

PACCAR INC
Form 10-Q
August 07, 2014
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 2014

Commission File No. 001-14817

PACCAR Inc

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

91-0351110
(I.R.S. Employer Identification No.)

777 - 106th Ave. N.E., Bellevue, WA
(Address of principal executive offices)

98004
(Zip Code)

(425) 468-7400

(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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Edgar Filing: PACCAR INC - Form 10-Q

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, \$1 par value 354,768,689 shares as of July 31, 2014

Table of Contents

PACCAR Inc Form 10-Q

INDEX

	Page
PART I. <u>FINANCIAL INFORMATION:</u>	
ITEM 1. <u>FINANCIAL STATEMENTS:</u>	
<u>Consolidated Statements of Comprehensive Income</u>	
<u>Three and Six months ended June 30, 2014 and 2013 (Unaudited)</u>	3
<u>Consolidated Balance Sheets</u>	
<u>June 30, 2014 (Unaudited) and December 31, 2013</u>	4
<u>Condensed Consolidated Statements of Cash Flows</u>	
<u>Six months ended June 30, 2014 and 2013 (Unaudited)</u>	6
<u>Notes to Consolidated Financial Statements (Unaudited)</u>	7
ITEM 2. <u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	32
ITEM 3. <u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	48
ITEM 4. <u>CONTROLS AND PROCEDURES</u>	48
PART II. <u>OTHER INFORMATION:</u>	
ITEM 1. <u>LEGAL PROCEEDINGS</u>	48
ITEM 1A. <u>RISK FACTORS</u>	48
ITEM 2. <u>UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u>	49
ITEM 6. <u>EXHIBITS</u>	49
<u>SIGNATURE</u>	50
<u>INDEX TO EXHIBITS</u>	51

Table of Contents

PACCAR Inc Form 10-Q

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Consolidated Statements of Comprehensive Income (Unaudited)

(Millions Except Per Share Amounts)

	Three Months Ended June 30		Six Months Ended June 30	
	2014	2013	2014	2013
TRUCK, PARTS AND OTHER:				
Net sales and revenues	\$ 4,267.0	\$ 4,011.7	\$ 8,353.2	\$ 7,642.9
Cost of sales and revenues	3,719.4	3,494.6	7,314.9	6,683.9
Research and development	49.9	61.8	102.6	133.9
Selling, general and administrative	114.8	112.3	236.2	230.0
Interest and other (income) expense, net	(.9)	(.4)	.5	1.1
	3,883.2	3,668.3	7,654.2	7,048.9
Truck, Parts and Other Income Before Income Taxes	383.8	343.4	699.0	594.0
FINANCIAL SERVICES:				
Interest and fees	114.7	115.0	227.6	228.8
Operating lease, rental and other revenues	187.9	173.8	368.7	353.1
Revenues	302.6	288.8	596.3	581.9
Interest and other borrowing expenses	33.7	39.4	70.3	78.3
Depreciation and other expense	148.4	138.9	292.7	283.0
Selling, general and administrative	24.8	23.7	48.4	47.2
Provision for losses on receivables	4.0	5.3	7.7	11.8
	210.9	207.3	419.1	420.3
Financial Services Income Before Income Taxes	91.7	81.5	177.2	161.6
Investment income	5.5	8.0	11.3	14.5
Total Income Before Income Taxes	481.0	432.9	887.5	770.1

Income taxes	161.8	141.3	294.4	242.4
Net Income	\$ 319.2	\$ 291.6	\$ 593.1	\$ 527.7
Net Income Per Share:				
Basic	\$.90	\$.82	\$ 1.67	\$ 1.49
Diluted	\$.90	\$.82	\$ 1.67	\$ 1.49
Weighted Average Number of Common Shares Outstanding:				
Basic	355.1	354.1	355.0	354.0
Diluted	356.3	355.0	356.2	354.8
Dividends declared per share	\$.22	\$.20	\$.42	\$.40
Comprehensive Income	\$ 368.7	\$ 220.7	\$ 647.9	\$ 377.3

See Notes to Consolidated Financial Statements.

Table of Contents

PACCAR Inc Form 10-Q

Consolidated Balance Sheets (Millions)

	June 30 2014 (Unaudited)	December 31 2013*
ASSETS		
TRUCK, PARTS AND OTHER:		
Current Assets		
Cash and cash equivalents	\$ 1,304.8	\$ 1,657.7
Trade and other receivables, net	1,232.2	1,019.6
Marketable debt securities	1,335.0	1,267.5
Inventories, net	969.1	813.6
Other current assets	301.3	308.1
Total Truck, Parts and Other Current Assets	5,142.4	5,066.5
Equipment on operating leases, net	992.1	1,038.3
Property, plant and equipment, net	2,499.8	2,513.3
Other noncurrent assets, net	519.9	477.3
Total Truck, Parts and Other Assets	9,154.2	9,095.4
FINANCIAL SERVICES:		
Cash and cash equivalents	75.5	92.4
Finance and other receivables, net	8,879.6	8,812.1
Equipment on operating leases, net	2,349.9	2,290.1
Other assets	448.2	435.5
Total Financial Services Assets	11,753.2	11,630.1
	\$ 20,907.4	\$ 20,725.5

* The December 31, 2013 consolidated balance sheet has been derived from audited financial statements. See Notes to Consolidated Financial Statements.

Table of Contents**PACCAR Inc Form 10-Q****Consolidated Balance Sheets (Millions)**

	June 30 2014 (Unaudited)	December 31 2013*
LIABILITIES AND STOCKHOLDERS EQUITY		
TRUCK, PARTS AND OTHER:		
Current Liabilities		
Accounts payable, accrued expenses and other	\$ 2,340.5	\$ 2,155.0
Dividend payable		318.8
Current portion of long-term debt		150.0
Total Truck, Parts and Other Current Liabilities	2,340.5	2,623.8
Residual value guarantees and deferred revenues	1,042.1	1,093.8
Other liabilities	768.1	734.4
Total Truck, Parts and Other Liabilities	4,150.7	4,452.0
FINANCIAL SERVICES:		
Accounts payable, accrued expenses and other	345.3	391.7
Commercial paper and bank loans	2,710.3	2,508.9
Term notes	5,609.4	5,765.3
Deferred taxes and other liabilities	932.4	973.3
Total Financial Services Liabilities	9,597.4	9,639.2
STOCKHOLDERS EQUITY		
Preferred stock, no par value: Authorized 1.0 million shares, none issued		
Common stock, \$1 par value: Authorized 1.2 billion shares, issued 354.7 and 354.3 million shares		
	354.7	354.3
Additional paid-in capital	131.9	106.2
Retained earnings	6,609.2	6,165.1
Accumulated other comprehensive income	63.5	8.7
Total Stockholders Equity	7,159.3	6,634.3
	\$ 20,907.4	\$ 20,725.5

* The December 31, 2013 consolidated balance sheet has been derived from audited financial statements. See Notes to Consolidated Financial Statements.

- 5 -

Table of Contents

PACCAR Inc Form 10-Q

Condensed Consolidated Statements of Cash Flows (Unaudited)

(Millions)

	Six Months Ended	
	June 30	
	2014	2013
OPERATING ACTIVITIES:		
Net income	\$ 593.1	\$ 527.7
Adjustments to reconcile net income to cash provided by operations:		
Depreciation and amortization:		
Property, plant and equipment	133.0	97.2
Equipment on operating leases and other	314.5	285.1
Provision for losses on financial services receivables	7.7	11.8
Other, net	(33.0)	13.1
Change in operating assets and liabilities:		
Trade and other receivables	(206.5)	(111.5)
Wholesale receivables on new trucks	64.8	(66.9)
Sales-type finance leases and dealer direct loans on new trucks	(6.3)	5.7
Inventories	(152.0)	(70.7)
Accounts payable and accrued expenses	122.4	367.7
Income taxes, warranty and other	3.1	93.4
Net Cash Provided by Operating Activities	840.8	1,152.6
INVESTING ACTIVITIES:		
Originations of retail loans and direct financing leases	(1,471.4)	(1,432.4)
Collections on retail loans and direct financing leases	1,387.5	1,240.6
Net decrease in wholesale receivables on used equipment	4.6	15.1
Purchases of marketable securities	(619.1)	(408.1)
Proceeds from sales and maturities of marketable securities	549.3	365.0
Payments for property, plant and equipment	(158.0)	(269.7)
Acquisitions of equipment for operating leases	(533.9)	(608.3)
Proceeds from asset disposals	187.8	159.8
Net Cash Used in Investing Activities	(653.2)	(938.0)
FINANCING ACTIVITIES:		
Payments of cash dividends	(467.8)	(141.4)
Proceeds from stock compensation transactions	13.3	17.5

Edgar Filing: PACCAR INC - Form 10-Q

Net increase (decrease) in commercial paper and short-term bank loans	243.7	(657.7)
Proceeds from long-term debt	951.5	1,345.1
Payments of long-term debt	(1,306.4)	(565.5)
Net Cash Used in Financing Activities	(565.7)	(2.0)
Effect of exchange rate changes on cash	8.3	(43.1)
Net (Decrease) Increase in Cash and Cash Equivalents	(369.8)	169.5
Cash and cash equivalents at beginning of period	1,750.1	1,272.4
Cash and cash equivalents at end of period	\$ 1,380.3	\$ 1,441.9

See Notes to Consolidated Financial Statements.

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

NOTE A - Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and six months ended June 30, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014. For further information, refer to the consolidated financial statements and footnotes included in PACCAR Inc's (PACCAR or the Company) Annual Report on Form 10-K for the year ended December 31, 2013.

Earnings per Share: Basic earnings per common share are computed by dividing earnings by the weighted average number of common shares outstanding, plus the effect of any participating securities. Diluted earnings per common share are computed assuming that all potentially dilutive securities are converted into common shares under the treasury stock method. The dilutive and antidilutive options are shown separately in the table below.

	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2014	2013	2014	2013
Additional shares	1,154,100	906,200	1,129,400	836,000
Antidilutive options	655,800	828,800	661,700	1,391,700

New Accounting Pronouncements: In June 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-12, *Compensation - Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved After the Requisite Service Period*. The amendment in this ASU requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Compensation costs should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service has been rendered. This ASU is effective for annual periods and interim periods beginning after December 15, 2015 and early adoption is permitted. This amendment may be applied (a) prospectively to all awards granted or modified after the effective date or (b) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. The Company does not expect the adoption of the ASU to have a material impact on its consolidated financial statements.

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers*. This ASU amends the existing accounting standards for revenue recognition. Under the new revenue recognition model, a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. The ASU is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that

reporting period. Early adoption is not permitted. The amendment may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of initial application. The Company is currently evaluating the transition alternatives and impact on the Company's consolidated financial statements.

In July 2013, the FASB issued ASU 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*. This ASU requires an unrecognized tax benefit, or a portion

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

of an unrecognized tax benefit, to be presented in the consolidated financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward if available under the applicable tax jurisdiction. The ASU was effective for annual periods beginning after December 15, 2013 and interim periods within those annual periods. The Company adopted ASU 2013-11 in the first quarter of 2014; the implementation of this amendment did not have a material impact on the Company's consolidated financial statements.

NOTE B - Investments in Marketable Debt Securities

The Company's investments in marketable debt securities are classified as available-for-sale. These investments are stated at fair value with any unrealized gains or losses, net of tax, included as a component of accumulated other comprehensive income (AOCI).

The Company utilizes third-party pricing services for all of its marketable debt security valuations. The Company reviews the pricing methodology used by the third-party pricing services including the manner employed to collect market information. On a quarterly basis, the Company also performs review and validation procedures on the pricing information received from the third-party providers. These procedures help ensure that the fair value information used by the Company is determined in accordance with applicable accounting guidance.

The Company evaluates its investment in marketable debt securities at the end of each reporting period to determine if a decline in fair value is other than temporary. Realized losses are recognized upon management's determination that a decline in fair value is other than temporary. The determination of other-than-temporary impairment is a subjective process, requiring the use of judgments and assumptions regarding the amount and timing of recovery. The Company reviews and evaluates its investments at least quarterly to identify investments that have indications of other-than-temporary impairments. It is reasonably possible that a change in estimate could occur in the near term relating to other-than-temporary impairment. Accordingly, the Company considers several factors when evaluating debt securities for other-than-temporary impairment, including whether the decline in fair value of the security is due to increased default risk for the specific issuer or market interest rate risk.

In assessing default risk, the Company considers the collectability of principal and interest payments by monitoring changes to issuers' credit ratings, specific credit events associated with individual issuers as well as the credit ratings of any financial guarantor, and the extent and duration to which amortized cost exceeds fair value.

In assessing market interest rate risk, including benchmark interest rates and credit spreads, the Company considers its intent for selling the securities and whether it is more likely than not the Company will be able to hold these securities until the recovery of any unrealized losses.

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

Marketable debt securities at June 30, 2014 and December 31, 2013 consisted of the following:

At June 30, 2014	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. tax-exempt securities	\$ 328.8	\$ 1.5		\$ 330.3
U.S. corporate securities	60.0	.2		60.2
U.S. government and agency securities	5.5	.1		5.6
Non-U.S. corporate securities	647.4	3.4	\$.1	650.7
Non-U.S. government securities	200.4	1.5	.4	201.5
Other debt securities	86.6	.1		86.7
	\$ 1,328.7	\$ 6.8	\$.5	\$ 1,335.0

At December 31, 2013	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. tax-exempt securities	\$ 214.9	\$ 1.2		\$ 216.1
U.S. corporate securities	78.2	.1	\$.1	78.2
U.S. government and agency securities	5.5			5.5
Non-U.S. corporate securities	608.5	1.2	.4	609.3
Non-U.S. government securities	217.3	.7	.5	217.5
Other debt securities	140.5	.4		140.9
	\$ 1,264.9	\$ 3.6	\$ 1.0	\$ 1,267.5

The cost of marketable debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. Amortization, accretion, interest and dividend income and realized gains and losses are included in investment income. The cost of securities sold is based on the specific identification method. Gross realized gains were \$.6 and \$.2 for the six months ended June 30, 2014 and 2013, respectively, and gross realized losses were \$.1 for both the six months ended June 30, 2014 and 2013.

Marketable debt securities with continuous unrealized losses and their related fair values were as follows:

	June 30, 2014		December 31, 2013
	Less than Twelve Months	Twelve Months or Greater	Less than Twelve Months or Greater

Edgar Filing: PACCAR INC - Form 10-Q

Fair value	\$ 134.0	\$ 15.9	\$ 388.3	\$ 28.4
Unrealized losses	.3	.2	.9	.1

For the investment securities in gross unrealized loss positions identified above, the Company does not intend to sell the investment securities. It is more likely than not that the Company will not be required to sell the investment securities before recovery of the unrealized losses, and the Company expects that the contractual principal and interest will be received on the investment securities. As a result, the Company recognized no other-than-temporary impairments during the periods presented.

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

Contractual maturities on marketable debt securities at June 30, 2014 were as follows:

	Amortized Cost	Fair Value
Maturities:		
Within one year	\$ 448.0	\$ 448.5
One to five years	880.3	886.1
More than ten years	.4	.4
	\$ 1,328.7	\$ 1,335.0

NOTE C - Inventories

Inventories are stated at the lower of cost or market. Cost of inventories in the U.S. is determined principally by the last-in, first-out (LIFO) method. Cost of all other inventories is determined principally by the first-in, first-out (FIFO) method.

Inventories include the following:

	June 30 2014	December 31 2013
Finished products	\$ 580.9	\$ 440.6
Work in process and raw materials	561.1	545.2
	1,142.0	985.8
Less LIFO reserve	(172.9)	(172.2)
	\$ 969.1	\$ 813.6

Under the LIFO method of accounting (used for approximately 40% of June 30, 2014 inventories), an actual valuation can be made only at the end of each year based on year-end inventory levels and costs. Accordingly, interim valuations are based on management's estimates of those year-end amounts.

NOTE D - Finance and Other Receivables

Finance and other receivables include the following:

	June 30	December 31
	2014	2013
Loans	\$ 4,031.2	\$ 3,977.4
Direct financing leases	2,798.3	2,680.8
Sales-type finance leases	896.1	921.1
Dealer wholesale financing	1,548.6	1,616.5
Operating lease and other trade receivables	118.5	121.3
Unearned interest: Finance leases	(382.0)	(375.7)
	\$ 9,010.7	\$ 8,941.4
Less allowance for losses:		
Loans and leases	(113.2)	(110.9)
Dealer wholesale financing	(10.2)	(10.4)
Operating lease and other trade receivables	(7.7)	(8.0)
	\$ 8,879.6	\$ 8,812.1

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

Recognition of interest income and rental revenue is suspended (put on non-accrual status) when the receivable becomes more than 90 days past the contractual due date or earlier if some other event causes the Company to determine that collection is not probable. Accordingly, no finance receivables more than 90 days past due were accruing interest at June 30, 2014 or December 31, 2013. Recognition is resumed if the receivable becomes current by the payment of all amounts due under the terms of the existing contract and collection of remaining amounts is considered probable (if not contractually modified) or if the customer makes scheduled payments for three months and collection of remaining amounts is considered probable (if contractually modified). Payments received while the finance receivable is on non-accrual status are applied to interest and principal in accordance with the contractual terms.

Allowance for Credit Losses

The Company continuously monitors the payment performance of its finance receivables. For large retail finance customers and dealers with wholesale financing, the Company regularly reviews their financial statements and makes site visits and phone contact as appropriate. If the Company becomes aware of circumstances that could cause those customers or dealers to face financial difficulty, whether or not they are past due, the customers are placed on a watch list.

The Company modifies loans and finance leases as a normal part of its Financial Services operations. The Company may modify loans and finance leases for commercial reasons or for credit reasons. Modifications for commercial reasons are changes to contract terms for customers that are not considered to be in financial difficulty. Modifications for credit reasons are changes to contract terms for customers considered to be in financial difficulty. The Company's modifications typically result in granting more time to pay the contractual amounts owed and charging a fee and interest for the term of the modification.

On average, modifications extended contractual terms by approximately four months in 2014 and six months in 2013 and did not have a significant effect on the weighted average term or interest rate of the total portfolio at June 30, 2014 and December 31, 2013.

When considering whether to modify customer accounts for credit reasons, the Company evaluates the creditworthiness of the customers and modifies those accounts that the Company considers likely to perform under the modified terms. When the Company modifies loans and finance leases for credit reasons and grants a concession, the modifications are classified as troubled debt restructurings (TDRs). The Company does not typically grant credit modifications for customers that do not meet minimum underwriting standards since the Company normally repossesses the financed equipment in these circumstances. When such modifications do occur, they are considered TDRs.

The Company has developed a systematic methodology for determining the allowance for credit losses for its two portfolio segments, retail and wholesale. The retail segment consists of retail loans and direct and sales-type finance leases, net of unearned interest. The wholesale segment consists of truck inventory financing loans to dealers that are collateralized by trucks and other collateral. The wholesale segment generally has less risk than the retail segment.

Wholesale receivables generally are shorter in duration than retail receivables, and the Company requires monthly reporting of the wholesale dealer's financial condition, conducts periodic audits of the trucks being financed and in many cases, obtains personal guarantees or other security such as dealership assets. In determining the allowance for credit losses, retail loans and finance leases are evaluated together since they relate to a similar customer base, their contractual terms require regular payment of principal and interest generally over 36 to 60 months and they are secured by the same type of collateral. The allowance for credit losses consists of both specific and general reserves.

The Company individually evaluates certain finance receivables for impairment. Finance receivables that are evaluated individually for impairment consist of all wholesale accounts and certain large retail accounts with past due balances or otherwise determined to be at a higher risk of loss. A finance receivable is impaired if it is considered probable the Company will be unable to collect all contractual interest and principal payments as scheduled. In addition, all retail loans and leases which have been classified as TDRs and all customer accounts over 90 days past due are considered impaired. Generally, impaired accounts are on non-accrual status. Impaired accounts classified as TDRs which have been performing for 90 consecutive days are placed on accrual status if it is deemed probable that the Company will collect all principal and interest payments.

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

Impaired receivables are generally considered collateral dependent. Large balance retail and all wholesale impaired receivables are individually evaluated to determine the appropriate reserve for losses. The determination of reserves for large balance impaired receivables considers the fair value of the associated collateral. When the underlying collateral fair value exceeds the Company's recorded investment, no reserve is recorded. Small balance impaired receivables with similar risk characteristics are evaluated as a separate pool to determine the appropriate reserve for losses using the historical loss information discussed below.

For finance receivables that are not individually impaired, the Company collectively evaluates and determines the general allowance for credit losses for both retail and wholesale receivables based on historical loss information, using past due account data and current market conditions. Information used includes assumptions regarding the likelihood of collecting current and past due accounts, repossession rates, the recovery rate on the underlying collateral based on used truck values and other pledged collateral or recourse. The Company has developed a range of loss estimates for each of its country portfolios based on historical experience, taking into account loss frequency and severity in both strong and weak truck market conditions. A projection is made of the range of estimated credit losses inherent in the portfolio from which an amount is determined as probable based on current market conditions and other factors impacting the creditworthiness of the Company's borrowers and their ability to repay. After determining the appropriate level of the allowance for credit losses, a provision for losses on finance receivables is charged to income as necessary to reflect management's estimate of incurred credit losses, net of recoveries, inherent in the portfolio.

In determining the fair value of the collateral, the Company uses a pricing matrix and categorizes the fair value as Level 2 in the hierarchy of fair value measurement. The pricing matrix is reviewed quarterly and updated as appropriate. The pricing matrix considers the make, model and year of the equipment as well as recent sales prices of comparable equipment through wholesale channels to the Company's dealers (principal market). The fair value of the collateral also considers the overall condition of the equipment.

Accounts are charged-off against the allowance for credit losses when, in the judgment of management, they are considered uncollectible (generally upon repossession of the collateral). Typically the timing between the repossession and charge-off is not significant. In cases where repossession is delayed (e.g., for legal proceedings), the Company records partial charge-offs. The charge-off is determined by comparing the fair value of the collateral, less cost to sell, to the recorded investment.

For the following credit quality disclosures, finance receivables are classified as dealer wholesale, dealer retail and customer retail segments. The dealer wholesale segment consists of truck inventory financing to PACCAR dealers. The dealer retail segment consists of loans and leases to participating dealers and franchises that use the proceeds to fund customers' acquisition of commercial vehicles and related equipment. The customer retail segment consists of loans and leases directly to customers for the acquisition of commercial vehicles and related equipment. Customer retail receivables are further segregated between fleet and owner/operator classes. The fleet class consists of customer retail accounts operating more than five trucks. All other customer retail accounts are considered owner/operator. Each individual class has similar measurement attributes, risk characteristics and common methods to monitor and assess credit risk.

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

The allowance for credit losses is summarized as follows:

	Dealer		2014 Customer		Total
	Wholesale	Retail	Retail	Other*	
Balance at January 1	\$ 10.4	\$ 13.4	\$ 97.5	\$ 8.0	\$ 129.3
Provision for losses	(.2)	(.5)	7.3	1.1	7.7
Charge-offs			(7.6)	(1.7)	(9.3)
Recoveries			2.6	.3	2.9
Currency translation and other			.5		.5
Balance at June 30	\$ 10.2	\$ 12.9	\$ 100.3	\$ 7.7	\$ 131.1

	Dealer		2013 Customer		Total
	Wholesale	Retail	Retail	Other*	
Balance at January 1	\$ 11.8	\$ 13.4	\$ 99.2	\$ 5.6	\$ 130.0
Provision for losses	(.4)	(1.0)	12.7	.5	11.8
Charge-offs	(.1)		(13.4)	(.8)	(14.3)
Recoveries			3.0	.5	3.5
Currency translation and other	(.3)	(.1)	(1.5)	(.1)	(2.0)
Balance at June 30	\$ 11.0	\$ 12.3	\$ 100.0	\$ 5.7	\$ 129.0

* Operating lease and other trade receivables.

Information regarding finance receivables evaluated and determined individually and collectively is as follows:

At June 30, 2014	Dealer		Customer		Total
	Wholesale	Retail	Retail		
Recorded investment for impaired finance receivables evaluated individually	\$ 8.0		\$ 38.4		\$ 46.4
Allowance for impaired finance receivables determined individually		1.3		5.3	6.6

Recorded investment for finance receivables evaluated collectively	1,540.6	\$ 1,503.0	5,802.2	8,845.8
Allowance for finance receivables determined collectively	8.9	12.9	95.0	116.8
At December 31, 2013	Wholesale	Dealer Retail	Customer Retail	Total
Recorded investment for impaired finance receivables evaluated individually	\$ 8.5		\$ 42.1	\$ 50.6
Allowance for impaired finance receivables determined individually	1.4		5.9	7.3
Recorded investment for finance receivables evaluated collectively	1,608.0	\$ 1,525.6	5,635.9	8,769.5
Allowance for finance receivables determined collectively	9.0	13.4	91.6	114.0

- 13 -

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

The recorded investment for finance receivables that are on non-accrual status is as follows:

	June 30 2014	December 31 2013
Dealer:		
Wholesale	\$ 8.0	\$ 8.0
Customer retail:		
Fleet	27.2	30.5
Owner/operator	6.9	8.6
	\$ 42.1	\$ 47.1

Impaired Loans

Impaired loans with no specific reserves were \$5.8 and \$10.7 at June 30, 2014 and December 31, 2013, respectively. Impaired loans with a specific reserve are summarized below for which the impaired loans with specific reserve represent the unpaid principal balance. The recorded investment of impaired loans as of June 30, 2014 and December 31, 2013 was not significantly different than the unpaid principal balance.

	Dealer		Customer Retail		Total
	Wholesale	Retail	Fleet	Owner/ Operator	
At June 30, 2014					
Impaired loans with a specific reserve	\$ 8.0		\$ 10.9	\$ 2.6	\$ 21.5
Associated allowance	(1.3)		(1.8)	(.6)	(3.7)
Net carrying amount of impaired loans	\$ 6.7		\$ 9.1	\$ 2.0	\$ 17.8
Average recorded investment*	\$ 7.1		\$ 24.3	\$ 3.6	\$ 35.0

* Represents the average during the 12 months ended June 30, 2014.

	Dealer		Customer Retail		Total
	Wholesale	Retail	Fleet	Owner/ Operator	
At December 31, 2013					

Edgar Filing: PACCAR INC - Form 10-Q

Impaired loans with a specific reserve	\$ 8.5	\$ 10.8	\$ 3.1	\$ 22.4
Associated allowance	(1.4)	(2.1)	(.6)	(4.1)
Net carrying amount of impaired loans	\$ 7.1	\$ 8.7	\$ 2.5	\$ 18.3
Average recorded investment*	\$ 3.6	\$ 37.1	\$ 6.9	\$ 47.6

* Represents the average during the 12 months ended June 30, 2013.

- 14 -

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

During the period the loans above were considered impaired, interest income recognized on a cash basis is as follows:

	Three Months Ended June 30		Six Months Ended June 30	
	2014	2013	2014	2013
Interest income recognized:				
Dealer wholesale		\$.1	\$.1	\$.1
Customer retail - fleet	\$.3	.9	.6	1.3
Customer retail - owner/operator	.1	.2	.2	.4
	\$.4	\$ 1.2	\$.9	\$ 1.8

Credit Quality

The Company's customers are principally concentrated in the transportation industry in North America, Europe and Australia. The Company's portfolio is diversified over a large number of customers and dealers with no single customer or dealer balances representing over 5% of the total portfolio. The Company retains as collateral a security interest in the related equipment.

At the inception of each contract, the Company considers the credit risk based on a variety of credit quality factors including prior payment experience, customer financial information, credit-rating agency ratings, loan-to-value ratios and other internal metrics. On an ongoing basis, the Company monitors credit quality based on past due status and collection experience as there is a meaningful correlation between the past due status of customers and the risk of loss.

The Company has three credit quality indicators: performing, watch and at-risk. Performing accounts pay in accordance with the contractual terms and are not considered high-risk. Watch accounts include accounts 31 to 90 days past due and large accounts that are performing but are considered to be high-risk. Watch accounts are not impaired. At-risk accounts are accounts that are impaired, including TDRs, accounts over 90 days past due and other accounts on non-accrual status. The tables below summarize the Company's finance receivables by credit quality indicator and portfolio class.

At June 30, 2014	Dealer		Customer Retail		Total
	Wholesale	Retail	Fleet	Owner/ Operator	
Performing	\$ 1,504.4	\$ 1,501.6	\$ 4,601.0	\$ 1,174.9	\$ 8,781.9
Watch	36.2	1.4	15.3	11.0	63.9

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

At June 30, 2014	Dealer		Customer Retail		Total
	Wholesale	Retail	Fleet	Owner/ Operator	
Current and up to 30 days past due	\$ 1,544.7	\$ 1,503.0	\$ 4,619.5	\$ 1,177.2	\$ 8,844.4
31 - 60 days past due	1.0		12.0	8.3	21.3
Greater than 60 days past due	2.9		15.3	8.3	26.5
	\$ 1,548.6	\$ 1,503.0	\$ 4,646.8	\$ 1,193.8	\$ 8,892.2

At December 31, 2013	Dealer		Customer Retail		Total
	Wholesale	Retail	Fleet	Owner/ Operator	
Current and up to 30 days past due	\$ 1,611.7	\$ 1,525.6	\$ 4,417.5	\$ 1,221.4	\$ 8,776.2
31 - 60 days past due	1.7		9.2	6.3	17.2
Greater than 60 days past due	3.1		15.8	7.8	26.7
	\$ 1,616.5	\$ 1,525.6	\$ 4,442.5	\$ 1,235.5	\$ 8,820.1

Troubled Debt Restructurings

The balance of TDRs was \$26.4 and \$27.6 at June 30, 2014 and December 31, 2013, respectively. At modification date, the pre-modification and post-modification recorded investment balances for finance receivables modified during the period by portfolio class are as follows:

	Three Months Ended June 30, 2014		Six Months Ended June 30, 2014	
	Recorded Investment		Recorded Investment	
	Pre-Modification	Post-Modification	Pre-Modification	Post-Modification
Fleet	\$.5	\$.5	\$ 5.4	\$ 5.4
Owner/operator	.3	.3	1.3	1.3
	\$.8	\$.8	\$ 6.7	\$ 6.7

Three Months Ended June 30, 2013		Six Months Ended June 30, 2013	
Recorded Investment		Recorded Investment	
Pre-Modification	Post-Modification	Pre-Modification	Post-Modification

Edgar Filing: PACCAR INC - Form 10-Q

Fleet	\$ 3.5	\$	3.5	\$ 7.7	\$	7.6
Owner/operator	.2		.2	.7		.7
	\$ 3.7	\$	3.7	\$ 8.4	\$	8.3

The effect on the allowance for credit losses from such modifications was not significant at June 30, 2014 and 2013.

TDRs modified during the previous twelve months that subsequently defaulted (i.e., became more than 30 days past due) during the period by portfolio class are as follows:

Six Months Ended June 30,	2014		2013	
Fleet	\$	.3	\$	1.4
Owner/operator		.6		.2
	\$	.9	\$	1.6

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

The TDRs that subsequently defaulted did not significantly impact the Company's allowance for credit losses at June 30, 2014 and 2013.

Repossessions

When the Company determines a customer is not likely to meet its contractual commitments, the Company repossesses the vehicles which serve as collateral for the loans, finance leases and equipment under operating lease. The Company records the vehicles as used truck inventory included in Financial Services other assets on the Consolidated Balance Sheets. The balance of repossessed inventory at June 30, 2014 and December 31, 2013 was \$15.3 and \$13.7, respectively. Proceeds from the sales of repossessed assets were \$32.1 and \$33.1 for the six months ended June 30, 2014 and 2013, respectively. These amounts are included in proceeds from asset disposals in the Condensed Consolidated Statements of Cash Flows. Write-downs of repossessed equipment on operating leases are recorded as impairments and included in Financial Services depreciation and other expense on the Consolidated Statements of Comprehensive Income.

NOTE E - Product Support Liabilities

Product support liabilities are estimated future payments related to product warranties, optional extended warranties and repair and maintenance (R&M) contracts. The Company generally offers one year warranties covering most of its vehicles and related aftermarket parts. For vehicles equipped with engines manufactured by PACCAR, the Company generally offers two year warranties on the engine. Specific terms and conditions vary depending on the product and the country of sale. Optional extended warranty and R&M contracts can be purchased for periods which generally range up to five years. Warranty expenses and reserves are estimated and recorded at the time products or contracts are sold based on historical data regarding the source, frequency and cost of claims, net of any recoveries. The Company periodically assesses the adequacy of its recorded liabilities and adjusts them as appropriate to reflect actual experience. Revenue from extended warranty and R&M contracts is deferred and recognized to income generally on a straight-line basis over the contract period. Warranty and R&M costs on these contracts are recognized as incurred.

Changes in product support liabilities are summarized as follows:

	2014	2013
Balance at January 1	\$ 630.5	\$ 540.7
Cost accruals and revenue deferrals	322.2	224.7
Payments and revenue recognized	(228.9)	(196.7)
Currency translation	2.4	(9.1)
Balance at June 30	\$ 726.2	\$ 559.6

Edgar Filing: PACCAR INC - Form 10-Q

In prior periods, cost accruals and revenue deferrals for the R&M contracts were netted against payments and revenue recognized instead of showing these amounts gross. The netting of these amounts affected only the disclosure in Note E; there was no effect on the Consolidated Statements of Comprehensive Income, the Consolidated Balance Sheets or the Condensed Consolidated Statements of Cash Flows. The table below presents Cost accruals and revenue deferrals and Payments and revenue recognized as previously reported in Note E and as revised:

	Three Months Ended March 31, 2014		Three Months Ended March 31, 2013		Six Months Ended June 30, 2013	
	Previously Reported	Revised	Previously Reported	Revised	Previously Reported	Revised
Cost accruals and revenue deferrals	\$ 130.8	\$ 170.2	\$ 68.6	\$ 103.3	\$ 158.3	\$ 224.7
Payments and revenue recognized	(74.8)	(114.2)	(58.5)	(93.2)	(130.3)	(196.7)

- 17 -

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

NOTE F Stockholders Equity**Comprehensive Income**

The components of comprehensive income are as follows:

	Three Months Ended June 30		Six Months Ended June 30	
	2014	2013	2014	2013
Net income	\$ 319.2	\$ 291.6	\$ 593.1	\$ 527.7
Other comprehensive income (OCI):				
Unrealized (losses) gains on derivative contracts	(1.3)	10.1	.4	13.3
Tax effect	.8	(3.0)	.2	(4.1)
	(.5)	7.1	.6	9.2
Unrealized gains (losses) on marketable debt securities	2.5	(5.5)	3.7	(5.8)
Tax effect	(.8)	1.5	(1.0)	1.6
	1.7	(4.0)	2.7	(4.2)
Pension plans	1.1	13.0	7.5	34.3
Tax effect	(.5)	(4.4)	(2.6)	(11.1)
	.6	8.6	4.9	23.2
Foreign currency translation gains (losses)	47.7	(82.6)	46.6	(178.6)
Net other comprehensive income (loss)	49.5	(70.9)	54.8	(150.4)
Comprehensive income	\$ 368.7	\$ 220.7	\$ 647.9	\$ 377.3

Accumulated Other Comprehensive Income

The components of AOCI as of June 30, 2014 and December 31, 2013 and the changes in AOCI, net of tax, included in the Consolidated Balance Sheets, consisted of the following:

	Derivative Contracts	Marketable Debt Securities	Pension Plans	Foreign Currency Translation	Total
Balance at December 31, 2013	\$ (15.1)	\$ 1.7	\$ (262.2)	\$ 284.3	\$ 8.7
Recorded into AOCI	(22.7)	2.8	(2.6)	46.6	24.1
Reclassified out of AOCI	23.3	(.1)	7.5		30.7
Net other comprehensive income	.6	2.7	4.9	46.6	54.8
Balance at June 30, 2014	\$ (14.5)	\$ 4.4	\$ (257.3)	\$ 330.9	\$ 63.5

- 18 -

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

The components of AOCI as of June 30, 2013 and December 31, 2012 and the changes in AOCI, net of tax, included in the Consolidated Balance Sheets, consisted of the following:

	Derivative Contracts	Marketable Debt Securities	Pension Plans	Foreign Currency Translation	Total
Balance at December 31, 2012	\$ (27.2)	\$ 6.6	\$ (496.5)	\$ 357.6	\$ (159.5)
Recorded into AOCI	54.1	(4.2)	8.5	(176.6)	(118.2)
Reclassified out of AOCI	(44.9)		14.7	(2.0)	(32.2)
Net other comprehensive income (loss)	9.2	(4.2)	23.2	(178.6)	(150.4)
Balance at June 30, 2013	\$ (18.0)	\$ 2.4	\$ (473.3)	\$ 179.0	\$ (309.9)

Table of Contents

PACCAR Inc Form 10-Q

Notes to Consolidated Financial Statements (Unaudited)

(Millions, Except Share Amounts)

Reclassifications out of AOCI during the six months ended June 30, 2014 are as follows:

AOCI Components	Line Item in the Consolidated Statements of Comprehensive Income	Amount Reclassified Out of AOCI
Unrealized gains and losses on derivative contracts:		
<i>Truck, Parts and Other</i>		
Foreign-exchange contracts	Cost of sales and revenues	\$ 1.8
	Interest and other (income) expense, net	.1
<i>Financial Services</i>		
Interest-rate contracts	Interest and other borrowing expenses	31.6
	Pre-tax expense increase	33.5
	Tax benefit	(10.2)
	After-tax expense increase	23.3
Unrealized gains and losses on marketable debt securities:		
Marketable debt securities	Investment income	(.2)
	Tax expense	.1
	After-tax income increase	(.1)
Pension plans:		
<i>Truck, Parts and Other</i>		
Actuarial loss	Cost of sales and revenues \$5.6, SG&A \$4.3	9.9
Prior service costs	Cost of sales and revenues \$.5, SG&A \$.1	.6
<i>Financial Services</i>		
Actuarial loss	SG&A	.6
	Pre-tax expense increase	11.1
	Tax benefit	(3.6)
	After-tax expense increase	7.5
Total reclassifications out of AOCI		\$ 30.7

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

Reclassifications out of AOCI during the six months ended June 30, 2013 are as follows:

AOCI Components	Line Item in the Consolidated Statements of Comprehensive Income	Amount Reclassified Out of AOCI
Unrealized gains and losses on derivative contracts:		
<i>Truck, Parts and Other</i>		
Foreign-exchange contracts	Cost of sales and revenues	\$ (2.3)
	Interest and other (income) expense, net	.3
<i>Financial Services</i>		
Interest-rate contracts	Interest and other borrowing expenses	(61.9)
	Pre-tax expense reduction	(63.9)
	Tax expense	19.0
	After-tax expense reduction	(44.9)
Pension plans:		
<i>Truck, Parts and Other</i>		
Prior service costs	Cost of sales and revenues	.6
Actuarial loss	Cost of sales and revenues \$11.5, SG&A \$9.6, R&D \$1	21.2
<i>Financial Services</i>		
Actuarial loss	SG&A	.8
	Pre-tax expense increase	22.6
	Tax benefit	(7.9)
	After-tax expense increase	14.7
Foreign currency translation:		
<i>Truck, Parts and Other</i>		
	Interest and other (income) expense, net	(1.1)
<i>Financial Services</i>		
	Interest and other borrowing expenses	(.9)
	Expense reduction	(2.0)
Total reclassifications out of AOCI		\$ (32.2)

Stock Compensation Plans

Stock-based compensation expense was \$2.9 and \$10.4 for the three and six months ended June 30, 2014, respectively, and \$2.7 and \$8.5 for the three and six months ended June 30, 2013, respectively. Realized tax benefits related to the excess of deductible amounts over expense recognized amounted to \$.2 and \$1.5 for the three and six months ended June 30, 2014, respectively, and \$.9 and \$1.6 for the three and six months ended June 30, 2013, respectively, and have been classified as a financing cash flow.

During the first half of 2014, the Company issued 452,658 common shares under deferred and stock compensation arrangements.

NOTE G - Income Taxes

The effective income tax rate in the second quarter of 2014 of 33.6% increased from 32.6% in the same period of 2013, and the effective income tax rate in the first half of 2014 of 33.2% increased from 31.5% in the same period of 2013. The increases in the effective tax rates for the second quarter and first half were primarily due to a higher proportion of income generated in higher taxed jurisdictions in 2014 as compared to 2013.

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

NOTE H - Segment Information

PACCAR operates in three principal segments: Truck, Parts and Financial Services.

	Three Months Ended June 30		Six Months Ended June 30	
	2014	2013	2014	2013
Net sales and revenues:				
Truck	\$ 3,679.4	\$ 3,432.2	\$ 7,168.0	\$ 6,508.0
Less intersegment	(224.4)	(162.2)	(383.8)	(304.7)
External customers	3,455.0	3,270.0	6,784.2	6,203.3
Parts	790.1	721.4	1,527.3	1,399.8
Less intersegment	(12.1)	(11.9)	(22.7)	(22.9)
External customers	778.0	709.5	1,504.6	1,376.9
Other	34.0	32.2	64.4	62.7
	4,267.0	4,011.7	8,353.2	7,642.9
Financial Services	302.6	288.8	596.3	581.9
	\$ 4,569.6	\$ 4,300.5	\$ 8,949.5	\$ 8,224.8
Income (loss) before income taxes:				
Truck	\$ 259.6	\$ 238.4	\$ 471.9	\$ 403.4
Parts	126.7	109.4	238.8	204.7
Other	(2.5)	(4.4)	(11.7)	(14.1)
	383.8	343.4	699.0	594.0
Financial Services	91.7	81.5	177.2	161.6
Investment income	5.5	8.0	11.3	14.5
	\$ 481.0	\$ 432.9	\$ 887.5	\$ 770.1
Depreciation and amortization:				
Truck	\$ 100.5	\$ 84.0	\$ 200.2	\$ 161.7
Parts	1.3	1.4	2.7	2.7
Other	2.7	2.4	5.3	4.9

	104.5	87.8	208.2	169.3
Financial Services	123.2	109.8	239.3	213.0
	\$ 227.7	\$ 197.6	\$ 447.5	\$ 382.3

Truck and Parts

The Truck segment includes the manufacture of trucks and the Parts segment includes the distribution of related aftermarket parts, both of which are sold through the same network of independent dealers. These segments derive a large proportion of their revenues and operating profits from operations in North America and Europe. The Truck segment incurs substantial costs to design, manufacture and sell trucks to its customers. The sale of new trucks provides the Parts segment with the basis for parts sales that may continue over the life of the truck, but are generally concentrated in the first five years after truck delivery. To reflect the benefit the Parts segment receives from costs incurred by the Truck segment, certain expenses are allocated from the Truck segment to the Parts segment. The expenses allocated are based on a percentage of the average annual expenses for factory overhead, engineering, research and development (R&D) and selling, general and administrative (SG&A) expenses for the preceding five years. The allocation is

Table of Contents

PACCAR Inc Form 10-Q

Notes to Consolidated Financial Statements (Unaudited)

(Millions, Except Share Amounts)

based on the ratio of the average parts direct margin dollars (net sales less material and labor costs) to the total truck and parts direct margin dollars for the previous five years. The Company believes such expenses have been allocated on a reasonable basis. Truck segment assets related to the indirect expense allocation are not allocated to the Parts segment.

Financial Services

The Financial Services segment includes finance and leasing of primarily PACCAR products and services provided to truck customers and dealers. Revenues are primarily generated from operations in North America and Europe.

Other

Included in Other is the Company's industrial winch manufacturing business. Also within this category are other sales, income and expense not attributable to a reportable segment, including a portion of corporate expenses.

The accounting policies of the reportable segments are the same as those applied in the consolidated financial statements as described in Note A of the Company's Annual Report on Form 10-K for the year ended December 31, 2013.

NOTE I - Derivative Financial Instruments

As part of its risk management strategy, the Company enters into derivative contracts to hedge against interest rates and foreign currency risk. Certain derivative instruments designated as either cash flow hedges or fair value hedges are subject to hedge accounting. Derivative instruments that are not subject to hedge accounting are held as economic hedges. The Company's policies prohibit the use of derivatives for speculation or trading. At the inception of each hedge relationship, the Company documents its risk management objectives, procedures and accounting treatment. All of the Company's interest-rate and certain foreign exchange contracts are transacted under International Swaps and Derivatives Association (ISDA) master agreements. Each agreement permits the net settlement of amounts owed in the event of default and certain other termination events. For derivative financial instruments, the Company has elected not to offset derivative positions in the balance sheet with the same counterparty under the same agreements and is not required to post or receive collateral. Exposure limits and minimum credit ratings are used to minimize the risks of counterparty default. The Company had no material exposures to default at June 30, 2014.

The Company uses regression analysis to assess effectiveness of interest-rate contracts on a quarterly basis. For foreign-exchange contracts, the Company performs quarterly assessments to ensure that critical terms continue to match. All components of the derivative instrument's gain or loss are included in the assessment of hedge effectiveness. Gains or losses on the ineffective portion of cash flow hedges are recognized currently in earnings. Hedge accounting is discontinued prospectively when the Company determines that a derivative financial instrument has ceased to be a highly effective hedge.

Interest-Rate Contracts: The Company enters into various interest-rate contracts, including interest-rate swaps and cross currency interest-rate swaps. Interest-rate swaps involve the exchange of fixed for floating rate or floating for fixed rate interest payments based on the contractual notional amounts in a single currency. Cross currency interest-rate swaps involve the exchange of notional amounts and interest payments in different currencies. The Company is exposed to interest-rate and exchange-rate risk caused by market volatility as a result of its borrowing activities. The objective of these contracts is to mitigate the fluctuations on earnings, cash flows and fair value of borrowings. Net amounts paid or received are reflected as adjustments to interest expense.

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

At June 30, 2014, the notional amount of the Company's interest-rate contracts was \$4,091.2. Notional maturities for all interest-rate contracts are \$564.2 for the remainder of 2014, \$1,413.0 for 2015, \$1,177.6 for 2016, \$533.6 for 2017, \$315.0 for 2018 and \$87.8 thereafter. The majority of these contracts are floating to fixed swaps that effectively convert an equivalent amount of commercial paper and other variable rate debt to fixed rates.

Foreign-Exchange Contracts: The Company enters into foreign-exchange contracts to hedge certain anticipated transactions and assets and liabilities denominated in foreign currencies, particularly the Canadian dollar, the euro, the British pound, the Australian dollar, the Brazilian real and the Mexican peso. The objective is to reduce fluctuations in earnings and cash flows associated with changes in foreign currency exchange rates. At June 30, 2014, the notional amount of the outstanding foreign-exchange contracts was \$238.0. Foreign-exchange contracts mature within one year.

The following table presents the balance sheet classification, fair value, gross and pro-forma net amounts of derivative financial instruments:

	June 30, 2014		December 31, 2013	
	Assets	Liabilities	Assets	Liabilities
Derivatives designated under hedge accounting:				
<i>Interest-rate contracts:</i>				
Financial Services:				
Other assets	\$ 30.5		\$ 46.3	
Deferred taxes and other liabilities		\$ 62.0		\$ 67.7
<i>Foreign-exchange contracts:</i>				
Truck, Parts and Other:				
Other current assets	.1			
Accounts payable, accrued expenses and other		1.6		.6
Total	\$ 30.6	\$ 63.6	\$ 46.3	\$ 68.3
Economic hedges:				
<i>Interest-rate contracts:</i>				
Financial Services:				
Deferred taxes and other liabilities		\$.5		
<i>Foreign-exchange contracts:</i>				
Truck, Parts and Other:				
Other current assets	\$.3		\$.6	
Accounts payable, accrued expenses and other		.6		.2
Financial Services:				

Edgar Filing: PACCAR INC - Form 10-Q

Other assets		.1		1.1		
Deferred taxes and other liabilities			1.9			.1
Total	\$	.4	\$	3.0	\$	1.7
					\$	.3
Gross amounts recognized in Balance Sheet	\$	31.0	\$	66.6	\$	48.0
Less amounts not offset in financial instruments:						
Truck, Parts and Other:						
Foreign-exchange contracts		(.2)		(.2)		(.2)
Financial Services:						
Interest-rate contracts		(10.6)		(10.6)		(16.1)
Pro-forma net amount	\$	20.2	\$	55.8	\$	31.7
					\$	52.3

- 24 -

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

Fair Value Hedges

Changes in the fair value of derivatives designated as fair value hedges are recorded in earnings together with the changes in fair value of the hedged item attributable to the risk being hedged. The (income) or expense recognized in earnings related to fair value hedges was included in interest and other borrowing expenses in the Financial Services segment of the Consolidated Statements of Comprehensive Income as follows:

	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2014	2013	2014	2013
Interest-rate swaps	\$ (.6)	\$.2	\$ (.5)	\$.4
Term notes	(.1)	(1.3)	(1.2)	(2.7)

Cash Flow Hedges

Substantially all of the Company's interest-rate contracts and some foreign-exchange contracts have been designated as cash flow hedges. Changes in the fair value of derivatives designated as cash flow hedges are recorded in AOCI to the extent such hedges are considered effective. The maximum length of time over which the Company is hedging its exposure to the variability in future cash flows is 6.7 years.

Amounts in AOCI are reclassified into net income in the same period in which the hedged transaction affects earnings. Net realized gains and losses from interest-rate contracts are recognized as an adjustment to interest expense. Net realized gains and losses from foreign-exchange contracts are recognized as an adjustment to cost of sales or to Financial Services interest expense, consistent with the hedged transaction. The Company recognized losses on the ineffective portions of \$.3 and nil for the second quarter of 2014 and 2013, respectively, and losses of \$.3 and gains of \$.1 for the first six months of 2014 and 2013, respectively.

The following table presents the pre-tax effects of derivative instruments recognized in OCI:

	Three Months Ended		Six Months Ended	
	June 30, 2014		June 30, 2014	
	Interest- Rate Contracts	Foreign- Exchange Contracts	Interest- Rate Contracts	Foreign- Exchange Contracts
Loss recognized in OCI:				
Truck, Parts and Other		\$ (3.0)		\$ (2.8)
Financial Services	\$ (38.7)		\$ (30.3)	

\$ (38.7) \$ (3.0) \$ (30.3) \$ (2.8)

	Three Months Ended June 30, 2013		Six Months Ended June 30, 2013	
	Interest- Rate Contracts	Foreign- Exchange Contracts	Interest- Rate Contracts	Foreign- Exchange Contracts
Gain recognized in OCI:				
Truck, Parts and Other		\$ 1.3		\$ 2.9
Financial Services	\$ 54.7		\$ 74.4	
	\$ 54.7	\$ 1.3	\$ 74.4	\$ 2.9

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

Expense (income) reclassified out of AOCI into income:

	Three Months Ended June 30, 2014		Six Months Ended June 30, 2014	
	Interest- Rate Contracts	Foreign- Exchange Contracts	Interest- Rate Contracts	Foreign- Exchange Contracts
Truck, Parts and Other:				
Cost of sales and revenues		\$ 1.7		\$ 1.8
Interest and other (income) expense, net		.2		.1
Financial Services:				
Interest and other borrowing expenses	\$ 38.5		\$ 31.6	
	\$ 38.5	\$ 1.9	\$ 31.6	\$ 1.9
	Three Months Ended June 30, 2013		Six Months Ended June 30, 2013	
	Interest- Rate Contracts	Foreign- Exchange Contracts	Interest- Rate Contracts	Foreign- Exchange Contracts
Truck, Parts and Other:				
Cost of sales and revenues				\$ (2.3)
Interest and other (income) expense, net		\$.5		.3
Financial Services:				
Interest and other borrowing expenses	\$ (46.3)		\$ (61.9)	
	\$ (46.3)	\$.5	\$ (61.9)	\$ (2.0)

The amount of loss recorded in AOCI at June 30, 2014 that is estimated to be reclassified to interest expense or cost of sales in the following 12 months if interest rates and exchange rates remain unchanged is approximately \$24.7, net of taxes. The fixed interest earned on finance receivables will offset the amount recognized in interest expense, resulting in a stable interest margin consistent with the Company's risk management strategy.

Economic Hedges

For other risk management purposes, the Company enters into derivative instruments that do not qualify for hedge accounting. These derivative instruments are used to mitigate the risk of market volatility arising from borrowings and foreign currency denominated transactions. Changes in the fair value of economic hedges are recorded in earnings in

the period in which the change occurs.

- 26 -

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

The expense (income) recognized in earnings related to economic hedges is as follows:

	Three Months Ended June 30, 2014		Six Months Ended June 30, 2014	
	Interest- Rate Contracts	Foreign- Exchange Contracts	Interest- Rate Contracts	Foreign- Exchange Contracts
Truck, Parts and Other:				
Cost of sales and revenues		\$ (.4)		\$ (.2)
Interest and other (income) expense, net		1.2		.3
Financial Services:				
Interest and other borrowing expenses	\$.3	4.3	\$.3	4.8
	\$.3	\$ 5.1	\$.3	\$ 4.9
	Three Months Ended June 30, 2013		Six Months Ended June 30, 2013	
	Interest- Rate Contracts	Foreign- Exchange Contracts	Interest- Rate Contracts	Foreign- Exchange Contracts
Truck, Parts and Other:				
Cost of sales and revenues		\$.5		\$.4
Interest and other (income) expense, net		(1.3)		.4
Financial Services:				
Interest and other borrowing expenses	\$ (.1)	(4.9)	\$ (1.4)	(4.6)
	\$ (.1)	\$ (5.7)	\$ (1.4)	\$ (3.8)

NOTE J - Fair Value Measurements

Fair value represents the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Inputs to valuation techniques used to measure fair value are either observable or unobservable. These inputs have been categorized into the fair value hierarchy described below.

Level 1 Valuations are based on quoted prices that the Company has the ability to obtain in actively traded markets for identical assets or liabilities. Since valuations are based on quoted prices that are readily and regularly available in an active market or exchange traded market, valuation of these instruments does not require a significant degree of

judgment.

Level 2 Valuations are based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 Valuations are based on model-based techniques for which some or all of the assumptions are obtained from indirect market information that is significant to the overall fair value measurement and which require a significant degree of management judgment.

Table of Contents

PACCAR Inc Form 10-Q

Notes to Consolidated Financial Statements (Unaudited)

(Millions, Except Share Amounts)

There were no transfers of assets or liabilities between Level 1 and Level 2 of the fair value hierarchy during the six months ended June 30, 2014. The Company's policy is to recognize transfers between levels at the end of the reporting period.

The Company uses the following methods and assumptions to measure fair value for assets and liabilities subject to recurring fair value measurements.

Marketable Securities: The Company's marketable debt securities consist of municipal bonds, government obligations, investment-grade corporate obligations, commercial paper, asset-backed securities and term deposits. The fair value of U.S. government obligations is determined using the market approach and is based on quoted prices in active markets and are categorized as Level 1.

The fair value of U.S. government agency obligations, non-U.S. government bonds, municipal bonds, corporate bonds, asset-backed securities, commercial paper and term deposits is determined using the market approach and is primarily based on matrix pricing as a practical expedient which does not rely exclusively on quoted prices for a specific security. Significant inputs used to determine fair value include interest rates, yield curves, credit rating of the security and other observable market information and are categorized as Level 2.

Derivative Financial Instruments: The Company's derivative contracts consist of interest-rate swaps, cross currency swaps and foreign currency exchange contracts. These derivative contracts are traded over the counter, and their fair value is determined using industry standard valuation models, which are based on the income approach (i.e., discounted cash flows). The significant observable inputs into the valuation models include interest rates, yield curves, currency exchange rates, credit default swap spreads and forward spot rates and are categorized as Level 2.

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

Assets and Liabilities Subject to Recurring Fair Value Measurement

The Company's assets and liabilities subject to recurring fair value measurements are either Level 1 or Level 2 as follows:

At June 30, 2014	Level 1	Level 2	Total
Assets:			
Marketable debt securities			
U.S. tax-exempt securities		\$ 330.3	\$ 330.3
U.S. corporate securities		60.2	60.2
U.S. government and agency securities	\$ 5.3	.3	5.6
Non-U.S. corporate securities		650.7	650.7
Non-U.S. government securities		201.5	201.5
Other debt securities		86.7	86.7
Total marketable debt securities	\$ 5.3	\$ 1,329.7	\$ 1,335.0
Derivatives			
Cross currency swaps		\$ 27.3	\$ 27.3
Interest-rate swaps		3.2	3.2
Foreign-exchange contracts		.5	.5
Total derivative assets		\$ 31.0	\$ 31.0
Liabilities:			
Derivatives			
Cross currency swaps		\$ 38.9	\$ 38.9
Interest-rate swaps		23.6	23.6
Foreign-exchange contracts		4.1	4.1
Total derivative liabilities		\$ 66.6	\$ 66.6

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

At December 31, 2013	Level 1	Level 2	Total
Assets:			
Marketable debt securities			
U.S. tax-exempt securities		\$ 216.1	\$ 216.1
U.S. corporate securities		78.2	78.2
U.S. government and agency securities	\$ 5.2	.3	5.5
Non-U.S. corporate securities		609.3	609.3
Non-U.S. government securities		217.5	217.5
Other debt securities		140.9	140.9
Total marketable debt securities	\$ 5.2	\$ 1,262.3	\$ 1,267.5
Derivatives			
Cross currency swaps		\$ 40.9	\$ 40.9
Interest-rate swaps		5.4	5.4
Foreign-exchange contracts		1.7	1.7
Total derivative assets		\$ 48.0	\$ 48.0
Liabilities:			
Derivatives			
Cross currency swaps		\$ 42.1	\$ 42.1
Interest-rate swaps		25.6	25.6
Foreign-exchange contracts		.9	.9
Total derivative liabilities		\$ 68.6	\$ 68.6

Fair Value Disclosure of Other Financial Instruments

For financial instruments that are not recognized at fair value, the Company uses the following methods and assumptions to determine the fair value. These instruments are categorized as Level 2, except cash which is categorized as Level 1 and fixed rate loans which are categorized as Level 3.

Cash and Cash Equivalents: Carrying amounts approximate fair value.

Financial Services Net Receivables: For floating-rate loans, wholesale financings, and operating lease and other trade receivables, carrying values approximate fair values. For fixed rate loans, fair values are estimated using the income approach by discounting cash flows to their present value based on current rates for comparable loans. Finance lease receivables and related allowance for credit losses have been excluded from the accompanying table.

Debt: The carrying amounts of financial services commercial paper, variable rate bank loans and variable rate term notes approximate fair value. For fixed rate debt, fair values are estimated using the income approach by discounting cash flows to their present value based on current rates for comparable debt.

Table of Contents**PACCAR Inc Form 10-Q****Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

The Company's estimate of fair value for fixed rate loans and debt that are not carried at fair value was as follows:

	June 30, 2014		December 31, 2013	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets:				
Financial Services fixed rate loans	\$ 3,675.0	\$ 3,733.3	\$ 3,592.7	\$ 3,627.3
Liabilities:				
Truck, Parts and Other fixed rate debt			150.0	151.1
Financial Services fixed rate debt	3,574.2	3,602.9	4,039.1	4,087.0

NOTE K - Employee Benefit Plans

The Company has several defined benefit pension plans, which cover a majority of its employees. The following information details the components of net pension expense for the Company's defined benefit plans:

	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2014	2013	2014	2013
Service cost	\$ 17.0	\$ 17.8	\$ 34.0	\$ 36.7
Interest on projected benefit obligation	23.1	20.1	46.1	40.4
Expected return on assets	(32.2)	(29.7)	(64.2)	(59.6)
Amortization of prior service costs	.3	.3	.6	.6
Recognized actuarial loss	5.2	11.1	10.4	22.0
Net pension expense	\$ 13.4	\$ 19.6	\$ 26.9	\$ 40.1

During the three and six months ended June 30, 2014, the Company contributed \$4.1 and \$8.3 to its pension plans, respectively, and \$2.7 and \$6.1 for the three and six months ended June 30, 2013, respectively.

Table of Contents**PACCAR Inc Form 10-Q****ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****OVERVIEW:**

PACCAR is a global technology company whose Truck segment includes the design and manufacture of high-quality, light-, medium- and heavy-duty commercial trucks. In North America, trucks are sold under the Kenworth and Peterbilt nameplates, in Europe, under the DAF nameplate and in Australia and South America, under the Kenworth and DAF nameplates. The Parts segment includes the distribution of aftermarket parts for trucks and related commercial vehicles. The Company's Financial Services segment derives its earnings primarily from financing or leasing PACCAR products in North America, Europe and Australia. The Company's Other business is the manufacturing and marketing of industrial winches.

Consolidated net sales and revenues in the second quarter of 2014 increased to \$4.57 billion from \$4.30 billion in the second quarter of 2013. In the first six months of 2014, net sales and revenue increased to \$8.95 billion from \$8.22 billion in the same period in 2013. The Company's worldwide truck net sales and revenues in the second quarter of 2014 increased to \$3.46 billion from \$3.27 billion in the second quarter of 2013. In the first six months of 2014, truck net sales increased to \$6.78 billion from \$6.20 billion in the same period of 2013. Increases in truck sales were primarily due to higher sales volume in the U.S. and Canada and higher price realization for higher content Euro 6 emission vehicles. The Company's worldwide parts net sales and revenues increased to \$778.0 million in the second quarter of 2014 from \$709.5 million in the second quarter of 2013. In the first six months of 2014 worldwide parts net sales and revenues increased to \$1.50 billion from \$1.38 billion in the same period in 2013. Parts growth was primarily due to higher aftermarket demand in the U.S. and Canada and Europe. Financial Services revenues increased to \$302.6 million in the second quarter of 2014 from \$288.8 million in the second quarter of 2013. In the first six months of 2014, Financial Services revenues increased to \$596.3 million from \$581.9 million in the same period in 2013. The increase in Financial Services revenues for both periods was primarily due to higher average earning assets.

Second quarter 2014 net income increased to \$319.2 million (\$.90 per diluted share) from \$291.6 million (\$.82 per diluted share) in the second quarter of 2013. For the first six months of 2014, net income improved to \$593.1 million (\$1.67 per diluted share) from \$527.7 million (\$1.49 per diluted share) in the first six months of 2013. The results reflect improving truck sales in the U.S. and Canada and strong aftermarket Parts and Financial Services results worldwide.

In the second quarter of 2014, DAF introduced a new range of Euro 6 CF and XF four-axle trucks and tractors for heavy-duty applications. These new vehicles expand DAF's product range in the construction, container and refuse markets and complement DAF's award-winning Euro 6 on-highway trucks. In addition, Kenworth and Peterbilt launched their new medium-duty cab-over-engine distribution trucks with extensive exterior and interior enhancements.

PACCAR plans to begin construction of a new 176,000 square-foot distribution center in Renton, Washington, in the fourth quarter of 2014. This new facility will more than double the distribution capacity for the Company's dealers and customers in the northwestern U.S. and western Canada.

In the second quarter and first half of 2014, the Company's research and development (R&D) expenses were \$49.9 million and \$102.6 million compared to \$61.8 million and \$133.9 million in the second quarter and first half of

2013. R&D declined as new truck models and engines began production. R&D is focused on engine and new vehicle development.

Truck and Parts Outlook

Truck industry retail sales in the U.S. and Canada in 2014 are expected to be 230,000-250,000 units compared to 212,200 units in 2013 driven primarily by ongoing replacement of the aging truck population and improving construction and automotive sectors. The truck market in 2014 may also benefit from some expansion of industry fleet capacity, reflecting improved freight demand. In Europe, the 2014 truck industry registrations for over 16-tonne vehicles are expected to be 210,000-230,000 units, compared to 240,800 units in 2013.

Table of Contents**PACCAR Inc Form 10-Q**

In 2014, Parts industry aftermarket sales are expected to increase 4-8%, reflecting modest economic growth in the U.S. and Canada and Europe.

Capital investments in 2014 are expected to be \$250 to \$300 million, focused on enhanced powertrain development and increased operating efficiency for assembly facilities. R&D in 2014 is expected to be \$200 to \$225 million.

Financial Services Outlook

Average earning assets in 2014 are expected to increase approximately 5%, reflecting higher Financial Services asset levels at the start of the year. Current levels of freight tonnage, freight rates and fleet utilization are contributing to customers' profitability and cash flow. If current freight transportation conditions decline due to weaker economic conditions, past due accounts, truck repossessions and credit losses would likely increase from the current low levels.

See the Forward-Looking Statements section of Management's Discussion and Analysis for factors that may affect these outlooks.

RESULTS OF OPERATIONS:

(\$ in millions, except per share amounts)	Three Months Ended		Six Months Ended	
	2014	2013	2014	2013
Net sales and revenues:				
Truck	\$ 3,455.0	\$ 3,270.0	\$ 6,784.2	\$ 6,203.3
Parts	778.0	709.5	1,504.6	1,376.9
Other	34.0	32.2	64.4	62.7
Truck, Parts and Other	4,267.0	4,011.7	8,353.2	7,642.9
Financial Services	302.6	288.8	596.3	581.9
	\$ 4,569.6	\$ 4,300.5	\$ 8,949.5	\$ 8,224.8
Income (loss) before taxes:				
Truck	\$ 259.6	\$ 238.4	\$ 471.9	\$ 403.4
Parts	126.7	109.4	238.8	204.7
Other	(2.5)	(4.4)	(11.7)	(14.1)
Truck, Parts and Other	383.8	343.4	699.0	594.0
Financial Services	91.7	81.5	177.2	161.6
Investment income	5.5	8.0	11.3	14.5
Income taxes	(161.8)	(141.3)	(294.4)	(242.4)

Edgar Filing: PACCAR INC - Form 10-Q

Net income	\$	319.2	\$	291.6	\$	593.1	\$	527.7
Diluted earnings per share	\$	.90	\$	.82	\$	1.67	\$	1.49

Return on revenues	7.0%	6.8%	6.6%	6.4%
--------------------	-------------	------	-------------	------

The following provides an analysis of the results of operations for the Company's three reportable segments, Truck, Parts and Financial Services. Where possible, the Company has quantified the factors identified in the following discussion and analysis. In cases where it is not possible to quantify the impact of factors, the Company lists them in estimated order of importance. Factors for which the Company is unable to specifically quantify the impact include market demand, fuel prices, freight tonnage and economic conditions affecting the Company's results of operations.

- 33 -

Table of Contents**PACCAR Inc Form 10-Q****2014 Compared to 2013:****Truck**

The Company's Truck segment accounted for 75.6% and 75.8% of revenues in the second quarter and first six months of 2014 compared to 76.0% and 75.4% in the second quarter and first six months of 2013.

(\$ in millions)	Three Months Ended June 30			Six Months Ended June 30		
	2014	2013	% Change	2014	2013	% Change
Truck net sales and revenues:						
U.S. and Canada	\$ 2,123.2	\$ 1,842.3	15	\$ 4,082.3	\$ 3,452.5	18
Europe	857.7	829.1	3	1,820.3	1,680.5	8
Mexico, South America, Australia and other	474.1	598.6	(21)	881.6	1,070.3	(18)
	\$ 3,455.0	\$ 3,270.0	6	\$ 6,784.2	\$ 6,203.3	9
Truck income before income taxes	\$ 259.6	\$ 238.4	9	\$ 471.9	\$ 403.4	17
Pre-tax return on revenues	7.5%	7.3%		7.0%	6.5%	

The Company's worldwide truck net sales and revenues in the second quarter of 2014 increased to \$3.46 billion from \$3.27 billion in 2013, primarily due to higher truck deliveries in the U.S. and Canada, higher price realization in Europe related to higher content Euro 6 emission vehicles, partially offset by lower truck deliveries in Europe, Mexico and Australia. The Company's worldwide truck net sales and revenues in the first six months of 2014 increased to \$6.78 billion from \$6.20 billion in 2013, primarily due to higher truck deliveries in the U.S., higher price realization in Europe related to higher content Euro 6 emission vehicles, partially offset by lower truck deliveries in Europe, Mexico and Australia.

For the second quarter and first half of 2014, Truck segment income before income taxes and pre-tax return on revenues reflect higher truck unit deliveries in the U.S. and lower R&D spending, partially offset by lower deliveries in foreign markets.

The Company's new truck deliveries are summarized below:

	Three Months Ended June 30			Six Months Ended June 30		
	2014	2013	% Change	2014	2013	% Change
U.S.	17,800	15,300	16	33,900	28,000	21
Canada	2,700	2,600	4	5,200	5,300	(2)
U.S. and Canada	20,500	17,900	15	39,100	33,300	17
Europe	8,900	11,100	(20)	18,200	21,700	(16)
Mexico, South America, Australia and other	4,300	5,700	(25)	8,200	10,300	(20)
Total units	33,700	34,700	(3)	65,500	65,300	

In the first six months of 2014, industry retail sales in the heavy-duty market in the U.S. and Canada increased to 113,600 units from 99,600 units in the same period of 2013. The Company's heavy-duty truck retail market share was 27.3% in the first half of 2014 compared to 27.6% in the first half of 2013. The medium-duty market was 36,000 units in the first half of 2014 compared to 32,800 units in the same period of 2013. The Company's medium-duty market share was 15.5% in the first six months of 2014 compared to 14.1% in the first six months of 2013.

Table of Contents**PACCAR Inc Form 10-Q**

The over 16-tonne truck market in Western and Central Europe in the first six months of 2014 was 109,000 units, a 5% increase from 103,700 units in the first six months of 2013. The largest increases were in Germany, Spain and Czech Republic, partially offset by reductions in the U.K., France and the Netherlands. The Company's market share was 12.6% in the first six months of 2014, a decrease from 15.8% in the same period of 2013. The decrease in market share was primarily due to lower DAF registrations in the U.K. and the Netherlands which were impacted by the Euro 5/Euro 6 transition rules. The 6- to 16-tonne market in the first six months of 2014 was 22,800 units compared to 25,800 units in the first six months of 2013. DAF market share in the 6- to 16-tonne market in the first six months of 2014 was 7.6% compared to 11.4% in the same period of 2013. The decline in market share is a result of reduced registrations in the U.K. which were also affected by the Euro 5/Euro 6 transition rules.

The major factors for the change in net sales and revenues, cost of sales and revenues and gross margin for the three months ended June 30, 2014 for the Truck segment are as follows:

(\$ in millions)	Net Sales	Cost of Sales	Gross Margin
Three Months Ended June 30, 2013	\$ 3,270.0	\$ 2,943.3	\$ 326.7
Increase (decrease)			
Truck delivery volume	37.4	40.5	(3.1)
Average truck sales prices	139.9		139.9
Average per truck material, labor and other direct costs		124.9	(124.9)
Factory overhead and other indirect costs		3.9	(3.9)
Operating leases	(2.7)	(4.1)	1.4
Currency translation	10.4	9.5	.9
Total increase	185.0	174.7	10.3
Three Months Ended June 30, 2014	\$ 3,455.0	\$ 3,118.0	\$ 337.0

Truck delivery volume reflects higher truck deliveries in the U.S. and Canada which resulted in higher sales (\$275.5 million) and cost of sales (\$228.8 million), partially offset by lower deliveries in Europe, Mexico and Australia which lowered sales (\$248.1 million) and cost of sales (\$198.4 million).

Average truck sales prices increased sales by \$139.9 million, primarily due to higher content Euro 6 emission vehicles in Europe (\$90.5 million) and improved price realization in the U.S. and Canada (\$35.3 million).

Cost of sales increased \$124.9 million due to higher average cost per truck, primarily from the effect of higher content Euro 6 emission vehicles in Europe (\$113.7 million).

Factory overhead and other indirect costs increased \$3.9 million primarily due to higher salaries and related costs (\$6.8 million) and depreciation expense (\$4.4 million), partially offset by lower Euro 6 project expenses (\$6.6 million).

Operating lease revenues and cost of sales decreased due to lower volume of expiring contracts. Gross margins improved due to higher average margins in the portfolio.

Truck gross margin in the second quarter of 2014 of 9.8% decreased slightly from 10.0% in the same period in 2013 due to the factors noted above.

Table of Contents**PACCAR Inc Form 10-Q**

The major factors for the change in net sales and revenues, cost of sales and revenues and gross margin for the six months ended June 30, 2014 for the Truck segment are as follows:

(\$ in millions)	Net Sales	Cost of Sales	Gross Margin
Six Months Ended June 30, 2013	\$ 6,203.3	\$ 5,609.6	\$ 593.7
Increase (decrease)			
Truck delivery volume	276.9	251.3	25.6
Average truck sales prices	288.3		288.3
Average per truck material, labor and other direct costs		243.6	(243.6)
Factory overhead and other indirect costs		34.2	(34.2)
Operating leases	15.7	12.2	3.5
Currency translation		(.2)	.2
Total increase	580.9	541.1	39.8
Six Months Ended June 30, 2014	\$ 6,784.2	\$ 6,150.7	\$ 633.5

Truck delivery volume reflects higher deliveries in the U.S. which resulted in higher sales (\$610.5 million) and cost of sales (\$518.9 million), partially offset by lower truck deliveries in Mexico, Europe and Australia with lower sales (\$363.0 million) and cost of sales (\$290.2 million).

Average truck sales prices increased sales by \$288.3 million, primarily due to higher content Euro 6 emission vehicles in Europe (\$183.1 million) and improved price realization in the U.S. and Canada (\$74.3 million).

Cost of sales increased \$243.6 million due to higher average cost per truck, primarily from the effect of higher content Euro 6 emission vehicles in Europe (\$205.2 million).

Factory overhead and other indirect costs increased \$34.2 million primarily due to higher salaries and related costs (\$31.6 million) and depreciation expense (\$12.0 million), partially offset by lower Euro 6 project expenses (\$11.7 million).

Operating lease revenues and depreciation expense increased due to a higher operating lease portfolio in Europe.

Truck gross margin in the first six months of 2014 of 9.3% decreased slightly from 9.6% in the same period in 2013 due to the factors noted above.

Truck selling, general and administrative (SG&A) expenses of \$50.1 million in the second quarter of 2014 was comparable to \$50.4 million in the second quarter of 2013. In the first six months of 2014, Truck SG&A of \$104.1 million was comparable to \$103.5 million in the first six months of 2013.

As a percentage of sales, Truck SG&A for both second quarter of 2014 and 2013 was 1.5%. For the first six months of 2014, Truck SG&A as a percentage of sales decreased to 1.5% from 1.7% in the first six months of 2013, reflecting higher sales volume.

Table of Contents

PACCAR Inc Form 10-Q

Parts

The Company's Parts segment accounted for 17.0% and 16.8% of revenues in the second quarter and first six months of 2014 compared to 16.5% and 16.7% in the second quarter and first six months of 2013.

(\$ in millions)	Three Months Ended			Six Months Ended		
	2014	June 30 2013	% Change	2014	June 30 2013	% Change
Parts net sales and revenues:						
U.S. and Canada	\$ 464.4	\$ 408.7	14	\$ 888.4	\$ 791.4	12
Europe	220.6	204.6	8	438.8	404.6	8
Mexico, South America, Australia and other	93.0	96.2	(3)	177.4	180.9	(2)
	\$ 778.0	\$ 709.5	10	\$ 1,504.6	\$ 1,376.9	9
Parts income before income taxes	\$ 126.7	\$ 109.4	16	\$ 238.8	\$ 204.7	17
Pre-tax return on revenues	16.3%	15.4%		15.9%	14.9%	

The Company's worldwide parts net sales and revenues increased in the second quarter and first six months of 2014 due to higher aftermarket demand, primarily in the U.S., Canada and Europe. The increase in Parts segment income before taxes and pre-tax return on revenues in the second quarter and first six months of 2014 was primarily due to higher sales.

The major factors for the change in net sales and revenues, cost of sales and revenues and gross margin for the three months ended June 30, 2014 for the Parts segment are as follows:

(\$ in millions)	Net Sales	Cost of Sales	Gross Margin
Three Months Ended June 30, 2013	\$ 709.5	\$ 524.6	\$ 184.9
Increase (decrease)			
Aftermarket parts volume	51.3	31.6	19.7
Average aftermarket parts sales prices	9.8		9.8
Average aftermarket parts direct costs		13.9	(13.9)
Warehouse and other indirect costs		1.2	(1.2)
Currency translation	7.4	4.5	2.9
Total increase	68.5	51.2	17.3

Three Months Ended June 30, 2014	\$ 778.0	\$ 575.8	\$ 202.2
---	-----------------	-----------------	-----------------

Higher market demand, primarily in the U.S., Canada and Europe, resulted in increased aftermarket parts sales volume of \$51.3 million and related cost of sales by \$31.6 million.

Average aftermarket parts sales prices increased sales by \$9.8 million reflecting improved price realization.

Average aftermarket parts direct costs increased \$13.9 million due to higher material costs.

Warehouse and other indirect costs increased \$1.2 million primarily due to additional costs to support higher sales volume.

Parts gross margins in the second quarter of 2014 of 26.0% decreased from 26.1% in the second quarter of 2013 due to the factors noted above.

Table of Contents**PACCAR Inc Form 10-Q**

The major factors for the change in net sales and revenues, cost of sales and revenues and gross margin for the six months ended June 30, 2014 for the Parts segment are as follows:

(\$ in millions)	Net Sales	Cost of Sales	Gross Margin
Six Months Ended June 30, 2013	\$ 1,376.9	\$ 1,022.2	\$ 354.7
Increase (decrease)			
Aftermarket parts volume	80.4	51.5	28.9
Average aftermarket parts sales prices	38.4		38.4
Average aftermarket parts direct costs		33.3	(33.3)
Warehouse and other indirect costs		3.0	(3.0)
Currency translation	8.9	4.9	4.0
Total increase	127.7	92.7	35.0
Six Months Ended June 30, 2014	\$ 1,504.6	\$ 1,114.9	\$ 389.7

Higher market demand, primarily in the U.S., Canada and Europe, resulted in increased aftermarket parts sales volume of \$80.4 million and related cost of sales by \$51.5 million.

Average aftermarket parts sales prices increased sales by \$38.4 million reflecting improved price realization.

Average aftermarket parts direct costs increased \$33.3 million due to higher material costs.

Warehouse and other indirect costs increased \$3.0 million primarily due to additional costs to support higher sales volume.

Parts gross margins in the first half of 2014 of 25.9% increased from 25.8% in the first half of 2013 due to the factors noted above.

Parts SG&A for the second quarter increased to \$52.5 million in 2014 from \$51.0 million in 2013, and in the first half of 2014, Parts SG&A increased to \$104.3 million from \$101.8 million in 2013. The increase in both periods was primarily due to higher salaries and related expenses.

As a percentage of sales, Parts SG&A decreased to 6.7% in the second quarter of 2014 from 7.2% in the second quarter of 2013 due to higher sales volume. For the first six months of 2014, Parts SG&A as a percentage of sales was

6.9%, down from 7.4% in the first six months of 2013, reflecting higher sales volume.

Table of Contents**PACCAR Inc Form 10-Q****Financial Services**

The Company's Financial Services segment accounted for 6.6% and 6.7% of revenues in the second quarter and first six months of 2014 compared to 6.7% and 7.1% in the second quarter and first six months of 2013.

(\$ in millions)	Three Months Ended June 30			Six Months Ended June 30		
	2014	2013	% Change	2014	2013	% Change
New loan and lease volume:						
U.S. and Canada	\$ 780.4	\$ 704.2	11	\$ 1,260.4	\$ 1,181.0	7
Europe	249.8	199.2	25	474.8	390.5	22
Mexico and Australia	170.8	243.0	(30)	329.1	436.9	(25)
	\$ 1,201.0	\$ 1,146.4	5	\$ 2,064.3	\$ 2,008.4	3
New loan and lease volume by product:						
Loans and finance leases	\$ 903.4	\$ 894.5	1	\$ 1,614.3	\$ 1,575.1	2
Equipment on operating lease	297.6	251.9	18	450.0	433.3	4
	\$ 1,201.0	\$ 1,146.4	5	\$ 2,064.3	\$ 2,008.4	3
New loan and lease unit volume:						
Loans and finance leases	8,500	8,420	1	15,300	15,120	1
Equipment on operating lease	2,730	2,440	12	4,230	4,240	
	11,230	10,860	3	19,530	19,360	1
Average earning assets:						
U.S. and Canada	\$ 6,650.8	\$ 6,254.7	6	\$ 6,588.6	\$ 6,221.6	6
Europe	2,787.8	2,384.1	17	2,761.7	2,380.3	16
Mexico and Australia	1,730.1	1,781.8	(3)	1,725.1	1,758.4	(2)
	\$ 11,168.7	\$ 10,420.6	7	\$ 11,075.4	\$ 10,360.3	7
Average earning assets by product:						
Loans and finance leases	\$ 7,264.1	\$ 6,790.5	7	\$ 7,215.3	\$ 6,788.3	6
Dealer wholesale financing	1,469.5	1,448.8	1	1,452.2	1,417.8	2
Equipment on lease and other	2,435.1	2,181.3	12	2,407.9	2,154.2	12
	\$ 11,168.7	\$ 10,420.6	7	\$ 11,075.4	\$ 10,360.3	7
Revenues:						
U.S. and Canada	\$ 159.2	\$ 153.5	4	\$ 312.6	\$ 314.3	(1)
Europe	81.2	73.9	10	161.3	146.2	10
Mexico and Australia	62.2	61.4	1	122.4	121.4	1
	\$ 302.6	\$ 288.8	5	\$ 596.3	\$ 581.9	2

Edgar Filing: PACCAR INC - Form 10-Q

Revenues by product:									
Loans and finance leases	\$	101.6	\$	101.6	\$	202.1	\$	202.8	
Dealer wholesale financing		13.1		13.4	(2)	25.5		26.0	
Equipment on lease and other		187.9		173.8	8	368.7		353.1	
	\$	302.6	\$	288.8	5	\$	596.3	\$	581.9
Income before income taxes	\$	91.7	\$	81.5	13	\$	177.2	\$	161.6

New loan and lease volume of \$1,201.0 million and \$2,064.3 million in the second quarter and first six months of 2014, respectively, was comparable to \$1,146.4 million and \$2,008.4 million in the second quarter and first six months of 2013. In the second quarter of 2014, finance market share on new PACCAR trucks sales was 30.4% compared to 29.9% in the second quarter of 2013, reflecting higher market share in Europe. In the first six months of 2014, finance market share on new PACCAR trucks sales was 28.8%, comparable to 29.0% in the same period of 2013.

Table of Contents**PACCAR Inc Form 10-Q**

In the second quarter of 2014, Financial Services revenues increased to \$302.6 million from \$288.8 million in 2013, and in the first six months of 2014, Financial Services revenues increased to \$596.3 million from \$581.9 million in 2013. The increase for both periods was primarily due to higher average earning asset balances, offset by lower yields. Income before income taxes increased to \$91.7 million in the second quarter of 2014 from \$81.5 million in 2013, and for the first six months of 2014, income before income taxes increased to \$177.2 million from \$161.6 million in 2013. The increase in income before income taxes for both periods was primarily due to higher finance and lease margins and a lower provision for losses on receivables.

The major factors for the change in interest and fees, interest and other borrowing expenses and finance margin for the three months ended June 30, 2014 are outlined in the table below:

(\$ in millions)	Interest and Fees	Interest and Other Borrowing Expenses	Finance Margin
Three Months Ended June 30, 2013	\$ 115.0	\$ 39.4	\$ 75.6
Increase (decrease)			
Average finance receivables	6.5		6.5
Average debt balances		1.4	(1.4)
Yields	(6.6)		(6.6)
Borrowing rates		(7.1)	7.1
Currency translation	(.2)		(.2)
Total (decrease) increase	(.3)	(5.7)	5.4
Three Months Ended June 30, 2014	\$ 114.7	\$ 33.7	\$ 81.0

Average finance receivables increased \$492.1 million (excluding foreign exchange effects) in the second quarter of 2014 as a result of retail portfolio new business volume exceeding repayments and an increase in dealer wholesale financing.

Average debt balances increased \$353.2 million in the second quarter of 2014. The higher average debt balances reflect funding for a higher average earning asset portfolio, including loans, finance leases and equipment on operating leases.

Lower market rates resulted in lower portfolio yields (5.3% in 2014 compared to 5.6% in 2013) and lower borrowing rates (1.6% in 2014 compared to 2.0% in 2013).

The major factors for the change in interest and fees, interest and other borrowing expenses and finance margin for the six months ended June 30, 2014 are outlined in the table below:

(\$ in millions)	Interest and Fees	Interest and Other Borrowing Expenses	Finance Margin
Six Months Ended June 30, 2013	\$ 228.8	\$ 78.3	\$ 150.5
Increase (decrease)			
Average finance receivables	13.5		13.5
Average debt balances		3.4	(3.4)
Yields	(12.7)		(12.7)
Borrowing rates		(10.8)	10.8
Currency translation	(2.0)	(.6)	(1.4)
Total (decrease) increase	(1.2)	(8.0)	6.8
Six Months Ended June 30, 2014	\$ 227.6	\$ 70.3	\$ 157.3

Average finance receivables increased \$509.1 million (excluding foreign exchange effects) in the first six months of 2014 as a result of retail portfolio new business volume exceeding repayments and an increase in dealer wholesale financing.

Table of Contents**PACCAR Inc Form 10-Q**

Average debt balances increased \$400.9 million in the first six months of 2014. The higher average debt balances reflect funding for a higher average earning asset portfolio, including loans, finance leases and equipment on operating leases.

Lower market rates resulted in lower portfolio yields (5.3% in 2014 compared to 5.6% in 2013) and lower borrowing rates (1.7% in 2014 compared to 2.0% in 2013).

The following table summarizes operating lease, rental and other revenues and depreciation and other expense:

(\$ in millions)	Three Months Ended June 30		Six Months Ended June 30	
	2014	2013	2014	2013
Operating lease revenues	\$ 180.7	\$ 163.1	\$ 354.2	\$ 320.5
Used truck sales and other	7.2	10.7	14.5	32.6
Operating lease, rental and other revenues	\$ 187.9	\$ 173.8	\$ 368.7	\$ 353.1
Depreciation of operating lease equipment	\$ 117.0	\$ 105.8	\$ 231.8	\$ 207.1
Vehicle operating expenses	26.9	24.3	52.3	47.6
Cost of used truck sales and other	4.5	8.8	8.6	28.3
Depreciation and other expense	\$ 148.4	\$ 138.9	\$ 292.7	\$ 283.0

The major factors for the change in operating lease, rental and other revenues, depreciation and other expense and lease margin for the three months ended June 30, 2014 are outlined below:

(\$ in millions)	Operating Lease, Rental and Other Revenues	Depreciation and Other Expense	Lease Margin
Three Months Ended June 30, 2013	\$ 173.8	\$ 138.9	\$ 34.9
Increase (decrease)			
Operating lease impairments		.5	(.5)
Used truck sales	(3.4)	(3.4)	
Results on returned lease assets		(3.2)	3.2
Average operating lease assets	10.5	8.0	2.5
Revenue and cost per asset	4.8	5.9	(1.1)

Currency translation and other		2.2		1.7		.5
Total increase		14.1		9.5		4.6
Three Months Ended June 30, 2014	\$	187.9	\$	148.4	\$	39.5

A lower volume of used truck sales decreased operating lease, rental and other revenues by \$3.4 million and decreased depreciation and other expense by \$3.4 million.

Average operating lease assets increased \$253.8 million, which increased revenues by \$10.5 million and related depreciation and other expense by \$8.0 million.

Revenue and cost per asset increased \$4.8 million and \$5.9 million, respectively. Operating lease margin decreased by \$1.1 million mainly due to lower fleet utilization and higher vehicle related expenses.

Table of Contents**PACCAR Inc Form 10-Q**

The major factors for the change in operating lease, rental and other revenues, depreciation and other expense and lease margin for the six months ended June 30, 2014 are outlined below:

(\$ in millions)	Operating Lease, Rental and Other Revenues	Depreciation and Other Expense	Lease Margin
Six Months Ended June 30, 2013	\$ 353.1	\$ 283.0	\$ 70.1
Increase (decrease)			
Operating lease impairments		.2	(.2)
Used truck sales	(17.8)	(18.2)	.4
Results on returned lease assets		(2.8)	2.8
Average operating lease assets	23.2	18.1	5.1
Revenue and cost per asset	7.0	10.2	(3.2)
Currency translation and other	3.2	2.2	1.0
Total increase	15.6	9.7	5.9
Six Months Ended June 30, 2014	\$ 368.7	\$ 292.7	\$ 76.0

A lower volume of used truck sales decreased operating lease, rental and other revenues by \$17.8 million and decreased depreciation and other expense by \$18.2 million.

Average operating lease assets increased \$253.7 million, which increased revenues by \$23.2 million and related depreciation and other expense by \$18.1 million.

Revenue and cost per asset increased \$7.0 million and \$10.2 million, respectively. Operating lease margin decreased by \$3.2 million due to lower fleet utilization and higher vehicle related expenses.

The following table summarizes the provision for losses on receivables and net charge-offs:

(\$ in millions)	Three Months Ended June 30, 2014		Six Months Ended June 30, 2014	
	Provision For Losses on	Net Charge-Offs	Provision For Losses on	Net Charge-Offs

	Receivables		Receivables	
U.S. and Canada	\$ 1.4	\$ 1.5	\$ 2.9	\$ 2.0
Europe	1.2	.9	3.4	3.1
Mexico and Australia	1.4	1.3	1.4	1.3
	\$ 4.0	\$ 3.7	\$ 7.7	\$ 6.4

(\$ in millions)	Three Months Ended June 30, 2013		Six Months Ended June 30, 2013	
	Provision For Losses on Receivables	Net Charge-Offs	Provision For Losses on Receivables	Net Charge-Offs
U.S. and Canada	\$ 2.1	\$.8	\$ 4.0	\$ 2.4
Europe	2.6	6.5	5.7	8.0
Mexico and Australia	.6		2.1	.4
	\$ 5.3	\$ 7.3	\$ 11.8	\$ 10.8

Table of Contents**PACCAR Inc Form 10-Q**

The provision for losses on receivables was \$4.0 million for the second quarter of 2014, a decrease of \$1.3 million compared to the same period in 2013, reflecting improved portfolio performance in the U.S., Canada and Europe. For the first half of 2014, the provision for losses was \$7.7 million, a decrease of \$4.1 million compared to the same period in 2013 due to improved portfolio performance in all regions.

The Company modifies loans and finance leases as a normal part of its Financial Services operations. The Company may modify loans and finance leases for commercial reasons or for credit reasons. Modifications for commercial reasons are changes to contract terms for customers that are not considered to be in financial difficulty. Insignificant delays are modifications extending terms up to three months for customers experiencing some short-term financial stress, but not considered to be in financial difficulty. Modifications for credit reasons are changes to contract terms for customers considered to be in financial difficulty. The Company's modifications typically result in granting more time to pay the contractual amounts owed and charging a fee and interest for the term of the modification. When considering whether to modify customer accounts for credit reasons, the Company evaluates the creditworthiness of the customers and modifies those accounts that the Company considers likely to perform under the modified terms. When the Company modifies loans and finance leases for credit reasons and grants a concession, the modifications are classified as troubled debt restructurings (TDR).

The post-modification balance of accounts modified during the six months ended June 30, 2014 and 2013 are summarized below:

(\$ in millions)	2014		2013	
	Recorded Investment	% of Total Portfolio*	Recorded Investment	% of Total Portfolio*
Six Months Ended June 30,				
Commercial	\$ 100.7	2.7%	\$ 139.0	4.1%
Insignificant delay	47.7	1.3%	69.1	2.0%
Credit - no concession	11.8	.3%	15.0	.5%
Credit - TDR	6.7	.2%	8.3	.2%
	\$ 166.9	4.5%	\$ 231.4	6.8%

* Recorded investment immediately after modification as a percentage of ending retail portfolio, on an annualized basis.

During the first six months of 2014, total modification activity decreased compared to 2013 primarily due to lower modifications for commercial reasons and insignificant delays. The decrease in commercial modifications primarily reflects lower levels of additional equipment financed and end-of-contract modifications. The decline in modifications for insignificant delays reflect 2013 extensions granted to two customers in Australia primarily due to business disruptions arising from flooding.

The following table summarizes the Company's 30+ days past due accounts:

	June 30 2014	December 31 2013	June 30 2013
Percentage of retail loan and lease accounts 30+ days past due:			
U.S. and Canada	.2%	.3%	.3%
Europe	.9%	.7%	1.8%
Mexico and Australia	2.0%	1.4%	1.4%
Worldwide	.6%	.5%	.7%

Accounts 30+ days past due were .6% at June 30, 2014 and have increased .1% from December 31, 2013 due to higher past due accounts in Europe, Australia and Mexico. The Company continues to focus on maintaining low past due balances.

When the Company modifies a 30+ days past due account, the customer is then generally considered current under the revised contractual terms. The Company modified \$4.3 million of accounts worldwide during the second quarter of 2014, \$4.9 million during the fourth quarter of 2013 and \$10.9 million during the second quarter of 2013 that were 30+ days past due and became current at the

Table of Contents**PACCAR Inc Form 10-Q**

time of modification. Had these accounts not been modified and continued to not make payments, the pro forma percentage of retail loan and lease accounts 30+ days past due would have been as follows:

	June 30 2014	December 31 2013	June 30 2013
Pro forma percentage of retail loan and lease accounts 30+ days past due:			
U.S. and Canada	.2%	.3%	.3%
Europe	1.1%	.8%	2.0%
Mexico and Australia	2.1%	1.7%	2.1%
Worldwide	.7%	.6%	.9%

Modifications of accounts in prior quarters that were more than 30 days past due at the time of modification are included in past dues if they were not performing under the modified terms at June 30, 2014, December 31, 2013 and June 30, 2013. The effect on the allowance for credit losses from such modifications was not significant at June 30, 2014, December 31, 2013 and June 30, 2013.

For the second quarter and first six months of 2014, the Company's annualized pre-tax return on average earning assets for Financial Services was 3.3% and 3.1% compared to 3.2% and 3.1% for the same periods in 2013.

Other

Other includes the winch business as well as sales, income and expenses not attributable to a reportable segment, including a portion of corporate expense. Other sales represent approximately 1% of consolidated net sales and revenues for both the second quarter and first six months of 2014 and 2013. Other SG&A for the second quarter was \$12.3 million in 2014 and \$10.7 million in 2013, and for the first six months, Other SG&A was \$27.8 million in 2014 compared to \$24.6 million in 2013. The increase in SG&A for both periods was primarily due to higher salaries and related expenses. For the second quarter, other income (loss) before tax was a loss of \$2.5 million in 2014 and a loss of \$4.4 million in 2013. For the first six months, other income (loss) before tax was a loss of \$11.7 million in 2014 compared to a loss of \$14.1 million in 2013. The lower loss for both periods was primarily due to higher income before tax from the winch business.

Investment income for the second quarter was \$5.5 million in 2014 compared to \$8.0 million in 2013, and for the first six months, investment income was \$11.3 million in 2014 compared to \$14.5 million in 2013. The lower investment income in the second quarter and first six months of 2014 primarily reflects lower yields on investments due to lower market interest rates, partially offset by higher average investment balances.

The effective income tax rate in the second quarter of 2014 of 33.6% increased from 32.6% in the same period of 2013, and the effective income tax rate in the first half of 2014 of 33.2% increased from 31.5% in the same period of 2013. The increases in the effective tax rates for the second quarter and first half were primarily due to a higher

proportion of income generated in higher taxed jurisdictions in 2014 as compared to 2013.

- 44 -

Table of Contents

PACCAR Inc Form 10-Q

(\$ in millions)	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2014	2013	2014	2013
Domestic income before taxes	\$ 308.3	\$ 194.2	\$ 538.5	\$ 341.4
Foreign income before taxes	172.7	238.7	349.0	428.7
Total income before taxes	\$ 481.0	\$ 432.9	\$ 887.5	\$ 770.1
Domestic pre-tax return on revenues	12.6%	9.2%	11.5%	8.7%
Foreign pre-tax return on revenues	8.1%	10.9%	8.2%	10.0%
Total pre-tax return on revenues	10.5%	10.1%	9.9%	9.4%

For the second quarter and first six months of 2014, the improvement in income before income taxes and return on revenues for domestic operations was primarily due to higher revenues from truck and parts operations and higher truck margins. The lower income before income taxes and return on revenues for foreign operations were primarily due to lower revenues and margins from truck operations from all foreign truck markets.

LIQUIDITY AND CAPITAL RESOURCES:

(\$ in millions)	June 30	December 31
	2014	2013
Cash and cash equivalents	\$ 1,380.3	\$ 1,750.1
Marketable debt securities	1,335.0	1,267.5
	\$ 2,715.3	\$ 3,017.6

The Company's total cash and marketable debt securities at June 30, 2014 decreased \$302.3 million from the balances at December 31, 2013 primarily due to a decrease in cash and cash equivalents.

The change in cash and cash equivalents is summarized below:

(\$ in millions)	2014	2013
Six Months Ended June 30,		
Operating activities:		
Net income	\$ 593.1	\$ 527.7
Net income items not affecting cash	422.2	407.2
Changes in operating assets and liabilities, net	(174.5)	217.7

Net cash provided by operating activities	840.8	1,152.6
Net cash used in investing activities	(653.2)	(938.0)
Net cash used in financing activities	(565.7)	(2.0)
Effect of exchange rate changes on cash	8.3	(43.1)
Net (decrease) increase in cash and cash equivalents	(369.8)	169.5
Cash and cash equivalents at beginning of the period	1,750.1	1,272.4
Cash and cash equivalents at end of the period	\$ 1,380.3	\$ 1,441.9

Operating activities: Cash provided by operations was \$840.8 million in the first half of 2014 compared to \$1,152.6 million in 2013. Lower operating cash flow was primarily due to a lower inflow for purchases of goods and services in accounts payable and accrued expenses in excess of payments of \$245.3 million. In addition, there were higher cash outflows due to a decrease in cash receipts for sales of goods and services in accounts receivable exceeding sales of \$95.0 million, a higher increase in net purchases of inventories of \$81.3 million and a higher decrease in income tax liabilities of \$43.9 million. These cash outflows were partially offset by \$65.4 million of higher net income and \$131.7 million from Financial Services segment wholesale receivables, whereby cash receipts exceeded sales in 2014 (\$64.8 million) versus sales exceeding cash receipts in 2013 (\$66.9 million).

Table of Contents**PACCAR Inc Form 10-Q**

Investing activities: Cash used in investing activities of \$653.2 million decreased \$284.8 million from the \$938.0 million used in the first half of 2013, primarily due to lower payments for property, plant and equipment of \$111.7 million and lower cash used in the acquisitions of equipment for operating leases of \$74.4 million. In addition, net new loan and lease originations in the Financial Services segment in the first half of 2014 were \$107.9 million lower than in the first half of 2013.

Financing activities: Cash used in financing activities increased to \$565.7 million from \$2.0 million in the first half of 2013. The Company paid \$467.8 million of dividends in the first half of 2014 compared to the \$141.4 million paid in the first half of 2013, an increase of \$326.4 million. The higher dividends in 2014 reflect a special dividend declared in 2013 and paid in early 2014. In 2013, there was no special dividend payment, as the 2012 special dividend was declared and paid in 2012. In addition, in the first half of 2014, the Company issued \$951.5 million of long-term debt and \$243.7 million of commercial paper and short-term bank loans to repay long-term debt of \$1,306.4 million. In the first half of 2013, the Company issued \$1,345.1 million in long-term debt to reduce its outstanding commercial paper and short-term bank loans of \$657.7 million and long-term debt of \$565.5 million. This resulted in cash used in borrowing activities of \$111.2 million in the first half of 2014, \$233.1 million higher than the cash provided by borrowing activities of \$121.9 million in the first half of 2013.

Credit Lines and Other

The Company has line of credit arrangements of \$3.50 billion, of which \$3.30 billion were unused at June 30, 2014. Included in these arrangements are \$3.0 billion of syndicated bank facilities, of which \$1.0 billion matures in June 2015, \$1.0 billion matures in June 2018 and \$1.0 billion matures in June 2019. The Company intends to replace these credit facilities as they expire with facilities of similar amounts and duration. These credit facilities are maintained primarily to provide backup liquidity for commercial paper borrowings and maturing medium-term notes. There were no borrowings under the syndicated bank facilities for the six months ended June 30, 2014.

In December 2011, PACCAR Inc filed a shelf registration under the Securities Act of 1933. The current registration expires in the fourth quarter of 2014 and does not limit the principal amount of debt securities that may be issued during the period. Upon maturity in February 2014, \$500.0 million of medium-term notes, of which \$150.0 million was manufacturing debt, were repaid in full. There were no medium-term notes outstanding for PACCAR Inc as of June 30, 2014.

In December 2011, PACCAR's Board of Directors approved the repurchase of \$300.0 million of the Company's common stock, and as of June 30, 2014, \$192.0 million of shares have been repurchased pursuant to the authorization.

Truck, Parts and Other

The Company provides funding for working capital, capital expenditures, R&D, dividends, stock repurchases and other business initiatives and commitments primarily from cash provided by operations. Management expects this method of funding to continue in the future.

Investments for property, plant and equipment in the first half of 2014 decreased to \$108.9 million from \$209.2 million, as the first half of 2013 included higher spending for new product development and construction of the Eindhoven parts distribution center in Europe and DAF Brasil factory. Over the past decade, the Company's

combined investments in worldwide capital projects and R&D totaled \$5.81 billion, which have significantly increased operating capacity and efficiency of its facilities and the competitive advantage of the Company's premium products.

- 46 -

Table of Contents

PACCAR Inc Form 10-Q

In 2014, capital investments are expected to be approximately \$250 to \$300 million and are targeted for enhanced powertrain development and increased operating efficiency of the Company's assembly facilities. Spending on R&D in 2014 is expected to be \$200 to \$225 million as PACCAR will continue to focus on new products and services.

The Company conducts business in Spain, Italy, Portugal, Ireland and Greece, which have been experiencing significant financial stress. As of June 30, 2014, the Company had finance and trade receivables in these countries of approximately 1% of consolidated total assets. As of June 30, 2014, the Company did not have any marketable debt security investments in corporate or sovereign government securities in these countries. In addition, the Company had no derivative counterparty credit exposures in these countries as of June 30, 2014.

Financial Services

The Company funds its financial services activities primarily from collections on existing finance receivables and borrowings in the capital markets. The primary sources of borrowings in the capital markets are commercial paper and medium-term notes issued in the public markets and, to a lesser extent, bank loans. An additional source of funds is loans from other PACCAR companies.

The Company issues commercial paper for a portion of its funding in its Financial Services segment. Some of this commercial paper is converted to fixed interest rate debt through the use of interest rate swaps, which are used to manage interest rate risk. In the event of a future significant disruption in the financial markets, the Company may not be able to issue replacement commercial paper. As a result, the Company is exposed to liquidity risk from the shorter maturity of short-term borrowings paid to lenders compared to the longer timing of receivable collections from customers. The Company believes its cash balances and investments, collections on existing finance receivables, syndicated bank lines and current investment-grade credit ratings of A+/A1 will continue to provide it with sufficient resources and access to capital markets at competitive interest rates and therefore contribute to the Company maintaining its liquidity and financial stability. A decrease in these credit ratings could negatively impact the Company's ability to access capital markets at competitive interest rates and the Company's ability to maintain liquidity and financial stability.

In November 2012, the Company's U.S. finance subsidiary, PACCAR Financial Corp. (PFC), filed a shelf registration under the Securities Act of 1933. The total amount of medium-term notes outstanding for PFC as of June 30, 2014 was \$4.05 billion. The registration expires in November 2015 and does not limit the principal amount of debt securities that may be issued during that period.

As of June 30, 2014, the Company's European finance subsidiary, PACCAR Financial Europe, had 417.6 million available for issuance under a 1.50 billion medium-term note program registered with the London Stock Exchange. The program was renewed in the second quarter of 2014 and is renewable annually through the filing of a new prospectus.

In April 2011, PACCAR Financial Mexico registered a 10.00 billion peso medium-term note and commercial paper program with the Comision Nacional Bancaria y de Valores. The registration expires in 2016 and limits the amount of commercial paper (up to one year) to 5.00 billion pesos. At June 30, 2014, 8.44 billion pesos remained available for issuance.

PACCAR believes its Financial Services companies will be able to continue funding receivables, servicing debt and paying dividends through internally generated funds, access to public and private debt markets and lines of credit.

FORWARD-LOOKING STATEMENTS:

Certain information presented in this report contains forward-looking statements made pursuant to the Private Securities Litigation Reform Act of 1995, which are subject to risks and uncertainties that may affect actual results. Risks and uncertainties include, but are not limited to: a significant decline in industry sales; competitive pressures; reduced market share; reduced availability of or higher prices for fuel; increased safety, emissions, or other regulations resulting in higher costs and/or sales restrictions; currency or commodity price fluctuations; lower used truck prices; insufficient or under-utilization of manufacturing capacity; supplier

Table of Contents

PACCAR Inc Form 10-Q

interruptions; insufficient liquidity in the capital markets; fluctuations in interest rates; changes in the levels of the Financial Services segment new business volume due to unit fluctuations in new PACCAR truck sales or reduced market shares; changes affecting the profitability of truck owners and operators; price changes impacting truck sales prices and residual values; insufficient supplier capacity or access to raw materials; labor disruptions; shortages of commercial truck drivers; increased warranty costs or litigation; or legislative and governmental regulations. A more detailed description of these and other risks is included under the heading Part 1, Item 1A, Risk Factors in the Company's Annual Report on Form 10-K for the year ended December 31, 2013.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There were no material changes in the Company's market risk during the six months ended June 30, 2014. For additional information, refer to Item 7A as presented in the 2013 Annual Report on Form 10-K.

ITEM 4. CONTROLS AND PROCEDURES

The Company's management, with the participation of the Principal Executive Officer and Principal Financial Officer, conducted an evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)) as of the period covered by this report. Based on that evaluation, the Principal Executive Officer and Principal Financial Officer concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report.

There have been no significant changes in the Company's internal controls over financial reporting that occurred during the fiscal quarter covered by this quarterly report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II OTHER INFORMATION

For Items 3, 4 and 5, there was no reportable information for the six months ended June 30, 2014.

ITEM 1. LEGAL PROCEEDINGS

The Company and its subsidiaries are parties to various lawsuits incidental to the ordinary course of business. Management believes that the disposition of such lawsuits will not materially affect the Company's business or financial condition.

In January 2011, the European Union (EU) Competition Commission commenced an investigation of all major European commercial vehicle manufacturers, including subsidiaries of the Company, concerning whether such companies participated in agreements or concerted practices to coordinate their commercial policy in the EU. The Company's subsidiaries are cooperating fully with the EU Competition Commission.

ITEM 1A. RISK FACTORS

For information regarding risk factors, refer to Part I, Item 1A as presented in the 2013 Annual Report on Form 10-K. There have been no material changes in the Company's risk factors during the six months ended June 30, 2014.

- 48 -

Table of Contents

PACCAR Inc Form 10-Q

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

For items 2(a) and (b), there was no reportable information for the six months ended June 30, 2014.

(c) Issuer purchases of equity securities.

On December 6, 2011, the Company's Board of Directors approved a plan to repurchase up to \$300 million of the Company's outstanding common stock. As of June 30, 2014, \$192.0 million of shares have been repurchased under this plan. There were no repurchases made under this plan during the first six months of 2014.

ITEM 6. EXHIBITS

Any exhibits filed herewith are listed in the accompanying index to exhibits.

Table of Contents

PACCAR Inc Form 10-Q

SIGNATURE

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.

PACCAR Inc
(Registrant)

Date August 7, 2014

By /s/ M. T. Barkley
M. T. Barkley
Vice President and Controller
(Authorized Officer and Chief Accounting Officer)

- 50 -

Table of Contents**PACCAR Inc Form 10-Q****INDEX TO EXHIBITS**Exhibit (in order of assigned index numbers)

Exhibit Number	Exhibit Description	Date of First Form Filing	Exhibit Number	File Number
(3) (i)	Articles of Incorporation:			
	(a) Restated Certificate of Incorporation of PACCAR Inc	8-K	September 19, 2005	99.3 001-14817
	(b) Certificate of Amendment of Certificate of Incorporation of PACCAR Inc dated April 28, 2008	10-Q	May 2, 2008	3(b) 001-14817
(3) (ii)	Bylaws:			
	(a) Second Amended and Restated Bylaws of PACCAR Inc	8-K	July 13, 2012	3(ii) 001-14817
	(b) Third Amended and Restated Bylaws of PACCAR Inc	8-K	December 13, 2013	3(ii) 001-14817
(4)	Instruments defining the rights of security holders, including indentures:			
	(a) Indenture for Senior Debt Securities dated as of November 20, 2009 between PACCAR Financial Corp. and The Bank of New York Mellon Trust Company, N.A.	10-K	February 26, 2010	4(c) 001-11677
	(b) Forms of Medium-Term Note, Series M (PACCAR Financial Corp.)	S-3	November 20, 2009	4.2 and 4.3 333-163273
	(c) Forms of Medium-Term Note, Series N (PACCAR Financial Corp.)	S-3	November 7, 2012	4.2 and 4.3 333-184808
	(d) Form of InterNotes, Series B (PACCAR Financial Corp.)	S-3	November 7, 2012	4.4 333-184808
	(e) Indenture for Senior Debt Securities dated as of December 19, 2011 between PACCAR Inc and The Bank of New York Mellon Trust Company, N.A.	S-3	December 19, 2011	4.1 333-178607
	(f) Forms of Medium-Term Note, Series B (Fixed- and Floating-Rate)	S-3	December 19, 2011	4.2A and 4.2B 333-178607

(g)	Terms and Conditions of the Notes applicable to the 1,500,000,000 Medium Term Note Programme of PACCAR Financial Europe B.V.	10-Q	November 7, 2013	4(i)	001-14817
-----	---	------	------------------	------	-----------

Table of Contents**PACCAR Inc Form 10-Q**

Exhibit Number	Exhibit Description	Form	Date of First Filing	Exhibit Number	File Number
	(h) Pursuant to the Instructions to Exhibits, certain instruments defining the rights of holders of long-term debt securities of the Company and its wholly owned subsidiaries are not filed because the total amount of securities authorized under any such instrument does not exceed 10 percent of the Company's total assets. The Company will file copies of such instruments upon request of the Commission.				
(10)	Material Contracts:				
	(a) PACCAR Inc Amended and Restated Supplemental Retirement Plan	10-K	February 27, 2009	10(a)	001-14817
	(b) Amended and Restated Deferred Compensation Plan	10-Q	May 5, 2012	10(b)	001-14817
	(c) Deferred Incentive Compensation Plan (Amended and Restated as of December 31, 2004)	10-K	February 27, 2006	10(b)	001-14817
	(d) Second Amended and Restated PACCAR Inc Restricted Stock and Deferred Compensation Plan for Non-Employee Directors	DEF14A	March 14, 2014	10(v)	001-14817
	(e) PACCAR Inc Restricted Stock and Deferred Compensation Plan for Non-Employee Directors, Form of Restricted Stock Agreement for Non-Employee Directors	10-K	February 27, 2009	10(e)	001-14817
	(f) PACCAR Inc Restricted Stock and Deferred Compensation Plan for Non-Employee Directors, Form of Deferred Restricted Stock Unit Agreement for Non-Employee Directors	8-K	December 10, 2007	99.3	001-14817
	(g) Amendment to Compensatory Arrangement with Non-Employee Directors	10-K	February 29, 2012	10(g)	001-14817
	(h) PACCAR Inc Senior Executive Yearly Incentive Compensation Plan	DEF14A	March 10, 2011	Appendix B	001-14817
	(i) PACCAR Inc Long Term Incentive Plan	DEF14A	March 10, 2011	Appendix A	001-14817
	(j) PACCAR Inc Long Term Incentive Plan, Nonstatutory Stock Option Agreement and Form of Option Grant Agreement	8-K	January 25, 2005	99.1	001-14817
	(k) Amendment One to PACCAR Inc Long Term Incentive Plan, Nonstatutory Stock	10-Q	August 7, 2013	10(k)	001-14817

Option Agreement and Form of Option
Grant Agreement

- 52 -

Table of Contents**PACCAR Inc Form 10-Q**

Exhibit Number	Exhibit Description	Form	Date of First Filing	Exhibit Number	File Number
(l)	PACCAR Inc Long Term Incentive Plan, 2014 Form of Nonstatutory Stock Option Agreement	10-Q	August 7, 2013	10(l)	001-14817
(m)	PACCAR Inc Long Term Incentive Plan, Form of Restricted Stock Award Agreement	8-K	February 5, 2007	99.1	001-14817
(n)	PACCAR Inc Long Term Incentive Plan, 2010 Form of Restricted Stock Award Agreement	10-K	February 26, 2010	10(m)	001-14817
(o)	PACCAR Inc Long Term Incentive Plan, Alternate Form of Restricted Stock Award Agreement	10-K	March 1, 2011	10(n)	001-14817
(p)	PACCAR Inc Long Term Incentive Plan, 2011 Form of Share Match Restricted Stock Award Agreement	10-K	March 1, 2011	10(p)	001-14817
(q)	PACCAR Inc Savings Investment Plan, Amendment and Restatement effective January 1, 2009	10-K	March 1, 2011	10(r)	001-14817
(r)	Memorandum of Understanding, dated as of May 11, 2007, by and among PACCAR Engine Company, the State of Mississippi and certain state and local supporting government entities	8-K	May 16, 2007	10.1	001-14817
(s)	Letter Waiver Dated as of July 22, 2008 amending the Memorandum of Understanding, dated as of May 11, 2007, by and among PACCAR Engine Company, the State of Mississippi and certain state and local supporting governmental entities	10-Q	October 27, 2008	10(o)	001-14817
(t)	Second Amendment to Memorandum of Understanding dated as of September 26, 2013, by and among PACCAR Engine Company, the Mississippi Development Authority and the Mississippi Major Economic Impact Authority	10-Q	November 7, 2013	10(u)	001-14817
(12)	Statements Re: Computation of Ratios:				
(a)	Computation of ratio of earnings to fixed charges of the Company pursuant to SEC reporting requirements for the six months ended June 30, 2014 and 2013*				

Table of Contents**PACCAR Inc Form 10-Q**

Exhibit Number	Exhibit Description	Form	Date of First Filing	Exhibit Number	File Number
	(b) Statement re: computation of ratio of earnings to fixed charges of the Company pursuant to SEC reporting requirements for each of the five years ended December 31, 2009 - 2013	10-K	February 27, 2014	12(a)	001-14817
(31)	Rule 13a-14(a)/15d-14(a) Certifications:				
	(a) Certification of Principal Executive Officer*				
	(b) Certification of Principal Financial Officer*				
(32)	Section 1350 Certifications:				
	Certification pursuant to rule 13a-14(b) and section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. section 1350)*				
(101.INS)	XBRL Instance Document*				
(101.SCH)	XBRL Taxonomy Extension Schema Document*				
(101.CAL)	XBRL Taxonomy Extension Calculation Linkbase Document*				
(101.DEF)	XBRL Taxonomy Extension Definition Linkbase Document*				
(101.LAB)	XBRL Taxonomy Extension Label Linkbase Document*				
(101.PRE)	XBRL Taxonomy Extension Presentation Linkbase Document*				

* filed herewith