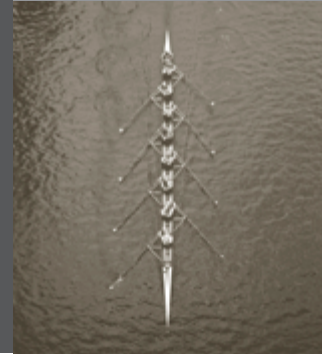


case  
9Harley-Davidson, Inc.,  
January 2007

*You've shown us how to be the best. You've been leaders in new technology. You've stuck by the basic American values of hard work and fair play . . . Most of all, you've worked smarter, you've worked better, and you've worked together . . . as you've shown again, America is someplace special. We're on the road to unprecedented prosperity . . . and we'll get there on a Harley.*

PRESIDENT RONALD REAGAN, HARLEY-DAVIDSON PLANT, YORK,  
PENNSYLVANIA, MAY 6, 1987

*The recovery of this company since the 1980s has been truly remarkable. When you were down in the dumps, people were saying American industry was finished, that we couldn't compete in the global economy, that the next century would belong to other countries and other places. Today, you're not just surviving – you're flourishing, with record sales and earnings; and one of the best-managed companies in America.*

PRESIDENT BILL CLINTON, HARLEY-DAVIDSON PLANT, YORK,  
PENNSYLVANIA, NOVEMBER 10, 1999

*I want to thank the folks here at the Harley plant for their wonderful hospitality. I've been impressed by Harley-Davidsons. It's one of America's finest products. And today I add to my impressions about the product the impressions of the workforce . . . I'm impressed by the esprit de corps, I'm impressed by the fact that these people really enjoy what they're doing, I'm impressed by the fact that they're impressed by the product they make.*

PRESIDENT GEORGE W. BUSH, HARLEY-DAVIDSON PLANT, YORK,  
PENNSYLVANIA, AUGUST 16, 2006

At the beginning of 2007, Harley-Davidson could claim to be America's most successful manufacturing company. Unlike America's struggling automobile producers 300 miles away in Detroit, Harley had beaten back Japanese competitors and established itself as market leader in heavyweight motorcycles and the world's most profitable motorcycle company. On January 18, CEO James Ziemer announced record annual sales and profits for the company for the 20th consecutive year. The 103-year-old company had never been in such robust health either financially or operationally.

Yet, Ziemer also knew that the next few years would be the most challenging of his 37-year career with Harley-Davidson. Wall Street's expectations of Harley-Davidson's profit performance had been fueled by past performance and by the company's own ambitious targets: Ziemer had committed to earnings-per-share growth of between 11 and 17% during each of the next three years. Ultimately, profit growth depended on Harley's ability to keep expanding the sales of its high-priced, heavyweight motorcycles. For 20 years, most of Harley's sales growth had been accounted for by expanding domestic sales. Yet the health of domestic demand was far from assured. Combined federal and trade deficits, record levels of consumer debt, and falling house prices posed a threat to any company selling leisure products priced between \$6,600 and \$22,000. Harley's potential for growing market share also seemed limited – for the past eight years, Harley's share of the US heavyweight market had hit a ceiling at just under 50%. Indeed, Harley's own market might be vulnerable to competition. 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 sports models produced by European and Japanese manufacturers. Such concerns were fueled by demographic trends. Harley's core market was the baby-boomer generation – and this cohort was moving more towards retirement homes than outdoor sports.

**TABLE 9.1** Annual shipments of motorcycles by Harley-Davidson (selected years)

Year	Production	Year	Production
1901	3	1994	95,811
1903	150	1995	105,104
1913	12,904	1996	118,771
1920	28,189	1997	132,285
1933	3,700	1998	150,818
1936	9,812	1999	177,187
1948	31,163	2000	204,592
1953	14,050	2001	234,500
1966	36,310	2002	263,700
1975	75,403	2003	291,147
1981	41,586	2004	317,289
1986	36,700	2005	329,017
1990	62,500	2006	349,196
1992	76,500		

SOURCE: WWW.HARLEY-DAVIDSON.COM

## **The History of Harley-Davidson**

### ***1903–1981: From Birth to Maturity***

Harley-Davidson, Inc. was founded in 1903 by William Harley and brothers William Davidson, Arthur Davidson, and Walter Davidson. Harley's 1903 model was made in the Davidson family shed and had a three-horsepower engine. In 1909 Harley introduced its first two-cylinder, V-twin engine, featuring the deep, rumbling sound for which Harley motorcycles are renowned. In 1953, the closure of Indian meant that Harley-Davidson was the sole survivor of the 150 US motorcycle producers that had existed in 1910.

The post-war era saw new challenges for Harley-Davidson. Growing affluence and the rise of youth culture created a growing demand for motorcycles. However, this was satisfied primarily by imports: first the British (by 1959, BSA, Triumph, and Norton took 49% of the US market), then the Japanese. While Harley initially benefitted from the Japanese-led expansion of motorcycling among Americans, soon Harley was facing direct competition. In 1969 Honda introduced its four-cylinder CB750, a huge technical advance on anything produced by Harley or the British. In the same year, Harley-Davidson was acquired by AMF, which proceeded to expand production capacity to 75,000 units a year – with disastrous consequences for product quality. By the end of the 1970s, Honda had replaced Harley as market leader in heavyweight motorcycles in the US.

### ***1981–2003: Rebirth***

In 1981, Harley's senior managers, led by Vaughn Beals, organized a leveraged buyout of AMF's Harley-Davidson subsidiary. Harley emerged as an independent, privately owned company, heavily laden with debt. The buyout coincided with a severe recession and soaring interest rates. Harley's 1982 unit sales were down by more than a third from 1979. During 1981 and 1982, Harley-Davidson lost a total of \$60 million. Struggling for survival, the new management dismissed 30% of office staff and drastically reduced hourly workers too.

At the same time, the management team also devoted itself to rebuilding production methods and working practices in order to cut costs and improve quality. Managers visited several Japanese automobile plants and carefully studied Toyota's just-in-time (JIT) system. Less than four months after the buyout, Harley management began a pilot JIT inventory and production-scheduling program called "MAN" (Materials As Needed) in its Milwaukee engine plant. The objective was to reduce inventories and costs and improve quality control. Within a year, all Harley's manufacturing operations were being converted to JIT: components and sub-assemblies were "pulled" through the production system in response to final demand.

The revolution in production methods and new spirit of cooperation between workers and management – plus help from the US government in the form of a temporary 49% tariff on imports of Japanese heavyweight motorcycles – soon fed through into both the top line and bottom line of Harley's income statement. To fuel its continuing development, Harley-Davidson went public in 1986. Between 1986 and 1990, Harley's share of the heavyweight market expanded steadily from about 30% to over 60%, with demand outstripping production. During this time,

management improved the quality and reliability of its product, and began to explore growth opportunities in retail clothing and international sales.

The 1990s saw year-on-year uninterrupted growth in the heavyweight motorcycle market and a continued increase in Harley's market share. The company's biggest challenge continued to be balancing production capacity with surging demand for its products. To overcome this constraint, in 1996, the company announced the ambitious Plan 2003. Plan 2003 was a vision to dramatically increase production capacity over the eight years preceding the company's 100th anniversary. New production plants in Kansas City and York, Pennsylvania, the launching of several new models, and international expansion resulted in sales approaching 300,000 in 2003 – an eightfold increase on 1983.

## The Heavyweight Motorcycle Market

The heavyweight segment (over 650 cc) was the most rapidly growing part of the world motorcycle market between 1990 and 2006, with the US accounting for a major part of this growth. Sales of heavyweight motorcycles in the major markets of the world almost trebled between 1990 and 2006. North America was the largest market for big bikes, representing 56% of the sales in the major world markets.

In North America, Harley consolidated its market leadership, accounting for almost half of big bike sales. Overseas, however, Harley was 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, pushing Honda into second place. In Europe, on the other hand, Harley lagged behind its Japanese competitors and BMW (see tables 9.2 and 9.3).

**TABLE 9.2** Retail sales of heavyweight motorcycles (651+ cc), 1996–2006 (in thousands of units)

	1996	1997	1998	1999	2000	2002	2003	2004	2005	2006
<i>United States (total)</i>	179	205	246	298	363	442	461	494	518	543
Harley-Davidson <sup>a</sup>	87	101	119	146	168	210	228	243	253	268
Market share (%)	48.6	49.3	48.5	49.0	46.3	47.5	49.5	49.2	49.0	49.4
<i>Europe (total)</i>	225	250	270	307	293	332	323	336	333	366
Harley-Davidson	15	16	17	20	22	24	26	25	29	34
Market share (%)	6.8	6.4	6.4	6.5	7.4	7.1	8.1	7.3	8.9	9.2%
<i>Japan/Australia (total)</i>	37	59	69	63	63	64	59	n.a.	n.a.	n.a.
Harley-Davidson <sup>b</sup>	8	10	11	12	13	14	15	10	11	13
Market share (%)	22.4	17.2	15.6	19.6	20.5	21.2	25.8	n.a.	n.a.	n.a.

<sup>a</sup> Excludes Buell.

<sup>b</sup> Years 2004–6 include Japan only.

**TABLE 9.3** Market shares in heavyweight motorcycles (651 cc+), 2003–2005 (%)

	North America			Europe		
	2003	2004	2005	2003	2004	2005
Harley-Davidson	48.1	48.2	47.8	8.1	7.7	8.9
Honda	18.6	18.8	16.6	16.7	15.4	13.0
Kawasaki	7.1	6.9	6.9	10.0	13.7	12.6
Suzuki	10.3	10.5	12.6	15.5	12.6	13.3
Yamaha	9.1	9.3	9.3	16.0	17.3	15.8
BMW	2.8	2.3	3.3	15.3	15.5	17.7
Ducati	–	–	–	6.0	5.1	5.2
Triumph	–	–	–	3.7	4.0	5.0
Other	4.0	4.0	4.5	8.7	8.7	8.5

SOURCE: HARLEY-DAVIDSON ANNUAL REPORT, 2003, 2005.

The heavyweight motorcycle market comprised three segments:

- *Cruiser motorcycles*: These were “big, noisy, low riding, unapologetically macho cycles,”<sup>1</sup> typically with V-twin, large displacement engines and an upright riding position. Their design reflected the dominance of styling over either comfort or speed. For the urban males (and some females) in Los Angeles, New York, Paris, and Tokyo, the cruiser motorcycle was practical transportation in congested metropolises, but was primarily a statement of style. The cruiser segment was practically created by Harley and was preeminent in the US, representing over half of the heavyweight market. Most of Harley’s competitors in this segment had imitated the main features of traditional Harley design.
- *Touring bikes*: These included cruisers specially equipped for longer distance riding and bikes specially 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 models*: These were based on racing bikes, with high-technology, high-revving engines, an emphasis on speed, acceleration, and race-track styling; minimal concessions were provided to rider comfort. The segment was the most important in the European and the Asian/Pacific markets, representing 62% and 66% of total heavyweight bike sales, respectively. The segment was dominated by Japanese motorcycle companies, with a significant representation of European specialists such as Ducati and Triumph. Harley entered the performance segment in 1993 through Buell Motorcycles, which it fully acquired in 1998.

It is worth noting that the conventional segmentation into lightweight, middle-weight, and heavyweight did not clearly define Harley-Davidson’s market. Harley’s

strength lay in just one part of the heavyweight market: the super-heavyweight segment, comprising bikes with cylinder displacement of more than 850 cc.

## Harley-Davidson in 2007

### *The Brand*

The Harley-Davidson image and the loyalty it engendered among its customers were its greatest assets. Harley-Davidson was one of the archetypes of American style. The famed spread eagle signified not just the brand of one of the world's oldest motorcycle companies, but 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."<sup>2</sup> Together with a few other companies – Walt Disney and Levi Strauss – 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 motives that brought people to America in the first place. As the sole surviving American motorcycle company from the pioneering days of the industry, Harley-Davidson represented a tradition of US engineering and manufacturing.

This appeal of 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. Prominent in annual reports of recent years were pictures and prose depicting the Harley Experience:

*A chill sweeps though 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.<sup>3</sup>*

If the appeal of the Harley motorcycle was the image it conveyed and the lifestyle it represented, then the company had to ensure that the experience matched the image. To increase Harley's involvement in its consumers' riding experience it formed the Harley Owners' Group in 1983. Through HOG, the company became involved in organizing social and charity events. Employees, from the CEO down, were encouraged to take an active role in HOG activities. During 2005, senior managers attended over 150 different shows, rallies, and rides. The bond between the company and its customers is captured in Willie G. Davidson's phrase: "We ride with you." HOG provided the organizational link for this sense of community: "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 . . . The atmosphere is more family reunion than organized meeting."<sup>4</sup> The loyalty of Harley owners was reflected in their repurchase and upgrading of Harley products. During 1999–2005, more than one half of all sales were to customers who had owned a Harley previously, while about 20% were first-time motorcycle buyers.

From the 1980s to the 2000s, the demographic and socioeconomic profile of Harley customers had shifted substantially. Traditionally, Harley owners were blue-collar men

in their 20s and 30s. By 2005, the median income of a Harley owner was over \$80,600, up from \$38,400 in 1987. The average age grew to 46, up from 35 in 1987. Also, women accounted for about 10% of sales – up from 2% in 1987.

### ***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 research expenditure 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: its motorcycles not only looked old-style, much of the technology was old-style. When Harley introduced its new Twin Cam 88 engine in 1998, *Motorcycle* magazine reported:

*Honda comes out with an average of two new (or reworked) motors every year. The other Japanese manufacturers are good for about one. Count on Ducati and BMW to do something every few years. That leaves only Moto Guzzi and Harley. So it goes to say that when either of these two old farts gets off the pot, they really raise a stink, so to speak.*

*The Twin Cam 88 is Harley's first new engine since the Evolution Sportster motor of 1986, and their first new Big Twin motor since the original Evolution, released in 1984. Fifteen years between engines is not really that long a span for Harley. The Evo's predecessor, the Shovelhead lasted 19 years (with a revision after five), and the Panhead lasted nearly as long.<sup>5</sup>*

Harley's engines were most representative of its technological backwardness. Long after Honda had moved to multiple valves per cylinder, overhead camshafts, liquid cooling, and electronic ignition, Harley continued to rely on air-cooled push-rod engines. In suspension systems, braking systems, and transmissions too, Harley lagged far behind Honda, Yamaha, and BMW. 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 also accessed automotive technology through alliances with other companies, including Porsche AG, Ford, and Gemini Racing Technologies.

Despite being a technological laggard, Harley was very active in new product development and the launching of new models. By 2006, Harley offered 36 models, of which seven had been added in that year. Harley's product development efforts were assisted by doubling the size of its Product Development Center in 2004 and the creation of a Prototyping Lab. Most of Harley's product development efforts involved style changes, new paint designs, and engineering improvements.

Between 2000 and 2006, Harley accelerated technological progress and new product development. Its V-Rod model introduced in October 2001 featured innovative

styling and an all-new liquid-cooled engine. The Buell range also offered Harley engineers an opportunity to be more innovative. The 2002 Buell Firebolt featured a new engine, an all-aluminum frame, and the “naked” styling pioneered by Ducati, while the 2006 Ulysses was Harley-Davidson’s first ever “adventure sportbike.” In 2006, Harley introduced another new engine, the Twin Cam 96, which featured electronic ignition and was teamed with a new six-speed gearbox.

Central to Harley’s product strategy was the idea that every Harley rider would own a unique, personalized motorcycle. This implied not just offering a wide model range, but providing a wide range of customization opportunities. New bikes allowed multiple options for seats, bars, pegs, controls, and paint jobs, with the potential for augmentation through a range of 7,000 accessories, and special services such as “Chrome Consulting.”

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 on key components. For example, among the 36 different Harley models there were three engine types (Evolution XL, Twin Cam 88, and Revolution), four basic frames, four styles of gas tank, and so on.

The Harley product line also covered a wide price range. The Sportster model was positioned as an entry-level bike and priced at \$6,595, less than one-third of the price of the Ultra Classic Electra Glide, with two-tone paint, at \$21,135 (see table 9.4).

## ***Buell***

Harley’s involvement with Buell was to broaden its customer base – especially overseas. Harley’s market research found that many potential riders were put off by motorcycles being “hard to learn,” with Harley models viewed as “intimidating” or “something an old guy would ride.” Founded by ex-Harley engineer Erik Buell, Buell Motor Company developed bikes that synthesized the comfort and style of a Harley cruiser with the performance attributes of a sports bike. Harley acquired complete ownership of Buell in 1998. Buell bikes used Harley engines and other components, but mounted them on a lighter, stiffer frame. The lighter weight and superior handling and acceleration of Buell models were seen as appealing to younger motorcyclists and also to the European market, where customers put greater emphasis on sporty performance and a cheaper price tag. In the US, the age of the typical Buell customer was seven years younger than that of Harley buyers, and the price was about \$10,000 compared with an average Harley price of \$17,000. Through the Buell Riders Adventure Group (BRAG), Buell attempted to foster the close relations with customers that characterized the Harley-Davidson brand. With the Buell Blast, an entirely new model with a 490 cc single cylinder engine and a price tag of \$4,595, Harley entered the middleweight motorcycle market for the first time since the 1970s. With the Buell Firebolt, Lightning, and Ulysses models, Buell positioned itself in direct competition with Japanese and European producers of high-performance sports bikes. Yet, despite heavy investments in developing and launching new models, there was little overall growth in Buell’s unit sales between 2001 and 2006.

## ***Distribution***

Upgrading Harley’s distribution network was a key aspect of its development strategy during the 1980s and 1990s. Many of Harley’s 620 US dealerships were poorly



**TABLE 9.4** Heavyweight motorcycles: price comparisons, 2007

Manufacturer and model	Engine	Recommended retail price (\$)
<i>Harley-Davidson</i>		
XL 883 Sportster	V-twin, air-cooled, 883 cc	6,595
Fat Boy FLSTF	V-twin, air-cooled, 1,540 cc	17,095
V-Rod VRSCX	V-twin, liquid-cooled, 1,131 cc	19,995
Heritage Softail Classic	V-twin, air-cooled, 1,450 cc	17,820
H-D Ultra Classic Electra Glide	V-twin 1,450 cc, injection (two tone)	21,135
<i>Honda</i>		
Shadow VLX	V-twin, liquid-cooled, OHC 745 cc	5,499
VTX1300C	V-twin, liquid-cooled, OHC 1,312 cc	9,599
VTX1800R	V-twin, liquid-cooled, OHC 1,800 cc	13,399
<i>Suzuki</i>		
Boulevard S50	V-twin, liquid-cooled, OHC, 850 cc	6,499
Boulevard C90	V-twin, air-cooled, OHC, 1,475 cc	10,499
Boulevard M109R	V-twin, liquid-cooled, 1,783 cc	12,599
<i>Kawasaki</i>		
Vulcan 900 Classic	V-twin, 8-valve, OHC	7,349
Vulcan 1600 Mean Streak	V-twin, air-cooled, 1,600 cc	11,039
<i>Yamaha</i>		
V-Star Custom	V-twin, OHC, air-cooled, push-rod, 649 cc	5,799
Road Star	V-twin, OHC air-cooled, push-rod, 1,670 cc	11,399
<i>BMW</i>		
R1200 Sports Tourer	1,170 cc, horizontal twin, air-cooled	14,990
K1200R	1,200 cc, 4-cylinder, liquid-cooled	14,350
<i>Polaris</i>		
Victory Kingpin	V-twin, 4-valve per cylinder, 1,634 cc	15,999

SOURCE: WEBSITES OF DIFFERENT MOTORCYCLE MANUFACTURERS.

managed shops, 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 were the primary point of contact between the company and its customers. Moreover, if Harley's future lay with customers who possessed the disposable income to lay out \$18,000 on a motorcycle for occasional leisure rides, then the retail environment had to be appropriate to the needs 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. The dealers were obliged to carry a full line of Harley replacement parts and accessories, and to perform service on Harley bikes. Training programs helped dealers to meet the higher service requirements, and encouraged them to recognize and meet the needs of the professional, middle-class clientele that Harley was now courting. Harley pioneered the introduction of new services to customers. These included test ride facilities, rider instruction classes, motorcycle rental, assistance for owners in

**TABLE 9.5** Harley-Davidson shipments 1997–2006

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
<i>H-D motorcycle shipments</i>										
United States ('000s)	96.3	110.9	135.6	158.9	186.9	212.8	237.7	260.6	266.5	273.2
Export ('000s)	36.1	39.9	41.6	45.8	47.5	50.8	53.5	56.7	62.5	76.0
<i>Motorcycle product mix (%)</i>										
Sportster	23.8	22.5	23.6	22.6	21.7	19.4	19.7	22.0	21.3	18.5
Custom <sup>a</sup>	53.5	51.3	49.6	49.3	50.5	53.7	52.0	48.6	45.2	46.2
Touring	22.8	26.2	26.8	28.1	27.9	26.8	28.4	29.4	33.5	35.4
<i>Buell motorcycle shipments</i>										
Worldwide ('000s)	3.1	5.5	6.8	6.9	9.9	10.9	10.0	9.9	11.2	12.5
<i>Company total</i>	135.5	156.3	184.0	211.6	244.3	274.5	301.2	337.2	340.2	361.6

<sup>a</sup> Includes VRSC models.

SOURCE: HARLEY-DAVIDSON 10-K AND 8-K REPORTS.

customizing their bikes through dealer-based design centers and chrome consultants, and insurance services. Close to 85% of Harley dealerships in the US were exclusive – far more than for any other motorcycle manufacturer.

Given the central role of dealers in the relationship between Harley-Davidson and its customers, dealer relations continued to be a strategic priority for Harley. Its Retail Environments Group liaised closely with dealers with a goal of bringing the same retail experience to customers everywhere in the world. Harley-Davidson University was established to “enhance dealer competencies in every area, from customer satisfaction to inventory management, service proficiency, and front-line sales.” Dealer relationships were critical to Harley’s goal of growing sales of financial services, parts and accessories, and general merchandise. Harley believed that the quality and effectiveness of its dealer network was a key determinant of the strong demand for its products. Despite a fivefold increase in production capacity since 1990, demand for Harley motorcycles continued to outstrip supply, with the result that used bikes frequently sold at higher prices than new bikes. More generally, the rate of price depreciation of Harleys was lower than for any other manufacturer.

### ***Other Products***

Sales of parts, accessories, and “general merchandise” (clothing and collectibles) represented 20% of total revenue in 2000 – much higher than for any other motorcycle company (see table 9.6). Clothing sales included not just traditional riding apparel, but a wide range of men’s, women’s, and children’s leisure apparel.

Only a small proportion of the clothing, collectibles, and other products bearing the Harley-Davidson trademark were sold through the Harley dealership network. Most of the “general merchandising” business represented licensing of the Harley name and trademarks to third-party manufacturers. For example, Nice Man Merchandising supplied Harley-Davidson children’s clothes; a giftware company supplied Harley holiday bulb ornaments, music boxes, and a Road King pewter motorcycle

**TABLE 9.6** Harley-Davidson's revenues from parts and accessories, general merchandise, and financial services, 1992–2005 (\$ million)

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Parts and accessories	103.6	127.8	162.0	192.1	210.2	241.9	297.1	362.6	447.9	509.6	629.2	712.8	781.6	815.7	862.3
General merchandise	52.1	71.2	94.3	100.2	90.7	95.1	114.5	132.7	151.4	163.9	231.5	211.4	223.7	247.9	277.5
Financial services	–	–	–	–	–	–	102.9	132.7	140.1	181.5	211.5	279.5	305.3	331.6	384.9

SOURCE: HARLEY-DAVIDSON 10-K REPORTS.

replica; L'Oréal offered a line of Harley-Davidson cologne; Harley-Davidson Cafés operated in Manhattan and Las Vegas.

Harley-Davidson Financial Services was established to supply credit, insurance, and extended warranties to Harley dealers and customers. Between 2000 and 2003 it was Harley's most rapidly growing source of profits, accounting for 15% of total operating income in 2003.

### *International Expansion*

A key part of Harley-Davidson's growth strategy was expanding sales outside of the US. A critical issue was the extent to which Harley needed to adapt its products, image, and customer approach to conditions in overseas markets. Harley's image was rooted in American culture – to what extent was Harley's appeal to European and Asian customers rooted in its status as an American icon? “The US and Harley are tied together,” observed Hugo Wilson of 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.”<sup>6</sup> At the same time, the composition of demand and the customer profiles were different in overseas markets.

Europe was the focal point of Harley's overseas ambitions, simply because it was the second largest heavyweight motorcycle market in the world. Europe was also a huge challenge for Harley. Unlike in the US, Harley had never had a major position in Europe – it needed to fight to take market share from the established leaders in the heavy bike segment: BMW, Honda, Kawasaki, and Yamaha. The European motorcycle market differed significantly from the American market in that 70% of the heavyweight motorcycle market was for performance bikes, while touring and cruiser bikes accounted for just 30%. European buyers were knowledgeable and style conscious, but their style preferences were different from those of US riders. Also, European roads and riding styles were different from the US. As a result, Harley modified some of its models for the European market. The US Sportster, for example, had a straight handlebar instead of curled buckhorns and a new suspension system to improve cornering. The name was also changed to the “Custom 53.” The Harley Softail also received a new look, becoming the “Night Train.” As in the US, HOG played a critical role in building brand image and customer loyalty. Harley's anniversary celebration in Barcelona on June 2003 attracted some 150,000 people, including Harley owners from all over Europe. Central to Harley's international strategy was building its dealer network. Between 2000 and 2006, Harley expanded its overseas dealership network and built a new European headquarters in Oxford, England. In 2006, Harley's dealer network comprised 667 in the US, 75 in Canada, 359 in Europe (including the Middle East and Africa), 118 in Asia/Pacific, and 31 in Latin America.

**TABLE 9.7** Harley-Davidson's main facilities, 2005

Location	Function	Square feet
<i>Wisconsin</i>		
Milwaukee	Corporate headquarters	515,000
Wauwatosa	Product development center	409,000
Wauwatosa	Engine manufacturing	422,000
Menomonee Falls	Engine and transmission production	479,000
Franklin	Parts/accessories distribution center	250,000
Tomahawk	Fiberglass parts production/painting	211,000
<i>Pennsylvania</i>		
York	Final assembly plant, parts and painting	1,321,000
<i>Missouri</i>		
Kansas City	Manufacturing, painting	450,000
<i>Brazil</i>		
Manaus	Assembly	35,000

SOURCE: HARLEY-DAVIDSON 10-K REPORT, 2005.

## Operations

Since emerging as an independent company in 1981, Harley-Davidson had continuously upgraded its manufacturing operations. This involved continuous investment in plant and equipment, both to introduce advanced process technologies and to expand capacity. Even more important was the development of manufacturing capabilities through total quality management, just-in-time scheduling, CAD/CAM, and the devolution of responsibility and decision making to the shopfloor. Table 9.7 shows Harley's main manufacturing and development facilities.

Despite constant development of its manufacturing facilities and operational capabilities, Harley's low production volumes relative to Honda and the other Japanese manufacturers imposed significant cost disadvantages. A key cost disadvantage was in the purchasing components. Bought-in, customized components accounted for a large proportion of manufacturing costs and Harley lacked the buying power of Honda or even BMW. To compensate for lack of bargaining clout, Harley fostered close relations with its key suppliers and placed purchasing managers at senior levels within its management structure. It's supplier advisory council (SAC) promoted collaboration and best practice sharing within the Harley network.<sup>7</sup> Harley's director of purchasing, Garry Berryman, commented: "Through the SAC, we're able to take some of the entrepreneurial aspects of our smaller, privately held suppliers and inject that enthusiasm, spirit, and energy into those that may be larger, publicly held companies. In this way, the SAC serves not only to improve purchasing efficiency, but also provides a forum to share information, ideas, and strategy."<sup>8</sup>

## People and Management

Central to Harley-Davidson's renaissance was the creation of a new relationship between management and employees. Following the management buyout in 1981, Harley's new management team systematically rethought management-employee

relationships, employee responsibilities, and organizational structure. The result was a transformation in employee commitment and job satisfaction. Harley's employee relations focused on involvement, self-management, open communication, and the provision of generous health and leave benefits. Harley's Kansas City assembly plant, opened in 1998, featured a management structure and working methods designed to promote employee commitment and involvement. The plant manager and other administrators worked in a "bullpen area" on the production floor rather than in separate offices, and the whole plant was organized around three types of work teams:

- *Natural work groups* – every worker belonged to a work group, with 8–15 people per group.
- *Process operating groups* – comprised representatives from each work group. There were four process operating groups, one for each of the plant's four operating divisions: paint, assembly, fabrication, and engine production.
- *Plant leadership groups* – a 14-member committee, responsible for governing the facility. It comprised the plant manager, the presidents of both unions representing the plant workforce, four elected representatives from the process groups, an elected representative from maintenance, and six administrators.<sup>9</sup>

Harley's belief in the effectiveness of non-hierarchical, team-based structures in fostering motivation and accelerating innovation and learning was evident throughout the company. The Harley-Davidson Operating System was a philosophy and a methodology for continuous improvement involving team-based efforts to identify wasted steps, pare costs, and enhance quality throughout manufacturing.

The movement toward a flatter, more team-based organizational structure extended to Harley's corporate headquarters. "In our new organization," explained Clyde Fessler, VP for Business Development, "the Harley-Davidson Motor Company has been divided into three broad, functional areas called Circles. They are: the Create Demand Circle (CDC), the Produce Product Circle (PPC), and the Provide Support Circle (PSC). Each Circle is composed of the leaders representing the functions within it. The flexibility of the organization extends even to the decision of which functional areas are identified within a given circle. It is quite possible that Circle definitions may shift from time to time, depending on the demands of the business."<sup>10</sup> Each Circle operated as a team with leadership moving from person to person, depending on the issue being addressed. Overall coordination was provided by the Strategic Leadership Council (SLC), comprising individuals nominated by each of the three Circles.

## **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. In competing against Harley, the Japanese manufacturers' key advantage was their sales volume – Honda produced over five million bikes per year.

In addition, Harley lacked the diversification of its rivals. 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 benefit from sharing technology, engineering capabilities, and marketing and distribution know-how across their different vehicle divisions. In addition, sheer size conferred greater bargaining power with suppliers.

Imitators also included several specialist companies producing retro-styled cruiser bikes. In recent years Excelsior, Polaris (Victory), and a resuscitated Indian had all entered the US super-heavyweight market.

Figure 9.1 shows competitive product offerings while table 9.4 shows price comparisons. Appendix 2 gives profiles of several leading competitors.

**FIGURE 9.1** Cruiser motorcycles, 2007 models



## Meeting the Challenges of Tomorrow

The Strategic Plan for Sustainable Growth, which emerged at the end of February 2004, offered a ten-year roadmap for Harley's future development. Bleustein recognized that the targets set – unit sales growth of 7 to 9% annually and annual earnings growth “in the mid-teens” – were ambitious. However, with growing sales of parts, accessories, and financial services and continued productivity increases from improved business processes, Bleustein considered these targets well within Harley's grasp. At the heart of the strategy were two core principles – growing value and strengthening the brand. Implementing these principles required a systematic approach to developing Harley's differentiation advantage, while working strenuously to contain costs. Throughout the whole range of Harley-Davidson's activities – from designing new motorcycles to interfacing with customers – Bleustein was satisfied that Harley had built a management system that was dedicated to excellence and continuous improvement. What concerned him were the possible potholes that the company might encounter on the road forward. In Donald Rumsfeld's words, what were the “unknown unknowns” that might throw Harley-Davidson off course?

In thinking through Harley's possible vulnerabilities, Bleustein grappled with some of the implications of a strategy that emphasized selling an experience rather than selling a product. The problem of selling experiences was that they were dependent upon the social and psychological identity and aspirations of the customer. Were the values embodied in the “Harley Experience” universal and enduring or were they the result of cultural, social demographic phenomena that were particular to the United States during the past two decades? To date, the market had absorbed Harley's additional production with no signs of indigestion. Would an additional 100,000 motorcycles per year be absorbed just as willingly, or would the very ubiquity of Harley bikes undermine the individuality that was closely linked to “The Experience”? While Harley's marketing emphasized the experience of motorcycling, Bleustein was acutely aware that purchasing a Harley was, for many of its owners, more a statement of style than a desire to ride the great American wilderness.

With the baby-boomers graduating from motorcycles to retirement homes, Harley would no longer be benefiting from favorable US demographic trends. In these circumstances Harley's ability to maintain its market share would depend increasingly on its ability to recruit new and younger customers. To date, Harley had had little success in selling to younger riders. Similar comments could be made about Harley's other potential growth market – overseas. For all its building of distribution networks and marketing efforts outside the US, Harley's overseas performance had been patchy: very successful in Japan, but only modest sales growth in Europe.

## Appendix 1

### Harley-Davidson: Summary of Financial Statements, 1994–2006

**TABLE 9.A1** Harley-Davidson: selected items from financial statements, 1994–2006 (\$ million)

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Net sales	1,159	1,350	1,531	1,762	2,064	2,453	2,906	3,407	4,091	4,624	5,015	5,342	5,801
Gross profit	358	411	490	586	691	836	991	1,153	1,418	1,666	1,900	2,040	2,233
R&D	28	30	37	53	59	70	76	130	140	150	171	179	n.a.
Selling, admin., engineering	204	234	269	329	377	448	513	552	639	684	727	762	n.a.
Operating income	154	181	228	270	334	416	515	663	883	1,149	1,361	1,470	1,603
<i>Of which:</i>													
Financial services	–	4	8	12	20	28	37	61	104	168	189	192	n.a.
Interest income	2	0	3	8	4	8	18	17	17	23	23	23	n.a.
Other income/(expense)	1	(5)	(4)	(2)	(1)	(3)	16	(7)	(13)	(6)	(5)	(5)	n.a.
Income before taxes	156	176	228	276	336	421	549	673	886	1,166	1,379	1,488	1,624
Provision for income taxes	60	65	84	102	123	154	n.a.	236	306	405	490	528	581
Net Income	104	112	166	174	213	267	348	438	580	761	890	960	1,043
<b>Balance sheet</b>													
<b>Assets</b>													
Cash	59	31	142	147	165	183	419	439	281	329	275	141	238
Finance receivables, net	–	170	184	249	319	355	581	921	1,139	1,391	1,656	1,943	2,101
Accounts receivable, net	143	134	141	103	113	102	98	119	109	112	121	122	143
Inventories	173	84	101	118	156	169	192	181	218	208	227	221	288
Total current assets	406	337	613	704	845	949	1,297	1,665	2,067	2,729	3,683	3,145	3,551
Property, plant, equipment	263	285	409	529	628	682	754	892	1,033	1,046	1,025	1,012	n.a.
Total assets	739	1,001	1,230	1,599	1,920	2,112	2,436	3,118	3,861	4,923	5,483	5,255	5,532
<b>Liabilities</b>													
<b>Current liabilities</b>													
Current portion of debt	18	3	9	91	147	181	89	217	383	324	495	205	832
Accounts payable	64	103	101	106	123	138	170	195	227	224	244	271	763
Total current liabilities	216	233	251	362	468	518	498	716	990	956	1,173	873	1,596
<b>Non-current liabilities</b>													
Debt	0	164	258	280	280	280	355	380	380	670	800	1,000	870
Other long-term liabilities	90	109	70	62	67	65	97	158	123	86	91	82	109
Post-retirement benefits	n.a.	n.a.	66	68	72	76	81	90	105	127	150	61	n.a.
Stockholders' equity	433	495	663	827	1,030	1,161	1,406	1,756	2,233	2,958	3,218	3,084	2,757
Total liabilities and equity	739	1,001	1,230	1,599	1,920	2,112	2,436	3,118	3,861	4,923	5,483	5,255	5,532
<b>Cash flows</b>													
Operating activities	81	169	228	310	318	416	565	757	546	597	832	961	762
Capital expenditures	(95)	(113)	(179)	(186)	(183)	(166)	(204)	(290)	(324)	(227)	(214)	(198)	(220)
Total investing activities	(97)	(188)	(214)	(406)	(340)	(300)	(171)	(772)	(720)	(540)	(570)	177	(35)
Financing activities	(3)	(10)	96	102	40	(98)	(158)	34	80	81	(316)	(1,272)	(637)
Net increase in cash	(18)	(26)	(111)	5	(18)	18	236	20	(95)	137	(54)	(134)	97

SOURCE: HARLEY-DAVIDSON FINANCIAL STATEMENTS (WWW.HARLEY-DAVIDSON.COM).



## Appendix 2

### Harley-Davidson's Competitors

**TABLE 9.A2** Comparative financial data for Harley-Davidson, Honda, and BMW (\$ million, unless otherwise indicated)

	Honda Motor		Yamaha Motor		BMW		Harley-Davidson	
	2004	2005	2004	2005	2004	2005	2004	2005
Revenue	75,912	80,446	9,711	11,648	60,473	55,255	5,015	5,342
Gross profit margin	31.30%	30.20%	27.35%	27.12%	23.20%	22.90%	37.89%	38.19%
SGA expense	16,175	16,324	1,983	2,284	8,902	8,137	727	762
Operating income	5,581	5,868	673	875	5,108	4,492	1,361	1,470
Net income after tax	3,619	3,628	366	542	3,031	2,652	890	960
Net margin	5.70%	5.60%	3.77%	4.65%	5.00%	4.80%	17.75%	17.97%
Operating income/total assets	7.21%	6.77%	9.14%	10.78%	5.55%	5.09%	24.82%	27.97%
Inventory turnover	7.33	7.42	4.10	4.40	4.75	5.15	14.86	15.36
Return on equity	13.54%	11.86%	14.00%	18.90%	12.69%	13.19%	27.60%	31.10%
Operating cash flow	6,630	6,944	416	562	12,700	12,661	832	961
Cash flow from investing activities	(8,997)	(7,513)	(425)	(610)	(16,309)	(14,168)	(570)	177
R&D expenditure	4,248	4,356	493	607	n.a	2,918	171	179
Advertising expenditure (all products)	2,038	1,932	n.a	n.a	n.a	n.a	49	67
Motorcycles shipped (thousands of units)	10,482	10,271	3,171	3,849	92	97	327	340
Employees	131,600	137,827	36,668	39,381	105,972	105,798	9,580	9,700

SOURCES: COMPANY FINANCIAL STATEMENTS.

## NOTES

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- 2 Marc Ballon, "Born to be wild," *Inc*, November 1997, p. 42.
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