

Case 7 Harley-Davidson, Inc., May 2012



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, PA, 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, PA, NOVEMBER 11, 1999

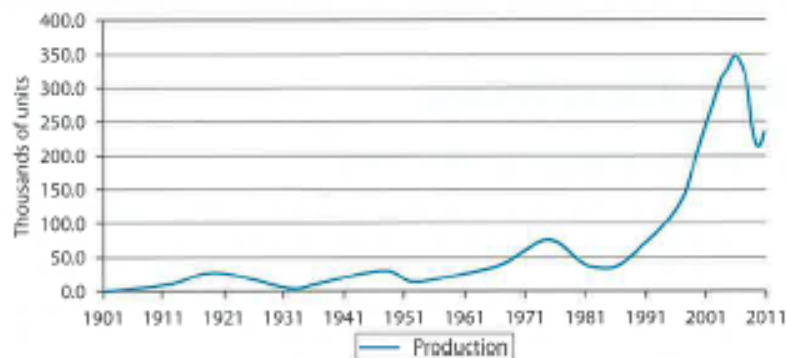
I've been impressed by Harley-Davidsons. It's one of America's finest products. And today I add to my impressions about the product, the impressions of the workforce . . . I'm impressed by the esprit de corps, I'm impressed by the fact that these people really enjoy what they're doing, I'm impressed by the fact that they're impressed by the product they make.

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

When Keith Wandell took over as CEO of Harley-Davidson, Inc. on May 1, 2009, he was the first outsider to be appointed to the top job since Harley-Davidson's management buyout in 1981. He was also the first CEO of Harley since that date to have presided over a period of declining output and sales.

From 1984 to 2008, Harley's output and revenue had grown in every single year. The financial crisis of 2008 put an abrupt end to Harley's growth trend (Figure 1). After decades of customer waiting lists and shortage of production capacity, Wandell was thrust into a situation of plummeting orders, excess inventory, and a growing mountain of bad debt as customers defaulted on their loan payments.

This case was prepared by Robert M. Grant. ©2012 Robert M. Grant.

FIGURE 1 Annual shipments of motorcycles by Harley-Davidson

Wandell's initial actions included restoring funding for Harley's consumer lending activity, cutting back production, laying off employees, discontinuing the Buell brand and closing its plant, and putting recently acquired MV Agusta up for sale. As a result of a sharp drop in sales revenue and one-off restructuring costs, Harley posted a net loss in 2009, its first in 25 years. (Appendix 1 provides details of Harley-Davidson's financial performance.)

Stabilizing the business was Wandell's immediate priority, but even more important was establishing "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."¹ During 2010 and 2011, Wandell led a comprehensive transformation strategy which included a rethinking and restructuring of Harley's manufacturing operations, the transformation of its product development system, and a drive to build distribution and grow sales in the emerging markets of Asia and Latin America.

Yet, despite the early successes of Wandell's turnaround strategy, there was still the worry that Harley's best days might be behind it.

Harley's long-term profit growth depended on its ability to keep expanding the sales of its high-priced, heavyweight motorcycles. With North America and Europe accounting for 88% of Harley's revenues and with both regions mired in debt, unemployment, and depressed consumer spending, it seemed likely that the demand for luxury leisure products costing between \$8,000 and \$28,000 would continue to be subdued.

If the world economy was unlikely to offer much tailwind, to grow sales Harley would need to grow its market share at the expense of rivals—but here Harley was constrained by the fact that it already accounted for more than 55% of the US heavyweight motorcycle market.

Indeed, Harley's own market position 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 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 represented?

The History of Harley-Davidson

From Birth to Maturity, 1903–1981

Harley-Davidson, Inc. was founded in 1903 by William Harley and brothers William Davidson, Arthur Davidson, and Walter Davidson. Their first model had a three-horsepower engine and was made in the Davidson's family shed. 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. With the closure of the Indian Motorcycle factory in Springfield, Massachusetts in 1953, Harley-Davidson became the sole survivor of the 150 US motorcycle producers that had existed in 1910.

The postwar era saw new challenges for Harley-Davidson. Increasing 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. Initially, Harley benefited from the rebirth of motorcycling as a leisure activity, but soon it was facing direct competition: in 1969, Honda introduced its four-cylinder CB750, a huge technical advance on anything produced by Harley or the British. Harley's acquisition by AMF compounded the problems: expansion of production capacity to 75,000 units a year led to horrendous product quality problems followed by financial losses and a declining market share.

Rebirth, 1981–2008

In 1981, Vaughn Beals and a group of Harley's senior managers led a leveraged buyout of Harley. Harley-Davidson emerged as an independent, privately owned company, heavily laden with debt. The buyout coincided with a severe recession and soaring interest rates. Harley's sales fell and during 1981 and 1982 it lost a total of \$60 million. Only by drastically cutting costs and gaining temporary protection from Japanese imports did Harley survive.

The management team devoted itself to rebuilding production methods and working practices. 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. Within a year, all of Harley's manufacturing operations were being converted to JIT: components and sub-assemblies were "pulled" through the production system in response to final demand, and management and labor collaborated in introducing quality management.

Increasing sales and a return to profitability allowed Harley to go public in 1986. The new funding supported investment in new models, in plants, and in dealerships. Harley's share of the super-heavyweight market (over 850cc) grew from about 30% in 1986 to over 60% in 1990. Growth continued throughout the 1990s, both in the heavyweight motorcycle market and in Harley's share of that market. Throughout 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. New production plants in Kansas City and York, Pennsylvania, the launch of new models, and international expansion resulted in sales exceeding 300,000 in 2004, a tenfold increase on 1983.

The Heavyweight Motorcycle Market

Until the financial crisis of 2008–2009, the heavyweight segment (over 650cc) had been the most rapidly growing part of the world motorcycle, with the US accounting for a major portion of this growth. Sales of heavyweight motorcycles in the major markets of the world almost trebled between 1990 and 2008.

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, pushing Honda into second place. The European market was more fragmented, with Harley being among a leading group that included Honda, BMW, Suzuki, Yamaha, Kawasaki, and Triumph, each with market shares in the 8–15% range (Table 2).

The heavyweight motorcycle market comprised three segments:

- *Cruiser motorcycles*: These were “big, noisy, low riding, unapologetically macho cycles,”² 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 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 half 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 specially equipped for longer-distance riding and bikes especially designed for comfort over long distances

TABLE 1 Retail sales of heavyweight motorcycles (651+ cc), 2003–2011 (thousands of units)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
<i>North America (total)</i>	495	531	554	579	555	477	304	260	271
Harley-Davidson	238	256	265	282	267	235	174	154	162 ^a
Market share (%)	48.1	48.2	47.8	48.6	48.7	49.3	53.2	54.9	55.7
<i>Europe (total)</i>	323	336	351	377	372	384	314	301	293
Harley-Davidson ^b	26	25	30	34	42	45	40	41	44
Market share (%)	8.1	7.3	8.5	9.1	11.3	11.7	12	12.7	13.7
<i>Asia-Pacific</i>									
Harley-Davidson	15	10	11	13	23	25	23	21	21 ^c
<i>Latin America</i>									
Harley Davidson	n.a.	n.a.	n.a.	n.a.	3	8	6	6	7

Notes:

^aOf which, US 151,683; Canada 10,502.

^bIncludes Middle East and Africa.

^cOf which Japan 11,015.

Source: Harley-Davidson 10-K reports.

TABLE 2 Market shares in heavyweight motorcycles (651 + cc), 2005–2007 (%)

	North America			Europe		
	2005	2006	2007	2005	2006	2007
Harley-Davidson	47.8	48.6	48.7	8.9	9.1	9.6
Honda	16.6	15.1	14.3	13.0	14.6	12.3
Kawasaki	6.9	7.1	7.5	12.6	10.7	11.3
Suzuki	12.6	13.1	12.7	13.3	14.8	16.5
Yamaha	9.3	8.8	9.2	15.8	15.5	13.6
BMW	3.3	—	—	17.7	16.5	15.1
Ducati	—	—	—	5.2	5.2	5.9
Triumph	—	—	—	5.0	5.1	6.5
Other	4.5	7.3	8.3	8.5	8.5	9.2

Source: Harley-Davidson, annual reports, 2005, 2007.

(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 with its offshoot, Buell Motorcycles.

Unlike its Japanese competitors, Harley was highly market focused. Harley's models were all concentrated on the narrow super-heavyweight segment (over 850cc).

Harley-Davidson in 2012

The Brand

Harley's top management team considered the Harley-Davidson image and the loyalty it engendered among its customers its greatest assets. Harley-Davidson was an archetype of American style. 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."²³ Together with a few other companies, possibly 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 quest 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. Harley-Davidson made relentless efforts in all its communications—whether to customers, dealers, investors, or suppliers—to convey this experience:

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.⁴

Customers and Customer Relations

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 (HOG) 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. Each year, senior managers typically attended a total of more than 150 shows, rallies, and rides. The bond between the company and its customers was captured by its chief designer, Willie G. Davidson: "We ride with you." The 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."⁵ The loyalty of Harley owners was reflected in their continuing reinvestment in Harley products: purchasing Harley-branded accessories and apparel, customizing and upgrading their bikes, and eventually trading them in for a new (typically more expensive) model. Almost half of all sales were to repeat customers.

Harley's success had been built upon a massive market repositioning. Traditionally, Harley owners had been blue-collar youngsters; during the 1980s and 1990s Harley owners became increasingly middle-aged and upper-income:

The average US retail purchaser of a new Harley-Davidson motorcycle is a married male in his mid to late forties (nearly two-thirds of US retail purchasers of new Harley-Davidson motorcycles are between the ages of 35 and 54) with a median household income of approximately \$87,000. Nearly three-quarters of the US retail sales of new Harley-Davidson motorcycles are to buyers with at least one year of education beyond high school and 32% of the buyers have college/graduate degrees. Approximately 12% of US retail motorcycle sales of new Harley-Davidson motorcycles are to female buyers.⁶

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 its 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: 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 . . . 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 1984.⁷

Harley's engines most clearly represented its commitment to tradition in the face of technological change. 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, 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 2012, Harley offered 34 different models. Harley's product development efforts had been 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 were limited to style changes, new paint designs, and engineering improvements. However, after 2000, Harley had accelerated technological progress and had introduced more-radical new-product developments. Its V-Rod model introduced in October 2001 featured innovative styling and an all-new liquid-cooled engine. The Buell range had also allowed greater scope for Harley's engineers, particularly in engines and frame designs. In 2006, Harley introduced another new engine, the Twin Cam 96, which featured electronic ignition and was teamed with a new six-speed gearbox.

It is notable that between January 2000 and April 2012, Harley was awarded 188 US patents, many of these related to 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, Suzuki 625, and Kawasaki 2,002.

Central to Harley's product strategy was the idea that every Harley rider would own a unique, personalized motorcycle as a result of the company offering 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. 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 Sportster model was positioned as an entry-level bike, beginning at \$7,999, less than one-third of the price of the Electra Glide Ultra Limited, with "custom color" at \$25,014. Top of the price range was the three-wheeler Tri-Glide at \$31,824 (with two-tone paint).

The Buell Exit

Founded by ex-Harley engineer Erik Buell, Buell Motor Company developed bikes that used Harley engines and other components but mounted them on a lighter, stiffer frame. Harley acquired complete ownership of Buell in 1998. Buell offered Harley the opportunity to broaden its appeal to younger riders and those more interested in speed and maneuverability. The lighter weight and superior handling were also seen as especially appealing to European customers. In the US, the typical Buell customer was seven years younger than the average Harley buyer; the price range of Buell bikes was also lower. The Buell Blast, with its 490cc single-cylinder engine and a price tag of \$4,595, was a major departure for Harley: its first entry into middleweight motorcycles since the 1970s. Yet, despite heavy investments in developing and launching new models, Buell's sales were disappointing (Table 3). Four months after his arrival at Harley-Davidson, Wandell announced the discontinuation of Buell and the closure of its plant.

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. The 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,

TABLE 3 Harley-Davidson shipments 2001–2011 (thousands of units)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
H-D motorcycles											
US	186.9	212.8	237.7	260.6	266.5	273.2	241.5	206.3	144.4	131.6	152.2
Export	47.5	50.8	53.5	56.7	62.5	76.0	89.1	97.2	78.5	78.8	80.9
Motorcycle product mix (%)											
Sportster	21.6	19.4	19.7	22.0	21.3	18.5	21.8	20.0	21.4	19.5	21.3
Custom	50.4	53.7	52.0	48.6	45.2	46.2	43.7	46.4	40.9	41.4	39.2
Touring	28.0	26.8	28.4	29.4	33.5	35.4	34.5	33.6	37.7	39.0	39.5
Buell motorcycles	9.9	10.9	10.0	9.9	11.2	12.5	11.5	13.1	9.5	2.6	0.2
Company total	244.3	274.5	301.2	327.2	340.2	361.6	342.1	316.4	232.4	213.0	233.2

Source: Harley-Davidson 10-K reports, various years.

rider instruction classes, motorcycle rental, consulting services for customizing bikes through dealer-based design centers and chrome consultants, and insurance services. 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.”⁸

Other Products

Sales of parts, accessories, and “general merchandise” (clothing and collectibles) represented 14.8% of total revenue in 2011 (Table 4), much higher than for most 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.

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-Davidson name and trademarks to third-party manufacturers of clothing, giftware, jewelry, toys, and other products. L’Oréal offered a line of Harley-Davidson cologne. To expand sales of licensed products, Harley dealers opened a number of secondary retail location and alternative retail outlets, which sold clothing, accessories, and giftware but not motorcycles.

Harley-Davidson Financial Services (HDFS) is Harley’s financial services arm supplying credit, insurance, and extended warranties to Harley dealers and customers. Between 2000 and 2007, it was Harley’s most rapidly growing source of profit, contributing almost 12% of operating profit in 2007. However, the credit crunch hit the business hard. Unable to securitize its customer loans, Harley was forced to retain these loans on its own books, causing a large increase in its current assets.

TABLE 4 Harley-Davidson's non-motorcycle sales, 2003–2011 (\$ million)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
Parts and accessories	712.8	781.6	815.7	862.3	868.3	858.7	767.2	749.2	816.5
General merchandise	211.4	223.7	247.9	277.5	305.4	313.8	282.2	259.1	274.1
Financial services	279.5	305.3	331.6	384.9	416.2	377.0	494.7	682.7	649.4

Source: Harley Davidson 10-K reports.

During 2010–2011, HDFS was placed on a firmer financial footing and its revenue and profit grew strongly with half of all US retail sales of motorcycles financed by HDFS. By 2011, HDFS contributed almost one-third of Harley's operating income.

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."⁹ At the same time, the composition of demand and customer profiles was 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. It had never had a major position in Europe. Also, the European motorcycle market was very different from the American market: 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. European roads and riding styles were also different from the US. As a result, Harley modified some of its models for the European market. The Sportster, for example, was given straight handlebars instead of curled buckhorns and a new suspension system to improve cornering. Its name was changed to the "Custom 53." As in the US, HOG played a critical role in building brand image and customer loyalty.

In July 2008, Harley extended its European presence with the \$105 million acquisition of MV Agusta, an Italian manufacturer of premium, high-performance sport motorcycles—including the F4-R with a 1078cc, four-cylinder, liquid-cooled engine, producing 190hp. Whatever plans Harley had to revitalize MV Agusta, to expand Harley's European dealership network, or to build a stronger presence among younger riders, they were not implemented. On August 6, 2010, Harley sold MV Agusta back to its previous owner for €3 (\$3.9).

With Europe mired in recession during 2009–2012, Harley's international strategy turned increasingly to the growth markets of Asia and Latin America. Harley established an Asia-Pacific regional headquarters in Singapore, which distributed to Harley dealers in Australia, China, India, and Japan; and Latin America headquarters based in Miami. In 2011, Harley opened an assembly plant in India. (This was

TABLE 5 Harley-Davidson's dealership network

	US		Canada		Europe		Asia Pacific		Latin America	
	2008	2011	2008	2011	2008	2011	2008	2011	2008	2011
Full-service dealerships	686	635	71	69	383	369	201	230	32	44

TABLE 6 Harley-Davidson's main facilities, 2011

Location	Function	Square Feet
Menomonee Falls, WI	Motorcycle powertrain production	881,600
Milwaukee, WI	Corporate office	515,000
Milwaukee, WI	Museum	130,000
Tomahawk, WI	Fiberglass/plastic parts production and painting	226,000
Wauwatosa, WI	Plant closed in 2010; production moved to Menomonee Falls, WI	430,000
Wauwatosa, WI	Product development center	409,000
Franklin, WI	Distribution center	255,000
York, PA	Motorcycle parts fabrication, painting, assembling Softail models	582,400
Kansas City, MO	Motorcycle parts fabrication and painting and Dyna, Sportster	450,000
Carson City, NV	Financial services	100,000
Naples, FL	Motorcycle testing	820,000
Yucca, AZ	Motorcycle testing	79,000
Bawal, India	Assembly of bikes for Indian market	68,200
Manaus, Brazil	Assembly of bikes for Brazilian market	100,000
Adelaide, Australia	Motorcycle wheels; to be fully outsourced by 2013	485,000

Source: Harley-Davidson 10-K report, 2011.

its second overseas assembly plant; the first was in Brazil in 1999.) Table 1 shows Harley's overseas sales.

Establishing dealerships was the key to penetrating international markets. Table 5 shows Harley's dealership network.

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 plant 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. Table 6 shows Harley's main manufacturing and development facilities.

Despite the 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, 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.”¹⁰

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. To cut costs, Harley initiated a program of plant consolidation. The two Milwaukee-area powertrain plants would be combined into a single facility and the separate paint and frame operations at York, Pennsylvania would be merged into a single plant. 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. The new system would mean that manufacturing would be driven by customer demand, every production line would have the flexibility to build every model, and inventories would be reduced.

People and Management

Central to Harley-Davidson’s renaissance during the 1980s and 1990s was the creation of a new relationship between management and employees. After the 1981 management buyout, Harley’s new management team systematically rethought management–employee relationships and implemented a new approach built on involvement, self-management, open communication, and team-based organizations. At the Kansas plant, production was performed by 8- to 15-member *natural work groups*; representatives from these teams formed four *process operating groups* for fabrication, engine production, assembly, and painting; overall plant management was performed by a 14-member *plant leadership group*.¹¹ Team-based structures extended up to top management level, where three functional teams—the Create Demand Circle (CDC), the Produce Product Circle, and the Provide Support—were coordinated by the Strategic Leadership Council.¹²

Despite Harley’s commitment to employee participation and development, the production cut-backs and cost cutting pressures during 2009–2012 created tensions between the company and its employees. On April 1, 2012, a new labor agreement went into effect whereby Harley’s unions agreed to headcount reductions and more flexible working practices.¹³

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 the scale advantages deriving from vastly greater volume. However, despite their large price premium,

Harley-Davidson motorcycles benefitted from a much smaller 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 benefit from sharing technology, engineering capabilities, and marketing and distribution across their different vehicle divisions—and their size conferred purchasing power.

Harley's success attracted imitators. These included not only the Japanese big four which introduced retro-styled, V-twin cruisers but also new domestic competitors—including Excelsior, Polaris (Victory), and a resuscitated Indian—had all entered the super-heavyweight market with cruiser bikes selling at prices exceeding those of Harley (the Indian Vintage Chief cost \$35,499).

Figure 2 shows competitive product offerings, while Table 7 shows price comparisons. Appendix 2 gives profiles of several leading competitors.

Meeting the Challenges of Tomorrow

By May 2012, Keith Wandell's confidence that Harley could adapt to the difficult economic circumstances that had proceeded the 2008–2009 financial crisis seemed justified. The first-quarter financial results for 2012 showed a year-on-year revenue growth of 16.7% and a net income growth of 44.3%. Increases in manufacturing

TABLE 7 Price comparison of V-twin, cruiser motorcycles, 2009

Manufacturer/model	Engine	Retail price (\$)
Harley-Davidson		
Sportster 883 Low	V-twin, air-cooled, 883cc	6,999
Fat Boy	V-twin, air-cooled, 1540cc	15,999
VRSC V-Rod Muscle	V-twin, liquid-cooled, 1131cc	17,199
Heritage Softail Classic	V-twin, air-cooled, 1450cc	17,999
Honda		
Shadow Spirit 750	V-twin, liquid-cooled, OHC, 745cc	7,699
VTX1300C	V-twin, liquid-cooled, OHC, 1312cc	10,299
VTX1800N	V-twin, liquid-cooled, OHC, 1800cc	13,699
Suzuki		
Boulevard S50	V-twin, liquid-cooled, OHC, 805cc	7,199
Boulevard C90	V-twin, air-cooled, OHC, 1475cc	11,299
Boulevard M109R	V-twin, liquid-cooled, 1783cc	13,799
Kawasaki		
Vulcan 900 Classic	V-twin, 8-valve, OHC	7,499
Vulcan 1600 Mean Streak	V-twin, air-cooled, 1552cc	11,099
Yamaha		
V-Star Custom Road Star	V-twin, OHC, air-cooled, push-rod, 649cc	6,290
Polaris		
Victory Kingpin	V-twin, 4-valve per cylinder, 1634cc	16,399

Source: Websites of different motorcycle manufacturers.

FIGURE 2 Cruiser motorcycles

Harley-Davidson Fat Boy



Honda Shadow Spirit 750



Yamaha Roadstar



Suzuki Boulevard C50



Kawasaki Vulcan 900



Polaris Victory Kingpin

efficiency had contributed a large proportion of the improvements in profitability. Looking to 2013, Wandell anticipated that Harley's restructuring program would generate cost savings of around \$310 million over the year.

Yet, despite the vast improvement as compared with the dark days of 2009, Harley was a long way from returning to its traditional growth trajectory. Wendell estimated that Harley's total sales in 2012 would be between 245,000 and 250,000 bikes, a long way short of the 361,600 bikes it shipped in 2006.

Morningstar's Jamie Katz emphasized the demographic factors which would hold back Harley's market potential within the US:

We estimate the median age of a Harley buyer to be just younger than 50 . . . and according to the US Census the [40- to 49-year-old group] is set to decline 2.5% between 2010 and 2015 . . . With a shrinking core customer base and an increasing

proportion of baby boomers moving out of this age segment, we believe more conservative behavior on the part of this older group could act as a drag on sales growth.¹⁴

A major thrust of Harley's marketing had been to broaden its demographic base with programs targeting women riders, "Harlistas" (Latino riders), "Iron Elite" (African American riders), and "Harley's Heroes" (military and veteran riders). However, the big challenge was appealing to the upcoming generations. As the *New York Times* noted, "As Harley keeps most of its focus on its aging consumers, rivals like BMW, Honda and Yamaha are attracting younger customers who seem less interested in cruising on what their old man rides."¹⁵

The very success of Harley in expanding its output and market share may have contributed to its declining desirability. "Traditionally, Harley-Davidson had a very loyal consumer," commented Anthony Gikas, senior research analyst at Piper Jaffray. "But those riders lost interest in the brand because everyone has a Harley bike. It's not a club anymore."¹⁶

One 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 (and what Harley itself has suggested, intermittently, it may do): 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?¹⁷

Appendix 1: Selected Items from Harley-Davidson Financial Statements, 2003–2011 (\$million)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
Income statement									
Net sales	4,624	5,015	5,342	5,801	5,727	5,594	4,781	4,859	5,311
Gross profit	1,666	1,900	2,040	2,233	2,114	1,931	1,386	1,427	1,555
R & D	150	171	179	177.7	186	164	143	136	145
Selling, administrative and engineering expense	684	727	762	846	901	985	702	756	788
Operating income, of which:	1,149	1,361	1,470	1,603	1,426	1,029	197	559	829
–Financial services	168	189	192	211	212	83	(117)	181	268
–Interest income	23	23	23	27	22	9	434	635	598
–Other income/(expense)	26	25	25	25		5	74	47	50
–Income before taxes	1,166	1,379	1,488	1,624	1,448	1,034	178	390	792
–Income taxes	405	490	528	581	514	379	108	130	244
–Net income	761	890	960	1,043	934	655	(55)	146	599
Balance sheet									
Assets									
Cash	329	275	141	238	403	594	1,630	1,021	1,526
Finance receivables held for investment	1,391	1,656	1,943	2,101	1,575	1,378	1,436	1,080	1,168
Accounts receivable, net	112	121	122	143	181	296	269	262	219
Inventories	208	227	221	288	350	401	323	326	418
Total current assets	2,729	3,683	3,145	3,551	3,467	5,378	4,341	4,066	4,542
Property, plant and equipment, net	1,046	1,025	1,012	1,024	1,061	1,094	906	815	809
Total assets	4,923	5,483	5,255	5,532	5,657	7,829	9,155	9,430	9,674
Liabilities									
Current portion of long-term debt	324	495	205	832	398	0	1,332	0	399
Accounts payable	224	244	271	763	300	324	162	225	255
Total current liabilities	956	1,173	873	1,596	1,905	2,604	2,268	2,013	2,698
Non-current liabilities									
Long-term debt	670	800	1,000	870	980	2,176	4,144	2,516	2,396
Other long-term liabilities	86	91	82	109	152	175	155	152	140
Post-retirement healthcare benefits	127	150	61	201	193	274	264	254	268
Stockholders' equity	2,958	3,218	3,084	2,757	2,375	2,116	2,108	2,207	2,420
Total liabilities and equity	4,923	5,483	5,255	5,532	6,796	6,786	9,155	9,430	9,674
Cash flows									
Operating activities	597	832	961	762	798	2,685	609	1,163	885
Capital expenditures	2,227	2,214	2,198	2,220	2,242	2,232	116	170	189
Total investing activities	2,540	2,570	177	235	391	2,393	(863)	145	(63)
Financing activities	81	2,316	21,272	2,637	21,038	1,293	1,381	(1,856)	308
Net increase in cash	137	254	2,134	97	164	191	1,134	(542)	(505)

Note:

Figures in parentheses denote a loss.

Source: Harley-Davidson 10-K reports, various years (www.harleydavidson.com).

Appendix 2: Comparative Financial Data for Honda, Yamaha, and Harley-Davidson (\$million, unless otherwise indicated)

	Honda Motor			Yamaha Motor			Harley-Davidson		
	2009	2010	2011	2009	2010	2011	2009	2010	2011
Revenue	101,916	92,210	107,479	4,676	4,458	4,496	4,781	4,859	5,311
Gross margin (%)	26	25	27	37	35	37	39	43	42
SGA expense	18,720	14,374	16,629	1,579	1,500	1,484	702	756	788
Operating income	1,931	3,910	9,852	141	73	158	197	559	829
Net income after tax	1,395	3,038	6,777	(210)	(53)	61	(55)	146	599
Net margin	1.37	3.29	6.31	(4.49)	(1.19)	1.36	3.05	12.33	(1.04)
Op. income/assets (%)	1.60	3.13	7.08	3.39	1.70	3.37	2.15	5.93	8.57
Total assets	120,319	124,990	139,157	4,163	4,322	4,701	9,155	9,430	9,674
Cost of goods sold	75,532	68,946	78,134	2,956	2,885	2,854	2,900	2,749	3,106
Inventory turnover	5.96	6.86	7.22	3.60	3.86	3.31	8.98	8.43	7.43
Inventories	12,664	10,056	10,822	821	747	862	323	326	418
Total equity	40,795	46,525	53,517	2,497	2,538	2,824	2,108	2,207	2,420
Return on equity (%)	3	7	13	(8)	(2)	2	(3)	7	25
Operating cash flow	3,906	16,597	12,878	(22.75)	428.53	272.35	609	1,163	885
Cash flow from investing activities	(11,538)	(6,403)	(8,796)	(265)	(137)	(117)	(863)	145	(63)
R & D expenditure	5,733	4,980	5,864	236	234	270	143	136	145
Advertising expenditure	n.a.	n.a.	n.a.	233	195	193	80	75	82
Motorcycles shipped (thousands of units)	10,114	9,639	11,445	n.a.	n.a.	n.a.	232	213	233.2
Employees	181,876	176,815	179,060	26,803	25,658	26,816	6,900	6,900	6,600

Note:

Figures in parentheses denote a loss.

Source: Harley-Davidson financial reports.

Notes

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