POLARIS INDUSTRIES INC/MN
Form 10-Q
April 24, 2019
Table of Contents

## UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark
one)
x
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2019
OR

## .. TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to
Commission File Number 1-11411

POLARIS INDUSTRIES INC.
(Exact name of registrant as specified in its charter)

| Minnesota | $41-1790959$ |
| :--- | :--- |
| (State or other jurisdiction of | (I.R.S. |
| incorporation or organization) | Employer |
|  | Identification |
| 2100 Highway 55, Medina MN | No.) |
| (Address of principal executive offices) | 55340 |

(763) 542-0500
(Registrant's telephone number, including area code)
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No * Indicate by check mark whether the registrant has submitted electronically, if any, every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes x No *
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one): Large accelerated filerx Accelerated filer
Non-accelerated filer " Smaller reporting company "
Emerging growth company ${ }^{*}$

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If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange
Act). Yes ${ }^{\text {. }}$ No x
APPLICABLE ONLY TO CORPORATE ISSUERS:
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.
As of April 17, 2019, 61,070,643 shares of Common Stock, $\$ .01$ par value, of the registrant were outstanding.

1

## Table of Contents

POLARIS INDUSTRIES INC.
FORM 10-Q
For Quarterly Period Ended March 31, 2019
Page
Part I FINANCIAL INFORMATION
Item 1 - Financial Statements ..... $\underline{3}$
Consolidated Balance Sheets ..... $\underline{3}$
Consolidated Statements of Income ..... 4
Consolidated Statements of Comprehensive Income ..... 5
Consolidated Statements of Equity ..... 6
Consolidated Statements of Cash Flows ..... 7
Notes to Consolidated Financial Statements ..... ㅇ
Item 2 - Management's Discussion and Analysis of ..... $\underline{23}$Financial Condition and Results of Operations
Results of Operations ..... $\underline{23}$Liquidity and Capital Resources
$\underline{27}$Inflation and Foreign Exchange Rates
Critical Accounting Policies$\underline{30}$
Note Regarding Forward Looking Statements ..... $\underline{31}$
Item 3 - Quantitative and Qualitative Disclosures$\underline{31}$
About Market Risk31
Part II OTHER INFORMATION
Item 1 - Legal Proceedings ..... $\underline{32}$
Item 1A - Risk Factors ..... 32
Item 2 - Unregistered Sales of Equity Securities and
Use of Proceeds ..... 33
Item 4 - Mine Safety Disclosures ..... $\underline{33}$
Item 6 - Exhibits ..... 33
SIGNATURES ..... 34

2

## Table of Contents

## Part I FINANCIAL INFORMATION

Item 1 - FINANCIAL STATEMENTS
POLARIS INDUSTRIES INC.
CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)
March 31, December 2019 31, 2018 (Unaudited)
Assets
Current assets:
Cash and cash equivalents $\quad \$ 151,439 \quad \$ 161,164$
Trade receivables, net
Inventories, net
206,812 197,082

Prepaid expenses and other
Income taxes receivable
Total current assets
Property and equipment, net
1,148,637 969,511

Investment in finance affiliate
106,512 121,472
25,550 36,474

Deferred tax assets
1,638,950 1,485,703

Goodwill and other intangible assets, net
868,128 843,122

Goodwill and other intangible assets, net
99,501 92,059

Operating lease assets
Other long-term assets
88,489 87,474

Total assets
1,506,414 1,517,594

Liabilities and Shareholders' Equity
Current liabilities:
Current portion of debt, finance lease obligations and notes payable \$66,512 \$66,543
Accounts payable
436,938 346,294
Accrued expenses:
Compensation $\quad 92,107 \quad 167,857$
Warranties 116,217 121,824
Sales promotions and incentives 167,621
Dealer holdback 125, 12,705 125,003
$\begin{array}{ll}\text { Other } & \text { 197,687 }\end{array}$
Current operating lease liabilities
Income taxes payable
34,814 -

Total current liabilities
Long-term income taxes payable
Finance lease obligations
Long-term debt
Deferred tax liabilities
Long-term operating lease liabilities
Other long-term liabilities
5,144 4,545
1,248,108 1,197,374

Total liabilities
29,379 28,602

Deferred compensation
15,926 16,140
2,018,844 1,879,887

Shareholders' equity:
Preferred stock $\$ 0.01$ par value, 20,000 shares authorized, no shares issued and outstanding -
Common stock $\$ 0.01$ par value, 160,000 shares authorized, 61,051 and 60,890 shares issued $\$ 611$
and outstanding, respectively
$\begin{array}{lll}\text { Additional paid-in capital } & 820,788 & 807,986\end{array}$

| Retained earnings | 127,513 | 121,114 |
| :--- | :--- | :--- |
| Accumulated other comprehensive loss, net | $(69,710$ | $)(62,973$ |
| Total shareholders' equity | 879,202 | 866,736 |
| Noncontrolling interest | 297 | 279 |
| Total equity | 879,499 | 867,015 |
| Total liabilities and equity | $\$ 4,408,717$ | $\$ 4,124,915$ |

The accompanying footnotes are an integral part of these consolidated statements.
3

## Table of Contents

## POLARIS INDUSTRIES INC.

CONSOLIDATED STATEMENTS OF INCOME
(In thousands, except per share data)
(Unaudited)

Sales
Cost of sales
Three months ended March 31, 20192018

Gross profit
\$1,495,690 \$1,297,473

Operating expenses:
Selling and marketing
Research and development
1,143,242 973,992
352,448 323,481

General and administrative
129,259 117,707

General and administrative $\quad 92,938 \quad$ 78,693
Total operating expenses
Income from financial services
289,317 261,630

Operating income
18,805 21,425
Non-operating expense:
Interest expense
81,936 83,276

Equity in loss of other affiliates
Other income, net
Income before income taxes
Provision for income taxes
20,419 8,048
$606 \quad 21,511$

Net income
Net income attributable to noncontrolling interest
Net income attributable to Polaris Industries Inc.
Net income per share attributable to Polaris Industries Inc. common shareholders:
Basic
$\$ 0.79$
\$0.88
Diluted $\quad \$ 0.78 \quad \$ 0.85$
Weighted average shares outstanding:
Basic
61,284 63,303
Diluted
$62,027 \quad 65,219$

The accompanying footnotes are an integral part of these consolidated statements.
4

## Table of Contents

POLARIS INDUSTRIES INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In thousands)
(Unaudited)

Net income
Three months ended March 31,
20192018
Other comprehensive income, net of tax:
Foreign currency translation adjustments
\$48,396 \$55,714

Unrealized gain (loss) on derivative instruments
(3,662 ) 10,978
Retirement plan and other activity
Comprehensive income
(2,469 ) 4,529
41,659 71,306
Comprehensive income attributable to noncontrolling interest (18 ) -
Comprehensive income attributable to Polaris Industries Inc. \$41,641 \$71,306
The accompanying footnotes are an integral part of these consolidated statements.

## Table of Contents

## POLARIS INDUSTRIES INC.

CONSOLIDATED STATEMENTS OF EQUITY
(In thousands, except per share data)
(Unaudited)

|  | Number of Shares | $\begin{aligned} & \text { Comm } \\ & \text { Stock } \end{aligned}$ | Additional <br> Paid- <br> In Capital | Retained Earnings | Accumulated Comprehens Income (loss) |  | HSn Contro Interes | Total <br> Equity |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Balance, December 31, 2018 | 60,890 | \$ 609 | \$807,986 | \$ 121,114 | \$ (62,973 |  | \$ 279 | \$867,015 |
| Employee stock compensation | 214 | 2 | 12,089 | - | - |  | - | 12,091 |
| Deferred compensation | - | - | (1,541 | (346 | - |  | - | (1,887 |
| Proceeds from stock issuances under employee plans | 18 | - | 3,207 | - | - |  | - | 3,207 |
| Cash dividends declared | - | - | - | (37,144 | - |  | - | (37,144 |
| Repurchase and retirement of common shares | (71 | - | (953 | ) (5,157 | ) - |  | - | (6,110 |
| Cumulative effect of adoption of accounting standards (ASU 2018-02) |  | - | - | 668 | (668 | ) | - | - |
| Net income | - | - | - | 48,378 | - |  | 18 | 48,396 |
| Other comprehensive loss | - | - | - | - | (6,069 |  | - | (6,069 |
| Balance, March 31, 2019 | 61,051 | 611 | 820,788 | 127,513 | (69,710 | ) | 297 | 879,499 |
|  | Number of Share | r Com es Stock | Addition <br> Paid- <br> In Capit | Retained Earnings | Accumula Comprehe Income (l |  | Othion <br> e Cont <br> Intere | Total Equity |
| Balance, December 31, 2017 | 63,075 | \$ 631 | \$733,894 | \$ \$242,763 | \$ (45,629 |  | ) \$ | -\$931,659 |
| Employee stock compensation | (5 | ) - | 12,032 | - | - |  | - | 12,032 |
| Deferred compensation | - | - | (392 | ) 812 | - |  | - | 420 |
| Proceeds from stock issuances under employee plans | 161 | 2 | 11,903 | - | - |  | - | 11,905 |
| Cash dividends declared | - | - | - | (37,796 | ) - |  | - | (37,796 |
| Repurchase and retirement of common shares | $\mathrm{nn}_{(133}$ | ) (2 | ) $(1,549$ | ) (13,436 | ) - |  | - | (14,987 |
| Cumulative effect of adoption of accounting standards (ASU 2016-16) | - | - | - | (1,077 | ) - |  | - | (1,077 |
| Net income | - | - | - | 55,714 | - |  | - | 55,714 |
| Other comprehensive loss | - | - | - | - | 15,592 |  | - | 15,592 |
| Balance, March 31, 2018 | 63,098 | 631 | 755,888 | 246,980 | (30,037 |  | ) - | 973,462 |

The accompanying footnotes are an integral part of these consolidated statements.

## Table of Contents

## POLARIS INDUSTRIES INC. CONSOLIDATED STATEMENTS OF CASH FLOWS <br> (In thousands) <br> (Unaudited)

Three months ended March 31, 20192018
Operating Activities:
Net income
$\$ 48,396 \quad \$ 55,714$
Adjustments to reconcile net income to net cash used for operating activities:
Depreciation and amortization
54,415 52,720
Noncash compensation $12,091 \quad 12,032$
Noncash income from financial services
Deferred income taxes
Impairment charges
$(7,655)(7,003$
(1,329 ) 113

Other, net
606 (10,700 )
Changes in operating assets and liabilities:
Trade receivables
Inventories
Accounts payable
Accrued expenses
Income taxes payable/receivable
Prepaid expenses and others, net
Net cash used for operating activities
Investing Activities:
Purchase of property and equipment
(70,254 ) (55,558 )
Investment in finance affiliate, net
Investment in other affiliates, net
Net cash used for investing activities
213256

Financing Activities:
Borrowings under debt arrangements / finance lease obligations
Repayments under debt arrangements / finance lease obligations
Repurchase and retirement of common shares
Cash dividends to shareholders
Proceeds from stock issuances under employee plans
Net cash provided by financing activities
Impact of currency exchange rates on cash balances
Net increase (decrease) in cash, cash equivalents and restricted cash
Cash, cash equivalents and restricted cash at beginning of period
Cash, cash equivalents and restricted cash at end of period
Supplemental Cash Flow Information:
Interest paid on debt borrowings
\$22,951 \$7,626

Income taxes paid
\$2,938 \$1,807
The following presents the classification of cash, cash equivalents and restricted cash within the consolidated balance sheets:
Cash and cash equivalents
\$151,439 \$166,357
Other long-term assets
32,041 24,990

The accompanying footnotes are an integral part of these consolidated statements.
7

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## Table of Contents

## POLARIS INDUSTRIES INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Significant Accounting Policies
Basis of presentation. The accompanying unaudited consolidated financial statements of Polaris Industries Inc. ("Polaris" or the "Company") have been prepared in accordance with accounting principles generally accepted in the United States for interim financial statements and, therefore, do not include all information and disclosures of results of operations, financial position and changes in cash flow in conformity with accounting principles generally accepted in the United States for complete financial statements. Accordingly, such statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2018 previously filed with the Securities and Exchange Commission ("SEC"). In the opinion of management, such statements reflect all adjustments (which include only normal recurring adjustments) necessary for a fair presentation of the financial position, results of operations, equity, and cash flows for the periods presented. Due to the seasonality trends for certain products and to certain changes in production and shipping cycles, results of such periods are not necessarily indicative of the results to be expected for the complete year.
Reclassifications. Certain reclassifications of previously reported balance sheet amounts have been made to conform to the current year presentation. The reclassifications had no impact on the consolidated statements of income, cash flows, or total assets, total liabilities, or total equity in the consolidated balance sheets, as previously reported. Fair value measurements. Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Assets and liabilities measured at fair value are classified using the following hierarchy, which is based upon the transparency of inputs to the valuation as of the measurement date: Level 1 - Quoted prices in active markets for identical assets or liabilities.
Level 2 - Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.
In making fair value measurements, observable market data must be used when available. When inputs used to measure fair value fall within different levels of the hierarchy, the level within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value measurement. The Company utilizes the market approach to measure fair value for its non-qualified deferred compensation assets and liabilities, and the income approach for foreign currency contracts, interest rate contracts, and commodity contracts. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities, and for the income approach, the Company uses significant other observable inputs to value its derivative instruments used to hedge foreign currency, interest rate, and commodity transactions.

## Table of Contents

Assets and liabilities measured at fair value on a recurring basis are summarized below (in thousands): Fair Value Measurements as of March 31, 2019

| Asset (Liability) | Total | Level 1 | Level 2 | Level 3 |  |
| :--- | :--- | :--- | :--- | :--- | :--- |
| Non-qualified deferred compensation assets | $\$ 48,330$ | $\$ 48,330$ | $\$-$ | $\$$ | - |
| Foreign exchange contracts, net | 1,976 | - | 1,976 | - |  |
| Total assets at fair value | $\$ 50,306$ | $\$ 48,330$ | $\$ 1,976$ | $\$$ | - |
| Non-qualified deferred compensation liabilities $\$(48,330$ | $)$ | $\$(48,330$ | $)$ | $\$-$ | $\$$ |
| Interest rate contracts, net | $(4,743$ | $)$ | - | $(4,743$ | $)$ |
| Total liabilities at fair value | $\$(53,073$ | $)$ | $\$(48,330$ | $)$ | $\$(4,743$ |
|  |  |  |  |  |  |

$\left.\begin{array}{llllll}\text { Asset (Liability) } & \text { Total } & \text { Level 1 } & \text { Level 2 } & \text { Level } 3 \\ \text { Non-qualified deferred compensation assets } & \$ 48,545 & \$ 48,545 & \$- & \$ & - \\ \text { Foreign exchange contracts, net } & 3,128 & - & 3,128 & - & \\ \text { Total assets at fair value } & \$ 51,673 & \$ 48,545 & \$ 3,128 & \$ & - \\ \text { Non-qualified deferred compensation liabilities } \$(48,545 & ) & \$(48,545 & ) & \$- & \$ \\ \text { Interest rate contracts, net } & (2,665 & ) & - & (2,665 & ) \\ \text { Total liabilities at fair value } & \$(51,210 & ) & \$(48,545 & ) & \$(2,665\end{array}\right) \$$

Fair value of other financial instruments. The carrying values of the Company's short-term financial instruments, including cash and cash equivalents, trade receivables and short-term debt, including current maturities of long-term debt, finance lease obligations and notes payable, approximate their fair values. At March 31, 2019 and December 31, 2018, the fair value of the Company's long-term debt, finance lease obligations and notes payable was approximately $\$ 2,164,529,000$ and $\$ 2,013,684,000$, respectively, and was determined primarily using Level 2 inputs, including quoted market prices or discounted cash flows based on quoted market rates for similar types of debt. The carrying value of long-term debt, finance lease obligations and notes payable including current maturities was $\$ 2,101,282,000$ and $\$ 1,962,570,000$ as of March 31, 2019 and December 31, 2018, respectively.
Inventories. Inventory costs include material, labor and manufacturing overhead costs, including depreciation expense associated with the manufacture and distribution of the Company's products. Inventories are stated at the lower of cost (first-in, first-out method) or net realizable value. The major components of inventories are as follows (in thousands):

$$
\begin{array}{ll}
\text { March 31, } & \text { December } \\
2019 & 31,2018
\end{array}
$$

Raw materials and purchased components \$280,249 \$233,258
Service parts, garments and accessories 355,042 342,593
Finished goods 565,601 442,003
Less: reserves $\quad(52,255)(48,343)$
Inventories
\$1,148,637 \$969,511
Product warranties. Polaris provides a limited warranty for its vehicles and boats for a period of six months to ten years, depending on the product. Polaris provides longer warranties in certain geographical markets as determined by local regulations and market conditions and may also provide longer warranties related to certain promotional programs. Polaris' standard warranties require the Company or its dealers to repair or replace defective products during such warranty periods at no cost to the consumer. The warranty reserve is established at the time of sale to the dealer or distributor based on management's best estimate using historical rates and trends. The Company records these amounts as a liability in the consolidated balance sheet until they are ultimately paid. Adjustments to the warranty reserve are made from time to time based on actual claims experience in order to properly estimate the amounts necessary to settle future and existing claims on products sold as of the balance sheet date. Factors that could have an impact on the warranty reserve in any given period include the following: change in manufacturing quality, shifts in product mix, changes in warranty coverage periods, snowfall and its impact on snowmobile usage, product recalls and any significant changes in sales volume.

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## Table of Contents

The activity in the warranty reserve during the periods presented was as follows (in thousands): Three months ended March 31,
20192018
Balance at beginning of period $\$ 121,824$ \$123,840
Additions charged to expense $26,019 \quad 16,031$
Warranty claims paid, net (31,626 ) (23,585 )
Balance at end of period \$116,217 \$116,286
New accounting pronouncements.
Leases. In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) and in July 2018, ASU No. 2018-10, Codification Improvements to Topic 842, Leases, and ASU 2018-11, Leases (Topic 842) - Targeted Improvements (collectively, "the new lease standard" or "ASC 842"). The new standard requires lessees to record assets and liabilities on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the income statement. The Company adopted the standard as of January 1, 2019 using the alternative transition method provided under ASC 842, which allowed the Company to initially apply the new lease standard at the adoption date. The Company elected the package of practical expedients permitted under the transition guidance within the new standard, which among other things, allowed the Company to carry forward the historical lease classification. The Company did not elect the hindsight practical expedient permitted under the transition guidance within the new lease standard.
The Company made an accounting policy election to not record leases with an initial term of 12 months or less on the balance sheet. The Company also elected the practical expedient to not separate non-lease components from the lease components to which they relate, and instead account for each separate lease and non-lease component associated with that lease component as a single lease component for all underlying asset classes. Accordingly, all costs associated with a lease contract are accounted for as lease cost.
The new standard resulted in the recognition of additional net lease assets and lease liabilities of approximately $\$ 115,681,000$ as of January 1, 2019. The adoption of ASC 842 did not have a material impact on the Company's consolidated results of operations, equity or cash flows as of the adoption date. Under the alternative method of adoption, comparative information was not restated, but will continue to be reported under the standards in effect for those periods. See Note 10 for further information regarding the Company's leases.
Derivatives and hedging. Effective January 1, 2019, the Company adopted ASU No. 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities. The adoption of this ASU did not have a material impact on the Company's consolidated financial position, results of operations, equity or cash flows.
Non-employee share-based payments. Effective January 1, 2019, the Company adopted ASU
No. 2018-07, Compensation - Stock Compensation (Topic 718): Improvements to Non-employee Share-based Payment Accounting. The adoption of this ASU did not have a material impact on the Company's consolidated financial position, results of operations, equity or cash flows.
Intangibles-Goodwill and Other. Effective January 1, 2019, the Company early adopted ASU
2017-04, Intangibles-Goodwill and Other (Topic 350). The new standard simplifies the subsequent measurement of goodwill by eliminating the second step of the goodwill impairment test.
Stranded Tax Effects. Effective January 1, 2019 the Company adopted ASU No. 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, which allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the reduction of the U.S. federal statutory income tax rate to $21 \%$ from $35 \%$ due to the enactment of the Tax Cuts and Jobs Act of 2017 (the "Tax Act"). As a result of the adoption of ASU 2018-02, the Company recorded a $\$ 668,000$ reclassification to decrease Accumulated Other Comprehensive Income and increase Retained Earnings.
Financial instruments. In June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, and in November 2018 issued a subsequent

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amendment, ASU 2018-19, Codification Improvements to Topic 326, Financial Instruments - Credit Losses. ASU 2016-13 significantly changes how entities will measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income. ASU 2016-13 will replace today's "incurred loss" approach with an "expected loss" model for instruments measured at amortized cost. ASU 2018-19 will affect loans, debt securities, trade receivables, net investments in

## Table of Contents

leases, off balance sheet credit exposures, reinsurance receivables, and any other financial assets not excluded from the scope of this amendment that have the contractual right to receive cash. ASU 2016-13 is effective for fiscal years and interim periods beginning after December 15, 2019, and is effective for the Company's fiscal year beginning January 1, 2020. The adoption of the ASU is not expected to have a material impact on the Company's consolidated financial position, results of operations, equity or cash flows.
There are no other new accounting pronouncements that are expected to have a significant impact on the Company's consolidated financial statements.

Note 2. Revenue Recognition
The following tables disaggregate the Company's revenue by major product type and geography (in thousands):
Three months ended March 31, 2019

|  | ORV / Motorcycles <br> Snowmobiles | Global <br> Adj. <br> Markets | Aftermarket Boats |
| :--- | :--- | :--- | :--- | :--- | :--- | Consolidated

Revenue by geography
United States
Canada
EMEA
APLA
Total revenue

| \$708,870 | \$ 67,897 | \$51,683 | \$ 211,616 | \$180,860 | \$ 1,220,926 |
| :---: | :---: | :---: | :---: | :---: | :---: |
| 51,631 | 6,021 | 1,053 | 8,919 | 3,950 | 71,574 |
| 78,726 | 30,716 | 51,403 | - | - | 160,845 |
| 28,220 | 13,308 | 817 | - | - | 42,345 |
| \$867,447 | \$ 117,942 | \$ 104,956 | \$ 220,535 | \$184,810 | \$ 1,495,690 |
| Three months ended March 31, 2018 |  |  |  |  |  |
| ORV / Snowmobiles Motorcycles |  | Global |  |  |  |
|  |  | Adj. <br> Markets | Aftermark | Boats Con | nsolidated |

Revenue by product type

| Wholegoods | $\$ 683,504$ | $\$ 114,108$ | $\$ 92,012$ | - | $\$$ | $\$ 889,624$ |
| :--- | :--- | :--- | :--- | :--- | :--- | :---: |
| PG\&A | 149,060 | 17,449 | 21,315 | $\$ 220,025$ | - | 407,849 |
| Total revenue | $\$ 832,564$ | $\$ 131,557$ | $\$ 113,327$ | $\$ 220,025$ | $\$$ | $\$ 1,297,473$ |

Revenue by geography

| United States | $\$ 662,595$ | $\$ 83,897$ | $\$ 50,053$ | $\$ 210,994$ | $\$$ | $\$ 1,007,539$ |
| :--- | :--- | :--- | :--- | :--- | :--- | :--- |
| Canada | 57,755 | 6,940 | 5,369 | 9,031 | - | 79,095 |
| EMEA | 78,929 | 26,671 | 56,921 | - | - | 162,521 |
| APLA | 33,285 | 14,049 | 984 | - | - | 48,318 |
| Total revenue | $\$ 832,564$ | $\$ 131,557$ | $\$ 113,327$ | $\$ 220,025$ | $\$$ | $\$ 1,297,473$ |

Revenue is recognized when obligations under the terms of a contract with the Company's customer are satisfied which generally occurs with the transfer of control of the wholegood vehicles, boats, parts, garments or accessories, and upon completion of the service or over the term of the agreement in proportion to the costs expected to be incurred in satisfying the obligations under the contract, for services. Revenue is measured as the amount of consideration the Company expects to receive in exchange for transferring goods or providing services. Sales, value add, and other taxes the Company collects concurrent with revenue-producing activities are excluded from revenue. Incidental items that are immaterial in the context of the contract are recognized as expense. The expected costs associated with the Company's limited warranties and field service bulletin actions continue to be recognized as expense when the products are sold. The Company recognizes revenue for vehicle service contracts that extend
mechanical and maintenance beyond the Company's limited warranties over the life of the contract. Revenue from goods and services transferred to customers at a point-in-time accounts for the majority of the Company's revenue. Revenue from products or services transferred over time is discussed in the deferred revenue section.

# Edgar Filing: POLARIS INDUSTRIES INC/MN - Form 10-Q 

## Table of Contents

ORV/Snowmobiles, Motorcycles and Global Adjacent Markets segments
Wholegood vehicles and parts, garments and accessories. For the majority of wholegood vehicles, parts, garments and accessories (PG\&A), the Company transfers control and recognizes a sale when it ships the product from its manufacturing facility, distribution center, or vehicle holding center to its customer (primarily dealers and distributors). The amount of consideration the Company receives and revenue it recognizes varies with changes in marketing incentives and rebates it offers to its dealers and their customers. Sales returns are not material. The Company adjusts its estimate of revenue at the earlier of when the most likely amount of consideration it expects to receive changes or when the consideration becomes fixed.
Depending on the terms of the arrangement, the Company may also defer the recognition of a portion of the consideration received because it has to satisfy a future obligation (e.g., free extended service contracts). The Company uses an observable price to determine the stand-alone selling price for separate performance obligations. The Company has elected to recognize the cost for freight and shipping when control over vehicles, parts, garments or accessories has transferred to the customer as an expense in cost of sales.
Extended Service Contracts. The Company sells separately-priced service contracts that extend mechanical and maintenance coverages beyond its base limited warranty agreements to vehicle owners. The separately priced service contracts range from 12 months to 84 months. The Company primarily receives payment at the inception of the contract and recognizes revenue over the term of the agreement in proportion to the costs expected to be incurred in satisfying the obligations under the contract.

## Aftermarket segment

The Company's Aftermarket products are sold through dealer, distributor, retail, and e-commerce channels. The Company transfers control and recognizes a sale when products are shipped or delivered to its customer. The amount of consideration the Company receives and revenue it recognizes varies with changes in marketing incentives and rebates it offers to its customers and their customers. When the Company gives its customers the right to return eligible parts and accessories, it estimates the expected returns based on an analysis of historical experience. The Company adjusts its estimate of revenue at the earlier of when the most likely amount of consideration it expects to receive changes or when the consideration becomes fixed.
Service revenue. The Company offers installation services for parts that it sells. Service revenues are recognized upon completion of the service.
Depending on the terms of the arrangement, the Company may also defer the recognition of a portion of the consideration received because it has to satisfy a future obligation (e.g., extended service contracts). The Company uses an observable price to determine the stand-alone selling price for separate performance obligations. The Company has elected to recognize the cost for freight and shipping when control over parts, garments or accessories has transferred to the customer as an expense in cost of sales.
Boats segment
Boats. For the majority of boats, the Company transfers control and recognizes a sale when it ships the product from its manufacturing facility or distribution center to its customer (primarily dealers). The amount of consideration the Company receives and revenue it recognizes varies with changes in marketing incentives and rebates it offers to its dealers and their customers. Sales returns are not material. The Company adjusts its estimate of revenue at the earlier of when the most likely amount of consideration it expects to receive changes or when the consideration becomes fixed. The Company has elected to recognize the cost for freight and shipping when control over boats has transferred to the customer as an expense in cost of sales.
Deferred revenue
In 2016, Polaris began financing its self-insured risks related to extended service contracts ("ESCs"). The premiums for ESCs are primarily recognized in income in proportion to the costs expected to be incurred over the contract period. Warranty costs are recognized as incurred.

## Table of Contents

The Company expects to recognize approximately $\$ 27,219,000$ of the unearned amount over the next 12 months and $\$ 36,281,000$ thereafter. The activity in the deferred revenue reserve during the periods presented was as follows (in thousands):

(1) The unamortized ESC premiums (deferred revenue) recorded in other current liabilities totaled \$27,219,000 and $\$ 20,510,000$ at March 31, 2019 and 2018, respectively, while the amount recorded in other long-term liabilities totaled $\$ 36,281,000$ and $\$ 28,835,000$ at March 31, 2019 and 2018, respectively.

Note 3. Acquisitions
2019 Acquisitions.
The Company did not complete any acquisitions in the first quarter of 2019.
2018 Acquisitions.

## Boat Holdings, LLC

On July 2, 2018, pursuant to the Agreement and Plan of Merger dated May 29, 2018, the Company completed the acquisition of Boat Holdings, LLC, a privately held Delaware limited liability company, headquartered in Elkhart, Indiana which manufactures boats ("Boat Holdings").
The transaction was structured as an acquisition of $100 \%$ of the outstanding equity interests in Boat Holdings for aggregate consideration of $\$ 806,658,000$, net of cash acquired, subject to customary adjustments based on, among other things, the amount of cash, debt and working capital in the business of Boat Holdings at the closing date. A portion of the aggregate consideration equal to $\$ 100,000,000$ will be paid in the form of a series of deferred annual payments over 12 years following the closing date.
The Company funded the purchase price for the acquisition by amending, extending, and up-sizing the Credit Facility and with the proceeds of the issuance of $4.23 \%$ Senior Notes, Series 2018, due July 3, 2028, described in Note 5.
The consolidated statements of income for the three months ended March 31, 2019 include $\$ 184,810,000$ of net sales and $\$ 36,164,000$ of gross profit related to Boat Holdings.
The following table summarizes the preliminary fair values assigned to the Boat Holdings net assets acquired and the determination of net assets (in thousands):
Cash and cash equivalents $\$ 16,534$
Trade receivables 17,528
Inventory 39,758
Other current assets 4,487
Property, plant and equipment 35,299
Customer relationships 341,080
Trademarks / trade names 210,680
Non-compete agreements 2,630
Goodwill 212,232
Accounts payable (30,064 )
Other liabilities assumed (26,972 )
Total fair value of net assets acquired 823,192
Less cash acquired (16,534 )
Total consideration for acquisition, less cash acquired $\$ 806,658$

On the acquisition date, amortizable intangible assets had a weighted-average useful life of approximately 19 years. The customer relationships were valued based on the Discounted Cash Flow Method and are amortized over 15-20 years,

13

## Table of Contents

depending on the customer class. The trademarks and trade names were valued on the Relief from Royalty Method and have indefinite remaining useful lives. Goodwill is deductible for tax purposes.
The following unaudited pro forma information represents the Company's results of operations as if the fiscal 2018 acquisition of Boat Holdings had occurred at the beginning of fiscal 2018 (in thousands, except per share data).

Three months ended
March 31,
20192018
Sales
Net income
\$1,495,690 \$1,462,115
49,180 61,890
Basic earnings per share $\quad \$ 0.80 \quad \$ 0.98$
Diluted earnings per common share $\$ 0.79 \quad \$ 0.95$
The results for the quarter ended March 31, 2019 have been adjusted to exclude the impact of approximately $\$ 1,053,000$ of transaction related costs (pre-tax) incurred by the Company that are directly attributable to the transaction.
The results for the quarter ended March 31, 2018 have been adjusted to include the pro forma impact of amortization of intangible assets and the depreciation of property, plant, and equipment, based on purchase price allocations; the pro forma impact of additional interest expense relating to the acquisition; and the pro forma tax effect of both income before taxes and the pro forma adjustments. These performance results may not be indicative of the actual results that would have occurred under the ownership and management of the Company.
The pro forma financial information has been prepared for comparative purposes only and includes certain adjustments, as noted above. The adjustments are estimates based on currently available information and actual amounts may differ materially from these estimates. They do not reflect the effect of costs or synergies that would have been expected to result from the integration of the Boat Holdings acquisition.

Note 4. Share-Based Compensation
The amount of compensation cost for share-based awards to be recognized during a period is based on the portion of the awards that are ultimately expected to vest. The Company estimates forfeitures at the time of grant and revises those estimates in subsequent periods if actual forfeitures differ from those estimates. The Company analyzes historical data to estimate pre-vesting forfeitures and records share-based compensation expense for those awards expected to vest.
Total share-based compensation expenses were comprised as follows (in thousands):

## Three months

ended March
31,
20192018
Option awards
\$1,312 \$3,057
Other share-based awards
9,618 5,889
Total share-based compensation before tax
10,930 8,946
Tax benefit
2,601 2,129
Total share-based compensation expense included in net income $\$ 8,329 \$ 6,817$
In addition to the above share-based compensation expenses, Polaris sponsors a qualified non-leveraged employee stock ownership plan (ESOP). Shares allocated to eligible participants' accounts vest at various percentage rates based on years of service and require no cash payments from the recipient.
At March 31, 2019, there was $\$ 138,467,000$ of total unrecognized share-based compensation expense related to unvested share-based equity awards. Unrecognized share-based compensation expense is expected to be recognized over a weighted-average period of 1.92 years. Included in unrecognized share-based compensation expense is approximately $\$ 43,469,000$ related to stock options and $\$ 94,998,000$ for restricted stock.

## Table of Contents

Note 5. Financing Agreements
The carrying value of debt, finance lease obligations, and notes payable and the average related interest rates were as follows (in thousands):

|  | Average interest rate at March 31, 2019 | Maturity | $\begin{aligned} & \text { March 31, } \\ & 2019 \end{aligned}$ | December <br> 31, 2018 |
| :---: | :---: | :---: | :---: | :---: |
| Revolving loan facility | 3.16\% | July 2023 | \$342,640 | \$187,631 |
| Term loan facility | 3.75\% | July 2023 | 1,135,000 | 1,150,000 |
| Senior notes-fixed rate | 4.60\% | May 2021 | 75,000 | 75,000 |
| Senior notes-fixed rate | 3.13\% | December 2020 | 100,000 | 100,000 |
| Senior notes-fixed rate | 4.23\% | July 2028 | 350,000 | 350,000 |
| Finance lease obligations | 5.08\% | Various through 2029 | 17,219 | 17,587 |
| Notes payable and other | 4.24\% | Various through 2030 | 86,399 | 87,608 |
| Debt issuance costs |  |  | (4,976 | (5,256 |
| Total debt, finance lease obligations, and notes payable |  |  | \$2,101,282 | \$ 1,962,570 |
| Less: current maturities |  |  | 66,512 | 66,543 |
| Total long-term debt, finance lease obligations, and notes payable |  |  | \$2,034,770 | \$1,896,027 |

In July 2018, Polaris amended its unsecured revolving loan facility to increase the facility to $\$ 700,000,000$ and increase its term loan facility to $\$ 1,180,000,000$, of which $\$ 1,135,000,000$ is outstanding as of March 31,2019 . The expiration date of the facility was extended to July 2023, and interest will continue to be charged at rates based on a LIBOR or "prime" base rate. Under the facility, the Company is required to make principal payments totaling $\$ 59,000,000$ over the next 12 months, which are classified as current maturities in the consolidated balance sheets. In December 2010, the Company entered into a Master Note Purchase Agreement to issue $\$ 25,000,000$ of unsecured senior notes due May 2018 and $\$ 75,000,000$ of unsecured senior notes due May 2021 (collectively, the "Senior Notes"). The Senior Notes were issued in May 2011. In December 2013, the Company entered into a First Supplement to Master Note Purchase Agreement, under which the Company issued $\$ 100,000,000$ of unsecured senior notes due December 2020. In July 2018, the Company entered into a Master Note Purchase Agreement to issue $\$ 350,000,000$ of unsecured senior notes due July 2028.
The unsecured revolving loan facility and the amended Master Note Purchase Agreement contain covenants that require Polaris to maintain certain financial ratios, including minimum interest coverage and maximum leverage ratios. Polaris was in compliance with all such covenants at March 31, 2019.
The debt issuance costs are recognized as a reduction in the carrying value of the related long-term debt in the consolidated balance sheets and are being amortized to interest expense in the consolidated statements of income over the expected remaining terms of the related debt.
A property lease agreement for a manufacturing facility which Polaris began occupying in Opole, Poland commenced in February 2014. The Poland property lease is accounted for as a finance lease. The outstanding balance is included in long-term debt and current portion of long-term debt in the consolidated balance sheets.
As a component of the Boat Holdings merger agreement, Polaris has committed to make a series of deferred payments to the former owners following the closing date of of the merger through July 2030. The original discounted payable was for $\$ 76,733,000$, all of which is outstanding as of March 31, 2019. The outstanding balance is included in long-term debt and current portion of long-term debt in the consolidated balance sheets.
The Company has a mortgage note payable agreement for land, on which Polaris built the Huntsville, Alabama manufacturing facility in 2016. The original mortgage note payable was for $\$ 14,500,000$, of which $\$ 9,666,000$ is outstanding as of March 31, 2019. The outstanding balance is included in Notes payable and other. The payment of principal and interest for the note payable is forgivable if the Company satisfies certain job commitments over the term of the note. The Company has met the required commitments to date.

## Table of Contents

Note 6. Goodwill and Other Intangible Assets
Goodwill and other intangible assets, net of accumulated amortization, at March 31, 2019 and December 31, 2018 are as follows (in thousands):

Goodwill
Other intangible assets, net
March 31, December
2019 31, 2018
\$646,453 \$647,077
859,961 870,517
Total goodwill and other intangible assets, net $\$ 1,506,414$ \$1,517,594
Additions to goodwill and other intangible assets in 2018 relate to the acquisition of Boat Holdings in July 2018. The aggregate purchase price was allocated on a preliminary basis to the assets acquired and liabilities assumed based on their estimated fair values at the date of acquisition. Boat Holding's financial results are included in the Company's consolidated results from the date of acquisition. As of March 31, 2019, the purchase price allocation remains preliminary. The pro forma financial results and the preliminary purchase price allocation are included in Note 3. There were no material additions to goodwill and other intangible assets for the three months ended March 31, 2019. The changes in the carrying amount of goodwill for the three months ended March 31, 2019 were as follows (in thousands):

|  | Three <br> months |
| :--- | :--- |
| ended |  |
|  | March 31, |
|  | 2019 |
| Goodwill, beginning of period | $\$ 647,077$ |
| Goodwill adjustments related to businesses acquired | 490 |
| Currency translation effect on foreign goodwill balances | $(1,114$ ) |
| Goodwill, end of period | $\$ 646,453$ |

The components of other intangible assets were as follows (in thousands):
Total estimated life (years)
Non-amortizable—indefinite lived:
Brand/trade names
$\begin{array}{ll}\text { March 31, December 31, } \\ 2019 & 2018\end{array}$

Amortizable:
$\begin{array}{llll}\text { Non-compete agreements } 4 & 2,630 & 2,630\end{array}$
$\begin{array}{llll}\text { Dealer/customer related } & 5-20 & 505,183 & 506,401\end{array}$
$\begin{array}{lll}\text { Developed technology } & 5-7 & 13,279 \\ 13,323\end{array}$
Total amortizable
521,092 522,354
Less: Accumulated amortization
Net amortized other intangible assets
$(103,182)(94,136)$
Total other intangible assets, net
417,910 428,218
\$859,961 \$ 870,517
Amortization expense for intangible assets for the three months ended March 31, 2019 and 2018 was $\$ 10,247,000$ and $\$ 6,126,000$, respectively. Estimated amortization expense for the remainder of 2019 through 2024 is as follows: 2019 (remainder), \$30,630,000; 2020, \$35,820,000; 2021, \$33,050,000; 2022, \$28,070,000; 2023, \$25,540,000; 2024, $\$ 25,010,000$; and after 2024, $\$ 239,790,000$. The preceding expected amortization expense is an estimate and actual amounts could differ due to additional intangible asset acquisitions, changes in foreign currency rates or impairment of intangible assets.

Note 7. Shareholders' Equity
During the three months ended March 31, 2019, Polaris paid $\$ 6,110,000$ to repurchase approximately 71,000 shares of its common stock. As of March 31, 2019, the Board of Directors has authorized the Company to repurchase up to an additional $3,180,000$ shares of Polaris stock. The repurchase of any or all such shares authorized for repurchase will be
governed by applicable SEC rules and dependent on management's assessment of market conditions. Polaris paid a regular cash dividend of $\$ 0.61$ per share on March 15, 2019 to holders of record at the close of business on March 1, 2019.

16

## Table of Contents

Cash dividends declared and paid per common share for the three months ended March 31, 2019 and 2018, were as follows:

> Three
> months
> ended
> March 31,
> 20192018

Cash dividends declared and paid per common share $\$ 0.61 \$ 0.60$
Net income per share
Basic income per share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding during each period, including shares earned under the Deferred Compensation Plan for Directors ("Director Plan") and the ESOP and deferred stock units under the 2007 Omnibus Incentive Plan ("Omnibus Plan"). Diluted income per share is computed under the treasury stock method and is calculated to compute the dilutive effect of outstanding stock options and certain shares issued under the Omnibus Plan. A reconciliation of these amounts is as follows (in thousands):
Three months
ended March
31,
20192018

Weighted average number of common shares outstanding $60,96163,050$
Director Plan and deferred stock units 193166
ESOP $130 \quad 87$
Common shares outstanding—basic 61,284 63,303
Dilutive effect of Omnibus Plan 743 1,916
Common and potential common shares outstanding-dilute 62,027 65,219
During the three months ended March 31, 2019, the number of options that were not included in the computation of diluted income per share because the option exercise price was greater than the market price, and therefore, the effect would have been anti-dilutive, was $4,416,000$ compared to $1,540,000$ for the same period in 2018.
Accumulated other comprehensive loss
Changes in the accumulated other comprehensive loss balance are as follows (in thousands):


The table below provides data about the amount of gains and losses, net of tax, reclassified from accumulated other comprehensive loss into the statements of income for cash flow derivatives designated as hedging instruments for the three months ended March 31, 2019 and 2018 (in thousands):

Derivatives in Cash Flow Hedging
Relationships and Other Activity
Foreign currency contracts
Foreign currency contracts
Interest rate contracts

Location of Gain (Loss) Reclassified from
Accumulated Other Comprehensive Loss into Income
Other expense, net
Cost of sales 55
Interest expense

Three months ended March 31, 20192018 \$1,204 \$157 55 (32 ) (31 ) -

Retirement plan activity
Total
Operating expenses
(62 ) (85 ) of income within the next 12 months is not expected to be material. See Note 12 for further information regarding derivative activities.

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## Table of Contents

## Note 8. Financial Services Arrangements

Polaris Acceptance, a joint venture between Polaris and Wells Fargo Commercial Distribution Finance Corporation, a direct subsidiary of Wells Fargo Bank, N.A. ("Wells Fargo"), which is supported by a partnership agreement between their respective wholly owned subsidiaries, finances substantially all of Polaris' United States sales of snowmobiles, ORVs, motorcycles, and related PG\&A, whereby Polaris receives payment within a few days of shipment of the product.
Polaris' subsidiary has a 50 percent equity interest in Polaris Acceptance. Polaris Acceptance sells a majority of its receivable portfolio to a securitization facility (the "Securitization Facility") arranged by Wells Fargo. The sale of receivables from Polaris Acceptance to the Securitization Facility is accounted for in Polaris Acceptance's financial statements as a "true-sale" under Accounting Standards Codification ("ASC") Topic 860. Polaris' allocable share of the income of Polaris Acceptance has been included as a component of income from financial services in the accompanying consolidated statements of income. The partnership agreement is effective through February 2022. Polaris' total investment in Polaris Acceptance of \$99,501,000 at March 31, 2019 is accounted for under the equity method, and is recorded in investment in finance affiliate in the accompanying consolidated balance sheets. At March 31, 2019, the outstanding amount of net receivables financed for dealers under this arrangement was $\$ 1,272,244,000$, which included $\$ 595,188,000$ in the Polaris Acceptance portfolio and $\$ 677,056,000$ of receivables within the Securitization Facility ("Securitized Receivables").
Polaris has agreed to repurchase products repossessed by Polaris Acceptance up to an annual maximum of 15 percent of the aggregate average month-end outstanding Polaris Acceptance receivables and Securitized Receivables during the prior calendar year. For calendar year 2019, the potential 15 percent aggregate repurchase obligation is approximately $\$ 180,557,000$. Polaris' financial exposure under this arrangement is limited to the difference between the amounts unpaid by the dealer with respect to the repossessed product plus costs of repossession and the amount received on the resale of the repossessed product. No material losses have been incurred under this agreement during the periods presented.
A subsidiary of TCF Financial Corporation ("TCF") finances a portion of Polaris' United States sales of boats whereby Polaris receives payment within a few days of shipment of the product. Polaris has agreed to repurchase products repossessed by TCF up to a maximum of 100 percent of the aggregate outstanding TCF receivables balance. At March 31, 2019, the potential aggregate repurchase obligation was approximately $\$ 270,400,000$. Polaris' financial exposure under this arrangement is limited to the difference between the amounts unpaid by the dealer with respect to the repossessed product plus costs of repossession and the amount received on the resale of the repossessed product. No material losses have been incurred under this agreement during the periods presented.
Polaris has agreements with Performance Finance, Sheffield Financial and Synchrony Bank, under which these financial institutions provide financing to end consumers of Polaris products. Polaris' income generated from these agreements has been included as a component of income from financial services in the accompanying consolidated statements of income.
Polaris also administers and provides extended service contracts to consumers and certain insurance contracts to dealers and consumers through various third-party suppliers. Polaris finances its self-insured risks related to extended service contracts, but does not retain any insurance or financial risk under any of the other arrangements. Polaris' service fee income generated from these arrangements has been included as a component of income from financial services in the accompanying consolidated statements of income.

Note 9. Investment in Other Affiliates
The Company has certain investments in nonmarketable securities of strategic companies. The Company had $\$ 5,527,000$ and $\$ 6,133,000$ of such investments as of March 31, 2019, and December 31, 2018, respectively, and are recorded as a component of other long-term assets in the accompanying consolidated balance sheets.
During 2018, the Company had an investment in Eicher-Polaris Private Limited (EPPL), a joint venture established in 2012 with Eicher Motors Limited ("Eicher") intended to design, develop and manufacture a full range of new vehicles for India and other emerging markets. However, during the first quarter of 2018, the Board of Directors of EPPL approved a shut down of the operations of the EPPL joint venture. As a result of the expected closure, the Company
recognized $\$ 19,630,000$ of costs, including impairment, associated with the wind-down of EPPL for the three months ended March 31, 2018. The investment was fully impaired as of March 31, 2019 and December 31, 2018.
Polaris will impair or write off an investment and recognize a loss if and when events or circumstances indicate there is impairment in the investment that is other-than-temporary. When necessary, Polaris evaluates investments in nonmarketable securities for impairment, utilizing Level 3 fair value inputs.

## Table of Contents

In October 2017, an agreement was signed to sell the assets of Brammo, Inc. to a third party. During the first quarter of 2018 , Polaris received additional distributions from Brammo and recognized a gain of $\$ 13,478,000$, which is included in Other income on the consolidated statements of income.

## Note 10. Leases

The Company leases certain manufacturing facilities, retail stores, warehouses, distribution centers, office space, land, and equipment. Leases with an initial term of 12 months or less are not recorded on the balance sheet; the Company recognizes lease expense for these leases on a straight-line basis over the lease term. The Company does not separate non-lease components from the lease components to which they relate, and instead accounts for each separate lease and non-lease component associated with that lease component as a single lease component for all underlying asset classes.
Some leases include one or more options to renew, with renewal terms that can extend the lease term from one to 20 years or more. The exercise of lease renewal options is at the Company's sole discretion. Certain leases also include options to purchase the leased property. The depreciable life of assets and leasehold improvements are limited by the expected lease term, unless there is a transfer of title or purchase option reasonably certain of exercise. Certain lease agreements include rental payments that are variable based on usage or are adjusted periodically for inflation. The Company's lease agreements do not contain any material residual value guarantees or material restrictive covenants. Information on the Company's leases is summarized as follows (in thousands):

| Classification | March |
| :--- | :--- |
|  | 31,2019 |

Assets
Operating lease assets Operating lease assets \$112,286
Finance lease assets Property and equipment, net ${ }^{(1)} 13,689$
Total leased assets \$125,975
Liabilities
Current
Operating lease liabilities Current operating lease liabilities $\$ 34,814$
Finance lease liabilities Current portion of debt, finance lease obligations and notes payable 1,293
Long-term
Operating lease liabilities Long-term operating lease liabilities 79,736
Finance lease liabilities Finance lease obligations 15,926
Total lease liabilities \$ 131,769
${ }^{(1)}$ Finance lease assets are recorded net of accumulated amortization of \$6,581 as of March 31, 2019.


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2021
2022
2023
Thereafter
Total lease payments
Less: interest
$22,422 \quad 2,113 \quad 24,535$
15,379 $2,076 \quad 17,455$
11,009 2,076 13,085
13,952 11,959 25,911
\$123,299 \$21,939 \$145,238
Present value of lease payments $\$ 114,550 \$ 17,219$
19

## Table of Contents

${ }^{(1)}$ Operating lease payments include $\$ 4,211,000$ related to options to extend lease terms that are reasonably certain of being exercised.

|  | March |
| :--- | :--- |
| Lease Term and Discount Rate | 31, |
|  | 2019 |
| Weighted-average remaining lease term (years) |  |
| Operating leases | 4.43 |
| Finance leases | 10.12 |
| Weighted-average discount rate |  |
| Operating leases | $3.37 \%$ |
| Finance leases | $5.08 \%$ |

Other Information
Three months
ended
March
31,
2019
Cash paid for amounts included in the measurement of lease liabilities Operating cash flows from operating leases
\$ 10,169
Operating cash flows from finance leases 147
Financing cash flows from finance leases 371
Leased assets obtained in exchange for new operating lease liabilities 4,042
Note 11. Commitments and Contingencies
Product liability. Polaris is subject to product liability claims in the normal course of business. The Company carries excess insurance coverage for catastrophic product liability claims. Polaris self-insures product liability claims before the policy date and up to the purchased catastrophic insurance coverage after the policy date. The estimated costs resulting from any losses are charged to operating expenses when it is probable a loss has been incurred and the amount of the loss is reasonably estimable. The Company utilizes historical trends and actuarial analysis tools, along with an analysis of current claims, to assist in determining the appropriate loss reserve levels. At March 31, 2019, the Company had an accrual of $\$ 55,036,000$ for the probable payment of pending claims related to continuing product liability litigation associated with Polaris products. This accrual is included as a component of other accrued expenses in the accompanying consolidated balance sheets.
Litigation. Polaris is a defendant in lawsuits and subject to other claims arising in the normal course of business, including matters related to intellectual property, commercial matters, product liability claims, and putative class action lawsuits. As of March 31, 2019, the Company is party to two putative class actions pending against Polaris in the United States, alleging that certain Polaris products caused personal injury, economic losses, and other damages resulting from unresolved fire hazards and excessive heat hazards. The Company is unable to provide an evaluation of the likelihood that a loss will be incurred or an estimate of the range of possible loss.
In the opinion of management, it is unlikely that any legal proceedings pending against or involving Polaris will have a material adverse effect on Polaris' financial position, results of operations, or cash flows. However, in many of these matters, it is inherently difficult to determine whether a loss is probable or reasonably possible or to estimate the size or range of the possible loss given the variety and potential outcomes of actual and potential claims, the uncertainty of future rulings, the behavior or incentives of adverse parties, and other factors outside of the control of the Company. Accordingly, the Company's loss reserve may change from time to time, and actual losses could exceed the amounts accrued by an amount that could be material to our consolidated financial position, results of operations, or cash flows in any particular reporting period.

Regulatory. In the normal course of business, the Company's products are subject to extensive laws and regulations relating to safety, environmental and other regulations promulgated by the United States federal government and individual states, as well as international regulatory authorities. Failure to comply with applicable regulations could result in fines, penalties or other costs.

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## Table of Contents

Note 12. Derivative Instruments and Hedging Activities
The Company is exposed to certain risks relating to its ongoing business operations. From time to time, the primary risks managed by using derivative instruments are foreign currency risk, interest rate risk and commodity price fluctuations. Derivative contracts on various currencies are entered into in order to manage foreign currency exposures associated with certain product sourcing activities and intercompany cash flows. Interest rate swaps are occasionally entered into in order to maintain a balanced risk of fixed and floating interest rates associated with the Company's long-term debt. Commodity hedging contracts are occasionally entered into in order to manage fluctuating market prices of certain purchased commodities and raw materials that are integrated into the Company's end products. The Company's foreign currency management objective is to mitigate the potential impact of currency fluctuations on the value of its U.S. dollar cash flows and to reduce the variability of certain cash flows at the subsidiary level. The Company actively manages certain forecasted foreign currency exposures and uses a centralized currency management operation to take advantage of potential opportunities to naturally offset foreign currency exposures against each other. The decision of whether and when to execute derivative instruments, along with the duration of the instrument, can vary from period to period depending on market conditions, the relative costs of the instruments and capacity to hedge. The duration is linked to the timing of the underlying exposure, with the connection between the two being regularly monitored. Polaris does not use any financial contracts for trading purposes.
At March 31, 2019 and December 31, 2018, the Company had the following open foreign currency contracts (in thousands):

March 31, 2019 December 31, 2018
Notional Amounts
Notional Amounts
Foreign Currency (in U.S. Net Unrealized Gain (in U.S. Net Unrealized Gain
Dollars) Dollars)
Australian Dollar \$8,729 \$ $57 \quad \$$ -
Canadian Dollar $100,035 \quad 1,062 \quad 55,133 \quad 2,564$
$\begin{array}{llll}\text { Mexican Peso } & 11,570 & 857 & 19,222 \\ 564\end{array}$
Total \$120,334 \$ 1,976 \$74,355 \$ 3,128
These contracts, with maturities through March 2020, met the criteria for cash flow hedges, and are recorded in other current assets or other current liabilities on the consolidated balance sheet. The unrealized gains or losses, after tax, are recorded as a component of accumulated other comprehensive loss in shareholders' equity.
During 2018, the Company entered into interest rate swap transactions to hedge the variable interest rate payments for the Term Loan Facility. In connection with this transaction, the Company pays interest based upon a fixed rate and receives variable rate interest payments based on the one-month LIBOR.
At March 31, 2019 and December 31, 2018, the Company had the following open interest rate swap contracts (in thousands):

Effective Date Termination Date
May 2, 2018
May 4, 2021
March 31, $2019 \quad$ December 31, 2018

September 28, 2018 September 30, 2019 250,000 (221 ) 250,000 (163 )
September 30, 2019 September 30, 2023 150,000 (4,757 ) 150,000 (2,899 )
Total $\$ 425,000 \$(4,743) \$ 425,000 \$(2,665)$
These contracts, with maturities through September 2023, met the criteria for cash flow hedges, and are recorded in other current assets or other current liabilities on the consolidated balance sheet. Assets and liabilities are offset in the consolidated balance sheet if the right of offset exists. The unrealized gains or losses, after tax, are recorded as a component of accumulated other comprehensive loss in shareholders' equity.

## Table of Contents

The table below summarizes the carrying values of derivative instruments as of March 31, 2019 and December 31, 2018 (in thousands):


Gains and losses on derivative instruments representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in the current statement of income.
The amount of gains (losses), net of tax, related to the effective portion of derivative instruments designated as cash flow hedges included in accumulated other comprehensive loss for the three months ended March 31, 2019 and 2018 were $\$(2,469,000)$ and $\$ 4,529,000$, respectively.
See Note 7 for information about the amount of gains and losses, net of tax, reclassified from accumulated other comprehensive loss into the statements of income for derivative instruments designated as hedging instruments. The ineffective portion of foreign currency contracts was not material for the three month period ended March 31, 2019.

## Note 13. Segment Reporting

The Company's reportable segments are based on the Company's method of internal reporting, which generally segregates the operating segments by product line, inclusive of wholegoods and PG\&A. The internal reporting of these operating segments is defined based, in part, on the reporting and review process used by the Company's Chief Executive Officer. The Company has six operating segments: 1) ORV, 2) Snowmobiles, 3) Motorcycles, 4) Global Adjacent Markets, 5) Aftermarket, and 6) Boats, and five reportable segments: 1) ORV/Snowmobiles, 2) Motorcycles, 3) Global Adjacent Markets, 4) Aftermarket, and 5) Boats.

Through June 30, 2018, the Company reported under four segments for segment reporting. However, during the third quarter ended September 30, 2018, as a result of the Boat Holdings acquisition, the Company established a new reporting segment, Boats.
The ORV/Snowmobiles segment includes the aggregated results of the Company's ORV and Snowmobiles operating segments. The Motorcycles, Global Adjacent Markets, Aftermarket, and Boats segments include the results for those respective operating segments. The Corporate amounts include costs that are not allocated to individual segments, which include incentive-based compensation and other unallocated manufacturing costs. Additionally, given the commonality of customers, manufacturing and asset management, the Company does not maintain separate balance sheets for each segment. Accordingly, the segment information presented below is limited to sales and gross profit data (in thousands):

22

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## Table of Contents

|  | Three months ended |  |
| :---: | :---: | :---: |
|  | March 31, |  |
|  | 2019 | 2018 |
| Sales |  |  |
| ORV/Snowmobiles | \$867,447 | \$832,564 |
| Motorcycles | 117,942 | 131,557 |
| Global Adjacent Markets | 104,956 | 113,327 |
| Aftermarket | 220,535 | 220,025 |
| Boats | 184,810 | - |
| Total sales | \$1,495,690 | \$1,297,473 |
| Gross profit |  |  |
| ORV/Snowmobiles | \$252,235 | \$243,561 |
| Motorcycles | 6,962 | 16,568 |
| Global Adjacent Markets | 29,829 | 31,258 |
| Aftermarket | 56,475 | 58,452 |
| Boats | 36,164 | - |
| Corporate | (29,217 | ) $(26,358$ |
| Total gross profit | \$352,448 | \$323,481 |

## Item 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF

 OPERATIONS
## Overview

The following discussion pertains to the results of operations and financial position of Polaris Industries Inc., a Minnesota corporation, for the three month period ended March 31, 2019 compared to the three month period ended March 31, 2018. The terms "Polaris," the "Company," "we," "us," and "our" as used herein refer to the business and operation of Polaris Industries Inc., its subsidiaries and its predecessors, which began doing business in 1954. We design, engineer and manufacture powersports vehicles, which include Off-Road Vehicles (ORV), including all-terrain vehicles (ATV) and side-by-side vehicles; motorcycles; Global Adjacent Markets vehicles, including Commercial, Government, and Defense vehicles; boats; and related Parts, Garments and Accessories (PG\&A), as well as Aftermarket accessories and apparel. Due to the seasonality of certain products and to certain changes in production and shipping cycles, results of such periods are not necessarily indicative of the results to be expected for the complete year.
We reported net income of $\$ 48.4$ million, or $\$ 0.78$ per diluted share, compared to 2018 first quarter net income of $\$ 55.7$ million, or $\$ 0.85$ per diluted share. First quarter sales totaled $\$ 1,495.7$ million, an increase of 15 percent from last year's first quarter sales of $\$ 1,297.5$ million. The sales increase was driven primarily by the acquisition of Boat Holdings in the third quarter of 2018. Our unit retail sales to consumers in North America decreased three percent in the first quarter of 2019. Our first quarter sales to North American customers increased 19 percent, driven by Boats. Our sales to customers outside of North America decreased four percent, primarily driven by foreign exchange movements, partially offset by strong Indian and PG\&A sales.
Our gross profit of $\$ 352.4$ million increased nine percent from $\$ 323.5$ million in the comparable prior year first quarter. The increase in gross profit dollars during the quarter was primarily driven by sales related to the Boats acquisition. The decrease in gross profit margin was driven by tariff costs and the addition of Boats, which has lower gross profit margins, partially offset by higher selling prices. Our liquidity remained adequate with $\$ 151.4$ million of cash on hand and $\$ 357.3$ million of availability on the revolving loan facility at March 31, 2019.

## Results of Operations

Unless otherwise noted, all "quarter" comparisons are from the first quarter of 2019 to the first quarter of 2018. Sales:

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Quarter sales were $\$ 1,495.7$ million, a 15 percent increase from $\$ 1,297.5$ million of quarter sales in the prior year. The consolidated statement of income for the three months ended March 31, 2019 includes $\$ 184.8$ million of sales related to Boat Holdings. The following table is an analysis of the percentage change in total Company sales:

## Table of Contents

|  | Percent change in total <br> Company sales compared <br> to corresponding period <br> of the prior year |
| :--- | :--- |
| Three months ended |  |
| March 31,2019 |  |
| $(4$ | $) \%$ |
| Volume | 6 |
| Product mix and price | 14 |
| Acquisitions | $(1$ |

The volume decrease of four percent is primarily driven by decreased ORV and motorcycle shipments. Product mix and price contributed a six percent increase primarily due to higher average selling prices for ORVs. Acquisitions contributed 14 percent, primarily due to the Boat Holdings acquisition in July 2018.
Our sales by reporting segment, which includes the respective PG\&A, were as follows:
Three months ended March 31,
Percent Percent Percent
(\$ in millions)

ORV/Snowmobiles
Motorcycles
$\begin{array}{llllllll}\$ 867.5 & 58 & \% & \$ 832.6 & 64 & \% & 4 & \%\end{array}$

Global Adjacent Markets $105.0 \quad 7 \quad \% \quad 113.3 \quad 9 \quad \% \quad(7) \%$
$\begin{array}{llllllllll}\text { Aftermarket } & 220.5 & 15 & \% & 220.0 & 17 & \% & - & \%\end{array}$
Boats
$184.812 \%-\quad-\quad \%$
$\begin{array}{llllllllllllll}\text { Total sales } & \$ 1,495.7 & 100 & \% & \$ 1,297.5 & 100 & \% & 15 & \%\end{array}$
ORV/Snowmobiles
ORVs: ORV sales, inclusive of PG\&A sales, of $\$ 827.4$ million in the first quarter of 2019 increased four percent compared to $\$ 794.6$ million in 2018. This increase was driven by higher side-by-side sales, partially offset by lower ATV sales. Polaris North American ORV unit retail sales to consumers decreased mid-single digits percent for the first quarter of 2019 with side-by-side vehicles down low-single digits percent and ATV vehicles down low-double digits percent compared to the comparable prior year period. The Company estimates that North American industry ORV retail sales were down low-single digits percent from the first quarter of 2018. Polaris' North American dealer unit inventory was up mid-single digits percent compared to the first quarter of 2018 . For the first quarter of 2019 , the average ORV per unit sales price increased low-double digits percent compared to the first quarter of 2018's per unit sales price, driven by favorable mix and price increases.
Snowmobiles: Snowmobile sales, inclusive of PG\&A sales, increased six percent to $\$ 40.1$ million for the first quarter of 2019 , compared to $\$ 38.0$ million for the comparable prior year period, primarily due to higher PG\&A sales, partially offset by lower wholegood shipments due to timing. Polaris North American unit retail sales to consumers were up high-single digits percent during the first quarter of 2019 and up approximately 20 percent for the twelve month snowmobile season ending March 2019. The Company estimates that North American industry snowmobile retail sales were up low-double digits percent during the first quarter of 2019 and up low-single digits percent for the snowmobile season ending March 2019. Polaris gained significant market share for the snowmobile season.
Motorcycles
Motorcycle sales, inclusive of PG\&A sales, decreased 10 percent to $\$ 117.9$ million for the first quarter of 2019, compared to $\$ 131.6$ million for the comparable prior year period due to lower Slingshot sales, and to less of an extent, Indian Motorcycle sales, partly due to an ongoing challenging motorcycle market. Polaris North American unit retail sales to consumers decreased high-single digits percent during the first quarter of 2019. Indian Motorcycle retail sales
decreased mid-single digits percent during the quarter. Slingshot's retail sales decreased low-double digits percent during the quarter. The Company estimates North American industry retail sales, 900 cc and above (including Slingshot), decreased mid-single digits percent in 2019. Polaris' North American dealer unit inventory was down mid-single digits percent compared to the first quarter of 2018. The quarter average per unit sales price decreased one percent.

24

## Table of Contents

Global Adjacent Markets
Global Adjacent Markets sales, inclusive of PG\&A sales, decreased seven percent to $\$ 105.0$ million for the first quarter of 2019 , compared to $\$ 113.3$ million for the comparable prior year period, primarily due to decreased sales in our Aixam, Goupil and defense businesses.
Aftermarket
Aftermarket sales, which includes Transamerican Auto Parts (TAP), along with our other aftermarket brands of Klim, Kolpin, ProArmor, Trail Tech and 509, of $\$ 220.5$ million for the first quarter of 2019 were approximately flat compared to the comparable prior year period, due to increased sales in the other aftermarket brands, mostly offset by a two percent decrease in TAP's sales. TAP sales in the quarter were down as a result of lower wholesale sales and e-commerce demand.
Boats
Boat sales were $\$ 184.8$ million in the quarter.
Sales by Geography
Sales by geographic region were as follows:
Three months ended March 31,

| (\$ in millions) | 2019 |  |  | Percent Percent |  |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  |  | of | 2018 |  | Change |
|  |  | Total | 2018 | Total | 2019 vs |
|  |  | Sales |  | Sales | 2018 |
| United States | \$ 1,220.9 | 82 \% | \$ 1,007.6 | 78 \% | 21 \% |
| Canada | 71.6 | 5 \% | 79.1 | 6 \% | (9) \% |
| Other foreign countries | 203.2 | 13 \% | 210.8 | 16 \% | (4 )\% |
| Total sales | \$ 1,495.7 | 100 \% | \$ 1,297.5 | 100 \% | 15 \% |

United States: Sales in the United States for the first quarter of 2019 increased 21 percent compared to 2018, primarily due to the addition of Boat Holdings.
Canada: Sales in Canada for the first quarter of 2019 decreased nine percent compared to 2018, primarily due to unfavorable currency rate movements.
Other foreign countries: Sales in other foreign countries, primarily Europe, decreased four percent compared to 2018. Currency rate movements had an unfavorable impact of seven percent on quarter sales, which was partially offset by strong Indian Motorcycle and PG\&A sales.
Cost of Sales:
(\$ in millions)
Three months ended March 31,

| (\$ in millions) | Three months ended March 31, |  |  |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | 2019 | Percent of Total Cost of Sales |  | 2018 | $\begin{aligned} & \text { Percent of Change } \\ & \text { Total } \\ & \text { Cost of Salys. }{ }_{2019}^{\text {S. }} \text {. } \end{aligned}$ |  |  |
| Purchased materials and services | \$979.2 | 86 | \% | \$844.4 | 87 | \% 16 | 16 \% |
| Labor and benefits | 101.8 | 9 | \% | 81.8 |  | \% 24 | 24 |
| Depreciation and amortization | 36.2 | 3 | \% | 31.7 |  | \% 14 | 14 |
| Warranty costs | 26.0 | 2 | \% | 16.0 |  | \% 62 | 62 |
| Total cost of sales | \$1,143.2 | 100 | \% | \$973.9 |  | \% 17 | 17 |
| Percentage of sales | 76.4 |  |  | 75.1 |  | basis |  |

Cost of sales increased during the quarter due to the addition of Boats, which contributed $\$ 148.6$ million in cost of sales, and tariff costs.

## Table of Contents

Gross Profit:


Consolidated. Consolidated gross profit, as a percentage of sales, decreased in the first quarter of 2019 primarily due to tariff costs and the addition of Boat Holdings, which has lower gross profit margins. We expect additional tariff costs to continue throughout the remainder of 2019 and adversely affect our gross profit.
ORV/Snowmobiles. Gross profit, as a percentage of sales, decreased slightly for the quarter, primarily due to higher tariff costs, partially offset by higher average selling prices and favorable product mix.
Motorcycles. Gross profit, as a percentage of sales, decreased for the quarter, primarily due to lower sales volumes and tariff costs.
Global Adjacent Markets. Gross profit, as a percentage of sales, increased for the quarter, primarily due to favorable mix.

Aftermarket. Gross profit, as a percentage of sales, decreased for the quarter, primarily due to unfavorable mix.
Boats. Segment gross profit, which relates to the Boat Holdings acquisition which closed on July 2, 2018, was $\$ 36.2$ million in the quarter.
Operating Expenses:

| (\$ in millions) | 2019 | 2018 | Change $2019 \text { vs. } 2018$ |
| :---: | :---: | :---: | :---: |
| Selling and marketing | \$129.3 | \$117.7 | 10 |
| Research and development | 67.1 | 65.2 | 3 |
| General and administrative | 92.9 | 78.7 | 18 |
| Total operating expenses | \$289.3 | \$261.6 | 11 |
| Percentage of sales | 19.3 | 20.2 | -82 basis poin |

Operating expenses, in absolute dollars, for the quarter increased primarily due to the Boat Holdings acquisition completed during the third quarter of 2018 and investments in strategic projects. Operating expenses, as a percentage of sales, decreased primarily due to the addition of Boat Holdings which inherently has a lower operating expense to sales ratio.
Income from Financial Services:
Three months ended March 31,
(\$ in millions)
20192018 Change
2019 vs. 2018
Income from financial services \$18.8 \$21.4 (12 )\%
Percentage of sales $\quad 1.3 \quad \% \quad 1.7 \quad \% \quad-39$ basis points
The decrease for the quarter in income from financial services is due to lower retail sales. Further discussion can be found in the "Liquidity and Capital Resources" section below.

## Table of Contents

Remainder of the Statement of Income:
(\$ in millions, except per share data)
Interest expense
Equity in loss of other affiliates
Other income, net
Income before taxes
Provision for income taxes
Effective income tax rate

| Three months ended March 31, |  |  |  |
| :---: | :---: | :---: | :---: |
| 2019 | 2018 | $\begin{aligned} & \text { Change } \\ & 2019 \text { vs. } 2018 \end{aligned}$ |  |
|  |  |  |  |
| \$20.4 | \$8.0 | 155 | \% |
| \$0.6 | \$21.5 | (97 | )\% |
| \$(3.5) | \$(20.0) | (82 | )\% |
| \$64.4 | \$73.7 | (13 | )\% |
| \$ 16.0 | \$ 18.0 | (11 | )\% |
| 24.9 \% | 24.4 \% | +47 pts |  |
| \$48.4 | \$55.7 | (13 | )\% |
| \$0.78 | \$0.85 | (8 | )\% |
| 62.0 | 65.2 | (5 | )\% |

Interest expense: Interest expense increased primarily due to increased debt levels to finance the Boat Holdings acquisition and higher interest rates on our variable interest rate debt.
Equity in loss of other affiliates: Equity in loss of other affiliates decreased in the quarter due to an impairment of our investment in the Eicher-Polaris Private Limited joint venture in the first quarter of 2018.
Other income, net: Other income primarily includes foreign currency exchange rate movements and the corresponding effects on foreign currency transactions related to the Company's foreign subsidiaries. In the first quarter of 2018, in addition to the impact of foreign currency exchange rate movements, the Company reported a $\$ 13.5$ million gain on the sale of the Company's investment in Brammo Inc.
Provision for income taxes: The increase in the effective income tax rates from the prior year period is primarily due to an increase in state taxes as well as a slight decrease in R\&D credits.
Weighted average shares outstanding: Over the time period within and between the comparable periods, weighted average shares outstanding decreased by five percent in the quarter due to share repurchases made in 2018.
Cash Dividends:
We paid a regular cash dividend of $\$ 0.61$ per share on March 15,2019 to holders of record at the close of business on March 1, 2019.

Liquidity and Capital Resources
Our primary sources of funds have been cash provided by operating and financing activities. Our primary uses of funds have been for acquisitions, repurchase and retirement of common stock, capital investment, new product development and cash dividends to shareholders.
We believe that existing cash balances and cash flow to be generated from operating activities and borrowing capacity under the credit facility arrangement will be sufficient to fund operations, new product development, cash dividends, share repurchases and capital requirements for the foreseeable future. At this time, management is not aware of any factors that would have a material adverse impact on cash flow.

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## Table of Contents

## Cash Flows

The following table summarizes the cash flows from operating, investing and financing activities:

> Three months ended
(\$ in millions)
Total cash provided by (used for):
Operating activities
Investing activities
Financing activities
March 31,
20192018 Change

Impact of currency exchange rates on cash balances (1.0 ) $1.9 \quad(2.9 \quad)$
Increase in cash, cash equivalents and restricted cash $\$(9.6) \$ 29.8 \quad \$(39.4)$
Operating activities: Net cash used for operating activities was $\$ 38.2$ million for the three months ended March 31 , 2019 , compared to $\$ 3.2$ million for the same period in 2018 . The increase in net cash used for operating activities for the 2019 period was primarily the result of higher factory inventory due to the timing of shipments, preparation for new product launches and additional costs related to tariffs.
Investing activities: The primary use of cash was for the purchase of property and equipment and tooling for continued capacity and capability at our manufacturing facilities and for product development.
Financing activities: Cash provided by financing activities changed primarily due to increased net borrowings under debt arrangements, finance lease obligations and notes payable, which were $\$ 139.7$ million and $\$ 116.1$ million for the three months ended March 31, 2019 and 2018, respectively. Common stock repurchases were $\$ 6.1$ million and $\$ 15.0$ million for the three months ended March 31, 2019 and 2018, respectively, and proceeds from the issuance of stock under employee plans were $\$ 3.2$ million and $\$ 11.9$ million for the three months ended March 31, 2019 and 2018, respectively. Additionally, we paid cash dividends of $\$ 37.1$ million and $\$ 37.8$ million for the three months ended March 31, 2019 and 2018, respectively.
The seasonality of production and shipments cause working capital requirements to fluctuate during the year.
Debt and Capital
We are party to an unsecured $\$ 700.0$ million variable interest rate bank lending agreement and a Master Note Purchase Agreement, as amended and supplemented, under which we have unsecured borrowings. We are also party to a $\$ 1,180.0$ million term loan facility, of which $\$ 1,135.0$ million is outstanding as of March $31,2019$.
We enter into leasing arrangements to finance the use of certain property and equipment.
As a component of the Boat Holdings merger agreement, Polaris has committed to make a series of deferred payments to the former owners following the closing date of of the merger through July 2030. The original discounted payable was for $\$ 76,733,000$, all of which is outstanding as of March 31, 2019. The outstanding balance is included in current and long-term debt.
We have a mortgage note payable agreement for land, on which we built our Huntsville, Alabama manufacturing facility in 2016. The original mortgage note payable was for $\$ 14.5$ million, of which $\$ 9.7$ million is outstanding as of March 31, 2019. The payment of principal and interest for the note payable is forgivable if we satisfy certain job commitments over the term of the note. We have met the required commitments to date and expect to comply with the commitments in the future.

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## Table of Contents

Debt, finance lease obligations, notes payable, and the average related interest rates at March 31, 2019 were as follows:

|  | Average interest rate at March 31, | Maturity | March |
| :--- | :--- | :--- | :--- |
| (\$ in millions) | 2019 | 31,2019 |  |
| Revolving loan facility | $3.16 \%$ | July 2023 | $\$ 342.6$ |
| Term loan facility | $3.75 \%$ | July 2023 | $1,135.0$ |
| Senior notes—fixed rate | $4.60 \%$ | May 2021 | 75.0 |
| Senior notes—fixed rate | $3.13 \%$ | December 2020 | 100.0 |
| Senior notes—fixed rate | $4.23 \%$ | July 2028 | 350.0 |
| Finance lease obligations | $5.08 \%$ | Various through | 17.2 |
| Notes payable and other | $4.24 \%$ | 2029 |  |
| Debt issuance costs |  | Various through | 86.4 |
| Total debt, finance lease obligations, and notes |  |  | $(4.9)$ |
| payable |  | $\$ 2,101.3$ |  |
| Less: current maturities |  | 66.5 |  |
| Long-term debt, finance lease obligations, and notes |  | $\$ 2,034.8$ |  |
| payable |  |  |  |

Our debt to total capital ratio was 71 percent at March 31, 2019. Additionally, at March 31, 2019, we had letters of credit outstanding of $\$ 12.6$ million, primarily related to purchase obligations for raw materials.
Share Repurchases
Our Board of Directors has authorized the cumulative repurchase of up to 90.5 million shares of our common stock. Of that total, approximately 87.3 million shares have been repurchased cumulatively from 1996 through March 31, 2019. We repurchased approximately 0.1 million shares of our common stock for $\$ 6.1$ million during the first three months of 2019, which had an immaterial impact on earnings per share. We have authorization from our Board of Directors to repurchase up to an additional 3.2 million shares of our common stock as of March 31, 2019. The repurchase of any or all such shares authorized remaining for repurchase will be governed by applicable SEC rules. Other Financial Arrangements
Polaris Acceptance, a joint venture between Polaris and Wells Fargo Commercial Distribution Finance Corporation ("WFCDF"), a direct subsidiary of Wells Fargo Bank, N.A. ("Wells Fargo"), which is supported by a partnership agreement between their respective wholly owned subsidiaries, finances substantially all of our U.S. sales of snowmobiles, ORVs, motorcycles, and related PG\&A, whereby we receive payment within a few days of shipment of the product. The partnership agreement is effective through February 2022.
Polaris Acceptance sells a majority of its receivables portfolio (the "Securitized Receivables") to a securitization facility ("Securitization Facility") arranged by Wells Fargo, a WFCDF affiliate. Polaris Acceptance is not responsible for any continuing servicing costs or obligations with respect to the Securitized Receivables. At March 31, 2019, the outstanding amount of net receivables financed for dealers under this arrangement, including Securitized Receivables, was $\$ 1,272.2$ million, a six percent increase from $\$ 1,203.6$ million at March 31, 2018.
We account for our investment in Polaris Acceptance under the equity method. Polaris Acceptance is funded through equal equity cash investments from the partners and a loan from an affiliate of WFCDF. We do not guarantee the outstanding indebtedness of Polaris Acceptance. The partnership agreement provides that all income and losses of Polaris Acceptance are shared 50 percent by our wholly owned subsidiary and 50 percent by WFCDF's subsidiary. Our total investment in Polaris Acceptance at March 31, 2019 was $\$ 99.5$ million. Our exposure to losses of Polaris Acceptance is limited to our equity in Polaris Acceptance. Credit losses in the Polaris Acceptance portfolio have been modest, averaging less than one percent of the portfolio.
We have agreed to repurchase products repossessed by Polaris Acceptance up to an annual maximum of 15 percent of the aggregate average month-end outstanding Polaris Acceptance receivables and Securitized Receivables during the prior calendar year. For calendar year 2019, the potential 15 percent aggregate repurchase obligation is approximately
$\$ 180.6$ million. Our financial exposure under this arrangement is limited to the difference between the amount paid to the finance company for repurchases and the amount received on the resale of the repossessed product. No material losses have been incurred under this agreement.
A subsidiary of TCF Financial Corporation ("TCF") finances a portion of our United States sales of boats whereby we receive payment within a few days of shipment of the product. We have agreed to repurchase products repossessed by TCF up to a maximum of 100 percent of the aggregate outstanding TCF receivables balance. At March 31, 2019, the potential aggregate repurchase obligation was approximately $\$ 270.4$ million. Our financial exposure under this arrangement is limited

29

## Edgar Filing: POLARIS INDUSTRIES INC/MN - Form 10-Q

## Table of Contents

to the difference between the amounts unpaid by the dealer with respect to the repossessed product plus costs of repossession and the amount received on the resale of the repossessed product. No material losses have been incurred under this agreement during the periods presented.
We have agreements with certain financial institutions, under which these financial institutions provide financing to end consumers of our products in the United States. The income generated from these agreements has been included as a component of income from financial services in the accompanying consolidated statements of income. At March 31, 2019, the agreements in place were as follows:
Financial institution Agreement expiration date
Performance Finance December 2021
Sheffield Financial December 2020
Synchrony Bank December 2020

## Inflation and Foreign Exchange Rates

The changing relationships of the U.S. dollar to the Mexican peso, the Canadian dollar, the Australian dollar, the Euro, the Swiss franc and other foreign currencies have had a material impact from time to time. We actively manage our exposure to fluctuating foreign currency exchange rates by entering into foreign exchange hedging contracts. Mexican Peso: With increased production at our Monterrey, Mexico facility, our costs in the Mexican peso have continued to increase. We also market and sell to customers in Mexico through a wholly owned subsidiary. Fluctuations in the peso to U.S. dollar exchange rate primarily impact sales, cost of sales, and net income. Canadian Dollar: We operate in Canada through a wholly owned subsidiary. The relationship of the U.S. dollar in relation to the Canadian dollar impacts both sales and net income.
Other currencies: We operate in various countries, principally in Europe and Australia, through wholly owned subsidiaries. We also sell to certain distributors in other countries. We purchase components from certain suppliers directly for our U.S. operations in transactions denominated in Euros and other foreign currencies. The relationship of the U.S. dollar to these other currencies impacts sales, cost of sales and net income.
At March 31, 2019, we had the following open foreign currency hedging contracts:
Foreign currency hedging contracts
Notional

## amounts

## Foreign Currency Currency Position <br> (in Average exchange rate of open contracts of U.S. Dollars) <br> $\begin{array}{lll}\text { Australian Dollar } & \text { Long } & \$ 8,729 \$ 0.71 \text { to } 1 \text { AUD } \\ \text { Canadian Dollar } & \text { Long } & 100,035 \$ 0.76 \text { to } 1 \mathrm{CAD} \\ \text { Mexican Peso } & \text { Short } & 11,57021.39 \text { Peso to } \$ 1\end{array}$

The assets and liabilities in all our foreign entities are translated at the foreign exchange rate in effect at the balance sheet date. Translation gains and losses are reflected as a component of accumulated other comprehensive loss, net in the shareholders' equity section of the accompanying consolidated balance sheets. Revenues and expenses in our foreign entities are translated at the average foreign exchange rate in effect for each month of the quarter. Certain assets and liabilities related to intercompany positions reported on our consolidated balance sheet that are denominated in a currency other than the entity's functional currency are translated at the foreign exchange rates at the balance sheet date and the associated gains and losses are included in net income. We expect currencies to have a negative impact on net income in 2019 compared to 2018.
We are subject to market risk from fluctuating market prices of certain purchased commodities and raw materials, including steel, aluminum, petroleum-based resins, certain rare earth metals and diesel fuel. In addition, we are a purchaser of components and parts containing various commodities, including steel, aluminum, rubber and others, which are integrated into the Company's end products. While such materials are typically available from numerous suppliers, commodity raw materials are subject to price fluctuations. This includes the effects of new or modified
tariffs or penalties on raw materials, commodities, and products manufactured outside of the United States. We generally buy these commodities and components based upon market prices that are established with the vendor as part of the purchase process and from time to time will enter into derivative contracts to hedge a portion of the exposure to commodity risk. At March 31, 2019, we did not have any outstanding commodity derivative contracts in place. Based on our current outlook for commodity prices, the total impact of commodities, including tariff costs, is expected to have a negative impact on our gross profit margins for 2019 when compared to 2018.

30

## Edgar Filing: POLARIS INDUSTRIES INC/MN - Form 10-Q

## Table of Contents

We are a party to a credit agreement with various lenders consisting of a $\$ 700.0$ million revolving loan facility and a $\$ 1,180.0$ million term loan facility. Interest accrues on the revolving loan at variable rates based on LIBOR or "prime" plus the applicable add-on percentage as defined. At March 31, 2019, we had an outstanding balance of $\$ 342.6$ million on the revolving loan facility, and an outstanding balance of $\$ 1,135.0$ million on the term loan facility. The Company entered into interest rate swap transactions to hedge the variable interest rate payments for the Term Loan Facility. In connection with these transactions, the Company will pay interest based upon a fixed rate and receive variable rate interest payments based on the one-month LIBOR.

## Critical Accounting Policies

See our most recent Annual Report on Form 10-K for the year ended December 31, 2018 for a discussion of our critical accounting policies.

Note Regarding Forward Looking Statements
Certain matters discussed in this report are "forward-looking statements" intended to qualify for the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These "forward-looking statements," including but not limited to the impact of foreign exchange rate movements on sales and net income, and commodity price changes on gross profit margins, can generally be identified as such because the context of the statement will include words such as the Company or management "believes," "anticipates," "expects," "estimates" or words of similar import. Similarly, statements that describe the Company's future plans, objectives or goals are also forward-looking. Forward-looking statements may also be made from time to time in oral presentations, including telephone, conferences and/or webcasts open to the public. Shareholders, potential investors and others are cautioned that all forward-looking statements involve risks and uncertainties that could cause results in future periods to differ materially from those anticipated by some of the statements made in this report, including the risks and uncertainties described under the heading titled "Item 1A-Risk Factors" appearing in the Company's Annual Report on Form 10-K for the year ended December 31, 2018 and in this Quarterly Report on Form 10-Q. In addition to the factors discussed above, among the other factors that could cause actual results to differ materially are the following: future conduct of litigation processes; product recalls and warranty expenses; overall economic conditions, including inflation and consumer confidence and spending; interruptions in informal supply arrangements; raw material, commodity and transportation costs; tariffs and other changes to international trade policies; foreign currency exchange rate fluctuations; product offerings, promotional activities and pricing strategies by competitors; disruptions in manufacturing facilities; the ability to provide products that respond to consumer's needs and preferences; strategic partners' sensitivity to economic conditions; acquisition integration costs; environmental and product safety regulatory activity; appropriate levels of dealer and distributor relationships; uncertainty in the retail and wholesale credit markets and relationships with Performance Finance, Sheffield Financial and Synchrony Bank; the ability to protect our intellectual property; the ability to manage our international operations; effects of weather; impairment of goodwill or trade names; the ability to comply with our outstanding debt agreements; changes in tax policy; attracting and retaining skilled employees; and disruptions or breaches of information technology systems. The Company does not undertake any duty to any person to provide updates to its forward-looking statements.

## Item 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2018 for a complete discussion on the Company's market risk. There have been no material changes in market risk from those disclosed in the Company's Form 10-K for the year ended December 31, 2018.

## Item 4 - CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures
The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and its Executive Vice President - Finance and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures
(as defined in the Securities Exchange Act of 1934 Rule 13a-15) as of the end of the period covered by this report. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this Quarterly Report on Form 10-Q, the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Securities Exchange Act of

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## Table of Contents

1934 is (1) recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms, and (2) accumulated and communicated to the Company's management, including its Chief Executive Officer and Executive Vice President - Finance and Chief Financial Officer, in a manner that allows timely decisions regarding required disclosure.
Changes in Internal Controls
There have been no changes in the Company's internal controls over financial reporting during the period covered by this quarterly report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting, except for the implementation of certain information technology system and process enhancements over significant processes specific to the internal control environment at Polaris Boats (formally Boat Holdings, LLC), which was acquired on July 2, 2018.

## Part II OTHER INFORMATION

Item 1 - LEGAL PROCEEDINGS
We are involved in a number of legal proceedings incidental to our business, none of which is expected to have a material effect on the financial results of our business.
Class action lawsuits. As of the date hereof, we are party to two putative class actions pending against Polaris in the U.S., both of which were previously reported in the Company's 10-Q quarterly report for the period ended October 31, 2018.

One putative class action is pending in the United States District Court for the District of Minnesota and arises out of allegations that certain Polaris products suffer from unresolved fire hazards allegedly resulting in economic loss, and is the result of the consolidation of the three putative class actions we reported in our April 26, 2018 quarterly report and that were filed between April 5-10, 2018: In re Polaris Marketing, Sales Practices, and Product Liability Litigation (D. Minn.), June 15, 2018.

The second putative class action is also pending in the United States District Court for the District of Minnesota and alleges excessive heat hazards on certain other Polaris products and seeks damages for alleged personal injury and economic loss: Riley Johannessohn, Daniel Badilla, James Kelley, Kevin Wonders, William Bates and James Pinion, individually and on behalf of all others similarly situated v. Polaris Industries (D. Minn.), October 4, 2016. With respect to both class action lawsuits, the Company is unable to provide any reasonable evaluation of the likelihood that a loss will be incurred or any reasonable estimate of the range of possible loss.
Shareholder derivative lawsuit. On January 22, 2019, a shareholder of the Company filed a purported derivative complaint in the Hennepin County District Court for the State of Minnesota naming ten current officers and directors of the Company as defendants. The complaint alleges that defendants made materially false or misleading public statements about the Company's business, operations, forecasts, and compliance policies relating to certain of its Off-Road Vehicle products and product recalls. The complaint also alleges that several of the officer defendants benefited from improper insider sales of Polaris stock. The complaint asserts claims for breach of fiduciary duties, unjust enrichment, and other related claims. For relief, the complaint seeks damages in an unspecified amount, corporate governance changes, disgorgement and restitution of benefits and compensation paid, and an award of attorneys' fees and expenses. The Company has filed a motion to dismiss in this matter.

## Item 1A - RISK FACTORS

Please consider the factors discussed in "Part I, Item 1A. Risk Factors" in our fiscal 2018 Annual Report filed on Form 10-K. There have been no material changes or additions to our risk factors discussed in such reports, which could materially affect the Company's business, financial condition, or future results.

## Table of Contents

Item 2 - UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS
Total Maximum
Number of Number of
Total Average Shares Shares
Period
Number of Price Purchased That May

Shares Paid as Part of Yet Be
Purchased per Share Publicly Purchased
Announced Under the
Program Program (1)
January $1-31,201926,000 \quad \$ 83.87$ 26,000 3,225,000
February $1-28,20192,000 \quad \$ 87.5632,000 \quad 3,193,000$
March 1 - 31, 2019 13,000 $\$ 84.94$ 13,000 3,180,000
Total 71,000 \$ 85.73 71,000 3,180,000
(1) The Board of Directors has authorized the cumulative repurchase of up to an aggregate of 90.5 million shares of the Company's common stock (the "Program"). Of that total, 87.3 million shares have been repurchased cumulatively from 1996 through March 31, 2019. The Program does not have an expiration date.

## Item 4 - MINE SAFETY DISCLOSURES

Not applicable.
Item 6 - EXHIBITS
A list of exhibits to this Form $10-\mathrm{Q}$ is set forth on the Exhibit Index and is incorporated herein by reference.
Exhibit Index
Exhibit
Number
Description
3.a
3.b
31.a Certification of Chief Executive Officer required by Exchange Act Rule 13a-14(a).
31.b Certification of Chief Financial Officer required by Exchange Act Rule 13a-14(a).

101 The following financial information from Polaris Industries Inc.'s Quarterly Report on Form 10-Q for the period ended March 31, 2019, filed with the SEC on April 24, 2019, formatted in Extensible Business Reporting Language (XBRL): (i) the Consolidated Balance Sheets at March 31, 2019 and December 31, 2018, (ii) the Consolidated Statements of Income for the three month periods ended March 31, 2019 and 2018 , (iii) the Consolidated Statements of Comprehensive Income for the three month periods ended March 31, 2019 and 2018, (iv) the Consolidated Statements of Equity for the three month periods ended March 31,

2019 and 2018, (v) the Consolidated Statements of Cash Flows for the three month periods ended March 31, 2019 and 2018, and (vi) Notes to Consolidated Financial Statements.

## Table of Contents

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

POLARIS INDUSTRIES INC.
(Registrant)
Date: April 24, 2019 /s/ SCOTT W. WINE
Scott W. Wine
Chairman and Chief Executive Officer
(Principal Executive Officer)
Date: April 24, 2019 /s/ MICHAEL T. SPEETZEN
Michael T. Speetzen
Executive Vice President - Finance
and Chief Financial Officer
(Principal Financial and Chief Accounting Officer)
34

