

PACCAR INC  
Form 10-Q  
November 07, 2012  
[Table of Contents](#)

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

Washington, D.C. 20549

**FORM 10-Q**

**Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
For the quarterly period ended September 30, 2012

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

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.

Edgar Filing: PACCAR INC - Form 10-Q

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 353,030,892 shares as of October 31, 2012

**Table of Contents**

**PACCAR Inc Form 10-Q**

**INDEX**

	Page
<b><u>PART I. FINANCIAL INFORMATION:</u></b>	
ITEM 1. <b><u>FINANCIAL STATEMENTS:</u></b>	
<b><u>Consolidated Statements of Comprehensive Income Three and Nine months ended September 30, 2012 and 2011 (Unaudited)</u></b>	3
<b><u>Consolidated Balance Sheets September 30, 2012 (Unaudited) and December 31, 2011</u></b>	4
<b><u>Condensed Consolidated Statements of Cash Flows Nine months ended September 30, 2012 and 2011 (Unaudited)</u></b>	6
<b><u>Notes to Consolidated Financial Statements (Unaudited)</u></b>	7
ITEM 2. <b><u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u></b>	27
ITEM 3. <b><u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u></b>	42
ITEM 4. <b><u>CONTROLS AND PROCEDURES</u></b>	42
<b><u>PART II. OTHER INFORMATION:</u></b>	
ITEM 1. <b><u>LEGAL PROCEEDINGS</u></b>	43
ITEM 1A. <b><u>RISK FACTORS</u></b>	43
ITEM 2. <b><u>UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u></b>	43
ITEM 6. <b><u>EXHIBITS</u></b>	44
<b><u>SIGNATURE</u></b>	45
<b><u>INDEX TO EXHIBITS</u></b>	46

**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 September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
<b>TRUCK AND OTHER:</b>				
Net sales and revenues	\$ 3,546.7	\$ 3,993.0	\$ 12,252.5	\$ 10,738.3
Cost of sales and revenues	3,108.5	3,484.0	10,660.9	9,347.4
Research and development	66.8	70.0	212.9	215.9
Selling, general and administrative	113.9	113.1	362.2	331.6
Interest and other expense (income), net	.3	4.0	(.2)	7.1
	3,289.5	3,671.1	11,235.8	9,902.0
<b>Truck and Other Income Before Income Taxes</b>	<b>257.2</b>	<b>321.9</b>	<b>1,016.7</b>	<b>836.3</b>
<b>FINANCIAL SERVICES:</b>				
Interest and fees	115.5	106.5	336.9	313.4
Operating lease, rental and other income	158.0	157.6	464.1	449.7
Revenues	273.5	264.1	801.0	763.1
Interest and other borrowing expenses	40.6	44.6	118.4	137.2
Depreciation and other expense	127.2	123.0	367.5	352.9
Selling, general and administrative	22.6	24.0	70.8	71.8
Provision for losses on receivables	2.7	10.7	15.2	32.2
	193.1	202.3	571.9	594.1
<b>Financial Services Income Before Income Taxes</b>	<b>80.4</b>	<b>61.8</b>	<b>229.1</b>	<b>169.0</b>
Investment income	7.8	11.0	24.9	28.9
<b>Total Income Before Income Taxes</b>	<b>345.4</b>	<b>394.7</b>	<b>1,270.7</b>	<b>1,034.2</b>
Income taxes	111.8	113.1	412.6	319.6
<b>Net Income</b>	<b>\$ 233.6</b>	<b>\$ 281.6</b>	<b>\$ 858.1</b>	<b>\$ 714.6</b>
<b>Net Income Per Share:</b>				
Basic	\$ .66	\$ .78	\$ 2.41	\$ 1.96
Diluted	\$ .66	\$ .77	\$ 2.41	\$ 1.95
<b>Weighted Average Common Shares Outstanding:</b>				
Basic	353.7	363.3	355.5	365.0
Diluted	354.3	364.2	356.3	366.2
Dividends declared per share	\$ .20	\$ .18	\$ .58	\$ .42

<b>Comprehensive Income</b>	<b>\$ 308.9</b>	<b>\$ 11.2</b>	<b>\$ 916.5</b>	<b>\$ 642.3</b>
-----------------------------	-----------------	----------------	-----------------	-----------------

See Notes to Consolidated Financial Statements.

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

	September 30 2012 (Unaudited)	December 31 2011*
<b>ASSETS</b>		
<b>TRUCK AND OTHER:</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 1,685.0	\$ 1,990.6
Trade and other receivables, net	1,003.6	977.8
Marketable debt securities	955.9	910.1
Inventories, net	915.6	710.4
Other current assets	333.2	249.1
<b>Total Truck and Other Current Assets</b>	<b>4,893.3</b>	<b>4,838.0</b>
Equipment on operating leases, net	808.2	679.1
Property, plant and equipment, net	2,182.2	1,973.3
Other noncurrent assets, net	241.3	280.9
<b>Total Truck and Other Assets</b>	<b>8,125.0</b>	<b>7,771.3</b>
<b>FINANCIAL SERVICES:</b>		
Cash and cash equivalents	65.5	116.1
Finance and other receivables, net	8,133.0	7,259.7
Equipment on operating leases, net	1,932.1	1,710.7
Other assets	436.9	314.9
<b>Total Financial Services Assets</b>	<b>10,567.5</b>	<b>9,401.4</b>
	<b>\$ 18,692.5</b>	<b>\$ 17,172.7</b>

\* The December 31, 2011 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)**

	September 30 2012 (Unaudited)	December 31 2011*
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
<b>TRUCK AND OTHER:</b>		
<b>Current Liabilities</b>		
Accounts payable, accrued expenses and other	\$ 2,479.7	\$ 2,377.4
Dividend payable	70.6	250.3
<b>Total Truck and Other Current Liabilities</b>	<b>2,550.3</b>	2,627.7
Long-term debt	150.0	150.0
Residual value guarantees and deferred revenues	850.2	712.0
Other liabilities	531.2	507.0
<b>Total Truck and Other Liabilities</b>	<b>4,081.7</b>	3,996.7
<b>FINANCIAL SERVICES:</b>		
Accounts payable, accrued expenses and other	319.0	363.4
Commercial paper and bank loans	3,371.3	3,909.9
Term notes	4,143.0	2,595.5
Deferred taxes and other liabilities	915.4	942.8
<b>Total Financial Services Liabilities</b>	<b>8,748.7</b>	7,811.6
<b>STOCKHOLDERS EQUITY</b>		
Preferred stock, no par value: Authorized 1.0 million shares, none issued		
Common stock, \$1 par value: Authorized 1.2 billion shares, issued 357.2 and 356.8 million shares	357.2	356.8
Additional paid-in capital	71.8	52.1
Treasury stock, at cost - 4.2 million and nil shares	(162.1)	
Retained earnings	5,755.8	5,174.5
Accumulated other comprehensive loss	(160.6)	(219.0)
<b>Total Stockholders Equity</b>	<b>5,862.1</b>	5,364.4
	<b>\$ 18,692.5</b>	<b>\$ 17,172.7</b>

\* The December 31, 2011 consolidated balance sheet has been derived from audited financial statements.  
See Notes to Consolidated Financial Statements.

**Table of Contents****PACCAR Inc Form 10-Q****Condensed Consolidated Statements of Cash Flows (Unaudited)**

(Millions)

Nine Months Ended September 30	2012	2011
<b>OPERATING ACTIVITIES:</b>		
Net income	\$ 858.1	\$ 714.6
Adjustments to reconcile net income to cash provided by operations:		
Depreciation and amortization:		
Property, plant and equipment	144.6	146.4
Equipment on operating leases and other	377.8	359.3
Provision for losses on financial services receivables	15.2	32.2
Other, net	58.1	24.8
Pension contributions	(93.7)	(12.9)
Change in operating assets and liabilities:		
Trade and other receivables	(27.6)	(419.1)
Wholesale receivables on new trucks	(177.6)	(429.1)
Sales-type finance leases and dealer direct loans on new trucks	(112.1)	(18.6)
Inventories	(201.0)	(197.7)
Accounts payable and accrued expenses	13.9	663.4
Income taxes, warranty and other	60.9	288.0
<b>Net Cash Provided by Operating Activities</b>	<b>916.6</b>	<b>1,151.3</b>
<b>INVESTING ACTIVITIES:</b>		
Retail loans and direct financing leases originated	(2,332.3)	(1,862.1)
Collections on retail loans and direct financing leases	1,773.8	1,560.1
Marketable securities purchases	(498.5)	(1,424.9)
Marketable securities sales and maturities	445.8	951.8
Payments for property, plant and equipment	(334.6)	(214.7)
Acquisition of equipment for operating leases	(962.7)	(1,013.6)
Proceeds from asset disposals	251.2	247.6
Other, net	(4.9)	(29.5)
<b>Net Cash Used in Investing Activities</b>	<b>(1,662.2)</b>	<b>(1,785.3)</b>
<b>FINANCING ACTIVITIES:</b>		
Cash dividends paid	(455.9)	(153.1)
Purchase of treasury stock	(162.1)	(250.2)
Stock compensation transactions	7.4	4.4
Net (decrease) increase in commercial paper and short-term bank loans	(557.9)	989.8
Proceeds from long-term debt	1,951.1	1,065.5
Payments of long-term debt	(402.6)	(1,144.1)
<b>Net Cash Provided by Financing Activities</b>	<b>380.0</b>	<b>512.3</b>
Effect of exchange rate changes on cash	9.4	(39.5)
<b>Net Decrease in Cash and Cash Equivalents</b>	<b>(356.2)</b>	<b>(161.2)</b>
Cash and cash equivalents at beginning of period	2,106.7	2,040.8
Cash and cash equivalents at end of period	\$ 1,750.5	\$ 1,879.6

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 nine months ended September 30, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012. For further information, refer to the consolidated financial statements and footnotes included in PACCAR Inc's (the Company) Annual Report on Form 10-K for the year ended December 31, 2011.

*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 September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
Additional shares	<b>689,000</b>	876,000	<b>746,000</b>	1,211,000
Antidilutive options	<b>2,497,000</b>	1,697,000	<b>2,561,000</b>	770,000

*New Accounting Pronouncements:* In May 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. While many of the amendments are clarifications to the existing guidance and are intended to align U.S. GAAP and International Financial Reporting Standards (IFRS), the ASU changes some fair value measurement principles and disclosure requirements. The Company adopted ASU 2011-04 in the first quarter of 2012; the implementation of this amendment resulted in additional disclosures (see note J), but did not have a significant impact on the Company's consolidated financial statements.

The FASB issued ASU 2011-05, *Presentation of Comprehensive Income*, in June 2011, which was subsequently amended by ASU 2011-12 in December 2011. The new guidance requires entities to present components of net income and comprehensive income in either a combined financial statement or in two separate but consecutive statements of net income and comprehensive income. The Company adopted ASU 2011-05 as amended in the first quarter of 2012 and has elected to present components of net income combined with a total for comprehensive income in a single continuous statement in its consolidated interim financial statements. The Company is currently evaluating which method to adopt in the consolidated annual 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 (loss).

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 periodic 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.

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

(Millions, Except Share Amounts)

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.

Marketable debt securities at September 30, 2012 and December 31, 2011 consisted of the following:

At September 30, 2012	AMORTIZED COST	UNREALIZED GAINS	UNREALIZED LOSSES	FAIR VALUE
U.S. tax-exempt securities	\$ 299.7	\$ 2.6		\$ 302.3
U.S. corporate securities	27.9	.3		28.2
U.S. government and agency securities	1.2			1.2
Non-U.S. government securities	386.1	7.4		393.5
Non-U.S. corporate securities	150.3	1.1		151.4
Other debt securities	78.6	.7		79.3
	\$ 943.8	\$ 12.1		\$ 955.9

At December 31, 2011	AMORTIZED COST	UNREALIZED GAINS	UNREALIZED LOSSES	FAIR VALUE
U.S. tax-exempt securities	\$ 291.9	\$ 2.6	\$ .1	\$ 294.4
U.S. corporate securities	27.4	.3	.2	27.5
U.S. government and agency securities	1.9			1.9
Non-U.S. government securities	361.2	6.0	.1	367.1
Non-U.S. corporate securities	148.0	.5	.2	148.3
Other debt securities	70.3	.6		70.9
	\$ 900.7	\$ 10.0	\$ .6	\$ 910.1

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. The proceeds from sales and maturities of marketable securities for the nine months ended September 30, 2012 were \$445.8. Gross realized gains were \$1.9 and \$2.2 and gross realized losses were \$.1 and \$.6 for the nine months ended September 30, 2012 and 2011, respectively.



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

(Millions, Except Share Amounts)

The fair value of marketable debt securities that have been in an unrealized loss position for 12 months or greater at September 30, 2012 was \$2.6 and the associated unrealized loss was \$.01. At September 30, 2011, there were no marketable debt securities in an unrealized loss position for greater than 12 months.

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.

Contractual maturities on marketable debt securities at September 30, 2012 were as follows:

Maturities:	AMORTIZED COST	FAIR VALUE
<b>Within one year</b>	<b>\$ 326.6</b>	<b>\$ 328.3</b>
<b>One to five years</b>	<b>615.7</b>	<b>626.1</b>
<b>Six to ten years</b>	<b>.2</b>	<b>.2</b>
<b>More than ten years</b>	<b>1.3</b>	<b>1.3</b>
	<b>\$ 943.8</b>	<b>\$ 955.9</b>

Marketable debt securities included \$1.3 and \$7.1 of variable rate demand obligations (VRDOs) at September 30, 2012 and December 31, 2011, respectively. VRDOs are debt instruments with long-term scheduled maturities which have interest rates that reset periodically.

**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:

	September 30 2012	December 31 2011
Finished products	<b>\$ 486.3</b>	\$ 436.2
Work in process and raw materials	<b>597.6</b>	439.6
	<b>1,083.9</b>	875.8
Less LIFO reserve	<b>(168.3)</b>	(165.4)
	<b>\$ 915.6</b>	\$ 710.4

Under the LIFO method of accounting (used for approximately 47% of September 30, 2012 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.



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

(Millions, Except Share Amounts)

**NOTE D - Finance and Other Receivables**

Finance and other receivables include the following:

	September 30 2012	December 31 2011
Loans	\$ 3,554.8	\$ 3,114.8
Retail direct financing leases	2,401.7	2,187.8
Sales-type finance leases	857.9	795.8
Dealer wholesale financing	1,702.4	1,517.1
Accrued rents and other trade receivables	111.5	111.0
Unearned interest on finance leases	(356.2)	(327.8)
	<b>8,272.1</b>	7,398.7
Less allowance for losses:		
Loans and leases	(120.6)	(118.5)
Dealer wholesale financing	(12.4)	(11.7)
Accrued rents and other trade receivables	(6.1)	(8.8)
	<b>\$ 8,133.0</b>	\$ 7,259.7

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, there were no finance receivables more than 90 days past due still accruing interest at September 30, 2012 or December 31, 2011. 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 after the customer has made scheduled payments for three months and collection of remaining amounts is considered probable (if contractually modified). Payments received while the finance receivable is impaired or 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 all 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.

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.

---

**Table of Contents**

**PACCAR Inc Form 10-Q**

**Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

On average, modifications extended contractual terms by approximately eight months in 2012 and nine months in 2011 and did not have a significant effect on the weighted average term or interest rate of the total portfolio at September 30, 2012 and December 31, 2011.

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 wholesale 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 which 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. All impaired accounts are on non-accrual status.

Impaired receivables are 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 loss exposure, 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, the 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 model and categorizes the fair value as Level 2 in the hierarchy of fair value measurement. The pricing model is reviewed quarterly and updated as appropriate. The pricing model 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.

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

(Millions, Except Share Amounts)

Accounts are charged-off against the allowance for credit losses when, in the judgment of management, they are considered uncollectable (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.

The allowance for credit losses is summarized as follows:

	2012			TOTAL
	WHOLESALE	RETAIL	OTHER*	
<b>Balance at January 1</b>	<b>\$ 11.7</b>	<b>\$ 118.5</b>	<b>\$ 8.8</b>	<b>\$ 139.0</b>
<b>Provision for losses</b>	<b>2.3</b>	<b>10.5</b>	<b>2.4</b>	<b>15.2</b>
<b>Charge-offs</b>		<b>(17.1)</b>	<b>(4.8)</b>	<b>(21.9)</b>
<b>Recoveries</b>	<b>.1</b>	<b>4.6</b>	<b>.3</b>	<b>5.0</b>
<b>Currency translation and other</b>	<b>(1.7)</b>	<b>4.1</b>	<b>(.6)</b>	<b>1.8</b>
<b>Balance at September 30</b>	<b>\$ 12.4</b>	<b>\$ 120.6</b>	<b>\$ 6.1</b>	<b>\$ 139.1</b>

  

	2011			TOTAL
	WHOLESALE	RETAIL	OTHER*	
Balance at January 1	\$ 7.5	\$ 131.5	\$ 6.0	\$ 145.0
Provision for losses	4.4	17.1	10.7	32.2
Charge-offs	(1.0)	(29.6)	(8.7)	(39.3)
Recoveries		7.0	.8	7.8
Currency translation	(.1)	(2.9)	.7	(2.3)
Balance at September 30	\$ 10.8	\$ 123.1	\$ 9.5	\$ 143.4

\* Accrued rents and other trade receivables.

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

At September 30, 2012	WHOLESALE	RETAIL	TOTAL
<b>Recorded investment for impaired finance receivables evaluated individually</b>	<b>\$ 3.3</b>	<b>\$ 82.9</b>	<b>\$ 86.2</b>
<b>Allowance for impaired finance receivables determined individually</b>	<b>\$ 2.2</b>	<b>\$ 19.3</b>	<b>\$ 21.5</b>
<b>Recorded investment for finance receivables evaluated collectively</b>	<b>\$ 1,699.1</b>	<b>\$ 6,375.3</b>	<b>\$ 8,074.4</b>
<b>Allowance for finance receivables determined collectively</b>	<b>\$ 10.2</b>	<b>\$ 101.3</b>	<b>\$ 111.5</b>

  

At December 31, 2011	WHOLESALE	RETAIL	TOTAL
Recorded investment for impaired finance receivables evaluated individually	\$ 18.4	\$ 96.0	\$ 114.4
Allowance for impaired finance receivables determined individually	\$ 2.2	\$ 25.7	\$ 27.9
Recorded investment for finance receivables evaluated collectively	\$ 1,498.7	\$ 5,674.6	\$ 7,173.3

## Edgar Filing: PACCAR INC - Form 10-Q

Allowance for finance receivables determined collectively	\$	9.5	\$	92.8	\$	102.3
-----------------------------------------------------------	----	-----	----	------	----	-------

The recorded investment for finance receivables that are on non-accrual status in the wholesale segment and the fleet and owner/operator portfolio classes (as defined in impaired loans below) as of September 30, 2012 was \$2.9, \$57.4 and \$12.8, respectively, and as of December 31, 2011 was \$18.4, \$63.9 and \$17.6, respectively.

- 12 -

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

(Millions, Except Share Amounts)

**Impaired Loans**

The Company's impaired loans are segregated by portfolio class. A portfolio class of receivables is a subdivision of a portfolio segment with similar measurement attributes and risk characteristics and common methods to monitor and assess credit risk. The Company's retail segment is subdivided into the fleet and owner/operator classes. Fleet consists of retail accounts with customers operating more than five trucks. All others are owner/operator.

Substantially all impaired loans have a specific reserve and are summarized below. The impaired loans with specific reserve represent the unpaid principal loan balance.

	WHOLESALE	FLEET	OWNER / OPERATOR	TOTAL
At September 30, 2012				
Impaired loans with specific reserve	\$ 3.3	\$ 42.4	\$ 8.3	\$ 54.0
Associated allowance	(2.2)	(8.5)	(1.7)	(12.4)
<b>Net carrying amount of impaired loans</b>	<b>\$ 1.1</b>	<b>\$ 33.9</b>	<b>\$ 6.6</b>	<b>\$ 41.6</b>
<b>Average recorded investment*</b>	<b>\$ 12.9</b>	<b>\$ 23.6</b>	<b>\$ 10.2</b>	<b>\$ 46.7</b>
At December 31, 2011				
Impaired loans with specific reserve	\$ 18.4	\$ 27.9	\$ 11.5	\$ 57.8
Associated allowance	(2.2)	(6.0)	(2.6)	(10.8)
<b>Net carrying amount of impaired loans</b>	<b>\$ 16.2</b>	<b>\$ 21.9</b>	<b>\$ 8.9</b>	<b>\$ 47.0</b>
<b>Average recorded investment*</b>	<b>\$ 11.7</b>	<b>\$ 30.9</b>	<b>\$ 15.1</b>	<b>\$ 57.7</b>

\* Represents the average during the 12 months ended September 30, 2012 and 2011.

During the period the loans above were considered impaired, all interest income recognized was recorded on a cash basis:

	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
Interest income recognized:				
Wholesale			\$ .1	\$ .3
Fleet	\$ .2	\$ .3	.9	1.2
Owner / Operator	.2	.2	.6	.7
	<b>\$ .4</b>	<b>\$ .5</b>	<b>\$ 1.6</b>	<b>\$ 2.2</b>

**Credit Quality**

## Edgar Filing: PACCAR INC - Form 10-Q

The Company's customers are principally concentrated in the transportation industry in North America, Europe and Australia. On a geographic basis, there is a proportionate concentration of credit risk in each area. 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

- 13 -

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

(Millions, Except Share Amounts)

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 the Company has found 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 Company uses historical data and known trends to estimate default rates for each credit quality indicator. The tables below summarize the Company's finance receivables by credit quality indicator and portfolio class.

At September 30, 2012	WHOLESALE	FLEET	OWNER / OPERATOR	TOTAL
Performing	\$ 1,663.8	\$ 4,984.4	\$ 1,355.9	\$ 8,004.1
Watch	35.3	21.9	13.1	70.3
At-risk	3.3	68.8	14.1	86.2
	\$ 1,702.4	\$ 5,075.1	\$ 1,383.1	\$ 8,160.6

At December 31, 2011	WHOLESALE	FLEET	OWNER / OPERATOR	TOTAL
Performing	\$ 1,451.9	\$ 4,262.8	\$ 1,361.0	\$ 7,075.7
Watch	46.7	37.2	13.7	97.6
At-risk	18.4	76.5	19.5	114.4
	\$ 1,517.0	\$ 4,376.5	\$ 1,394.2	\$ 7,287.7

The tables below summarize the Company's finance receivables by aging category. In determining past due status, the Company considers the entire contractual account balance past due when any installment is over 30 days past due. Substantially all customer accounts that were greater than 30 days past due prior to credit modification became current upon modification for aging purposes.

At September 30, 2012	WHOLESALE	FLEET	OWNER / OPERATOR	TOTAL
Current and up to 30 days past due	\$ 1,697.3	\$ 5,037.5	\$ 1,359.4	\$ 8,094.2
31 - 60 days past due	1.3	7.2	10.7	19.2
Greater than 60 days past due	3.8	30.4	13.0	47.2
	\$ 1,702.4	\$ 5,075.1	\$ 1,383.1	\$ 8,160.6

At December 31, 2011	WHOLESALE	FLEET	OWNER / OPERATOR	TOTAL
Current and up to 30 days past due	\$ 1,490.0	\$ 4,321.8	\$ 1,365.2	\$ 7,177.0
31 - 60 days past due	9.1	8.7	11.9	29.7
Greater than 60 days past due	17.9	46.0	17.1	81.0

Edgar Filing: PACCAR INC - Form 10-Q

\$ 1,517.0 \$ 4,376.5 \$ 1,394.2 \$ 7,287.7

- 14 -

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

(Millions, Except Share Amounts)

**Troubled Debt Restructurings**

For the three and nine months ended September 30, 2012, the decrease in the recorded investment for loans and leases modified as TDRs was \$.8 and \$1.5, respectively, resulting in post-modification recorded investment of \$14.5 and \$45.9, respectively. At modification date, the pre-modification and post-modification recorded investment balances by portfolio class are as follows:

	Three Months Ended September 30, 2012 Recorded Investment		Nine Months Ended September 30, 2012 Recorded Investment	
	Pre- Modification	Post- Modification	Pre- Modification	Post- Modification
<b>Fleet</b>	<b>\$ 14.7</b>	<b>\$ 13.9</b>	<b>\$ 45.3</b>	<b>\$ 43.8</b>
<b>Owner / Operator</b>	<b>.6</b>	<b>.6</b>	<b>2.1</b>	<b>2.1</b>
	<b>\$ 15.3</b>	<b>\$ 14.5</b>	<b>\$ 47.4</b>	<b>\$ 45.9</b>

	Three Months Ended September 30, 2011 Recorded Investment		Nine Months Ended September 30, 2011 Recorded Investment	
	Pre- Modification	Post- Modification	Pre- Modification	Post- Modification
<b>Fleet</b>	<b>\$ 3.4</b>	<b>\$ 3.4</b>	<b>\$ 24.5</b>	<b>\$ 24.3</b>
<b>Owner / Operator</b>	<b>.7</b>	<b>.7</b>	<b>5.2</b>	<b>5.2</b>
	<b>\$ 4.1</b>	<b>\$ 4.1</b>	<b>\$ 29.7</b>	<b>\$ 29.5</b>

The balance of TDRs was \$44.0 at September 30, 2012 and \$26.0 at December 31, 2011.

The recorded investment in finance receivables modified as TDRs during the previous twelve months that subsequently defaulted (i.e., became more than 30 days past-due) in the nine months ended September 30, 2012 was \$7.7 and \$.5 for fleet and owner/operator, respectively. Included in the \$7.7 of fleet redefaults is \$4.8 from one customer, for which the Company had a specific reserve of \$1.8 as of September 30, 2012. The TDRs that subsequently defaulted did not significantly impact the Company's allowance for credit losses at September 30, 2012.

**Repossessions**

When the Company determines that a past-due customer is not likely to meet its contractual commitments, the Company repossesses the vehicles which serve as collateral for loans, finance leases and equipment under operating lease. The Company records the repossessed vehicles as used truck inventory which is included in Financial Services other assets on the Consolidated Balance Sheets. The balance of repossessed inventory at September 30, 2012 and December 31, 2011 was \$10.8 and \$16.0, respectively. Proceeds from the sales of repossessed assets were \$48.7 and \$65.7 for the nine months ended September 30, 2012 and 2011, respectively. These amounts are included in proceeds from asset disposals on 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**

## Edgar Filing: PACCAR INC - Form 10-Q

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. Specific terms and conditions vary depending on the product and the country of sale. Optional extended warranty and

- 15 -

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

(Millions, Except Share Amounts)

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. Revenue from extended warranty contracts is deferred and recognized to income on a straight-line basis over the contract period. Warranty costs on these contracts are recognized as incurred. The Company periodically assesses the adequacy of its recorded liabilities and adjusts them as appropriate to reflect actual experience.

Changes in product support liabilities are summarized as follows:

	2012	2011
Balance at January 1	\$ 448.7	\$ 372.2
Cost accruals and revenue deferrals	234.6	219.1
Payments and revenue recognized	(168.0)	(161.3)
Currency translation	1.2	(1.2)
Balance at September 30	\$ 516.5	\$ 428.8

**NOTE F - Stockholders Equity****Comprehensive Income**

The components of comprehensive income, net of any related tax, were as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
Net income	\$ 233.6	\$ 281.6	\$ 858.1	\$ 714.6
Other comprehensive income:				
Currency translation gains (losses)	73.9	(267.0)	46.6	(82.3)
Derivative contracts decrease	(2.4)	(15.2)	(6.9)	(6.8)
Marketable securities increase	.8	2.5	2.7	4.2
Employee benefit plans increase	3.0	9.3	16.0	12.6
Net other comprehensive income (loss)	75.3	(270.4)	58.4	(72.3)
Comprehensive income	\$ 308.9	\$ 11.2	\$ 916.5	\$ 642.3

In the three and nine months ended September 30, 2012 and 2011, currency translation losses are primarily due to changes in the value of the euro compared to the U.S. dollar.

**Accumulated Other Comprehensive Loss**

Accumulated other comprehensive loss was comprised of the following:

Edgar Filing: PACCAR INC - Form 10-Q

	September 30 2012	December 31 2011
Currency translation adjustment	\$ 321.1	\$ 274.5
Net unrealized loss on derivative contracts	(28.9)	(22.0)
Net unrealized gain on investments	9.3	6.6
Employee benefit plans	(462.1)	(478.1)
Total accumulated other comprehensive loss	\$ (160.6)	\$ (219.0)

- 16 -

**Table of Contents**

**PACCAR Inc Form 10-Q**

**Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

**Stock Compensation Plans**

Stock-based compensation expense was \$2.6 and \$11.0 for the three and nine months ended September 30, 2012, respectively, and \$2.6 and \$11.1 for the three and nine months ended September 30, 2011, respectively. Realized tax benefits related to the excess of deductible amounts over expense recognized amounted to nil and \$.8 for the three and nine months ended September 30, 2012, respectively, and nil and \$.7 for the three and nine months ended September 30, 2011, respectively, and have been classified as a financing cash flow.

During the first three quarters of 2012, the Company issued 447,002 common shares under deferred and stock compensation arrangements.

**NOTE G - Income Taxes**

The effective income tax rate in the third quarter of 2012 was 32.4% an increase from 28.7% in the third quarter of 2011 due to a higher mix of foreign income in jurisdictions with higher tax rates. For the first nine months of 2012, the effective income tax rate was 32.5% an increase from 30.9% in the first nine months of 2011. The higher tax rate in the first nine months of 2012 primarily reflects an increased proportion of domestic income.

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

(Millions, Except Share Amounts)

**NOTE H - Segment Information**

The Company operates in two reportable segments, Truck and Financial Services.

	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
Net sales and revenues:				
Truck				
Total	\$ 3,662.5	\$ 4,145.1	\$ 12,694.6	\$ 11,275.5
Less intersegment	(152.5)	(183.9)	(559.9)	(621.8)
External customers	3,510.0	3,961.2	12,134.7	10,653.7
All other	36.7	31.8	117.8	84.6
Financial Services	273.5	264.1	801.0	763.1
	\$ 3,820.2	\$ 4,257.1	\$ 13,053.5	\$ 11,501.4
Income (loss) before income taxes:				
Truck	\$ 258.9	\$ 324.3	\$ 1,022.8	\$ 855.3
All other	(1.7)	(2.4)	(6.1)	(19.0)
Financial Services	257.2	321.9	1,016.7	836.3
Investment income	80.4	61.8	229.1	169.0
	\$ 345.4	\$ 394.7	\$ 1,270.7	\$ 1,034.2
Depreciation and amortization:				
Truck	\$ 76.5	\$ 78.8	\$ 237.9	\$ 236.3
All other	2.6	2.7	7.7	7.2
Financial Services	79.1	81.5	245.6	243.5
	\$ 176.2	\$ 174.3	\$ 522.4	\$ 505.7

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

**NOTE I - Derivative Financial Instruments**

## Edgar Filing: PACCAR INC - Form 10-Q

As part of its risk management strategy, the Company enters into derivative contracts to hedge exposures to fluctuations in interest rates and foreign currency exchange rates. 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.

The Company has elected not to offset derivative positions in the balance sheet with the same counterparty under the same master netting agreements. The Company is not required to post or receive collateral under these agreements. Exposure limits and minimum credit ratings are used to minimize the risks of counterparty default. The Company had no material exposures to default at September 30, 2012.

- 18 -

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

(Millions, Except Share Amounts)

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.

At September 30, 2012, the notional amount of the Company's interest-rate contracts was \$3,135.6. Notional maturities for all interest-rate contracts are \$56.8 for the remainder of 2012, \$716.9 for 2013, \$1,342.8 for 2014, \$775.4 for 2015, \$39.3 for 2016 and \$204.4 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 and the Mexican peso. The objective is to reduce fluctuations in earnings and cash flows associated with changes in foreign currency exchange rates. At September 30, 2012, the notional amount of the outstanding foreign-exchange contracts was \$188.1. Foreign-exchange contracts mature within one year.

The following table presents the balance sheet classifications and fair value of derivative financial instruments designated under hedge accounting:

	September 30, 2012		December 31, 2011	
	Assets	Liabilities	Assets	Liabilities
Derivatives designated under hedge accounting:				
<i>Interest-rate contracts:</i>				
Financial Services:				
Other assets	\$ 2.0		\$ 1.4	
Deferred taxes and other liabilities		\$ 113.5		\$ 107.6
<i>Foreign-exchange contracts:</i>				
Truck and Other:				
Other current assets	.6		.1	
Accounts payable, accrued expenses and other		.1		2.1
Total	\$ 2.6	\$ 113.6	\$ 1.5	\$ 109.7

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

(Millions, Except Share Amounts)

The following table presents the balance sheet classifications and fair value of derivative financial instruments designated as economic hedges:

	September 30, 2012		December 31, 2011	
	Assets	Liabilities	Assets	Liabilities
Economic hedges:				
<i>Interest-rate contracts:</i>				
Financial Services:				
Other assets			\$ .8	
Deferred taxes and other liabilities		\$ 1.1		\$ .4
<i>Foreign-exchange contracts:</i>				
Truck and Other:				
Other current assets	\$ .3		.1	
Accounts payable, accrued expenses and other		.4		.3
Financial Services:				
Deferred taxes and other liabilities				.1
Total	\$ .3	\$ 1.5	\$ .9	\$ .8

**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 expense or (income) 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		Nine Months Ended	
	September 30, 2012	September 30, 2011	September 30, 2012	September 30, 2011
Interest-rate swaps	\$ (2.4)	\$ (5.2)	\$ (4.0)	\$ (4.7)
Term notes	\$ 3.2	\$ 4.9	\$ 4.7	\$ 4.2

**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 accumulated other comprehensive income 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 5.7 years.

Amounts in accumulated other comprehensive income 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 ineffective portions were a gain of \$.2 and a loss of \$.1 during the third quarter of 2012 and 2011, respectively, and were gains of \$.4 and \$.7 during the first nine months of 2012 and 2011, respectively.



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

(Millions, Except Share Amounts)

The following table presents the pre-tax effects of derivative instruments recognized in other comprehensive income (OCI):

	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2012	
	Interest-rate Contracts	Foreign-exchange Contracts	Interest-rate Contracts	Foreign-exchange Contracts
Loss recognized in OCI:				
Truck and Other		\$ 1.3		\$ 2.2
Financial Services	\$ 5.7		\$ 29.4	
	\$ 5.7	\$ 1.3	\$ 29.4	\$ 2.2

	Three Months Ended September 30, 2011		Nine Months Ended September 30, 2011	
	Loss (gain) recognized in OCI:			
Truck and Other		\$ 1.8		\$ (5.9)
Financial Services	\$ 2.6		\$ 31.2	
	\$ 2.6	\$ 1.8	\$ 31.2	\$ (5.9)

Expense reclassified from accumulated OCI into income:

	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2012	
	Interest-rate Contracts	Foreign-exchange Contracts	Interest-rate Contracts	Foreign-exchange Contracts
Truck and Other:				
Cost of sales and revenues		\$ 1.6		\$ 4.3
Interest and other expense, net		.4		.4
Financial Services:				
Interest and other borrowing expenses	\$ 1.6		\$ 17.7	
	\$ 1.6	\$ 2.0	\$ 17.7	\$ 4.7

	Three Months Ended September 30, 2011		Nine Months Ended September 30, 2011	
	Truck and Other:			
Cost of sales and revenues		\$ (.7)		\$ (3.3)
Financial Services:				
Interest and other borrowing expenses	\$ (16.3)		\$ 20.2	
	\$ (16.3)	\$ (.7)	\$ 20.2	\$ (3.3)

## Edgar Filing: PACCAR INC - Form 10-Q

The amount of loss recorded in accumulated OCI at September 30, 2012 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 \$36.8, 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.

- 21 -

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

(Millions, Except Share Amounts)

**Economic Hedges**

For other risk management purposes, the Company enters into derivative instruments not designated as hedges 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.

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

	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2012	
	Interest- rate Contracts	Foreign- exchange Contracts	Interest- rate Contracts	Foreign- exchange Contracts
<b>Truck and Other:</b>				
Cost of sales and revenues				\$ (.3)
Interest and other expense, net		\$ 2.0		(.4)
<b>Financial Services:</b>				
Interest and other borrowing (income) expenses	\$ 1.6	(.5)	\$ 1.5	.6
	\$ 1.6	\$ 1.5	\$ 1.5	\$ (.1)
	Three Months Ended September 30, 2011		Nine Months Ended September 30, 2011	
<b>Truck and Other:</b>				
Cost of sales and revenues		\$ .1		\$ .1
Interest and other (income) expense, net		(.3)		(.3)
<b>Financial Services:</b>				
Interest and other borrowing income	\$ (5.0)	(.5)	\$ (5.0)	\$ (1.6)
	\$ (5.0)	\$ (.7)	\$ (5.0)	\$ (1.8)

**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 inputs from 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 inputs from 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.



**Table of Contents**

**PACCAR Inc Form 10-Q**

**Notes to Consolidated Financial Statements (Unaudited)**

(Millions, Except Share Amounts)

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

There were no transfers of assets or liabilities between Level 1 and Level 2 of the fair value hierarchy during the nine months ended September 30, 2012. 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 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 September 30, 2012	LEVEL 1	LEVEL 2	TOTAL
<b>Assets:</b>			
<b>Marketable debt securities</b>			
U.S. tax-exempt securities		\$ 302.3	\$ 302.3
U.S. corporate securities		28.2	28.2
U.S. government and agency securities	\$ .5	.7	1.2
Non-U.S. government securities		393.5	393.5
Non-U.S. corporate securities		151.4	151.4
Other debt securities		79.3	79.3
<b>Total marketable debt securities</b>	<b>\$ .5</b>	<b>\$ 955.4</b>	<b>\$ 955.9</b>
<b>Derivatives</b>			
Interest-rate swaps		\$ 1.1	\$ 1.1
Cross currency swaps		.9	.9
Foreign-exchange contracts		.9	.9
<b>Total derivative assets</b>		<b>\$ 2.9</b>	<b>\$ 2.9</b>
<b>Liabilities:</b>			
<b>Derivatives</b>			
Cross currency swaps		\$ 76.1	\$ 76.1
Interest-rate swaps		38.5	38.5
Foreign-exchange contracts		.5	.5
<b>Total derivative liabilities</b>		<b>\$ 115.1</b>	<b>\$ 115.1</b>

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

(Millions, Except Share Amounts)

At December 31, 2011	LEVEL 1	LEVEL 2	TOTAL
<b>Assets:</b>			
Marketable debt securities			
U.S. tax-exempt securities		\$ 294.4	\$ 294.4
U.S. corporate securities		27.5	27.5
U.S. government and agency securities	\$ 1.9		1.9
Non-U.S. government securities		367.1	367.1
Non-U.S. corporate securities		148.3	148.3
Other debt securities		70.9	70.9
<b>Total marketable debt securities</b>	<b>\$ 1.9</b>	<b>\$ 908.2</b>	<b>\$ 910.1</b>
<b>Derivatives</b>			
Interest-rate swaps		\$ 1.4	\$ 1.4
Cross currency swaps		.8	.8
Foreign-exchange contracts		.2	.2
<b>Total derivative assets</b>		<b>\$ 2.4</b>	<b>\$ 2.4</b>
<b>Liabilities:</b>			
<b>Derivatives</b>			
Cross currency swaps		\$ 74.7	\$ 74.7
Interest-rate swaps		33.3	33.3
Foreign-exchange contracts		2.5	2.5
<b>Total derivative liabilities</b>		<b>\$ 110.5</b>	<b>\$ 110.5</b>

**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 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 accrued rents 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 at September 30, 2012 and December 31, 2011 was as follows:

	September 30, 2012		December 31, 2011	
	CARRYING AMOUNT	FAIR VALUE	CARRYING AMOUNT	FAIR VALUE
<b>Assets:</b>				
Financial Services fixed-rate loans	\$ 3,190.6	\$ 3,243.7	\$ 2,740.1	\$ 2,776.1
<b>Liabilities:</b>				
Truck and Other fixed-rate debt	\$ 150.0	\$ 165.1	\$ 150.0	\$ 167.6
Financial Services fixed-rate debt	\$ 3,271.1	\$ 3,343.4	\$ 1,958.6	\$ 2,021.1

**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		Nine Months Ended	
	September 30		September 30	
	2012	2011	2012	2011
Service cost	\$ 16.0	\$ 11.9	\$ 48.0	\$ 34.6
Interest on projected benefit obligation	20.3	21.0	61.0	61.8
Expected return on assets	(27.6)	(26.5)	(82.8)	(79.1)
Amortization of prior service costs	.3	.3	1.1	1.0
Recognized actuarial loss	10.8	4.5	32.4	17.7
Net pension expense	\$ 19.8	\$ 11.2	\$ 59.7	\$ 36.0

During the three and nine months ended September 30, 2012, the Company contributed \$8.3 and \$93.7 to its pension plans, respectively, and \$6.1 and \$12.9 for the three and nine months ended September 30, 2011, 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, manufacture and distribution of high-quality, light-, medium- and heavy-duty commercial trucks and related aftermarket parts. 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 Company's Financial Services segment (PFS) derives its earnings primarily from financing or leasing PACCAR products in the U.S., Canada, Mexico, Europe and Australia. The Company's other business is the manufacturing and marketing of industrial winches.

Consolidated net sales and revenues in the third quarter of 2012 were \$3.82 billion compared to \$4.26 billion in the third quarter of 2011. The decrease in the third quarter of 2012 resulted from lower truck unit sales in Europe and the U.S. and Canada, reflecting lower industry truck orders. Third quarter truck unit sales were 31,100 units compared to 35,500 units in the same period in 2011. For the first nine months of 2012, consolidated net sales and revenues were \$13.05 billion compared to \$11.50 billion for the same period in 2011. For the first nine months of 2012 truck unit sales increased to 108,700 units from 97,100 units in the same period in 2011, primarily due to higher industry retail sales in the U.S. and Canada and record heavy duty truck market share in the U.S. and Canada, and Europe.

Third quarter 2012 net income was \$233.6 million (\$.66 per diluted share) compared to \$281.6 million (\$.77 per diluted share) in the third quarter of 2011. The third quarter 2012 results reflect lower sales in the Truck segment compared to the same period in 2011, partially offset by record Financial Services segment results. For the first nine months of 2012, net income was \$858.1 million (\$2.41 per diluted share) compared to \$714.6 million (\$1.95 per diluted share) in the first nine months of 2011. The increase in the first nine months of 2012 was primarily due to higher sales in the Truck segment and record Financial Services segment results from higher finance margin and a lower provision for losses on receivables.

The third quarter and first nine months of 2012 consolidated net sales and revenues were negatively affected by the translation of weaker foreign currencies primarily due to the euro. The translation effect decreased net sales and revenues by \$122.9 million and \$302.6 million for the third quarter of 2012 and the first nine months of 2012, respectively. The effect of weaker foreign currencies on income before income taxes for the third quarter and first nine months of 2012 was not significant.

During September 2012, the Company introduced the new DAF XF Euro 6 truck at the IAA truck show in Hannover, Germany. The new truck is powered by the PACCAR MX-13 Euro 6 engine and is the result of a multi-year design and development program. Production of the new truck will begin in 2013.

***Truck Outlook***

Industry retail sales in the U.S. and Canada in 2012 are expected to be 210,000-220,000 units compared to 197,000 in 2011. Estimates for U.S. and Canada industry Class 8 retail sales for 2013 are in the range of 210,000-240,000 units, driven primarily by ongoing replacement of the aging fleet. In Europe, 2012 industry sales for over 16-tonne vehicles are expected to be 215,000-225,000 units, lower than the 241,000 trucks in 2011, reflecting economic uncertainty in the Eurozone. Industry sales for over 16-tonne vehicles for 2013 are estimated in the range of 210,000-250,000 units as some customers may purchase Euro 5 vehicles ahead of the introduction of the Euro 6 emission requirement in 2014.

Capital investments in 2012 are expected to be \$475 to \$525 million. Capital investments in 2013 are expected to be \$400 to \$500 million, focused on the completion of a truck factory in Brasil and the development of products and services worldwide. Research and development (R&D) in 2012 is expected to be \$280 to \$290 million and for 2013 to be \$275 to \$325 million, focused on comprehensive product development programs and enhanced manufacturing operating efficiency.

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

Average earning assets in the fourth quarter of 2012 are expected to increase modestly from current levels. For 2013, average earning assets may grow approximately 5-10% as increased new business financing from slightly higher truck sales exceeds portfolio runoff. The Company's customers are benefiting from the current levels of freight tonnage, freight rates and fleet utilization that are contributing to customers profitability and cash flow. If current freight transportation conditions decline due to slowing economic conditions, past-due accounts, truck repossessions and net charge-offs could increase from current low levels.

See the Forward Looking Statement section of Management's Discussion and Analysis for factors that may affect the Truck and Financial Services outlook.

**RESULTS OF OPERATIONS:**

(\$ in millions, except per share amounts)	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
<b>Net sales and revenues:</b>				
Truck	\$ 3,510.0	\$ 3,961.2	\$ 12,134.7	\$ 10,653.7
Other	36.7	31.8	117.8	84.6
Truck and other	3,546.7	3,993.0	12,252.5	10,738.3
Financial Services	273.5	264.1	801.0	763.1
	\$ 3,820.2	\$ 4,257.1	\$ 13,053.5	\$ 11,501.4
<b>Income (loss) before taxes:</b>				
Truck	\$ 258.9	\$ 324.3	\$ 1,022.8	\$ 855.3
Other	(1.7)	(2.4)	(6.1)	(19.0)
Truck and Other	257.2	321.9	1,016.7	836.3
Financial Services	80.4	61.8	229.1	169.0
Investment income	7.8	11.0	24.9	28.9
Income taxes	(111.8)	(113.1)	(412.6)	(319.6)
Net income	\$ 233.6	\$ 281.6	\$ 858.1	\$ 714.6
Diluted earnings per share	\$ .66	\$ .77	\$ 2.41	\$ 1.95
Return on Revenues	6.1%	6.6%	6.6%	6.2%

The following provides an analysis of the results of operations for the Company's two reportable segments, Truck 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.

**Table of Contents****PACCAR Inc Form 10-Q****2012 Compared to 2011:****Truck**

The Company's Truck segment accounted for 92% and 93% of revenues in the third quarter and first nine months of 2012 compared to 93% in both the third quarter and first nine months of 2011.

(\$ in millions)	Three Months Ended September 30			Nine Months Ended September 30		
	2012	2011	% Change	2012	2011	% Change
Truck net sales and revenues:						
U.S. and Canada	\$ 1,820.0	\$ 2,191.6	(17)	\$ 7,017.7	\$ 5,560.1	26
Europe	930.4	1,185.8	(22)	2,954.1	3,529.8	(16)
Mexico, South America, Australia and other	759.6	583.8	30	2,162.9	1,563.8	38
	\$ 3,510.0	\$ 3,961.2	(11)	\$ 12,134.7	\$ 10,653.7	14
Truck income before income taxes	\$ 258.9	\$ 324.3	(20)	\$ 1,022.8	\$ 855.3	20

The Company's worldwide truck and parts sales and revenues decreased in the third quarter of 2012 compared to the same period in 2011 due to lower truck deliveries from lower demand in U.S. and Canada, and Europe, partially offset by increased truck demand in Mexico, South America, Australia and other markets. The decrease in Truck segment income before income taxes for the third quarter of 2012 reflects the lower truck deliveries.

In the first nine months of 2012, the Company's worldwide truck and parts sales and revenues increased compared to the same period in 2011 due to higher market demand in all markets except Europe. The increase in Truck segment income before income taxes for the first nine months of 2012 was due to higher truck unit sales, truck unit margins and aftermarket parts sales, partially offset by an increase in selling, general and administrative (SG&A) expenses to support a higher level of business activity.

The effect of foreign currencies on Truck income before income taxes in the third quarter and first nine months of 2012 was not significant.

The Company's new truck deliveries are summarized below:

	Three Months Ended September 30			Nine Months Ended September 30		
	2012	2011	% Change	2012	2011	% Change
United States	12,200	15,600	(22)	49,000	40,100	22
Canada	2,100	3,100	(32)	8,800	7,900	11
U.S. and Canada	14,300	18,700	(24)	57,800	48,000	20
Europe	10,200	11,800	(14)	32,200	35,100	(8)
Mexico, South America, Australia and other	6,600	5,000	32	18,700	14,000	34
Total units	31,100	35,500	(12)	108,700	97,100	12

The truck markets in the U.S. and Canada, and Europe declined in the third quarter of 2012 compared to 2011 as heightened economic uncertainty has led to reduced demand for new trucks. These lower truck markets were partially offset by stronger truck markets in the third

Edgar Filing: PACCAR INC - Form 10-Q

quarter of 2012 compared to 2011 in Mexico, South America, and Australia.

- 29 -

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

In the first nine months of 2012, the U.S. and Canada truck market improved from 2011 from higher freight volumes and the need to replace an aging truck fleet. Industry retail sales in the heavy-duty market in the U.S. and Canada increased to 169,600 units in the first nine months of 2012 compared to 133,900 units in the same period of 2011. The Company's heavy-duty truck retail market share increased to a record 29.0% in the first nine months of 2012 from 27.7% in the same period of 2011, reflecting higher deliveries to large fleet customers and overall strong demand for the Company's premium products. The medium-duty market was 48,900 units in the first nine months of 2012 compared to 45,200 units in the same period of 2011. The Company's medium-duty market share was 14.9% in the first nine months of 2012 compared to 11.4% in the same period of 2011.

The over 16-tonne truck market in Western and Central Europe was 167,900 units in the first nine months of 2012 compared to 180,200 units in the same period of 2011. The Company's market share was a record 16.0% in the first nine months of 2012, an increase from 15.2% in the same period of 2011. The 6- to 16-tonne market in the first nine months of 2012 was 42,300 units compared to 45,800 units in the same period of 2011. DAF market share in the 6- to 16-tonne market in the first nine months of 2012 was 11.6% compared to 8.4% in the same period of 2011.

Sales and revenues in Mexico, South America, Australia and other markets increased in the third quarter and first nine months of 2012 primarily due to higher new truck deliveries in the Andean region of South America.

The major factors for the change in net sales and revenues, cost of sales and revenues, and gross margin for the three months ended September 30, 2012 are as follows:

(\$ in millions)	NET SALES	COST OF SALES	GROSS MARGIN
Three Months Ended September 30, 2011	\$ 3,961.2	\$ 3,457.6	\$ 503.6
Increase (decrease)			
Truck delivery volume	(372.8)	(308.0)	(64.8)
Average truck sales prices	23.4		23.4
Average truck material, labor and other direct costs		32.5	(32.5)
Factory overhead, warehouse and other indirect costs		.3	(.3)
Aftermarket parts volume	(6.1)	(1.5)	(4.6)
Average aftermarket parts sales prices	19.1		19.1
Average aftermarket parts direct costs		10.9	(10.9)
Currency translation	(114.8)	(111.9)	(2.9)
Total decrease	(451.2)	(377.7)	(73.5)
<b>Three Months Ended September 30, 2012</b>	<b>\$ 3,510.0</b>	<b>\$ 3,079.9</b>	<b>\$ 430.1</b>

Truck delivery volume reflects lower truck deliveries in the U.S. and Canada, and Europe, partially offset by higher deliveries in Mexico, South America, Australia and other markets. Average truck sales prices increased sales by \$23.4 million reflecting increased price realization.

Average truck cost increased \$32.5 million primarily due to higher material costs.

Factory overhead, warehouse and other indirect costs increased \$.3 million primarily due to higher salaries and related costs (\$4.0 million), partially offset by lower manufacturing supplies and maintenance (\$3.3 million).

## Edgar Filing: PACCAR INC - Form 10-Q

Lower market demand in Europe lowered aftermarket parts volume by \$21.2 million and related cost of sales by \$11.1 million. This was partially offset by higher market demand in the U.S. and Canada, and Australia that increased aftermarket parts volume by \$15.1 million and related cost of sales by \$9.6 million.

Average aftermarket parts sales prices increased by \$19.1 million reflecting improved price realization, primarily in North America.

Average aftermarket parts costs increased \$10.9 million from higher material costs.

- 30 -

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

The currency translation effect on sales and cost of sales primarily reflects a decrease in the value of the euro compared to the U.S. dollar.

The major factors for the change in net sales and revenues, cost of sales and revenues, and gross margin for the nine months ended September 30, 2012 are as follows:

(\$ in millions)	NET SALES	COST OF SALES	GROSS MARGIN
Nine Months Ended September 30, 2011	\$ 10,653.7	\$ 9,275.7	\$ 1,378.0
Increase (decrease)			
Truck delivery volume	1,392.8	1,229.5	163.3
Average truck sales prices	247.1		247.1
Average truck material, labor and other direct costs		157.1	(157.1)
Factory overhead, warehouse and other indirect costs		88.3	(88.3)
Aftermarket parts volume	73.1	49.5	23.6
Average aftermarket parts sales prices	51.6		51.6
Average aftermarket parts direct costs		35.7	(35.7)
Currency translation	(283.6)	(265.9)	(17.7)
<b>Total increase</b>	<b>1,481.0</b>	<b>1,294.2</b>	<b>186.8</b>
<b>Nine Months Ended September 30, 2012</b>	<b>\$ 12,134.7</b>	<b>\$ 10,569.9</b>	<b>\$ 1,564.8</b>

The higher truck delivery volume primarily reflects improved truck markets and market share in North America. The increased demand for trucks also resulted in higher average truck sales prices which increased sales by \$247.1 million.

Average truck cost of sales increased \$157.1 million primarily due to higher material costs.

Factory overhead, warehouse and other indirect costs increased \$88.3 million primarily due to higher salaries and related costs (\$51.6 million), manufacturing supplies and maintenance (\$12.5 million), utilities (\$3.1 million) and other overhead costs (\$13.1 million) to support higher production levels.

Higher market demand, primarily in North America, increased aftermarket parts sales volume by \$73.1 million and related cost of sales by \$49.5 million.

Average aftermarket parts sales prices increased by \$51.6 million reflecting improved price realization.

Average aftermarket parts costs increased \$35.7 million from higher material costs.

The currency translation effect on sales and cost of sales primarily reflects a decrease in the value of the euro compared to the U.S. dollar.



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

Net sales and revenues and gross margins for truck units and aftermarket parts are provided below. The aftermarket parts gross margin includes direct revenues and costs, but excludes certain Truck segment costs.

(\$ in millions)	Three Months Ended September 30			Nine Months Ended September 30		
	2012	2011	% Change	2012	2011	% Change
<b>Net sales and revenues:</b>						
Trucks	\$ 2,859.9	\$ 3,305.7	(13)	\$ 10,138.0	\$ 8,735.4	16
Aftermarket parts	650.1	655.5	(1)	1,996.7	1,918.3	4
	\$ 3,510.0	\$ 3,961.2	(11)	\$ 12,134.7	\$ 10,653.7	14
<b>Gross Margin:</b>						
Trucks	\$ 205.8	\$ 276.9	(26)	\$ 873.9	\$ 709.9	23
Aftermarket parts	224.3	226.7	(1)	690.9	668.1	3
	\$ 430.1	\$ 503.6	(15)	\$ 1,564.8	\$ 1,378.0	14
<b>Gross Margin %:</b>						
Trucks	7.2%	8.4%		8.6%	8.1%	
Aftermarket parts	34.5%	34.6%		34.6%	34.8%	
	12.3%	12.7%		12.9%	12.9%	

Total Truck segment gross margins for the third quarter of 2012 were 12.3% compared to 12.7% in the same period in 2011. Total Truck segment gross margins for the first nine months of 2012 and 2011 were 12.9%. The lower truck sales gross margins for the third quarter of 2012 resulted from reduced truck deliveries in the U.S. and Canada, and Europe and decreased absorption of fixed costs resulting from lower truck production. The aftermarket parts gross margins in the third quarter and first nine months of 2012 were comparable to 2011.

Truck R&D expenditures in the third quarter and first nine months of 2012 decreased to \$66.7 million and \$212.6 million from \$69.9 million and \$215.5 million in the corresponding periods of 2011, respectively. R&D spending in both periods of 2012 reflects continued focus on product development activities, primarily for new truck models and engine development for North America and Europe. Foreign currency, primarily the euro, reduced R&D in the third quarter and first nine months of 2012 by \$5.5 million and \$12.4 million, respectively.

Truck SG&A of \$104.6 million in the third quarter of 2012 was comparable to \$105.6 million in the third quarter of 2011. In the first nine months of 2012, SG&A was \$330.6 million and \$306.2 million in the first nine months of 2011. The higher spending for the first nine months of 2012 is primarily due to higher salaries and personnel related expenses of \$19.0 million to support higher levels of business activity.

As a percentage of sales, SG&A increased to 3.0% in the third quarter of 2012 from 2.7% in the third quarter of 2011, reflecting lower sales volumes. For the first nine months of 2012, SG&A as a percentage of sales was 2.7%, down from 2.9% in the first nine months of 2011 due to higher sales volumes and ongoing cost control. Foreign currency, primarily the euro, reduced SG&A in the third quarter and first nine months of 2012 by \$5.2 million and \$12.5 million, respectively.

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

(\$ in millions)

	Three Months Ended September 30			Nine Months Ended September 30		
	2012	2011	% change	2012	2011	% change
<b>New loan and lease volume:</b>						
U.S. and Canada	\$ 735.5	\$ 638.0	15	\$ 2,124.1	\$ 1,673.3	27
Europe	202.3	215.7	(6)	646.0	684.5	(6)
Mexico and Australia	224.1	151.9	48	570.5	443.7	29
	\$ 1,161.9	\$ 1,005.6	16	\$ 3,340.6	\$ 2,801.5	19
<b>New loan and lease volume by product:</b>						
Loans and finance leases	\$ 902.2	\$ 783.5	15	\$ 2,621.1	\$ 2,060.6	27
Equipment on operating leases	259.7	222.1	17	719.5	740.9	(3)
	\$ 1,161.9	\$ 1,005.6	16	\$ 3,340.6	\$ 2,801.5	19
<b>New loan and lease unit volume:</b>						
Loans and finance leases	8,970	8,750	3	25,940	24,000	8
Equipment on operating leases	2,600	2,290	14	6,830	7,450	(8)
	11,570	11,040	5	32,770	31,450	4
<b>Average earning assets:</b>						
U.S. and Canada	\$ 6,149.6	\$ 4,710.8	31	\$ 5,791.4	\$ 4,443.0	30
Europe	2,197.7	2,268.8	(3)	2,263.8	2,184.4	4
Mexico and Australia	1,613.7	1,459.7	11	1,510.1	1,452.4	4
	\$ 9,961.0	\$ 8,439.3	18	\$ 9,565.3	\$ 8,079.8	18
<b>Average earning assets by product:</b>						
Loans and finance leases	\$ 6,323.0	\$ 5,342.7	18	\$ 6,080.5	\$ 5,229.8	16
Dealer wholesale financing	1,640.4	1,228.5	34	1,585.0	1,125.8	41
Equipment on lease and other	1,997.6	1,868.1	7	1,899.8	1,724.2	10
	\$ 9,961.0	\$ 8,439.3	18	\$ 9,565.3	\$ 8,079.8	18
<b>Revenue:</b>						
U.S. and Canada	\$ 149.5	\$ 131.1	14	\$ 427.9	\$ 374.9	14
Europe	67.2	79.9	(16)	210.1	232.5	(10)
Mexico and Australia	56.8	53.1	7	163.0	155.7	5
	\$ 273.5	\$ 264.1	4	\$ 801.0	\$ 763.1	5
<b>Revenue by product:</b>						
Loans and finance leases	\$ 100.2	\$ 94.4	6	\$ 290.3	\$ 279.0	4
Dealer wholesale financing	15.3	12.1	26	46.6	34.4	35
Equipment on lease and other	158.0	157.6		464.1	449.7	3
	\$ 273.5	\$ 264.1	4	\$ 801.0	\$ 763.1	5
Income before income taxes	\$ 80.4	\$ 61.8	30	\$ 229.1	\$ 169.0	36

In the third quarter of 2012, new loan and lease volume increased 16% to \$1.16 billion compared to the third quarter of 2011. The increase reflects higher finance market share of new PACCAR truck sales and a higher average amount financed per unit, partially offset by lower new

## Edgar Filing: PACCAR INC - Form 10-Q

PACCAR truck sales. In the third quarter of 2012, PFS market share on new PACCAR trucks increased to 33.1% compared to 29.1% in the same period of 2011 from higher market share in all markets except Mexico. In the first nine months of 2012, new loan and lease volume increased 19% to \$3.34 billion compared to the first nine months of 2011. The increase reflects higher new PACCAR truck sales and a higher average amount financed per unit. In the first nine months of 2012, finance market share of 29.8% decreased slightly compared to the 30.2% finance market share in the same period in 2011, primarily due to lower market share in the U.S. and Canada.

The increase in PFS revenues primarily resulted from higher average earning asset balances, partially offset by lower yields. PFS income before income taxes increased to \$80.4 million and \$229.1 million in the third quarter and first nine months of 2012 compared to \$61.8 million and \$169.0 million in the same periods in 2011 primarily due to higher finance margins and a lower provision for losses as noted below.

- 33 -

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

The major factors for the change in interest and fees, interest and other borrowing expenses and finance margin for the three months ended September 30, 2012 are outlined in the table below:

(\$ in millions)	INTEREST AND FEES	INTEREST AND OTHER BORROWING EXPENSES	FINANCE MARGIN
Three Months Ended September 30, 2011	\$ 106.5	\$ 44.6	\$ 61.9
Increase (decrease)			
Average finance receivables	23.2		23.2
Yields	(11.6)		(11.6)
Average debt balances		9.3	(9.3)
Borrowing rates		(12.0)	12.0
Currency translation	(2.6)	(1.3)	(1.3)
Total increase (decrease)	9.0	(4.0)	13.0
<b>Three Months Ended September 30, 2012</b>	<b>\$ 115.5</b>	<b>\$ 40.6</b>	<b>\$ 74.9</b>

Average finance receivables increased \$1.60 billion (excluding foreign currency effects of \$212.2 million) from an increase in retail portfolio new business volume exceeding repayments and an increase in dealer wholesale financing, primarily in the U.S. and Canada.

Lower market rates resulted in lower portfolio yields.

Average debt balances increased \$1.69 billion (including foreign currency effects of \$209.5 million) in the third quarter of 2012 and included increased medium-term note funding. The higher average debt balances reflect funding needed for the higher average finance receivable portfolio.

Borrowing rates declined in the third quarter of 2012 due to lower market interest rates.

Currency translation variances primarily reflect a decrease in the value of the euro compared to the U.S. dollar.

The major factors for the change in interest and fees, interest and other borrowing expenses and finance margin for the nine months ended September 30, 2012 are outlined in the table below:

(\$ in millions)	INTEREST AND FEES	INTEREST AND OTHER BORROWING EXPENSES	FINANCE MARGIN
Nine Months Ended September 30, 2011	\$ 313.4	\$ 137.2	\$ 176.2
Increase (decrease)			
Average finance receivables	70.3		70.3

Edgar Filing: PACCAR INC - Form 10-Q

Yields	(41.1)		(41.1)
Average debt balances		30.5	(30.5)
Borrowing rates		(46.6)	46.6
Currency translation	(5.7)	(2.7)	(3.0)
Total increase (decrease)	23.5	(18.8)	42.3
<b>Nine Months Ended September 30, 2012</b>	<b>\$ 336.9</b>	<b>\$ 118.4</b>	<b>\$ 218.5</b>

Average finance receivables increased \$1.50 billion (excluding foreign currency effects of \$190.8 million) from an increase in retail portfolio new business volume exceeding repayments and an increase in dealer wholesale financing, primarily in the U.S. and Canada.

Lower market rates resulted in lower portfolio yields.

Average debt balances increased \$1.73 billion (excluding foreign currency effects of \$173.8 million) in the first nine months of 2012 and included increased medium-term note funding. The higher average debt balances reflect funding needed for the higher average finance receivable portfolio.

Borrowing rates declined in the first nine months of 2012 due to lower market interest rates.

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

Currency translation variances primarily reflect a decrease in the value of the euro compared to the U.S. dollar. The following table summarizes operating lease, rental and other income and depreciation and other:

(\$ in millions)	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
Operating lease revenues	\$ 146.9	\$ 147.6	\$ 431.8	\$ 420.3
Used truck sales and other	11.1	10.0	32.3	29.4
<b>Operating lease, rental and other income</b>	<b>\$ 158.0</b>	<b>\$ 157.6</b>	<b>\$ 464.1</b>	<b>\$ 449.7</b>
Depreciation on operating lease	\$ 94.5	\$ 91.2	\$ 270.0	\$ 257.4
Vehicle operating expenses	23.3	25.9	72.4	76.3
Cost of used truck sales and other	9.4	5.9	25.1	19.2
<b>Depreciation and other</b>	<b>\$ 127.2</b>	<b>\$ 123.0</b>	<b>\$ 367.5</b>	<b>\$ 352.9</b>

The major factors for the change in lease, rental and other income, depreciation and other and lease margin for the three months ended September 30, 2012 are outlined in the table below:

(\$ in millions)	LEASE, RENTAL AND OTHER INCOME	DEPRECIATION AND OTHER	LEASE MARGIN
Three Months Ended September 30, 2011	\$ 157.6	\$ 123.0	\$ 34.6
Increase (decrease)			
Operating lease impairments		.2	(.2)
Results on returned lease assets		2.9	(2.9)
Average operating lease assets	5.7	4.6	1.1
Currency translation and other	(5.3)	(3.5)	(1.8)
<b>Total increase (decrease)</b>	<b>.4</b>	<b>4.2</b>	<b>(3.8)</b>
<b>Three Months Ended September 30, 2012</b>	<b>\$ 158.0</b>	<b>\$ 127.2</b>	<b>\$ 30.8</b>

Results on returned lease assets decreased \$2.9 million as the Company had net gains on sales of trucks returned from leases of \$.5 million in the third quarter of 2012 compared to \$3.5 million in the third quarter of 2011. The lower gains in 2012 primarily relate to the U.S. and Canada, and Europe.

Average operating lease assets increased \$210.4 million (excluding foreign currency effects of \$80.9 million) resulting in \$5.7 million in higher revenues and \$4.6 million in higher depreciation and other vehicle operating expenses.

Currency translation variances primarily reflect a decrease in the value of the euro compared to the U.S. dollar.



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

The major factors for the change in lease rental and other income, depreciation and other and lease margin for the nine months ended September 30, 2012 are outlined in the table below:

(\$ in millions)	LEASE, RENTAL AND OTHER INCOME	DEPRECIATION AND OTHER	LEASE MARGIN
Nine Months Ended September 30, 2011	\$ 449.7	\$ 352.9	\$ 96.8
Increase (decrease)			
Operating lease impairments		(2.1)	2.1
Results on returned lease assets		2.3	(2.3)
Average operating lease assets	25.8	20.8	5.0
Currency translation and other	(11.4)	(6.4)	(5.0)
<b>Total increase</b>	<b>14.4</b>	<b>14.6</b>	<b>(.2)</b>
<b>Nine Months Ended September 30, 2012</b>	<b>\$ 464.1</b>	<b>\$ 367.5</b>	<b>\$ 96.6</b>

Operating lease impairments decreased \$2.1 million in the first nine months of 2012 due to fewer impaired units.

Results on returned lease assets decreased \$2.3 million as the Company had net gains on sales of trucks returned from leases of \$8.3 million in the first nine months of 2012 compared to net gains of \$10.6 million in the first nine months of 2011. The lower gains in 2012 primarily relate to the U.S. and Canada, and Europe.

Average operating lease assets increased \$234.6 million (excluding foreign currency effects of \$59.0 million) resulting in \$25.8 million in higher revenue and \$20.8 million in higher depreciation expense.

Currency translation variances primarily reflect a decrease in the value of the euro compared to the U.S. dollar. The following tables summarize the provision for losses on receivables and net charge-offs:

(\$ in millions)	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2012	
	PROVISION FOR LOSSES		PROVISION FOR LOSSES	
	ON	NET	ON	NET
	RECEIVABLES	CHARGE-OFFS	RECEIVABLES	CHARGE-OFFS
U.S. and Canada	\$ (.4)	\$ 2.7	\$ 2.6	\$ 5.7
Europe	1.9	1.4	7.6	5.5
Mexico and Australia	1.2	1.5	5.0	5.7
	<b>\$ 2.7</b>	<b>\$ 5.6</b>	<b>\$ 15.2</b>	<b>\$ 16.9</b>

Edgar Filing: PACCAR INC - Form 10-Q

(\$ in millions)	Three Months Ended September 30, 2011		Nine Months Ended September 30, 2011	
	PROVISION FOR LOSSES ON		PROVISION FOR LOSSES ON	
	RECEIVABLES	NET CHARGE-OFFS	RECEIVABLES	NET CHARGE-OFFS
U.S. and Canada	\$ (.2)	\$ .7	\$ 3.6	\$ 4.5
Europe	4.4	2.7	13.4	13.2
Mexico and Australia	6.5	6.5	15.2	13.8
	\$ 10.7	\$ 9.9	\$ 32.2	\$ 31.5

The provision for losses on receivables for the third quarter and first nine months of 2012 declined \$8.0 million and \$17.0 million, respectively, compared to same periods in 2011 due to transportation industry conditions which have improved the profitability and cash flow for many of the Company's customers.

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

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.

The accounts modified during the nine months ended September 30, 2012 and 2011 are summarized below:

	Nine Months Ended			
	September 30, 2012		September 30, 2011	
	Recorded Investment	% of Total Portfolio*	Recorded Investment	% of Total Portfolio*
Commercial	\$ 168.0	2.7%	\$ 152.9	3.0%
Insignificant Delay	46.4	.8%	110.4	2.2%
Credit - No Concession	30.9	.5%	44.8	.9%
Credit - Troubled Debt Restructuring	45.9	.8%	29.5	.6%
	<b>\$ 291.2</b>	<b>4.8%</b>	<b>\$ 337.6</b>	<b>6.7%</b>

\* Recorded investment at time of modification as a percentage of ending portfolio, on an annualized basis.

Total modification activity decreased in 2012 compared to 2011 due to lower insignificant delay modifications in Australia. In the first quarter of 2011 due to severe flooding in the Queensland, Australia region, the Company provided modifications to credit qualified customers. In addition, the Company's TDR modifications increased in 2012 from 2011 due to one large customer account in Europe and one in the U.S. These were partially offset by higher commercial modifications reflecting growth in the portfolio.

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

	September 30 2012	December 31 2011	September 30 2011
Percentage of retail loan and lease accounts 30+ days past due:			
U.S. and Canada	.7%	1.1%	1.3%
Europe	1.0%	1.0%	1.4%
Mexico and Australia	1.8%	3.4%	5.3%
Worldwide	.9%	1.5%	2.1%

Worldwide PFS accounts 30+ days past due were .9% at September 30, 2012 and have improved from 1.5% at December 31, 2011 and 2.1% at September 30, 2011. The U.S. and Canada past-due percentage of .7% includes .5% from one customer. Excluding that customer, worldwide PFS accounts 30+ days past due at September 30, 2012 would have been .6%. At September 30, 2012, the Company had \$21.5 million of specific loss reserves for this customer and other accounts considered at risk. The Company continues to focus on maintaining low past-due balances.



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

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 \$10.5 million of accounts worldwide during the third quarter of 2012, \$4.5 million during the fourth quarter of 2011 and \$8.0 million during the third quarter of 2011 that were 30+ days past-due and became current at the time of modification. Of these modifications, \$9.9 million during the third quarter of 2012, \$4.4 million during the fourth quarter of 2011 and \$6.4 million during the third quarter of 2011 were in Mexico and Australia. 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:

	<b>September 30 2012</b>	December 31 2011	September 30 2011
Pro forma percentage of retail loan and lease accounts 30+ days past due:			
U.S. and Canada	<b>.7%</b>	1.1%	1.4%
Europe	<b>1.0%</b>	1.0%	1.4%
Mexico and Australia	<b>2.8%</b>	3.8%	6.0%
<b>Worldwide</b>	<b>1.1%</b>	1.5%	2.2%

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 September 30, 2012, December 31, 2011 and September 30, 2011. The effect on the allowance for credit losses from such modifications was not significant at September 30, 2012, December 31, 2011 and September 30, 2011.

For the third quarter of 2012, the Company's pretax return on revenue for Financial Services increased to 29.4% from 23.4% in the third quarter of 2011. For the first nine months of 2012, the Company's pretax return on revenue for Financial Services increased to 28.6% from 22.1% in the first nine months of 2011. The higher pretax returns in 2012 were primarily due to higher finance margin from a lower cost of funds as well as a lower provision for losses on receivables from improved portfolio quality.

**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 the third quarter and first nine months of 2012 and 2011. Other SG&A was \$9.4 million and \$31.6 million in the third quarter and first nine months of 2012 compared to \$7.6 million and \$25.4 million in the third quarter and first nine months of 2011, respectively. Other SG&A increased due to higher salary related expenses. Other income (loss) before tax was a loss of \$1.7 million and \$6.1 million in the third quarter and first nine months of 2012 compared to a loss of \$2.4 million and \$19.0 million in the same periods of 2011, primarily due to improved winch business results and lower equipment expenses.

Investment income was \$7.8 million and \$24.9 million in the third quarter and first nine months of 2012 compared to \$11.0 million and \$28.9 million in the same periods of 2011, respectively. The lower investment income in the third quarter and first nine months of 2012 primarily reflects lower market interest rates.

The effective income tax rate in the third quarter of 2012 was 32.4% an increase from 28.7% in the third quarter of 2011 due to a lower mix of foreign income in jurisdictions with lower tax rates. For the first nine months of 2012, the effective income tax rate was 32.5% an increase from 30.9% in the first nine months of 2011. The higher tax rate in the first nine months of 2012 primarily reflects an increased proportion of domestic income.

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

(\$ in millions)	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
Domestic income before taxes	\$ 137.5	\$ 161.7	\$ 608.3	\$ 342.5
Foreign income before taxes	207.9	233.0	662.4	691.7
<b>Total income before taxes</b>	<b>\$ 345.4</b>	<b>\$ 394.7</b>	<b>\$ 1,270.7</b>	<b>\$ 1,034.2</b>
Domestic pre-tax return on revenues	7.9%	8.1%	9.4%	6.7%
Foreign pre-tax return on revenues	10.0%	10.3%	10.1%	10.8%
<b>Total pre-tax return on revenues</b>	<b>9.0%</b>	<b>9.3%</b>	<b>9.7%</b>	<b>9.0%</b>

For the third quarter of 2012, the decrease in income before income taxes for domestic and foreign operations compared to the third quarter of 2011 was primarily due to Truck operations. The third quarter of 2012 return on revenues for domestic operations of 7.9% declined from 8.1% in 2011 and the third quarter of 2012 return on revenues for foreign operations of 10.0% declined from 10.3% in 2011. Both results reflect lower returns on Truck operations, partially offset by higher returns for Financial Services operations.

For the first nine months of 2012, the increase in income before taxes for domestic operations and the decrease in income before taxes for foreign operations compared to the first nine months of 2011 were primarily due to Truck operations. The decrease in foreign income before taxes for Truck operations was due to lower truck sales in Europe partially offset by higher sales in Latin America and Australia. The 2012 higher return on revenues for domestic operations of 9.4% compared to 6.7% in 2011 resulted from higher returns for both Truck and Financial Services operations. The 2012 lower return on revenues in foreign operations of 10.1% compared to 10.8% in 2011 resulted from lower returns on Truck operations partially offset by higher returns on Financial Services operations.

**LIQUIDITY AND CAPITAL RESOURCES:**

(\$ in millions)	September 30 2012	December 31 2011
Cash and cash equivalents	\$ 1,750.5	\$ 2,106.7
Marketable debt securities	955.9	910.1
	<b>\$ 2,706.4</b>	<b>\$ 3,016.8</b>

The Company's total cash and marketable debt securities decreased \$310.4 million at September 30, 2012 primarily from a decrease in cash and cash equivalents of \$356.2 million, partially offset by an increase in marketable debt securities of \$45.8 million.

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

The change in cash and cash equivalents is summarized below:

Nine Months Ended September 30 (\$ in millions)	2012	2011
<b>Operating activities:</b>		
Net income	\$ 858.1	\$ 714.6
Net income items not affecting cash	595.7	562.7
Pension contributions	(93.7)	(12.9)
Changes in operating assets and liabilities	(443.5)	(113.1)
Net cash provided by operating activities	916.6	1,151.3
Net cash used in investing activities	(1,662.2)	(1,785.3)
Net cash provided by financing activities	380.0	512.3
Effect of exchange rate changes on cash	9.4	(39.5)
Net decrease in cash and cash equivalents	(356.2)	(161.2)
Cash and cash equivalents at beginning of the period	2,106.7	2,040.8
Cash and cash equivalents at end of the period	\$ 1,750.5	\$ 1,879.6

*Operating activities:* Cash provided by operations decreased \$234.7 million to \$916.6 million in the first nine months of 2012. The lower operating cash flow was primarily due to a \$649.5 million lower increase in purchases of goods and services in accounts payable and accrued expenses greater than payments compared to the first nine months of 2011 as well as a \$170.2 million outflow from income tax payments exceeding expense in 2012 and income tax expense exceeding payments in 2011. In addition, lower operating cash flow resulted from a larger increase in Financial Services segment sales-type finance lease and dealer direct loan originations than payments of \$93.5 million as well as higher pension contributions of \$80.8 million. These were partially offset by \$391.5 million from a lower increase in sales of goods and services in accounts receivable greater than receipts compared to the first nine months of 2011, a \$251.5 million lower increase in Financial Services segment wholesale receivables and \$143.5 million of higher net income.

*Investing activities:* Cash used in investing activities of \$1.66 billion in the first nine months of 2012 decreased \$123.1 million from the \$1.79 billion used in the first nine months of 2011. In the first nine months of 2012, lower net purchases of marketable securities of \$420.4 million were made compared to the first nine months of 2011. The lower net purchases of marketable debt securities in the first nine months of 2012 was partially offset by \$256.5 million of higher net new loan and lease originations in the Financial Services segment reflecting increased portfolio growth.

*Financing activities:* Cash provided by financing activities in the first nine months of 2012 of \$380.0 million was \$132.3 million lower than the cash provided by financing activities in the first nine months of 2011. In the first nine months of 2012 the Company paid \$455.9 million of dividends, an increase of \$302.8 million compared to \$153.1 million paid in the first nine months ended 2011. The higher amounts paid results from a special dividend declared in 2011 and paid in 2012 and a higher regular quarterly dividend rate in 2012. Treasury stock purchases of \$162.1 million were \$88.1 million lower than 2011. The Company issued \$1.95 billion of long term debt, \$885.6 million higher than 2011. The proceeds were partially used to repay medium term debt of \$402.6 million and to reduce outstanding balances of commercial paper by \$557.9 million resulting in an increase in cash provided by net borrowings of \$990.6 million compared to \$911.2 million in 2011. In both periods cash provided by net borrowings was used to fund growth in the Financial Services portfolios.

**Credit Lines and Other**

The Company has line of credit arrangements of \$3.69 billion, of which \$3.44 billion were unused at September 30, 2012. Included in these arrangements are \$3.0 billion of syndicated bank facilities, of which \$1.0 billion matures in June 2013, \$1.0 billion matures in June 2016 and \$1.0 billion matures in June 2017. 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 nine months ended September 30, 2012.



---

**Table of Contents**

**PACCAR Inc Form 10-Q**

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. The total amount of medium-term notes outstanding for PACCAR Inc as of September 30, 2012 was \$500.0 million.

In December 2011, PACCAR's Board of Directors approved the repurchase of an additional \$300.0 million of the Company's common stock and as of September 30, 2012, \$192.0 million of shares have been repurchased pursuant to the authorization.

***Truck 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. Long-term debt totaled \$150.0 million as of September 30, 2012.

Expenditures for property, plant and equipment in the first nine months of 2012 totaled \$333.7 million compared to \$211.1 million in the first nine months of 2011 as the Company invested in tooling and factory equipment for new products. Capital spending in 2012 is expected to be approximately \$475 to \$525 million. The capital spending primarily relates to comprehensive product development programs and geographic expansion, including building a new DAF factory in Brasil. Spending on R&D in 2012 is expected to be \$280 to \$290 million. PACCAR continues to focus on new product programs, engine development and manufacturing efficiency improvements.

The Company conducts business in the countries of Spain, Italy, Portugal, Ireland and Greece, which have been experiencing significant financial stress. As of September 30, 2012, the Company had finance and trade receivables in these countries of approximately 1% of consolidated total assets. As of September 30, 2012, 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 September 30, 2012.

***Financial Services***

The Company funds its financial services activities primarily from collections on existing finance receivables and borrowings in the capital markets. An additional source of funds is loans from other PACCAR companies.

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.

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 future 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, 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 2009, the Company's U.S. finance subsidiary, PACCAR Financial Corp. (PFC), filed a shelf registration statement under the Securities Act of 1933 effective for a three year period. The total amount of medium-term notes outstanding for PFC as of September 30, 2012 was \$2.70 billion. PFC intends to file a new registration statement in November 2012.

---

**Table of Contents**

**PACCAR Inc Form 10-Q**

As of September 30, 2012, the Company's European finance subsidiary, PACCAR Financial Europe, had 717.3 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 2012 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 September 30, 2012, 8.06 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 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; changes affecting the profitability of truck owners and operators; price changes impacting equipment costs 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, 2011.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

There were no material changes in the Company's market risk during the nine months ended September 30, 2012. For additional information, refer to Item 7A as presented in the 2011 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.

**Table of Contents**

**PACCAR Inc Form 10-Q**

**PART II OTHER INFORMATION**

For Items 3, 4 and 5, there was no reportable information for the nine months ended September 30, 2012.

**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.

The Company received notice on April 24, 2012 that the Securities and Exchange Commission (SEC) had initiated a formal investigation relating to the Company's financial reporting from 2008 to 2011. The SEC has requested information concerning the Company's loan loss reserves, troubled debt restructuring and segment reporting. The Company is cooperating fully with the SEC's investigation.

On July 15, 2011, the National Labor Relations Board (NLRB) ruled unanimously that the Company is not required to compensate former employees of the Peterbilt plant in Madison, Tennessee for wages and benefits incurred during a work stoppage that ended on April 9, 2009. On December 20, 2011 the NLRB denied a motion to reconsider its decision filed by the union that represented the plant production employees. On April 17, 2012, the union filed a petition for review of the July 15, 2011 NLRB decision in the U.S. Court of Appeals for the Sixth Circuit. The Company believes the likelihood of an outcome adverse to the Company is remote.

In September 2010, the United Kingdom Office of Fair Trading (OFT) notified commercial vehicle manufacturers operating in the U.K., including two of the Company's subsidiaries, that it had commenced an investigation into whether such manufacturers agreed to set prices or limit supply of their products. On June 15, 2012 the OFT announced it had closed its investigation. The OFT stated that the European Commission was well placed to take the investigation forward as part of its investigation into the European truck industry.

**ITEM 1A. RISK FACTORS**

For information regarding risk factors, refer to Part I, Item 1A as presented in the 2011 Annual Report on Form 10-K. There have been no material changes in the Company's risk factors during the nine months ended September 30, 2012.

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

For items 2(a) and (b), there was no reportable information for the nine months ended September 30, 2012.

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

(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 September 30, 2012, \$192.0 million of shares have been repurchased under this plan. The following are details of repurchases made under the plan for the period covered by this report:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Maximum Dollar Value that May Yet be Purchased Under the Plans
July 1 - 31, 2012	48,909	\$ 39.96	\$ 128,664,193
August 1 - 31, 2012	414,941	\$ 39.68	\$ 112,184,782
September 1 - 30, 2012	106,585	\$ 39.20	\$ 108,003,152
Total	570,435	\$ 39.61	\$ 108,003,152

**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 November 7, 2012

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

- 45 -

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

<b>Exhibit Number</b>	<b>Exhibit Description</b>	<b>Form</b>	<b>Date of First Filing</b>	<b>Exhibit Number</b>	<b>File Number</b>
(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
(ii)	Bylaws:				
	(a) Amended and Restated Bylaws of PACCAR Inc	8-K	September 19, 2005	99.4	001-14817
	(b) Second Amended and Restated Bylaws of PACCAR Inc	8-K	July 13, 2012	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) Form of InterNotes, Series A (PACCAR Financial Corp.)	S-3	November 20, 2009	4.4	333-163273
	(d) Indenture for Senior Debt Securities dated as of November 18, 2008 between PACCAR Inc and Wilmington Trust Company	S-3	November 18, 2008	4.1	333-155429
	(e) Forms of Medium-Term Note, Series A	S-3	November 18, 2008	4.2A and 4.2B	333-155429
	(f) 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
	(g) Forms of Medium-Term Note, Series B (Fixed- and Floating-Rate)	S-3	December 19, 2011	4.2A and 4.2B	333-178607

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

<b>Exhibit Number</b>	<b>Exhibit Description</b>	<b>Form</b>	<b>Date of First Filing</b>	<b>Exhibit Number</b>	<b>File Number</b>
(h)	Terms and Conditions of the Notes applicable to the 1,500,000,000 Medium Term Note Programme of PACCAR Financial Europe B.V. and PACCAR Financial PLC	10-Q	November 5, 2009	4(f)	001-14817
(i)	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)	Amended and Restated PACCAR Inc Restricted Stock and Deferred Compensation Plan for Non-employee Directors	10-K	February 27, 2009	10(d)	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

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

<b>Exhibit Number</b>	<b>Exhibit Description</b>	<b>Form</b>	<b>Date of First Filing</b>	<b>Exhibit Number</b>	<b>File Number</b>
(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)	PACCAR Inc Long Term Incentive Plan, Form of Restricted Stock Award Agreement	8-K	February 5, 2007	99.1	001-14817
(l)	PACCAR Inc Long Term Incentive Plan, 2010 Form of Restricted Stock Award Agreement	10-K	February 26, 2010	10(m)	001-14817
(m)	PACCAR Inc Long Term Incentive Plan, Alternate Form of Restricted Stock Award Agreement	10-K	March 1, 2011	10(n)	001-14817
(n)	PACCAR Inc Long Term Incentive Plan, Amended Form of Share Match Restricted Stock Award Agreement	8-K	February 5, 2007	99.3	001-14817
(o)	PACCAR Inc Long Term Incentive Plan, 2008 Form of Share Match Restricted Stock Award Agreement	8-K	February 5, 2008	99.1	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
(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 nine month periods ended September 30, 2012 and 2011*				

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

<b>Exhibit Number</b>	<b>Exhibit Description</b>	<b>Form</b>	<b>Date of First Filing</b>	<b>Exhibit Number</b>	<b>File Number</b>
(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, 2007 - 2011	10-K	February 29, 2012	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:				
(a)	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