

EXPEDITORS INTERNATIONAL OF WASHINGTON INC  
Form 10-Q  
August 09, 2007

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended June 30, 2007**

**OR**

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

**For the transition period from            to**

**Commission File Number: 0-13468**

**EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.**

(Exact name of registrant as specified in its charter)

**Washington**

(State or other jurisdiction of  
incorporation or organization)

**91-1069248**

(IRS Employer Identification Number)

**1015 Third Avenue, 12th Floor, Seattle, Washington**

(Address of principal executive offices)

**98104**

(Zip Code)

**(206) 674-3400**

(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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

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Large accelerated filer

Accelerated filer

Non-accelerated filer

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

At August 6, 2007, the number of shares outstanding of the issuer's Common Stock was 213,122,438.

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**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements**EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIESCondensed Consolidated Balance Sheets  
(In thousands, except share data)

(Unaudited)

	June 30, 2007	December 31, 2006
<b>Assets</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 575,042	\$ 511,358
Short-term investments	466	578
Accounts receivable, less allowance for doubtful accounts of \$13,388 at June 30, 2007 and \$13,454 at December 31, 2006	829,202	811,486
Deferred Federal and state income taxes	7,613	7,490
Other current assets	25,438	10,925
Total current assets	1,437,761	1,341,837
Property and equipment, less accumulated depreciation and amortization of \$197,259 at June 30, 2007 and \$178,695 at December 31, 2006	455,639	450,856
Goodwill, less accumulated amortization of \$765 at June 30, 2007 and December 31, 2006	7,927	7,927
Other intangibles, net	6,853	7,584
Other assets, net	29,081	14,134
	\$ 1,937,261	\$ 1,822,338
<b>Liabilities and Shareholders Equity</b>		
<b>Current liabilities:</b>		
Short-term borrowings	213	
Accounts payable	583,632	544,028
Accrued expenses, primarily salaries and related costs	148,602	122,081
Federal, state and foreign income taxes	30,821	43,036
Total current liabilities	763,268	709,145
Deferred Federal and state income taxes	42,463	26,743
Minority interest	16,497	16,515
<b>Shareholders equity:</b>		
Preferred stock, par value \$.01 per share Authorized 2,000,000 shares; none issued		
Common stock, par value \$.01 per share Authorized 320,000,000 shares; issued and outstanding 212,995,326 shares at June 30, 2007, and 213,080,466 shares at December 31, 2006	2,130	2,131
Additional paid-in capital	63,581	119,582
Retained earnings	1,028,933	934,058
Accumulated other comprehensive income	20,389	14,164
Total shareholders equity	1,115,033	1,069,935

Commitments and contingencies

	\$	1,937,261	\$	1,822,338
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See accompanying notes to condensed consolidated financial statements.

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EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

Condensed Consolidated Statements of Earnings  
(In thousands, except share data)

(Unaudited)

	Three months ended June 30, 2007		Six months ended June 30, 2007	
		2006		2006
<b>Revenues:</b>				
Airfreight	\$	564,471	\$	545,273
Ocean freight and ocean services		450,431		380,280
Customs brokerage and other services		243,716		205,888
			\$	1,081,676
				\$
Total revenues		1,258,618		1,131,441
				2,377,564
				2,157,978
<b>Operating expenses:</b>				
Airfreight consolidation		437,446		429,976
Ocean freight consolidation		364,917		300,780
Customs brokerage and other services		101,681		84,998
Salaries and related costs		197,393		172,453
Rent and occupancy costs		15,744		15,489
Depreciation and amortization		10,275		8,626
Selling and promotion		9,581		8,957
Other		19,843		21,359
				41,355
				41,448
Total operating expenses		1,156,880		1,042,638
				2,181,301
				1,983,774
Operating income		101,738		88,803
				196,263
				174,204
Interest expense		118	(10	) 104
Interest income		5,531		10,750
Other, net		1,675		2,430
				2,132
Other income, net		7,324		4,845
				13,284
				10,759
Earnings before income taxes and minority interest		109,062		93,648
Income tax expense		43,315		35,503
				84,475
				72,555
Net earnings before minority interest		65,747		58,145
				125,072
				112,408
Minority interest	(258	)	(1,816	)
			(295	)
				(3,727
				)
Net earnings	\$	65,489	\$	56,329
			\$	124,777
				\$
Diluted earnings per share	\$	.30	\$	.25
			\$	.56
				\$
Basic earnings per share	\$	.31	\$	.26
			\$	.58
				\$
Dividends declared and paid per common share	\$	.14	\$	.11
			\$	.14
				\$
Weighted average diluted shares outstanding		221,716,414		224,374,720
				222,283,372
				224,051,286
Weighted average basic shares outstanding		213,251,710		213,725,395
				213,339,478
				213,574,773

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See accompanying notes to condensed consolidated financial statements.

Certain 2006 amounts have been reclassified to conform to the 2007 presentation.

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EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows  
(In thousands)

(Unaudited)

	Three months ended June 30, 2007		Six months ended June 30, 2006	
		2006		2006
<b>Operating activities:</b>				
Net earnings	\$	65,489	\$	56,329
			\$	124,777
			\$	108,681
Adjustments to reconcile net earnings to net cash provided by operating activities:				
Provision for losses on accounts receivable	(869	) 647	(355	) 493
Deferred income tax expense	6,772		12,240	12,589
Excess tax benefits from stock plans	(5,291	) (14,973	) (21,623	) (21,008
Stock compensation expense	12,043	9,418	23,503	17,816
Depreciation and amortization	10,275	8,626	19,850	16,679
Gain on sale of property and equipment	(79	) (68	) (202	) (215
Minority interest in earnings of consolidated entities	258	1,816	295	3,727
Other	354	787	688	1,861
Changes in operating assets and liabilities:				
Increase in accounts receivable	(70,962	) (49,838	) (13,261	) (28,999
Decrease (increase) in other current assets	173	(1,299	) (504	) (1,772
Increase in accounts payable and other current liabilities	76,080	40,164	62,445	69,016
(Decrease) increase in income taxes payable, net	(7,311	) (2,340	) (4,842	) 14,843
Net cash provided by operating activities	86,932	55,578	203,011	193,711
<b>Investing activities:</b>				
(Increase) decrease in short-term investments	76	(275	) 162	(283
Purchase of property and equipment	(12,904	) (100,334	) (26,342	) (121,833
Proceeds from sale of property and equipment	119	87	498	265
Prepayment on long-term land lease	(2,848	)	(2,848	)
Deposit on building purchase	(5,056	)	(5,056	)
Other	(1,188	) 692	(1,528	) 486
Net cash used in investing activities	(21,801	) (99,830	) (35,114	) (121,365
<b>Financing activities:</b>				
Proceeds (repayments) of short-term debt, net	(17	)	203	
Proceeds from issuance of common stock	12,602	20,513	27,868	26,020
Repurchases of common stock	(56,597	) (86,669	) (128,995	) (113,628
Excess tax benefits from stock plans	5,291	14,973	21,623	21,008
Dividends paid	(29,902	) (23,575	) (29,902	) (23,576
Net distributions to minority interest	(316	)	(316	)
Net cash used in financing activities	(68,939	) (74,758	) (109,519	) (90,176
Effect of exchange rate changes on cash	2,034	6,016	5,306	8,630
(Decrease) increase in cash and cash equivalents	(1,774	) (112,994	) 63,684	(9,200
Cash and cash equivalents at beginning of period	576,816	567,688	511,358	463,894
Cash and cash equivalents at end of period	\$ 575,042	\$ 454,694	\$ 575,042	\$ 454,694
<b>Interest and taxes paid:</b>				
Interest	\$	127	\$	8
			\$	138
			\$	32

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Income taxes	41,279	30,376	74,312	43,051
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See accompanying notes to condensed consolidated financial statements.

Certain 2006 amounts have been reclassified to conform to the 2007 presentation.

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EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

**Note 1. Summary of Significant Accounting Policies**

The attached condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. As a result, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted. The Company believes that the disclosures made are adequate to make the information presented not misleading. The condensed consolidated financial statements reflect all adjustments, consisting of normal recurring items, which are, in the opinion of management, necessary to a fair statement of the results for the interim periods presented. These condensed consolidated financial statements should be read in conjunction with the financial statements and related notes included in the Company's Form 10-K as filed with the Securities and Exchange Commission on or about March 1, 2007.

Certain 2006 amounts have been reclassified to conform to the 2007 presentation.

**Note 2. Comprehensive Income**

Comprehensive income consists of net income and other gains and losses affecting shareholders' equity that, under generally accepted accounting principles in the United States, are excluded from net income. For the Company, these consist of foreign currency translation gains and losses and unrealized gains and losses on securities, net of related income tax effects.

The components of total comprehensive income for interim periods are presented in the following table:

(in thousands)	Three months ended June 30, 2007		Six months ended June 30, 2007	
	2007	2006	2007	2006
Net earnings	\$ 65,489	\$ 56,329	\$ 124,777	\$ 108,681
Foreign currency translation adjustments net of tax of \$(2,456) and \$(2,586) for the 3 months ended June 30, 2007 and 2006, and \$(3,352) and \$(3,732) for the 6 months ended June 30, 2007 and 2006.	4,562	4,802	6,226	6,930
Unrealized gain (loss) on securities net of tax of \$(12) and \$9 for the 3 months ended June 30, 2007 and 2006, and \$1 and \$52 for the 6 months ended June 30, 2007 and 2006.	18	(13)	(1)	(33)
Total comprehensive income	\$ 70,069	\$ 61,118	\$ 131,002	\$ 115,578

**Note 3. Business Segment Information**

Statement of Financial Accounting Standards (SFAS) No. 131, "Disclosure about Segments of an Enterprise and Related Information" establishes standards for the way that public companies report selected information about segments in their financial statements.

The Company is organized functionally in geographic operating segments. Accordingly, management focuses its attention on revenues, net revenues, operating income, identifiable assets, capital expenditures, depreciation and amortization and equity generated in each of these geographical areas when evaluating the effectiveness of geographic management. The Company charges its subsidiaries and affiliates for services rendered in the United States on a cost recovery basis. Transactions among the Company's various offices are conducted using the same arms-length pricing methodologies the Company uses when its offices transact business with independent agents.



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Financial information regarding the Company's operations by geographic area for the three and six-months ended June 30, 2007 and 2006 are as follows:

(in thousands)	UNITED STATES	OTHER NORTH AMERICA	ASIA	EUROPE	AUSTRAL-ASIA	LATIN AMERICA	MIDDLE EAST	ELIMI-NATIONS	CONSOLI-DATED
<b>Three months ended June 30, 2007:</b>									
Revenues from unaffiliated customers	\$ 260,796	32,765	710,104	162,100	17,057	19,377	56,419		1,258,618
Transfers between geographic areas	25,856	1,989	4,470	8,172	1,853	3,078	3,340	(48,758)	)
Total revenues	\$ 286,652	34,754	714,574	170,272	18,910	22,455	59,759	(48,758)	) 1,258,618
Net revenues	\$ 143,206	15,377	100,479	58,600	9,812	10,950	16,150		354,574
Operating income	\$ 31,459	2,941	46,587	11,951	2,658	2,354	3,788		101,738
Identifiable assets at quarter end	\$ 893,335	69,599	431,106	395,022	30,617	37,310	82,642	(2,370)	) 1,937,261
Capital expenditures	\$ 7,843	688	1,188	2,141	198	267	579		12,904
Depreciation and amortization	\$ 5,304	331	1,222	2,393	225	417	383		10,275
Equity	\$ 1,256,503	32,692	326,036	134,925	20,114	19,571	39,555	(714,363)	) 1,115,033
<b>Three months ended June 30, 2006:</b>									
Revenues from unaffiliated customers	\$ 232,275	30,254	629,016	156,268	13,435	16,801	53,392		1,131,441
Transfers between geographic areas	27,485	1,962	4,171	7,900	1,621	2,111	2,680	(47,930)	)
Total revenues	\$ 259,760	32,216	633,187	164,168	15,056	18,912	56,072	(47,930)	) 1,131,441
Net revenues	\$ 128,278	15,871	88,945	53,330	8,024	8,287	12,952		315,687
Operating income	\$ 27,659	3,864	40,855	10,051	2,127	1,665	2,582		88,803
Identifiable assets at quarter end	\$ 839,926	57,363	369,930	329,676	22,431	32,241	58,371	5,612	1,715,550
Capital expenditures	\$ 91,578	198	4,467	3,096	109	468	418		100,334
Depreciation and amortization	\$ 4,417	345	1,210	1,729	189	382	354		8,626
Equity	\$ 1,106,283	24,124	276,872	95,304	14,245	13,256	25,951	(586,434)	) 969,601
<b>Six months ended June 30, 2007:</b>									
Revenues from unaffiliated customers	\$ 506,521	60,851	1,312,135	318,479	31,840	38,748	108,990		2,377,564
Transfers between geographic areas	48,354	3,967	8,450	15,933	3,550	5,584	6,763	(92,601)	)
Total revenues	\$ 554,875	64,818	1,320,585	334,412	35,390	44,332	115,753	(92,601)	) 2,377,564
Net revenues	\$ 278,673	30,077	193,632	114,627	18,739	20,745	32,217		688,710
Operating income	\$ 59,522	5,670	91,471	22,102	5,062	4,406	8,030		196,263
Identifiable assets at period end	\$ 893,335	69,599	431,106	395,022	30,617	37,310	82,642	(2,370)	) 1,937,261
Capital expenditures	\$ 16,548	1,012	2,521	3,526	892	762	1,081		26,342
Depreciation and amortization	\$ 10,473	662	2,597	4,130	425	817	746		19,850
Equity	\$ 1,256,503	32,692	326,036	134,925	20,114	19,571	39,555	(714,363)	) 1,115,033
<b>Six months ended June 30, 2006:</b>									
	\$ 453,442	58,635	1,185,711	296,633	25,788	32,910	104,859		2,157,978

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Revenues from unaffiliated customers									
Transfers between geographic areas	52,927	3,692	7,854	15,225	3,030	4,004	5,062	(91,794	)
Total revenues	\$ 506,369	62,327	1,193,565	311,858	28,818	36,914	109,921	(91,794	) 2,157,978
Net revenues	\$ 255,922	30,553	169,694	101,933	15,424	15,474	24,829		613,829
Operating income	\$ 52,227	7,203	82,139	20,624	4,108	2,939	4,964		174,204
Identifiable assets at period end	\$ 839,926	57,363	369,930	329,676	22,431	32,241	58,371	5,612	1,715,550
Capital expenditures	\$ 108,764	295	7,221	3,810	346	791	606		121,833
Depreciation and amortization	\$ 8,485	696	2,400	3,265	387	747	699		16,679
Equity	\$ 1,106,283	24,124	276,872	95,304	14,245	13,256	25,951	(586,434	) 969,601

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**Note 4. Basic and Diluted Earnings per Share**

The following table reconciles the numerator and the denominator of the basic and diluted per share computations for earnings per share for the three months and six-months ended June 30, 2007 and 2006:

(Amounts in thousands, except share and per share amounts)	Three months ended June 30,		
	Net Earnings	Weighted Average Shares	Earnings Per Share
<b>2007</b>			
Basic earnings per share	\$ 65,489	213,251,710	\$ .31
Effect of dilutive potential common shares		8,464,704	
Diluted earnings per share	\$ 65,489	221,716,414	\$ .30
<b>2006</b>			
Basic earnings per share	\$ 56,329	213,725,395	\$ .26
Effect of dilutive potential common shares		10,649,325	
Diluted earnings per share	\$ 56,329	224,374,720	\$ .25

(Amounts in thousands, except share and per share amounts)	Six months ended June 30,		
	Net Earnings	Weighted Average Shares	Earnings Per Share
<b>2007</b>			
Basic earnings per share	\$ 124,777	213,339,478	\$ .58
Effect of dilutive potential common shares		8,943,894	
Diluted earnings per share	\$ 124,777	222,283,372	\$ .56
<b>2006</b>			
Basic earnings per share	\$ 108,681	213,574,773	\$ .51
Effect of dilutive potential common shares		10,476,513	
Diluted earnings per share	\$ 108,681	224,051,286	\$ .49

The following shares have been excluded from the computation of diluted earnings per share because the effect would have been antidilutive:

	Three months ended		Six months ended	
	June 30, 2007	2006	June 30, 2007	2006
Shares	4,852,570	128,000	3,035,010	128,000

**Note 5. Stock and Cash Dividends**

On May 3, 2007, the Board of Directors declared a semi-annual cash dividend of \$.14 per share payable on June 15, 2007 to shareholders of record as of June 1, 2007. The dividend of \$30 million was paid on June 15, 2007.



On May 3, 2006, the Board of Directors declared a semi-annual cash dividend of \$.11 per share payable on June 15, 2006 to shareholders of record as of June 1, 2006. The dividend of \$24 million was paid on June 15, 2006.

On May 3, 2006, the Board of Directors declared a 2-for-1 stock split, effected in the form of a stock dividend of one share of common stock for every share outstanding. The stock dividend was distributed on June 23, 2006 to shareholders of record on June 9, 2006. All share and per share information, except par value per share, has been adjusted for all years to reflect the stock split.

**Note 6. Shareholders Equity**

**A. Stock Option Plans and Stock Purchase Plan**

The Company provides compensation benefits by granting stock options to its employees and directors and employee stock purchase rights to its employees. In accordance with SFAS No. 123R, Share-Based Payment (SFAS 123R) the Company recognizes compensation expense based on the estimated fair value of options awarded under its fixed stock option and employee stock purchase rights plans. The stock compensation expense is recognized on a straight-line basis over the period stock options become vested. The Company's annual grant of option awards generally takes place during the second quarter of each fiscal year. For the three and six-month periods ended June 30, 2007 and 2006, 1,930,510 and 3,109,000 options were granted, respectively. The grant of employee stock purchase rights and the issuance of shares under the employee stock purchase plan are generally made in the third quarter of each fiscal year and none were issued in the three and six-month periods ended June 30, 2007 and 2006.

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions used for grants issued during the six months ended June 30, 2007 and 2006.

	Six months ended June 30,					
	2007		2006			
Dividend yield	.65		%	.51		%
Volatility	35	41	%	41	43	%
Risk-free interest rates	4.69	4.75	%	5.03	5.11	%
Expected life (years) - stock option plans	6.54	8.70		7.21	8.89	
Weighted average fair value of stock options granted during the period	\$ 18.49			\$ 22.69		

Total stock compensation expense and the total related tax benefit recognized in the three and six-months ended June 30, 2007 and 2006 are as follows:

	Three months ended June 30,		Six months ended June 30,	
	2007	2006	2007	2006
Stock compensation expense	\$ 12,043	\$ 9,418	\$ 23,503	\$ 17,816
Recognized tax benefit	\$ 482	\$ 317	\$ 1,070	\$ 838

**Note 7. Income Taxes**

On January 1, 2007, the Company adopted the provisions of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48), supplemented by FASB Financial Staff Position FIN 48-1, Definition of Settlement in FASB Interpretation No. 48, issued May 2, 2007. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in the Company's financial statements in accordance with SFAS No. 109, Accounting for Income Taxes (SFAS 109). The interpretation establishes guidelines for recognition, measurement, presentation and disclosure of uncertain tax positions taken or expected to be taken in income tax returns. The adoption of FIN 48 had no material impact on the Company's consolidated financial condition or results of operations.

Based on management's review of the Company's tax positions the Company had no significant unrecognized tax benefits as of June 30, 2007 and January 1, 2007.

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The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction and various state, local and foreign jurisdictions. The Company is no longer subject to U.S. federal income tax examinations by tax authorities for years prior to 2003. With respect to state and local jurisdictions and countries outside of the United States, with limited exceptions, the Company and its subsidiaries are no longer subject to income tax audits for years prior to 2000. In the normal course of business, the Company is subject to examination by taxing authorities throughout the world. Although the outcome of tax audits is always uncertain, the Company believes that adequate amounts of tax, interest and penalties have been provided for any adjustments that may result from these open tax years.

The Company recognizes interest expense related to unrecognized tax benefits or underpayment of income taxes in interest expense and recognizes penalties in operating expenses. The Company has not changed its policy as a result of adopting FIN 48.

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Amounts accrued for the payment of interest and penalties were insignificant at the date of adoption of FIN 48. Accordingly, any interest and penalties expensed in relation to the underpayment of income taxes were insignificant for the three and six months ended June 30, 2007 and 2006.

#### **Note 8. Recent Accounting Pronouncements**

Effective January 1, 2007, the Company adopted Emerging Issues Task Force Issue 06-3, How Sales Taxes Collected From Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement, (EITF 06-3). The scope of EITF 06-3 includes any tax assessed by a governmental authority that is both imposed on and concurrent with a specific revenue-producing transaction between a seller and a customer, including but not limited to sales and value-added taxes. In EITF 06-3 a consensus was reached that entities may adopt a policy of presenting these taxes in the income statement on either a gross or net basis. If these taxes are significant, an entity should disclose its policy of presenting taxes and the amount of taxes if reflected on a gross basis in the income statement. The Company presents revenues net of sales and value-added taxes in its condensed consolidated statements of earnings and did not change its policy as a result of the adoption of EITF 06-3. The adoption of EITF 06-3 had no impact on the Company's condensed consolidated financial condition or results of operations.

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, Fair Value Measurements (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is required to and plans to adopt the provisions of SFAS 157 beginning in the first quarter of 2008. The Company is currently assessing the impact of the adoption of SFAS 157.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159). Under the provisions of SFAS 159, companies may choose to account for eligible financial instruments, warranties and insurance contracts at fair value on a contract-by-contract basis. Changes in fair value will be recognized in earnings each reporting period. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is required to and plans to adopt the provisions of SFAS 159 beginning in the first quarter of 2008. The Company is currently assessing the impact of the adoption of SFAS 159.

#### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

#### **SAFE HARBOR FOR FORWARD-LOOKING STATEMENTS UNDER SECURITIES LITIGATION REFORM ACT OF 1995; CERTAIN CAUTIONARY STATEMENTS**

Certain portions of this report on Form 10-Q including the section entitled Currency and Other Risk Factors and Liquidity and Capital Resources contain forward-looking statements which must be considered in connection with the discussion of the important factors that could cause actual results to differ materially from the forward-looking statements. In addition to risk factors identified elsewhere in this report, attention should be given to the factors identified and discussed in the report on Form 10-K filed on or about March 1, 2007.

#### **EXECUTIVE SUMMARY**

Expeditors International of Washington, Inc. is engaged in the business of global logistics management, including international freight forwarding and consolidation, for both air and ocean freight. The Company acts as a customs broker in its domestic and many of its international operating offices. The Company also provides additional services for its customers including value-added distribution, purchase order management, vendor consolidation and other logistics solutions. The Company does not compete for overnight courier or small parcel business. The Company does not own or operate aircraft or steamships.

#### **Note 7. Income Taxes**

International trade is influenced by many factors, including economic and political conditions in the United States and abroad, currency exchange rates, and United States and foreign laws and policies relating to tariffs, trade restrictions, foreign investments and taxation. Periodically, governments consider a variety of changes to current tariffs and trade restrictions. The Company cannot predict which, if any, of these proposals may be adopted, nor can the Company predict the effects the adoption of any such proposal will have on the Company's business. Doing business in foreign locations also subjects the Company to a variety of risks and considerations not normally encountered by domestic enterprises. In addition to being influenced by governmental policies concerning international trade, the Company's business may also be affected by political developments and changes in government personnel or policies in the nations in which it does business.

The Company derives its revenues from three principal sources: 1) airfreight, 2) ocean freight and 3) customs brokerage and other services and these are the revenue categories presented in the financial statements.

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As a non-asset based carrier, the Company does not own transportation assets. Rather, the Company generates the major portion of its air and ocean freight revenues by purchasing transportation services from direct (asset-based) carriers and reselling those services to its customers. The difference between the rate billed to customers (the sell rate), and the rate paid to the carrier (the buy rate) is termed net revenue or yield. By consolidating shipments from multiple customers and concentrating its buying power, the Company is able to negotiate favorable buy rates from the direct carriers, while at the same time offering lower sell rates than customers would otherwise be able to negotiate themselves.

Customs brokerage and other services involves providing services at destination, such as helping customers clear shipments through customs by preparing required documentation, calculating and providing for payment of duties and other taxes on behalf of the customers as well as arranging for any required inspections by governmental agencies, and arranging for delivery. This is a complicated function requiring technical knowledge of customs rules and regulations in the multitude of countries in which the Company has offices.

The Company's ability to provide services to its customers is highly dependent on good working relationships with a variety of entities including airlines, ocean steamship lines, and governmental agencies. The significance of maintaining acceptable working relationships with governmental agencies and asset-based providers involved in global trade has gained increased importance as a result of ongoing concern over terrorism. As each carrier labors to comply with governmental regulations implementing security policies and procedures, inherent conflicts emerge which can and do affect global trade to some degree. A good reputation helps to develop practical working understandings that will effectively meet security requirements while minimizing potential international trade obstacles. The Company considers its current working relationships with these entities to be satisfactory. However, changes in space allotments available from carriers, governmental deregulation efforts, modernization of the regulations governing customs brokerage, and/or changes in governmental quota restrictions could affect the Company's business in unpredictable ways.

Historically, the Company's operating results have been subject to a seasonal trend when measured on a quarterly basis. The first quarter has traditionally been the weakest and the third and fourth quarters have traditionally been the strongest. This pattern is the result of, or is influenced by, numerous factors including climate, national holidays, consumer demand, economic conditions and a myriad of other similar and subtle forces. In addition, this historical quarterly trend has been influenced by the growth and diversification of the Company's international network and service offerings. The Company cannot accurately forecast many of these factors nor can the Company estimate accurately the relative influence of any particular factor and, as a result, there can be no assurance that historical patterns, if any, will continue in future periods.

A significant portion of the Company's revenues are derived from customers in retail industries whose shipping patterns are tied closely to consumer demand, and from customers in industries whose shipping patterns are dependent upon just-in-time production schedules. Therefore, the timing of the Company's revenues are, to a large degree, impacted by factors out of the Company's control, such as a sudden change in consumer demand for retail goods and/or manufacturing production delays. Additionally, many customers ship a significant portion of their goods at or near the end of a quarter, and therefore, the Company may not learn of a shortfall in revenues until late in a quarter. To the extent that a shortfall in revenues or earnings was not expected by securities analysts, any such shortfall from levels predicted by securities analysts could have an immediate and adverse effect on the trading price of the Company's stock.

As further discussed under liquidity and capital resources, total capital expenditures in 2007 are expected to exceed \$106 million.

In terms of the opportunities, challenges and risks that management is focused on in 2007, the Company operates in 60 countries throughout the world in the competitive global logistics industry and Company activities are tied directly to the global economy. From the inception of the Company, management has believed that the elements required for a successful global service organization can only be assured through recruiting, training, and ultimately retaining superior personnel. The Company's greatest challenge is now and always has been perpetuating a consistent global culture which demands:

- Total dedication, first and foremost, to providing superior customer service;
- Aggressive marketing of all of the Company's service offerings;
- Ongoing development of key employees and management personnel via formal and informal means;
- Creation of unlimited advancement opportunities for employees dedicated to hard work, personal growth and continuous improvement;
- Individual commitment to the identification and mentoring of successors for every key position so that when inevitable change is required, a qualified and well-trained internal candidate is ready to step forward; and

- Continuous identification, design and implementation of system solutions, both technological and otherwise, to meet and exceed the needs of our customers while simultaneously delivering tools to make our employees more efficient and more effective.

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The Company has reinforced these values with a compensation system that rewards employees for profitably managing the things they can control. There is no limit to how much a key manager can be compensated for success. The Company believes in a real world environment in every operating unit where individuals are not sheltered from the profit implications of their decisions. At the same time, the Company insists on continued focus on such things as accounts receivable collection, cash flow management and credit soundness in an attempt to insulate managers from the sort of catastrophic errors that might end a career.

Any failure to perpetuate this unique culture on a self-sustained basis throughout the Company, provides a greater threat to the Company's continued success than any external force, which would be largely beyond our control. Consequently, management spends the majority of its time focused on creating an environment where employees can learn and develop while also building systems and taking preventative action to reduce exposure to negative events. The Company strongly believes that it is nearly impossible to predict events that, in the aggregate, could have a positive or a negative impact on future operations. As a result our focus is on building and maintaining a global culture of well-trained employees and managers that are prepared to identify and react to subtle changes as they develop and thereby help the Company adapt and thrive as major trends emerge.

### Critical Accounting Policies and Estimates

**Management believes that the nature of the Company's business is such that there are few, if any, complex challenges in accounting for operations.**

While judgments and estimates are a necessary component of any system of accounting, the Company's use of estimates is limited primarily to the following areas that in the aggregate are not a major component of the Company's statement of earnings:

- accounts receivable valuation;
- the useful lives of long-term assets;
- the accrual of costs related to ancillary services the Company provides;
- establishment of adequate insurance liabilities for the portion of the freight related exposure which the Company has self-insured; and
- accrual of tax expense on an interim basis.

Management believes that the methods utilized in all of these areas are non-aggressive in approach and consistent in application. Management believes that there are limited, if any, alternative accounting principles or methods which could be applied to the Company's transactions. While the use of estimates means that actual future results may be different from those contemplated by the estimates, the Company believes that alternative principles and methods used for making such estimates would not produce materially different results than those reported.

As described in Note 6 in the condensed consolidated financial statements in this quarterly report, the Company accounts for share-based compensation in accordance with SFAS 123R. This accounting standard requires the recognition of compensation expense based on an estimate of the fair value of options granted to employees and directors under the Company's stock option and employee stock purchase plans.

This expense is recorded on a straight-line basis over the option vesting periods.

Determining the appropriate option pricing model to use to estimate stock compensation expense requires judgment. Any option pricing model requires assumptions that are subjective and these assumptions also require judgment. Examples include assumptions about long-term stock price volatility, employee exercise patterns, pre-vesting option forfeitures, post-vesting option terminations, and the future interest rates and dividend yields.

The Company uses the Black-Scholes model for estimating the fair value of stock options. Refer to Note 6 in the condensed consolidated financial statements for the assumptions used for grants issued during the six months ended June 30, 2007 and 2006. The assumptions used by the Company for estimating the fair value of options granted under SFAS 123R were developed on a basis consistent with assumptions used for valuing previous grants.

Management believes that the nature of the Company's business is such that there are few, if any, complex challenges

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Management believes that these assumptions are appropriate, based upon the requirements of SFAS 123R and the guidance included in SAB 107 and the company's historical and currently expected future experience. Looking to future events, management has been strongly influenced by historical patterns which may not be valid predictors of future developments and any future deviation may be material.

The Company's expected volatility assumptions are based on the historical volatility of the Company's stock. The expected life assumption is primarily based on historical employee exercise patterns and employee post-vesting termination behavior. The risk-free interest rate for the expected term of the option is based on the corresponding yield curve in effect at the time of grant for U.S. Treasury bonds having the same term as the expected life of the option, i.e. a ten year bond rate is used for valuing an option with a

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ten year expected life. The expected dividend yield is based on the Company's historical experience. The forfeiture rate used to calculate compensation expense is primarily based on historical pre-vesting employee forfeiture patterns.

The use of different assumptions would result in different amounts of stock compensation expense. Keeping all other variables constant, the indicated change in each of the assumptions below increases or decreases the fair value of an option (and the resulting stock compensation expense), as follows:

Assumption	Change in assumption	Impact of fair value of options
Expected volatility	Higher	Higher
Expected life of option	Higher	Higher
Risk-free interest rate	Higher	Higher
Expected dividend yield	Higher	Lower

The fair value of an option is more significantly impacted by changes in the expected volatility and expected life assumptions. The pre-vesting forfeitures assumption is ultimately adjusted to the actual forfeiture rate. Therefore, changes in the forfeitures assumption would not impact the total amount of expense ultimately recognized over the vesting period. Different forfeitures assumptions would only impact the timing of expense recognition over the vesting period. Estimated forfeitures will be reassessed in subsequent periods and may change based on new facts and circumstances.

## Results of Operations

The following table shows the consolidated net revenues (revenues less transportation expenses) attributable to the Company's principal services and the Company's expenses for the three and six-month periods ended June 30, 2007 and 2006, expressed as percentages of net revenues. Management believes that net revenues are a better measure than total revenues of the relative importance of the Company's principal services since total revenues earned by the Company as a freight consolidator include the carriers' charges to the Company for carrying the shipment whereas revenues earned by the Company in its other capacities include only the commissions and fees actually earned by the Company.

The table and the accompanying discussion and analysis should be read in conjunction with the condensed consolidated financial statements and related notes thereto which appear elsewhere in this quarterly report.

	Three months ended June 30, 2007		2006		Six months ended June 30, 2007		2006	
	Amount (Amounts in thousands)	Percent of net revenues	Amount	Percent of net revenues	Amount	Percent of net revenues	Amount	Percent of net revenues
<b>Net revenues:</b>								
Airfreight	\$ 127,025	36 %	\$ 115,297	37 %	\$ 254,586	37 %	\$ 225,714	37 %
Ocean freight and ocean services	85,514	24	79,500	25	161,825	23	153,280	25
Customs brokerage and other services	142,035	40	120,890	38	272,299	40	234,835	38
Net revenues	354,574	100	315,687	100	688,710	100	613,829	100
<b>Overhead expenses:</b>								
Salaries and related costs	197,393	56	172,453	55	380,154	55	333,427	55
Other	55,443	16	54,431	17	112,293	17	106,198	17
Total overhead expenses	252,836	72	226,884	72	492,447	72	439,625	72
Operating income	101,738	28	88,803	28	196,263	28	174,204	28
Other income, net	7,324	2	4,845	2	13,284	2	10,759	2
<b>Earnings before income taxes and minority interest</b>								
Income tax expense	109,062	30	93,648	30	209,547	30	184,963	30
Income tax expense	43,315	12	35,503	11	84,475	12	72,555	12
<b>Net earnings before minority interest</b>								
Minority interest	65,747	18	58,145	19	125,072	18	112,408	18
Minority interest	(258)		(1,816)	(1)	(295)		(3,727)	
Net earnings	\$ 65,489	18 %	\$ 56,329	18 %	\$ 124,777	18 %	\$ 108,681	18 %

Airfreight net revenues increased 10% and 13% for the three and six-month periods ended June 30, 2007, respectively, as compared with the same periods for 2006. The increase in airfreight net revenues for the three month period was due to a 4% increase in airfreight tonnages handled by the Company during the second quarter of 2007 and a 136 basis point yield expansion (a 6% increase), as compared with the same period of 2006. The increase in airfreight net revenues for the six-month period was due to a 5% increase in airfreight tonnage and a 176 basis point yield expansion (an 8% increase), as compared with the same period of 2006.

The Company's North American airfreight net revenues increased 1% for the three months ended June 30, 2007, as compared to the same period for 2006. Airfreight net revenues for Asia and for the Middle East/Indian subcontinent increased 20% and 18%, respectively, for the three month comparative periods. For the same three month period there was no appreciable change in European airfreight net revenues. The increase in Asia is primarily the result of yield increases of 13% combined with tonnage increases of 7%. The increase in the Middle East/Indian subcontinent is primarily the result of yield increases of 16% partially offset by tonnage decreases of 6%.

Management believes that the nature of the Company's business is such that there are few, if any, complex challenges.





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For the six months ended June 30, 2007, as compared with the same period for 2006, the Company's North American airfreight net revenues increased 7% while airfreight net revenues for Asia, for Europe and for the Middle East/Indian subcontinent increased 20%, 3% and 19%, respectively. The increase in North America is primarily the result of tonnage increases of 6%. The increase in Asia is primarily the result of yield increases of 13% combined with tonnage increases of 7%. The increase in the Middle East/Indian subcontinent is primarily the result of yield increases of 19% partially offset by tonnage decreases of 11%.

Ocean freight volumes, measured in terms of forty-foot container equivalent units (FEUs), increased 19% for the three-month period ended June 30, 2007, as compared with the same period for 2006 while ocean freight and ocean services net revenues increased 8% during the same period. The difference between these two rates is a result of a year-over-year decrease in ocean freight yields which were partially offset by year-over-year increases in the Company's fee-based order management and ocean forwarding business. The primary reason for the decline in ocean freight yields was due to direct carrier cost increases that market conditions would not allow to be passed on in a timely manner. For the six-month period ended June 30, 2007, as compared with the same period for 2006, FEU count increased 16% while ocean freight and ocean services net revenues increased 6% during the same period. The difference in these two rates is attributable to the same dynamics as described for the three-month period.

The Company's North American ocean freight net revenues increased approximately 2% and 1% for the three and six-month periods ended June 30, 2007, respectively, as compared with the same periods for 2006. This was due to an increase in container traffic, primarily from Asia despite rising carrier costs as discussed above. Increases in order management and ocean forwarding business, were a result of continued marketing efforts and customer service initiatives. Ocean freight net revenues for Asia and for Europe increased 8% and 7%, respectively, for the three months ended June 30, 2007, and 3% and 10%, respectively, for the six months ended June 30, 2007, as compared with the same periods for 2006. These increases were also a result of continued marketing efforts and customer service initiatives.

Customs brokerage and other services net revenues increased 17% and 16% for the three and six-month periods ended June 30, 2007, respectively, as compared with the same periods for 2006 as a result of the Company's continued focus on providing high quality customer service. Consolidation within the customs brokerage market has also contributed to this increase as customers seek out customs brokers with more sophisticated computerized capabilities critical to an overall logistics management program. In addition, increased emphasis on regulatory compliance continues to benefit the Company's customs brokerage offerings.

Salaries and related costs increased 14% during the three and six-month periods ended June 30, 2007, as compared with the same periods in 2006 as a result of (1) the Company's increased hiring of sales, operations, and administrative personnel in existing and new offices to accommodate increases in business activity, and (2) increased compensation levels.

The effect of including stock-based compensation expense in salaries and related costs for the three and six months ended June 30, 2007 and 2006 are as follows:

	<b>For the three months ended June 30, 2007</b>		<b>2006</b>		<b>For the six months ended June 30, 2007</b>		<b>2006</b>	
Salaries and related costs	\$	197,393	\$	172,453	\$	380,154	\$	333,427
As a % of net revenue		55.7	%	54.6	%	55.2	%	54.3
Stock compensation expense	\$	12,043	\$	9,418	\$	23,503	\$	17,816
As a % of salaries and related costs		6.1	%	5.5	%	6.2	%	5.3
As a % of net revenue		3.4	%	3.0	%	3.4	%	2.9

Of the 104 and 88 basis point increase in salaries and related costs as a percentage of net revenue for the three and six-month periods ended June 30, 2007, respectively, as compared with the same periods for 2006, 41 and 51 basis points, respectively, are the result of the increase in stock compensation expense as a percentage of net revenue.

The remaining 63 and 37 basis point increase in salaries and related costs as a percentage of net revenue for the three and six-month periods ended June 30, 2007, respectively, as compared to the same period for 2006, can be attributed to increased staffing levels in anticipation of increased business volumes in the second half of the year. Historically, the relatively consistent relationship between salaries and net revenues is the result of a compensation philosophy that has been maintained since the inception of the Company: offer a modest base salary and the

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opportunity to share in a fixed and determinable percentage of the operating profit of the business unit controlled by each key employee. Using this compensation model, changes in individual compensation will occur in proportion to changes in Company profits. Management believes that the growth in revenues, net revenues and net earnings for the three and six-month periods ended June 30, 2007 are a result of the incentives inherent in the Company's compensation program.

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Management believes that the nature of the Company's business is such that there are few, if any, competitive challenges.

Other overhead expenses increased 2% and 6% for the three and six-month periods ended June 30, 2007, as compared with the same periods in 2006 as communications expense, quality and training expenses, and other costs expanded to accommodate the Company's growing operations. Other overhead expenses as a percentage of net revenues remained relatively constant for the three and six-month periods ended June 30, 2007, respectively, as compared with the same periods in 2006.

Other income, net, increased 51% and 23% for the three and six-month periods ended June 30, 2007, as compared with the same periods in 2006. Due to higher interest rates on higher average cash balances and short-term investments during the three and six months ended June 30, 2007, as compared with the same periods for 2006, interest income increased \$1 million and \$2 million, respectively.

The Company pays income taxes in the United States and other jurisdictions, as well as other taxes which are typically included in costs of operations. The Company's consolidated effective income tax rate during the three-month period ended June 30, 2007, was 39.7% as compared to 37.9% for the same period in 2006. The Company's consolidated effective income tax rate for the six month periods ended June 30, 2007 and 2006 was 40.3% and 39.2%, respectively. Although a tax benefit related to stock-based compensation expense is recorded for non-qualified stock options at the time the related compensation expense is recognized, the tax benefit received for disqualifying dispositions of incentive stock options cannot be anticipated. The higher consolidated effective income tax rate during the three and six-month periods ended June 30, 2007, as compared to the same periods in 2006, is partially the result of a larger tax benefit received for disqualifying dispositions of incentive stock options occurring during the second quarter of 2006 compared to 2007.

### **Currency and Other Risk Factors**

International air/ocean freight forwarding and customs brokerage are intensively competitive and are expected to remain so for the foreseeable future. There are a large number of entities competing in the international logistics industry; however, the Company's primary competition is confined to a relatively small number of companies within this group. While there is currently a marked trend within the industry toward consolidation into large firms with multinational offices and agency networks, regional and local broker/forwarders remain a competitive force.

Historically, the primary competitive factors in the international logistics industry have been price and quality of service, including reliability, responsiveness, expertise, convenience, and scope of operations. The Company emphasizes quality service and believes that its prices are competitive with those of others in the industry. Customers have exhibited a trend towards more sophisticated and efficient procedures for the management of the logistics supply chain by embracing strategies such as just-in-time inventory management. The Company believes that this trend has resulted in customers using fewer service providers with greater technological capacity and consistent global coverage. Accordingly, sophisticated computerized customer service capabilities and a stable worldwide network have become significant factors in attracting and retaining customers.

Developing these systems and a worldwide network has added a considerable indirect cost to the services provided to customers. Smaller and middle-tier competitors, in general, do not have the resources available to develop customized systems and a worldwide network. As a result, there is a significant amount of consolidation currently taking place in the industry. Management expects that this trend toward consolidation will continue for the short- to medium-term.

The nature of the Company's worldwide operations necessitates the Company dealing with a multitude of currencies other than the U.S. dollar. This results in the Company being exposed to the inherent risks of the international currency markets and governmental interference. Some of the countries where the Company maintains offices and/or agency relationships have strict currency control regulations which influence the Company's ability to hedge foreign currency exposure. The Company tries to compensate for these exposures by accelerating international currency settlements among its offices or agents. The Company enters into foreign currency hedging transactions only in limited locations where there are regulatory or commercial limitations on the Company's ability to move money freely or the short-term financial outlook is such that hedging is the way to avoid short-term exchange losses. Any such hedging activity during the three and six months ended June 30, 2007 and 2006 was insignificant. For the three and six months ended June 30, 2007, the Company had foreign exchange gains of approximately \$1,407 and \$1,297, respectively, on a net basis. For the same periods of 2006, respectively, the Company had foreign exchange losses of approximately \$246 and foreign exchange gains of approximately \$803, respectively, on a net basis. The Company had no foreign currency derivatives outstanding at June 30, 2007 and 2006.

### **Sources of Growth**

During the second quarter of 2007, the Company opened one satellite office in the United States, in Knoxville, Tennessee.

Acquisitions - Historically, growth through aggressive acquisition has proven to be a challenge for many of the Company's competitors and typically involves the purchase of significant goodwill, the value of which can be realized in large measure only by retaining the customers and profit margins of the acquired business. As a result, the Company has pursued a strategy emphasizing organic growth supplemented by certain

Management believes that the nature of the Company's business is such that there are few, if any, complex challenges.

strategic acquisitions, where future economic benefit significantly exceeds the goodwill recorded in the transaction.

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Management believes that the nature of the Company's business is such that there are few, if any, complex challenges

Internal Growth - Management believes that a comparison of same store growth is critical in the evaluation of the quality and extent of the Company's internally generated growth. This same store analysis isolates the financial contributions from offices that have been included in the Company's operating results for at least one full year. The table below presents same store comparisons for the three and six-months ended June 30, 2007 (which is the measure of any increase from the same period of 2006) and for the three and six-months ended June 30, 2006 (which measures growth over 2005).

	For the three months ended June 30, 2007		2006		For the six months ended June 30, 2007		2006	
Net revenue	12	%	25	%	12	%	26	%
Operating income	15	%	51	%	13	%	59	%

### Liquidity and Capital Resources

The Company's principal source of liquidity is cash generated from operating activities. Net cash provided by operating activities for the three and six months ended June 30, 2007, was \$87 million and \$203 million, as compared with \$56 million and \$194 million for the same periods of 2006. The \$31 million increase for the three months ended June 30, 2007, is primarily due to increased net earnings and a favorable swing in the timing of receipts and disbursements represented by accounts receivable and accounts payable balances. The \$9 million increase for the six months ended June 30, 2007, is principally due to increased net earnings offset by a decrease in taxes payable, net of prepaid taxes.

The Company's business is subject to seasonal fluctuations. Cash flow fluctuates as a result of this seasonality. Historically, the first quarter shows an excess of customer collections over customer billings. This results in positive cash flow. The increased activity associated with peak season (typically commencing late second or early third quarter) causes an excess of customer billings over customer collections. This cyclical growth in customer receivables consumes available cash.

As a customs broker, the Company makes significant 5-10 business day cash advances for its customers' obligations such as the payment of duties to the Customs and Border Protection of the Department of Homeland Security. These advances are made as an accommodation for a select group of credit-worthy customers. Cash advances are a pass through and are not recorded as a component of revenue and expense. The billings of such advances to customers are accounted for as a direct increase in accounts receivable to the customer and a corresponding increase in accounts payable to governmental customs authorities. As a result of these pass through billings, the conventional Days Sales Outstanding or DSO calculation does not directly measure collection efficiency.

Cash used in investing activities for the three and six months ended June 30, 2007, was \$22 million and \$35 million, as compared with \$100 million and \$121 million during the same periods of 2006. The largest use of cash in investing activities is cash paid for capital expenditures. As a non-asset based provider of integrated logistics services, the Company does not own any physical means of transportation (i.e., airplanes, ships, trucks, etc.). However, the Company does have need, on occasion, to purchase buildings to house staff and to facilitate the staging of customers' freight. The Company routinely invests in technology, office furniture and equipment and leasehold improvements. In the second quarter of 2007, the Company made capital expenditures of \$13 million as compared with \$100 million for the same period in 2006. The Company currently expects to spend approximately \$43 million for routine capital expenditures in 2007. In addition to property and equipment, normal capital expenditures include leasehold improvements, warehouse equipment, computer hardware and furniture and fixtures. Total capital expenditures in 2007 are estimated to be \$106 million. This includes normal capital expenditures as noted above, plus additional real estate acquisitions and development. In April 2007, the Company signed a commitment to purchase 48,300 square feet of office space in Kowloon, Hong Kong. The transaction closed in July 2007 for approximately \$34 million (HK\$263 million). The Company expects to finance capital expenditures in 2007 with cash.

Cash used in financing activities during the three and six months ended June 30, 2007 were \$69 million and \$110 million as compared with \$75 million and \$90 million for each of the same periods in 2006. The Company uses the proceeds from stock option exercises to repurchase the Company's stock on the open market. The Company follows a policy of repurchasing stock to limit growth in issued and outstanding shares as a result of stock option exercises. The increase in cash used in financing activities during the three and six months ended June 30, 2007 as compared with the same periods in 2006 is primarily the result of this policy. During the three months ended June 30, 2007 and 2006, the net use of cash in financing activities included the payment of dividends of \$.14 per share and \$.11 per share, respectively.

At June 30, 2007, working capital was \$674 million, including cash and short-term investments of \$576 million. The Company had no long-term debt at June 30, 2007.

Management believes that the nature of the Company's business is such that there are few, if any, complex challenges.

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The Company maintains international and domestic unsecured bank lines of credit. At June 30, 2007, the United States facility totaled \$50 million and international bank lines of credit, excluding the U. K. bank facility, totaled \$17 million. In addition, the Company maintains a bank facility with its U.K. bank for \$14 million which is available for issuances of standby letters of credit. At June 30, 2007 the Company had no amounts outstanding on these lines of credit but was contingently liable for \$65 million from

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Management believes that the nature of the Company's business is such that there are few, if any, complex challenges

standby letters of credit and guarantees related to these lines of credit and other obligations. The guarantees relate to obligations of the Company's foreign subsidiaries for credit extended in the ordinary course of business by direct carriers, primarily airlines, and for duty and tax deferrals available from governmental entities responsible for customs and value-added-tax (VAT) taxation. The total underlying amounts due and payable for transportation and governmental excises are properly recorded as obligations in the books of the respective foreign subsidiaries, and there would be no need to record additional expense in the unlikely event the parent company were to be required to perform.

Management believes that the Company's current cash position, bank financing arrangements, and operating cash flows will be sufficient to meet its capital and liquidity requirements for the foreseeable future, including meeting any contingent liabilities related to standby letters of credit and other obligations.

In some cases, the Company's ability to repatriate funds from foreign operations may be subject to foreign exchange controls. At June 30, 2007, cash and cash equivalent balances of \$450 million were held by the Company's non-U.S. subsidiaries, of which \$104 million was held in banks in the United States.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

The Company is exposed to market risks in the ordinary course of its business. These risks are primarily related to foreign exchange risk and changes in short-term interest rates. The potential impact of the Company's exposure to these risks is presented below:

#### **Foreign Exchange Risk**

The Company conducts business in many different countries and currencies. The Company's business often results in revenue billings issued in a country and currency which differs from that where the expenses related to the service are incurred. In the ordinary course of business, the Company creates numerous intercompany transactions. This brings a market risk to the Company's earnings.

Foreign exchange rate sensitivity analysis can be quantified by estimating the impact on the Company's earnings as a result of hypothetical changes in the value of the U.S. dollar, the Company's functional currency, relative to the other currencies in which the Company transacts business. All other things being equal, an average 10% weakening of the U.S. dollar, throughout the six-months ended June 30, 2007, would have had the effect of raising operating income approximately \$16 million. An average 10% strengthening of the U.S. dollar, for the same period, would have had the effect of reducing operating income approximately \$13 million. This analysis does not take in to account changes in shipping patterns based upon this hypothetical currency fluctuation. For example, a weakening in the U.S. dollar would be expected to increase exports from the United States and decrease imports into the United States over some relevant period of time, but the exact effect of this change cannot be quantified without making speculative assumptions.

At June 30, 2007, the Company had approximately \$3 million of net unsettled intercompany transactions. The Company currently does not use derivative financial instruments to manage foreign currency risk and only enters into foreign currency hedging transactions in limited locations where regulatory or commercial limitations restrict the Company's ability to move money freely. Any such hedging activity during the three and six months ended June 30, 2007, was insignificant. The Company had no foreign currency derivatives outstanding at June 30, 2007 and 2006. The Company instead follows a policy of accelerating international currency settlements to manage foreign exchange risk relative to intercompany billings. The majority of intercompany billings are resolved within 30 days and intercompany billings arising in the normal course of business are fully settled within 90 days.

#### **Interest Rate Risk**

At June 30, 2007, the Company had cash and cash equivalents and short-term investments of \$576 million, the vast majority of which is subject to variable short-term interest rates. The Company had \$213 in short-term borrowings at June 30, 2007. A hypothetical change in the interest rate of 10% would not have a significant impact on the Company's earnings.

In management's opinion, there has been no material change in the Company's market risk exposure in the second quarter of 2007.

### **Item 4. Controls and Procedures**

#### **Evaluation of Controls and Procedures**

The Company carried out an evaluation, under the supervision and with the participation of its management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in the Exchange Act Rule 13a-15(e)) as of the end of the period covered by this report. Based upon that evaluation, the Chief Executive



Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective.

**Changes in Internal Controls**

There were no changes in the Company's internal control over financial reporting that occurred during the most recent fiscal quarter that have materially affected or are reasonably likely to materially affect the Company's internal control over financial reporting.

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EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

**PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

The Company is ordinarily involved in claims and lawsuits which arise in the normal course of business, none of which currently, in management's opinion, will have a significant effect on the Company's financial position or results of operations.

**Item 1A. Risk Factors**

There have been no material changes in the Company's risk factors from those disclosed in the report on Form 10-K filed on or about March 1, 2007.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

## ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number of shares that may yet be purchased under the plans or programs
April 1-30, 2007	365,345	\$ 41.79	365,345	17,319,454
May 1-31, 2007	125,427	44.99	125,427	17,749,109
June 1-30, 2007	832,764	42.85	832,764	16,936,685
Total	1,323,536	\$ 42.76	1,323,536	16,936,685

In November 1993, the Company's Board of Directors authorized a Non-Discretionary Stock Repurchase Plan. This plan was amended in February 2001 to increase the authorization to repurchase up to 20 million shares of the Company's common stock. This authorization has no expiration date. This plan was disclosed in the Company's report on Form 10-K filed March 31, 1995. In the second quarter of 2007, 382,585 shares were repurchased under the Non-Discretionary Stock Repurchase Plan.

In November 2001, under a Discretionary Stock Repurchase Plan, the Company's Board of Directors authorized the repurchase of such shares as may be necessary to reduce the issued and outstanding stock to 200 million shares of common stock. The maximum number of shares available for repurchase under this plan will increase as the total number of outstanding shares increases. This authorization has no expiration date. This plan was announced on November 13, 2001. In the second quarter of 2007, 940,951 shares were repurchased under the Discretionary Stock Repurchase Plan. These discretionary repurchases were made to limit the growth in the number of issued and outstanding shares resulting from stock option exercises.

**Item 4. Submission of Matters to a Vote of Security Holders**

- (a) The annual meeting of the Shareholders was held on May 2, 2007.
- (b) The following directors were elected to the Board of Directors to serve a term of one year and until their successors are elected and qualified:

	For	Withheld
P.J. Rose	181,614,156	5,767,072
J.L.K. Wang	180,844,021	6,537,207
R.J. Gates	165,924,368	21,456,860
J.J. Casey	166,783,914	20,597,314
D.P. Kourkoumelis	182,416,964	4,964,264
M.J. Malone	185,480,747	1,900,481
J.W. Meisenbach	182,407,728	4,973,500

		<b>For</b>	<b>Against</b>	<b>Abstain</b>	<b>Non-Vote</b>
(c)	Adoption of the 2007 Stock Option Plan	111,382,415	56,140,520	277,700	19,580,594

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		For	Against	Abstain	Non-Vote
(d)	Amendment of the 2002 Employee Stock Purchase Plan	166,331,548	1,302,866	166,219	19,580,594
		For	Against	Abstain	Non-Vote
(e)	Ratification of KPMG LLP as the Company's Independent Auditor Selection	186,879,084	443,524	58,620	
		For	Against	Abstain	Non-Vote
(f)	Shareholder proposal to amend the Company's existing equal opportunity policy	73,592,113	89,350,968	4,857,552	19,580,594

**Item 5. Other Information**

(a) The Company's bylaws were amended by the Board of Directors on May 2, 2007 and were further amended on August 6, 2007. The Company's Amended and Restated Bylaws are filed as Exhibit 3.2 to this Form 10-Q.

(b) Not applicable.

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**Item 6. Exhibits**

<b>Exhibit Number</b>	<b>Description</b>
Exhibit 3.2	The Company's Amended and Restated Bylaws.
Exhibit 10.39.1	Amendment to the Amended 1993 Directors' Non-Qualified Stock Option Plan.
Exhibit 31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
Exhibit 31.2	Certification pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
Exhibit 32	Certification pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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SIGNATURES

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

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.

August 9, 2007

/s/ PETER J. ROSE  
Peter J. Rose, Chairman and Chief Executive Officer  
(Principal Executive Officer)

August 9, 2007

/s/ R. JORDAN GATES  
R. Jordan Gates, Executive Vice President-Chief Financial Officer  
(Principal Financial and Accounting Officer)

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EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

Form 10-Q Index and Exhibits

June 30, 2007

<b>Exhibit Number</b>	<b>Description</b>
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32	Certification pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
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