource planning (ERP) system at the York plant. Combined with Harley's "surge production," the new system meant customer demand would drive manufacturing, every production line would have the flexibility to build every model, and inventories could be reduced.

Human Resource Management

Central to Harley-Davidson's remarkable growth between 1981 and 2007 was the creation of a new relationship between management and employees that was forged following the buyout from AMF. The new approach to human resource management was built on participation, self-management, open communication, and team-based organization. Team-based organization extended from eight- to 15-member work groups at plant level right up to senior management where three functional teams—the Create Demand Circle (CDC), the Produce Product Circle, and the Provide Support—were coordinated by the Strategic Leadership Council.¹⁶

Despite Harley's commitment to employee participation and development, the production cutbacks and cost-cutting pressures during 2009–2012 created tensions between the company and its employees. These were resolved by the 2012 labor agreement, which created a new framework for workplace flexibility.¹⁷

Competition

Despite Harley's insistence that it was supplying a unique Harley experience rather than competing with other motorcycle manufacturers, the more it took market share from other manufacturers and expanded its product range and geographical scope, the more it came into direct competition with other producers. The clearest indication of direct competition was imitation: Honda, Suzuki, Yamaha, and Kawasaki had long been offering V-twin cruisers styled closely along the lines of the classic Harleys, but at lower prices and with more advanced technologies (Table 5). In competing against Harley, the Japanese manufacturers' key advantage was the scale economies that derived from vastly greater volume. However, despite their price premium, Harley-Davidson motorcycles benefitted from a lower rate of depreciation than other brands.

Almost all of Harley's competitors were, compared to Harley, highly diversified. Honda, BMW, and Suzuki were important producers of automobiles, and more than one-third of Yamaha's turnover came from boats and snowmobiles. These companies could share technologies, engineering capabilities, distribution, and brand awareness across their different vehicle divisions. Moreover, sheer size conferred purchasing power.

Imitators of Harley's retro-styled, V-twin cruisers were not only the Japanese motorcycle companies but also domestic competitors—including new entrants Excelsior, Polaris (Victory), and a resuscitated Indian. Their heavyweight cruisers typically sold at prices exceeding those of Harley.

Appendix Table A2 compares the financial performance of leading motorcycle companies.

TABLE 5 Recommended retail prices for V-twin, cruiser motorcycles, 2015

Model	Specifications	Price (\$)
Harley-Davidson		
Sportster 883 Low	V-twin, air-cooled, 883cc	8,249
VRSC V-Rod Muscle	V-twin, liquid-cooled, OHC, 1247cc	16,649
Fat Boy	V-twin, air-cooled, 1690cc	17,699
Heritage Softail Classic	V-twin, air-cooled, 1690cc	18,349
Honda		
Shadow 750 Aero	V-twin, liquid-cooled, OHC, 745cc	7,499
Fury	V-twin, liquid-cooled, OHC, 1312cc	9,999
Interstate ABS	V-twin, liquid-cooled, OHC, 1312cc	10,999
Suzuki		
C50	V-twin, liquid-cooled, OHC, 805cc	8,199
C90T	V-twin, liquid-cooled, OHC, 1462cc	12,899
Boulevard C90 B.O.S.S.	V-twin, liquid-cooled, 1462cc	12,389
Kawasaki		
Vulcan 900 Classic	V-twin, liquid-cooled, 8-valve, OHC, 903cc	7,499
Vulcan 900 Custom		8,499
Yamaha		
V-Star Custom	V-twin, OHC, 4-valve, air-cooled, 649cc	6,990
Stryker	V-twin, OHC, 8-valve, liquid-cooled, 1304cc	11,690
Polaris		
Victory Vegas 8-Ball	V-twin, 8-valve, air-cooled, 1731cc	14,999
Victory Hammer 8-Ball		17,899

Note:

OHC = overhead camshaft.

Source: Websites of different motorcycle manufacturers.

Meeting the Challenges of Tomorrow

Harley's first-half results for 2015 reinforced fears over the sustainability of Harley's top-line growth. Profits were 8% lower than in the year-ago period, sales revenue was 6% lower, and unit sales were down by 1.4%. Wandell's strategy had been strongly orientated around expanding sales to "non-core" customer segments. Among these were younger riders in the US and potential customers in overseas markets.

The need to attract younger riders was driven by unfavorable US demographic trends—the aging of the baby boomers and the smaller number of white males entering the 40–55 age band. However, would the Harley Experience have the same appeal for Generation X and Y as it did for the baby-boomers? As the *New York Times* noted, "BMW, Honda and Yamaha are attracting younger customers who seem less interested in cruising on what their old man rides."¹⁸

International markets also presented a major challenge: should Harley adapt to the different requirements of these markets or should it remain faithful to the traditional Harley image? "The US and Harley are tied together," observed Britain's *Bike* magazine, "the guy who's into Harleys here is also the guy who owns cowboy boots. You get a Harley and you're buying into the US mystique."¹⁹

Harley claimed that its new Street 500 and Street 750 models had met with an enthusiastic response both in the US and in India (the two countries where this model was manufactured). However, Harley's previous incursions into smaller motorcycles—including Buell—had not been successful.

A Milwaukee blogger summarized Harley's dilemma:

So what does Harley do? One tack would be to stay focused on what it does best: big bikes. While that strategy may make sense on some fronts (focus on what you know, stay loyal to the brand identity, etc.), that approach will mean greatly reduced growth prospects and could doom it if the current consumer spending environment holds out long term. And meanwhile its core audience just gets older.

Or it could do what people have been saying what it should do for years: Make smaller, more affordable bikes. That's harder than it sounds, as it would force Harley to compete against the Japanese manufacturers on their own turf. But if the market is moving away from Harley, does it have a choice?²⁰

Appendix: Financial Data

TABLE A1 Selected Items from Harley-Davidson financial statements, 2005–2014 (\$million)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Income statement items										
Net sales	5,342	5,801	5,727	5,594	4,781	4,859	5,311	5,581	5,900	6,229
R & D	179	178	186	164	143	136	145	137	152	138
Selling, administrative, and engineering expense	762	846	901	985	979	1,020	1,061	1,111	1,127	1,160
Operating income, of which:	1,470	1,603	1,426	1,029	197	559	829	1,000	1,154	1,281
–Financial services	192	211	212	83	(117)	181	268	259	283	278
Interest income/(expense)	23	27	22	9	(22)	(90)	(45)	(46)	(45)	(4)
Income before taxes	1,488	1,624	1,448	1,034	178	390	792	961	1,114	1,283
Income taxes	528	581	514	379	108	130	244	338	380	439
Net income	960	1,043	934	655	(55)	146	599	624	734	845
Balance sheet items										
Cash	141	238	403	594	1,630	1,021	1,526	1,327	1,067	907
Finance receivables	1,943	2,101	1,575	1,378	1,436	1,080	1,168	1,344	1,774	1,917
Accounts receivable, net	122	143	181	296	269	262	219	255	261	248
Inventories	221	288	350	401	323	326	418	428	425	449
Total current assets	3,145	3,551	3,467	5,378	4,341	4,066	4,542	4,216	3,989	3,948
Property, plant, and equipment, net	1,012	1,024	1,061	1,094	906	815	809	819	842	883
Total assets	5,255	5,532	5,657	7,829	9,155	9,430	9,674	9,513	9,405	9,528
Current portion of long-term debt	205	832	398	0	1,332	0	399	682	1,176	1,011
Accounts payable	271	763	300	324	162	225	255	248	240	197
Total current liabilities	873	1,596	1,905	2,604	2,268	2,013	2,698	0	2,510	2,389
Long-term debt	1,000	870	980	2,176	4,144	2,516	2,396	2,936	3,417	3,762
Post-retirement healthcare liability	61	201	193	274	264	254	268	258	216	203
Stockholders' equity	3,084	2,757	2,375	2,116	2,108	2,207	2,420	2,558	3,009	2,909
Cash flow items										
Operating activities	961	762	798	2,685	609	1,163	885	801	977	1,147
Capital expenditures	(2,198)	(2,220)	(2,242)	(2,232)	(116)	(170)	(189)	(189)	(208)	(232)
Total investing activities	(177)	(2,35)	(3,91)	(2,393)	(863)	145	(63)	(261)	(569)	(745)
Financing activities	1,272	2,637	1,038	1,293	1,381	(1,856)	(309)	(990)	(393)	(536)
Net increase in cash	2,134	97	164	191	1,134	(542)	(505)	(459)	(2)	(160)

TABLE A2 Comparative financial data for Honda, Yamaha, and Harley-Davidson

	Honda Motor Co. ^a		Yamaha Motor Co. ^b		Harley-Davidson	
	2013	2014	2013	2014	2013	2014
Revenue (\$bn)	117.8	115.0	14.9	14.1	5.9	6.2
Operating income (\$bn)	7.5	5.9	0.6	0.8	1.2	1.3
Net income after tax (\$bn)	5.7	4.8	0.5	0.6	0.7	0.8
Gross margin (%)	26	25	35	25	39	40
Operating margin (%)	6.3	5.2	3.9	5.7	19.6	20.6
Net margin (%)	4.8	4.2	4.0	4.5	12.4	13.6
Operating income/total assets (%)	4.8	3.9	1.7	3.4	12.3	13.4
Return on equity (%)	9.4	7.9	11.8	14.3	24.4	29.0
Inventory turnover	8.5	8.5	5.2	4.8	13.9	13.9
Debt/equity ratio	0.52	0.53	0.31	0.36	1.14	1.29
Capital expenditure (\$bn)	6.4	6.0	5.1	5.5	0.2	0.2
—of which motorcycles (\$bn)	0.6	0.6	3.0	3.8	0.2	0.2
R & D expenditure (\$bn)	6.5	6.1	0.8	0.8	0.2	0.1
Advertising expenditure (\$bn)	2.7	2.8	1.0	0.9	0.1	0.1
Motorcycles shipped (thousands of units)	10,343	10,742	6,010	5,800	213	233.2

Notes:

^aHonda's data relates to the whole company (motorcycles account for about 14% of Honda's total sales). Financial year 2013 covers 12 months to March 31, 2014; financial year 2014 covers 12 months to March 31, 2015.

^bYamaha's data relates to the whole company (motorcycles account for about 65% of Yamaha's total sales).

Sources: Company annual reports.

Notes

1. "The Company," http://www.harley-davidson.com/content/h-d/en_GB/company/becoming-a-dealer/the-company.html, accessed July 20, 2015.
2. "Harley-Davidson: Running Out of Road?" <http://www.forbes.com/newsletters/the-berman-value-folio/2015/05/01/harley-davidson-running-out-of-road/>, accessed July 20, 2015.
3. Buell Motor Company, founded by Harley engineer Erik Buell, built performance motorcycles using Harley engines and other components, and targeted younger riders. The Buell range included a 490cc single-cylinder bike with a price tag of \$4,595—Harley's cheapest motorcycle. However, Buell's sales both in the US and overseas had been disappointing.
4. Harley acquired MV Agusta, an Italian manufacturer of premium, high-performance motorcycles in July 2008. On August 6, 2010, Harley sold it back to its previous owner for €3 (\$3.90).
5. "Letter to Shareholders," Harley-Davidson, Inc. annual report for 2009.
6. The Indian plant was its second overseas assembly plant; the first was established in Brazil in 1999.
7. K. Wandell, "Chairman's Annual Letter," Harley-Davidson 2013 annual report.
8. G. Strauss, "Born to be Bikers," *USA Today* (November 5, 1997).
9. M. Ballon, "Born to be Wild," *Inc.* (November, 1997): 42.
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11. "Welcome Letter," Blackstone Valley HOG Chapter, <http://www.blackstonevalleyhog.com/HTML/Welcome.php>, accessed July 20, 2015.
12. "Analysis: As Boomers Age, Harley Hunts for Younger Riders," *Reuters*, June 21, 2013, <http://uk.reuters.com/article/2013/06/21/us-harleydavidson-boomers-analysis-idUSBRE95K0GU20130621>, accessed July 20, 2015.
13. "Letter to Shareholders," Harley-Davidson 2014 annual review.
14. Harley-Davidson, Inc., "Knowledge is Horsepower," annual report (2003).
15. K. R. Fitzgerald, "Harley's Supplier Council Helps Deliver Full Value," *Purchasing* (September 5, 1996).