

Harley-Davidson's Profit Drop Lures T. Rowe, Franklin (Update1)  
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(Updates stock price in 19th paragraph.)

By Alan Ohnsman

April 16 (Bloomberg) -- Harley-Davidson Inc., the biggest U.S. motorcycle maker, may report a third-straight quarterly earnings drop tomorrow. With demand for pricey bikes skidding and shares approaching an eight-year low, Gallatin Asset Management's Mark Keller is buying the stock.

``It has things we look for: outstanding cash flow and outstanding management and a rising dividend,'' said the chief investment officer for Gallatin in St. Louis. Keller, who oversees \$2.9 billion of stocks and bonds, added 135,938 Harley shares to his portfolio of high dividend-yield stocks in 2007's fourth quarter.

Keller isn't alone. Baltimore-based T. Rowe Price Associates Inc. more than doubled its holdings to a 3.3 percent stake, becoming the company's third-biggest stockholder as of Dec. 31, according to data compiled by Bloomberg. Chicago-based LSV Asset Management bought 5.5 million shares and Franklin Resources Inc., based in San Mateo, California, bought 5.4 million.

``The stock is extraordinarily cheap,'' said Jeffrey Malcom, an analyst at Towson, Maryland-based Horan Capital Management LLC, which purchased 383,948 Harley shares from January through March as part of the \$500 million it manages. ``If they report a terrible quarter, we'll continue buying,'' Malcom said.

#### Cheaper Than Ducati

Investors are attracted by a stock price valuing Milwaukee-based Harley at 9.9 times estimated earnings as of yesterday, less than half that of Italy's Ducati Motor Holding SpA, one of the few publicly traded companies focused on motorcycles.

Harley's 3.3 percent dividend yield is almost 50 percent greater than the payout on the average stock in the Standard & Poor's 500.

The company has boosted the dividend 18 times since 1994 and may increase it 14 percent in September, according to Bloomberg data.

Buyers are undeterred by analysts' projections for a second-straight annual profit decline as weak consumer sentiment cuts demand for Harley-Davidson cruisers. Prices for the motorcycles range from about \$7,000 to more than \$30,000.

Analysts project a 6.7 percent rebound in earnings, to \$3.86 a share, by 2009.

The 105-year-old company's recovery from near bankruptcy in the 1980s was built on aggressive brand promotion, new models based on classic 1950s cruisers, improved quality and conservative financial management.

#### Topping GM

The shares more than quadrupled from their initial public offering in 1986 to \$74.93 in 2006. Harley was awarded a market value of \$18.2 billion, exceeding that of General Motors Corp., the world's largest automaker, and No. 2 Ford Motor Co.

Shipments of Fat Boy and Softail cruisers, with their distinctive ``potato, potato, potato'' V-Twin engine rumble, climbed to a record 349,196 bikes in 2006, from 68,626 in 1991.

A three-week strike and cooling U.S. economy combined to reduce last year's shipments to 330,619 units.

The stock's 52 percent decline through yesterday from the 2006 high also reflects concern that Harley depends on aging baby boomers who flocked to its motorcycles in the past two decades.

``They are locked into a very loyal buyer base that wants a very specific type of motorcycle,'' said Ed Aaron, an analyst at RBC Capital Markets in Denver. He rates the shares ``sector perform'' and doesn't own any.

``How do they shake the trees to get the younger riders without alienating core customers?'' Aaron said. ``It's going to be tricky.''

#### Not an Issue

These concerns are premature, says Janna Sampson, co-chief investment officer at Oakbrook Investments LLC in Lisle, Illinois.

``It's going to be 10 to 15 years before demographics are a real issue,'' said Sampson, who manages \$1.4 billion in assets, including 158,654 Harley shares. ``Baby boomers are going to keep riding for a while, and generally people in their 50s and 60s also have more disposable income.''

The stock's decline suggests ``the public overreacted,'' she said. ``It will reverse and come back.''

Harley gained 25 cents to \$36.13 at 10:49 a.m. in New York Stock Exchange composite trading.

The company will also benefit from untapped sales potential in global markets where consumer wealth is growing and a weaker dollar makes U.S. products less costly.

#### `High Expectations'

``It's a great franchise the world is getting more acquainted with,'' said Ron Muhlenkamp, president of Muhlenkamp & Co. in Wexford, Pennsylvania, which oversees \$1.6 billion, including 820,365 Harley shares. ``I have high expectations for international business.''

Retail sales of Harley motorcycles overseas rose 14 percent last year to a record 86,002, countering a 6.2 percent drop in the U.S. International sales will continue to outpace U.S.

growth, Chief Executive Officer Jim Ziemer said January in a Bloomberg interview.

In Japan, home to Honda Motor Co., the world's largest motorcycle maker, Harley has led in sales of bikes with engines larger than 250 cubic centimeters for at least five years, with a 25 percent market share, according to Japan Automobile Manufacturers Association.

Honda sells more than 10 million motorcycles and scooters annually.

Harley may report first-quarter earnings of 77 cents a share, up 4.1 percent from 74 cents a year ago, the average of 17 analyst estimates compiled by Bloomberg. Results a year ago were hurt by the York, Pennsylvania, motorcycle plant strike.

(Harley-Davidson is scheduled to release first-quarter earnings at 7 a.m. New York time tomorrow, followed by a conference call at 9 a.m. Webcast at <http://www.harley-davidson.com>)

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--Editor: Charles W. Stevens, William Glasgall

To contact the reporter on this story:

Alan Ohnsman in Los Angeles at +1323-782-4236 or [aohnsman@bloomberg.net](mailto:aohnsman@bloomberg.net)

To contact the editor responsible for this story:

Dave Versical at +1-248-827-2944 or [dversical@bloomberg.net](mailto:dversical@bloomberg.net).