

EXPEDITORS INTERNATIONAL OF WASHINGTON INC

Form 10-Q

August 07, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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FORM 10-Q

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(Mark One)

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

For the quarterly period ended June 30, 2014

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 0-13468

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EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.

(Exact name of registrant as specified in its charter)

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Washington

(State or other jurisdiction of  
incorporation or organization)

91-1069248

(IRS Employer  
Identification Number)

1015 Third Avenue, 12<sup>th</sup>Floor, Seattle, Washington

(Address of principal executive offices)

(206) 674-3400

(Registrant's telephone number, including area code)

98104

(Zip Code)

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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 (§232.405 of this chapter) 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. (Check one):

Large accelerated filer ☒

Accelerated filer

☐

Non-accelerated filer ☐ (Do not check if a smaller reporting company)

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 ☒

At August 4, 2014, the number of shares outstanding of the issuer's Common Stock was 195,108,033.

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

## Condensed Consolidated Balance Sheets

(In thousands, except share data)

(Unaudited)

	June 30, 2014	December 31, 2013
Current Assets:		
Cash and cash equivalents	\$970,561	\$1,247,652
Short-term investments	86,149	26,337
Accounts receivable, less allowance for doubtful accounts of \$7,550 at June 30, 2014 and \$8,695 at December 31, 2013	1,150,531	1,073,500
Deferred Federal and state income taxes	19,148	18,396
Other	84,081	49,384
Total current assets	2,310,470	2,415,269
Property and equipment, less accumulated depreciation and amortization of \$366,800 at June 30, 2014 and \$348,282 at December 31, 2013	556,228	563,064
Goodwill	7,927	7,927
Other assets, net	55,315	28,552
Total assets	\$2,929,940	\$3,014,812
Current Liabilities:		
Accounts payable	717,141	648,156
Accrued expenses, primarily salaries and related costs	220,753	200,301
Federal, state and foreign income taxes	24,337	21,743
Total current liabilities	962,231	870,200
Deferred Federal and state income taxes	70,572	58,281
Commitments and contingencies		
Shareholders' Equity:		
Preferred stock, none issued	—	—
Common stock, par value \$0.01 per share. Issued and outstanding 195,036,823 shares at June 30, 2014 and 202,553,220 shares at December 31, 2013	1,951	2,025
Additional paid-in capital	2,701	1,647
Retained earnings	1,893,771	2,087,376
Accumulated other comprehensive loss	(3,609)	(6,265)
Total shareholders' equity	1,894,814	2,084,783
Noncontrolling interest	2,323	1,548
Total equity	1,897,137	2,086,331
Total liabilities and equity	\$2,929,940	\$3,014,812
See accompanying notes to condensed consolidated financial statements.		

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

Condensed Consolidated Statements of Earnings

(In thousands, except share data)

(Unaudited)

	Three months ended		Six months ended	
	June 30,		June 30,	
	2014	2013	2014	2013
Revenues:				
Airfreight services	\$667,257	\$642,969	\$1,314,395	\$1,263,343
Ocean freight and ocean services	536,438	492,007	1,005,662	937,486
Customs brokerage and other services	395,446	368,248	770,729	715,603
Total revenues	1,599,141	1,503,224	3,090,786	2,916,432
Operating Expenses:				
Airfreight services	503,213	483,016	986,095	947,935
Ocean freight and ocean services	423,716	380,727	791,091	725,650
Customs brokerage and other services	187,498	167,609	364,300	322,968
Salaries and related costs	260,767	255,569	516,709	503,986
Rent and occupancy costs	25,401	24,712	50,563	48,905
Depreciation and amortization	12,417	11,674	24,799	22,952
Selling and promotion	9,291	8,328	17,464	15,585
Other	34,395	28,010	62,119	56,354
Total operating expenses	1,456,698	1,359,645	2,813,140	2,644,335
Operating income	142,443	143,579	277,646	272,097
Other Income (Expense):				
Interest income	2,764	3,070	5,461	6,313
Other, net	3,190	4,325	2,909	5,856
Other income, net	5,954	7,395	8,370	12,169
Earnings before income taxes	148,397	150,974	286,016	284,266
Income tax expense	56,669	58,311	110,093	110,993
Net earnings	91,728	92,663	175,923	173,273
Less net earnings attributable to the noncontrolling interest	426	348	797	643
Net earnings attributable to shareholders	\$91,302	\$92,315	\$175,126	\$172,630
Diluted earnings attributable to shareholders per share	\$0.46	\$0.45	\$0.88	\$0.83
Basic earnings attributable to shareholders per share	\$0.46	\$0.45	\$0.88	\$0.84
Dividends declared and paid per common share	\$0.32	\$0.30	\$0.32	\$0.30
Weighted average diluted shares outstanding	197,126,243	207,192,534	199,482,932	207,421,805
Weighted average basic shares outstanding	196,451,912	206,444,464	198,772,260	206,459,701

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

## Condensed Consolidated Statements of Comprehensive Income

(In thousands)

(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Net earnings	\$91,728	\$92,663	\$175,923	\$173,273
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments, net of tax of \$2,723 and \$5,938 for the three months ended June 30, 2014 and 2013, and \$1,394 and \$11,416 for the six months ended June 30, 2014 and 2013	4,985	(11,013 )	2,608	(21,026 )
Reclassification adjustment for foreign currency realized losses, net of tax of \$61 for the three and six months ended June 30, 2014	111	—	111	—
Other comprehensive income (loss)	5,096	(11,013 )	2,719	(21,026 )
Comprehensive income	96,824	81,650	178,642	152,247
Less comprehensive income attributable to the noncontrolling interest	440	175	860	456
Comprehensive income attributable to shareholders	\$96,384	\$81,475	\$177,782	\$151,791
See accompanying notes to condensed consolidated financial statements.				

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

## Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Operating Activities:				
Net earnings	\$91,728	\$92,663	\$175,923	\$173,273
Adjustments to reconcile net earnings to net cash from operating activities:				
Provision for losses (recoveries) on accounts receivable	496	100	(619)	) 1,041
Deferred income tax expense	2,891	5,818	10,085	12,940
Excess tax benefits from stock plans	(495)	) (584)	) (984)	) (1,683)
Stock compensation expense	11,877	11,040	22,171	22,045
Depreciation and amortization	12,417	11,674	24,799	22,952
Other	68	241	206	449
Changes in operating assets and liabilities:				
Increase in accounts receivable	(84,618)	) (48,223)	) (72,390)	) (9,367)
Increase in accounts payable and accrued expenses	61,377	45,080	90,923	43,690
Decrease in income taxes payable, net	(47,370)	) (33,692)	) (29,165)	) (15,474)
Increase in other current assets	(3,485)	) (91)	) (2,206)	) (576)
Net cash from operating activities	44,886	84,026	218,743	249,290
Investing Activities:				
Purchase of short-term investments	(15,301)	) (89,899)	) (96,431)	) (89,899)
Proceeds from maturities of short-term investments	15,643	96	36,619	134
Purchase of property and equipment	(9,635)	) (17,141)	) (18,395)	) (27,209)
Escrow deposit for land acquisition	(27,101)	) —	(27,101)	) —
Other, net	(1,536)	) 1,264	134	820
Net cash from investing activities	(37,930)	) (105,680)	) (105,174)	) (116,154)
Financing Activities:				
Proceeds from issuance of common stock	22,125	7,548	30,017	18,477
Repurchases of common stock	(131,391)	) (21,600)	) (358,116)	) (39,281)
Excess tax benefits from stock plans	495	584	984	1,683
Dividends paid	(62,807)	) (61,899)	) (62,807)	) (61,899)
Purchase of noncontrolling interest	—	—	—	(7,730)
Distributions to noncontrolling interest	—	—	(85)	) —
Net cash from financing activities	(171,578)	) (75,367)	) (390,007)	) (88,750)
Effect of exchange rate changes on cash and cash equivalents	4,137	(11,557)	(653)	) (19,119)
(Decrease) increase in cash and cash equivalents	(160,485)	) (108,578)	) (277,091)	) 25,267
Cash and cash equivalents at beginning of period	1,131,046	1,394,687	1,247,652	1,260,842
Cash and cash equivalents at end of period	\$970,561	\$1,286,109	\$970,561	\$1,286,109
Taxes Paid:				
Income taxes	\$105,963	\$85,195	\$133,459	\$112,146

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(In thousands, except share data)

(Unaudited)

Note 1. Summary of Significant Accounting Policies

A. Basis of Presentation

Expeditors International of Washington, Inc. (“the Company”) is a non-asset based provider of global logistics services operating through a worldwide network of offices and exclusive or non-exclusive agents. The Company’s customers include retailing and wholesaling, electronics, industrial and manufacturing companies around the world.

The condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. As a result, certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP) have been condensed or omitted. The Company believes that the disclosures made are adequate to make the information presented not misleading. The condensed consolidated financial statements reflect all adjustments, consisting of normal recurring items, which are, in the opinion of management, necessary to a fair statement of the results for the interim periods presented. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Company's Form 10-K as filed with the Securities and Exchange Commission on February 27, 2014.

All significant intercompany accounts and transactions have been eliminated in consolidation. All dollar amounts in the notes are presented in thousands except for share data. Certain prior year amounts have been reclassified to conform to the 2014 presentation. The reclassifications include presenting rental income of \$2,771 and \$5,494 for the three and six months ended June 30, 2013, respectively, in customs brokerage and other services revenues while it was historically recorded in rent and occupancy costs and other operating expenses.

B. Accounts Receivable

The Company maintains an allowance for doubtful accounts, which is reviewed at least monthly for estimated losses resulting from the inability of its customers to make required payments for services and advances. Additional allowances may be necessary in the future if the ability of its customers to pay deteriorates. The Company has recorded an allowance for doubtful accounts in the amounts of \$7,550 as of June 30, 2014 and \$8,695 as of December 31, 2013. Additions and write-offs have not been significant in the periods presented.

C. Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of the assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. The Company uses estimates primarily in the following areas: accounts receivable valuation, accrual of costs related to ancillary services the Company provides, accrual of insurance liabilities for the portion of the related exposure which the Company has self-insured, accrual of various tax liabilities, accrual of loss contingencies and calculation of share-based compensation expense. Actual results could differ from those estimates.

D. Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09 (Topic 606) “Revenue from Contracts with Customers”. This update, which supersedes the revenue recognition requirements in Accounting Standards Codification (ASC) Topic 605 - “Revenue Recognition” and most industry-specific guidance throughout the industry topics of the FASB ASC, substantially converges revenue recognition guidance between U.S. GAAP and International Financial Reporting Standards (IFRS), providing a single, comprehensive framework for recognizing revenue. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2016. The Company is currently evaluating the impact of adopting ASU 2014-09 on its consolidated financial statements and related disclosures.





## Note 2. Share-Based Compensation

The Company provides compensation benefits by granting stock options and employee stock purchase rights to its employees and restricted shares to its directors. On May 7, 2014, the shareholders approved the 2014 Stock Option Plan, which made available 2,750,000 shares of the Company's common stock for purchase upon exercise of options granted. The Company has historically granted the majority of its options during the second quarter of each fiscal year. For the six months ended June 30, 2014 and 2013, 2,289,600 and 2,775,450 options were granted, respectively. On May 7, 2014 the shareholders approved an amendment to the Company's 2002 Employee Stock Purchase Plan to increase the Company's common stock available for purchase under that plan by 3,000,000 shares. The grant of employee stock purchase rights and the issuance of shares under the employee stock purchase plan are made in the third quarter of each fiscal year and none were issued in the six-month periods ended June 30, 2014 and 2013. On May 7, 2014 shareholders also approved the 2014 Directors' restricted stock plan, which made available 250,000 shares of common stock for issuance to independent directors. On May 20, 2014, 30,702 fully vested shares were granted to independent directors.

The Company recognizes stock compensation expense based on an estimate of the fair value of awards granted to employees and directors under the Company's stock option, director restricted stock and employee stock purchase rights plans. The expense, adjusted for expected forfeitures, is recognized on a straight-line basis over the stock awards' vesting period. The forfeiture assumption used to calculate compensation expense is primarily based on historical pre-vesting employee forfeiture patterns.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions:

	Six months ended June 30,			
	2014		2013	
Dividend yield	1.50	%	1.50	%
Volatility - stock option plans	36	%	38	%
Risk free interest rates	2.27	%	0.71 - 1.15%	
Expected life (years) - stock option plans	6.52 - 7.43		5.91 - 7.43	
Weighted average fair value of stock options granted during the period	\$ 14.08		\$ 11.17	

Total stock compensation expense and the total related tax benefit recognized are as follows:

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Stock compensation expense	\$ 11,877	\$ 11,040	\$ 22,171	\$ 22,045
Recognized tax benefit	\$ 1,183	\$ 900	\$ 2,126	\$ 1,549

## Note 3. Basic and Diluted Earnings per Share

The following table reconciles the numerator and the denominator of the basic and diluted per share computations for earnings attributable to shareholders:

(Amounts in thousands, except share and per share amounts)	Three months ended June 30,		
	Net earnings attributable to shareholders	Weighted average shares	Earnings per share
2014			
Basic earnings attributable to shareholders	\$91,302	196,451,912	\$ 0.46
Effect of dilutive potential common shares	—	674,331	—
Diluted earnings attributable to shareholders	\$91,302	197,126,243	\$ 0.46
2013			
Basic earnings attributable to shareholders	\$92,315	206,444,464	\$ 0.45
Effect of dilutive potential common shares	—	748,070	—
Diluted earnings attributable to shareholders	\$92,315	207,192,534	\$ 0.45

(Amounts in thousands, except share and per share amounts)	Six months ended June 30,		
	Net earnings attributable to shareholders	Weighted average shares	Earnings per share
2014			
Basic earnings attributable to shareholders	\$175,126	198,772,260	\$ 0.88
Effect of dilutive potential common shares	—	710,672	—
Diluted earnings attributable to shareholders	\$175,126	199,482,932	\$ 0.88
2013			
Basic earnings attributable to shareholders	\$172,630	206,459,701	\$ 0.84
Effect of dilutive potential common shares	—	962,104	—
Diluted earnings attributable to shareholders	\$172,630	207,421,805	\$ 0.83

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

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Shares	15,673,784	17,456,059	16,850,941	17,456,059

## Note 4. Components of Equity

The components of equity for the six months ended June 30, 2014 and 2013 are as follows:

	Shareholders' equity	Noncontrolling interest	Total equity
Balance at December 31, 2013	\$2,084,783	1,548	2,086,331
Exercise of stock options	30,017	—	30,017
Shares repurchased under provisions of stock repurchase plans	(358,116 )	—	(358,116 )
Stock compensation expense	22,171	—	22,171
Tax benefits from stock plans, net	984	—	984
Net earnings	175,126	797	175,923
Other comprehensive income	2,656	63	2,719
Dividends paid (\$0.32 per share)	(62,807 )	—	(62,807 )
Distributions to noncontrolling interest	—	(85 )	(85 )
Balance at June 30, 2014	\$1,894,814	2,323	1,897,137
Balance at December 31, 2012	\$2,027,699	4,871	2,032,570
Exercise of stock options	18,477	—	18,477
Shares repurchased under provisions of stock repurchase plans	(39,281 )	—	(39,281 )
Stock compensation expense	22,045	—	22,045
Tax benefits from stock plans, net	1,516	—	1,516
Net earnings	172,630	643	173,273
Other comprehensive loss	(20,839 )	(187 )	(21,026 )
Dividends paid (\$0.30 per share)	(61,899 )	—	(61,899 )
Purchase of noncontrolling interest	(507 )	(3,226 )	(3,733 )
Balance at June 30, 2013	\$2,119,841	2,101	2,121,942

The Company has a Non-Discretionary Stock Repurchase Plan to repurchase shares from the proceeds of stock option exercises. During the six months ended June 30, 2014, 651,982 shares were repurchased at an average price of \$44.26 per share. The Company also has a Discretionary Stock Repurchase Plan that was amended by the Board of Directors on February 24, 2014 to authorize management to reduce issued and outstanding stock to 190 million shares of common stock. During the six months ended June 30, 2014, 7,947,500 shares were repurchased at an average price of \$41.43 per share.

Accumulated other comprehensive loss consisted entirely of foreign currency translation adjustments, net of related income tax effects, for all the periods presented.

On May 7, 2014, the Board of Directors declared a semi-annual cash dividend of \$0.32 per share payable on June 16, 2014 to shareholders of record as of June 2, 2014. On May 1, 2013, the Board of Directors declared a semi-annual cash dividend of \$0.30 per share payable on June 17, 2013 to shareholders of record as of June 3, 2013.

## Note 5. Fair Value of Financial Instruments

The Company's financial instruments, other than cash, consist primarily of cash equivalents, short-term investments, accounts receivable, accounts payable and accrued expenses. The carrying value of these financial instruments approximates their fair value. Cash equivalents consist of highly liquid investments with a maturity of three months or less at date of purchase. Short-term investments have a maturity of greater than three months at date of purchase.

Cash, cash equivalents and short-term investments consist of the following:

	June 30, 2014		December 31, 2013	
	Cost	Fair Value	Cost	Fair Value
Cash and Cash Equivalents:				
Cash and overnight deposits	\$580,228	580,228	590,317	590,317
Corporate commercial paper	346,517	346,584	629,923	629,990
Time deposits	43,816	43,816	27,412	27,412
Total cash and cash equivalents	970,561	970,628	1,247,652	1,247,719
Short-Term Investments:				
Corporate commercial paper	86,107	86,233	26,296	26,321
Time deposits	42	42	41	41
Total short-term investments	86,149	86,275	26,337	26,362
Total	\$1,056,710	1,056,903	1,273,989	1,274,081

The fair value of corporate commercial paper is based on the use of market interest rates for identical or similar assets (Level 2 fair value measurement).

## Note 6. Contingencies

The Company is involved in claims, lawsuits, government investigations and other legal matters that arise in the ordinary course of business and are subject to inherent uncertainties. Currently, in management's opinion and based upon advice from legal advisors, none of these matters are expected to have a significant effect on the Company's operations or financial position. As of June 30, 2014, the amounts accrued for these claims, lawsuits, government investigations and other legal matters are not significant to the Company's operations or financial position. At this time the Company is unable to estimate any additional loss or range of reasonably possible losses, if any, beyond the amounts recorded, that might result from the resolution of these matters.

## Note 7. Business Segment Information

The Company is organized functionally in geographic operating segments. Accordingly, management focuses its attention on revenues, net revenues<sup>1</sup>, operating income, identifiable assets, capital expenditures, depreciation and amortization and equity generated in each of these geographical areas when evaluating the effectiveness of geographic management. The Company charges its subsidiaries and affiliates for services rendered in the United States on a cost recovery basis. Transactions among the Company's various offices are conducted using the same arms-length pricing methodologies the Company uses when its offices transact business with independent agents.

Financial information regarding the Company's operations by geographic area is as follows:

(in thousands)	UNITED STATES	OTHER NORTH AMERICA	LATIN AMERICA	ASIA PACIFIC	EUROPE and AFRICA	MIDDLE EAST and INDIA	ELIMI-NATIONS	CONSOLI-DATED
Three months ended June 30, 2014:								
Revenues from unaffiliated customers	\$416,454	55,343	22,003	780,834	244,642	79,865	—	1,599,141
Transfers between geographic areas	22,408	2,587	5,567	12,393	9,468	5,238	(57,661 )	—
Total revenues	\$438,862	57,930	27,570	793,227	254,110	85,103	(57,661 )	1,599,141
Net revenues <sup>1</sup>	\$200,106	25,533	16,648	138,445	78,638	25,344	—	484,714
Operating income	\$59,780	7,001	4,676	51,436	14,219	5,331	—	142,443
Identifiable assets at period end	\$1,328,312	110,498	57,588	743,190	511,149	173,425	5,778	2,929,940
Capital expenditures	\$5,547	422	171	1,907	1,262	326	—	9,635
Depreciation and amortization	\$7,879	296	227	2,108	1,471	436	—	12,417
Equity	\$1,044,386	72,681	35,578	481,899	204,952	94,390	(36,749 )	1,897,137
Three months ended June 30, 2013:								
Revenues from unaffiliated customers	\$395,495	56,626	21,421	749,282	206,020	74,380	—	1,503,224
Transfers between geographic areas	23,217	2,516	5,614	11,605	9,189	4,559	(56,700 )	—
Total revenues	\$418,712	59,142	27,035	760,887	215,209	78,939	(56,700 )	1,503,224
Net revenues <sup>1</sup>	\$193,509	25,440	15,522	141,439	71,068	24,894	—	471,872
Operating income	\$58,310	7,887	4,601	54,781	11,613	6,387	—	143,579
Identifiable assets at period end	\$1,531,739	101,721	53,795	809,827	418,077	155,058	(6,552 )	3,063,665
Capital expenditures	\$4,354	708	145	11,056	563	315	—	17,141
Depreciation and amortization	\$7,276	197	229	1,983	1,550	439	—	11,674
Equity	\$1,209,762	65,897	33,272	606,793	166,891	75,418	(36,091 )	2,121,942

(in thousands)	UNITED STATES	OTHER NORTH AMERICA	LATIN AMERICA	ASIA PACIFIC	EUROPE and AFRICA	MIDDLE EAST and INDIA	ELIMI-NATIONS	CONSOLI-DATED
Six months ended June 30, 2014:								
Revenues from unaffiliated customers	\$817,193	106,927	42,632	1,495,218	472,150	156,666	—	3,090,786
Transfers between geographic areas	42,419	4,962	10,771	24,402	18,425	10,100	(111,079 )	—
Total revenues	\$859,612	111,889	53,403	1,519,620	490,575	166,766	(111,079 )	3,090,786
Net revenues <sup>1</sup>	\$392,188	51,694	32,005	271,719	151,695	49,999	—	949,300
Operating income	\$111,678	15,376	9,535	104,277	25,285	11,495	—	277,646
Identifiable assets at period end	\$1,328,312	110,498	57,588	743,190	511,149	173,425	5,778	2,929,940
Capital expenditures	\$9,475	686	472	5,033	2,114	615	—	18,395
Depreciation and amortization	\$15,731	576	439	4,216	2,963	874	—	24,799
Equity	\$1,044,386	72,681	35,578	481,899	204,952	94,390	(36,749 )	1,897,137
Six months ended June 30, 2013:								
Revenues from unaffiliated customers	\$769,869	108,355	41,285	1,443,419	408,533	144,971	—	2,916,432
Transfers between geographic areas	43,243	5,060	10,490	22,235	18,069	8,886	(107,983 )	—
Total revenues	\$813,112	113,415	51,775	1,465,654	426,602	153,857	(107,983 )	2,916,432
Net revenues <sup>1</sup>	\$373,852	49,221	29,933	276,989	141,682	48,202	—	919,879
Operating income	\$105,663	14,499	8,690	107,665	23,539	12,041	—	272,097
Identifiable assets at period end	\$1,531,739	101,721	53,795	809,827	418,077	155,058	(6,552 )	3,063,665
Capital expenditures	\$9,733	895	404	13,608	1,761	808	—	27,209
Depreciation and amortization	\$14,033	404	470	3,971	3,179	895	—	22,952
Equity	\$1,209,762	65,897	33,272	606,793	166,891	75,418	(36,091 )	2,121,942

<sup>1</sup>Net revenues are a non-GAAP measure calculated as revenues less directly related operations expenses attributable to the Company's principal services. The Company's management believes that net revenues are a better measure than total revenues when evaluating the Company's operating segment performance since total revenues earned as a freight consolidator include the carriers' charges for carrying the shipment, whereas revenues earned in other capacities include primarily the commissions and fees earned by the Company. Net revenue is one of the Company's primary operational and financial measures and demonstrates the Company's ability to concentrate and leverage purchasing power through effective consolidation of shipments from customers utilizing a variety of transportation carriers and optimal routings.

The following table presents the calculation of consolidated net revenues:

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Total revenues	\$1,599,141	\$1,503,224	\$3,090,786	\$2,916,432

Expenses:

Airfreight services	503,213	483,016	986,095	947,935
Ocean freight and ocean services	423,716	380,727	791,091	725,650
Customs brokerage and other services	187,498	167,609	364,300	322,968
Net revenues	\$484,714	\$471,872	\$949,300	\$919,879

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

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

Certain portions of this report on Form 10-Q including the sections entitled "Overview," "Strategy and Culture," "International Trade and Competition," "Seasonality," "Critical Accounting Estimates," "Results of Operations," "Currency and Other Risk Factors" and "Liquidity and Capital Resources" contain forward-looking statements. Words such as "will likely result", "are expected to", "will continue", "is anticipated", "estimate", "project", "plan", "believe", "probable", "reasonably possible", "may", "could", "should", "intends", "foreseeable future" and variations of such words and similar expressions are intended to identify such forward-looking statements. In addition, any statements that refer to projections of future financial performance, our anticipated growth and trends in the Company's businesses, and other characterizations of future events or circumstances are forward-looking statements. These statements must be considered in connection with the discussion of the important factors that could cause actual results to differ materially from the forward-looking statements. Attention should be given to the factors identified and discussed in the Company's annual report on Form 10-K filed on February 27, 2014.

Overview

Expeditors International of Washington, Inc. is a global logistics company. The Company's services include air and ocean freight consolidation and forwarding, customs brokerage, warehousing and distribution, purchase order management, vendor consolidation, time-definite transportation services, cargo insurance and other logistics solutions. The Company does not compete for overnight courier or small parcel business. As a non-asset based carrier, the Company does not own or operate transportation assets.

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

The Company generates the major portion of its air and ocean freight revenues by purchasing transportation services on a wholesale basis from direct (asset-based) carriers and reselling those services to its customers on a retail basis. The difference between the rate billed to customers (the sell rate) and the rate paid to the carrier (the buy rate) is termed "net revenue" (a non-GAAP measure), "yield" or "margin." By consolidating shipments from multiple customers and concentrating its buying power, the Company is able to negotiate favorable buy rates from the direct carriers, while at the same time offering lower sell rates than customers would otherwise be able to negotiate themselves. The most significant drivers of changes in gross revenues and related transportation expenses are volume, sell rates and buy rates. Volume has a similar effect on the change in both gross revenues and related transportation expenses in each of the Company's three primary sources of revenue.

In most cases the Company acts as an indirect carrier. When acting as an indirect carrier, the Company will issue a House Airway Bill (HAWB) or a House Ocean Bill of Lading (HOBL) to customers as the contract of carriage. In turn, when the freight is physically tendered to a direct carrier, the Company receives a contract of carriage known as a Master Airway Bill for airfreight shipments and a Master Ocean Bill of Lading for ocean shipments. In these transactions, the Company is the primary obligor and is required to compensate direct carriers for services performed regardless of whether customers accept the service, has latitude in establishing price, has discretion in selecting the direct carrier and has credit risk. Therefore, the Company is the principal in these transactions and reports revenue and the related expenses on a gross basis.

For revenues earned in other capacities, for instance, when the Company does not issue a HAWB or a HOBL or otherwise acts solely as an agent for the shipper, only the commissions and fees earned for such services are included in revenues. In these transactions, the Company is not a principal and reports only commissions and fees earned in revenue.

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



The Company is managed along three geographic areas of responsibility: Americas; Asia Pacific; and Europe, Africa, Near/Middle East and Indian Subcontinent (EMAIR). Each area is divided into sub-regions which are composed of operating units with individual profit and loss responsibility. The Company's business involves shipments between operating units and typically touches more than one geographic area. The nature of the international logistics business necessitates a high degree of communication and cooperation among operating units. Because of this inter-relationship between operating units, it is very difficult to examine any one geographic area and draw meaningful conclusions as to its contribution to the Company's overall success on a stand-alone basis.

The Company's operating units share revenue using the same arms-length pricing methodologies the Company uses when its offices transact business with independent agents. The Company charges its subsidiaries and affiliates for services rendered in the United States on a cost recovery basis. The Company's strategy closely links compensation with operating unit profitability. Individual success is closely linked to cooperation with other operating units within the network.

The mix of services varies by segment based primarily on the import or export orientation of local operations in each region. In accordance with the Company's revenue recognition policy (see Note 1. E. to the consolidated financial statements in the Company's annual report on Form 10-K filed on February 27, 2014), almost all freight revenues and related expenses are recorded at origin and shipment profits are split between origin and destination offices by recording a commission fee or profit share revenue at destination and a corresponding commission or profit share expense as a component of origin consolidation costs. The Asia Pacific segment is the Company's largest export oriented region and accounted for 48% of revenues and 38% of operating income for the six months ended June 30, 2014. Asia Pacific's operating income as a percentage of revenue is lower than other segments due to the largely export nature of operations in that region.

#### Strategy and Culture

The Company has pursued a strategy emphasizing organic growth supplemented by certain strategic acquisitions. From the inception of the Company, management has believed that the elements required for a successful global service organization can only be assured through recruiting, training, and ultimately retaining superior personnel. The Company's greatest challenge is now and always has been perpetuating a consistent global corporate culture which demands:

- Total dedication, first and foremost, to providing superior customer service;
- Compliance with Company policies and government regulations;
- Aggressive marketing of all of the Company's service offerings;
- Ongoing development of key employees and management personnel via formal and informal means;
- Creation of unlimited advancement opportunities for employees dedicated to hard work, personal growth and continuous improvement;
- Individual commitment to the identification and mentoring of successors for every key position so that when inevitable change occurs, a qualified and well-trained internal candidate is ready to step forward; and
- Continuous identification, design and implementation of system solutions, both technological and otherwise, to meet and exceed the needs of our customers while simultaneously delivering tools to make the Company's employees more efficient and more effective.

The Company reinforces these values with a compensation system that rewards employees for profitably managing the things they can control. This compensation system has been in place since the Company became a publicly traded entity. There is no limit to how much a key manager can be compensated for success. The Company believes in a "real world" environment in every operating unit where individuals are not sheltered from the profit implications of their decisions. If these decisions result in operating losses, current management must make up these losses with future operating profits, in the aggregate, before any cash incentive compensation can be earned. At the same time, the Company insists on continued focus on such things as accounts receivable collection, cash flow management and credit soundness in an attempt to insulate managers from the sort of catastrophic errors that might end a career. Any failure to perpetuate this unique culture on a self-sustained basis throughout the Company provides a greater threat to the Company's continued success than any external force, which would be largely beyond its control. The Company strongly believes that it is nearly impossible to predict events that, in the aggregate, could have a positive or a negative impact on future operations. As a result, management's focus is on building and maintaining a global corporate culture and an environment where well-trained employees and managers are prepared to identify and react to subtle changes as they develop and thereby help the Company adapt and thrive as major trends emerge.

The Company's ability to provide services to its customers is highly dependent on good working relationships with a variety of entities including airlines, steamship lines, ground transportation providers and governmental agencies. The significance of maintaining acceptable working relationships with these entities has gained increased importance as a result of ongoing concern over terrorism and increased governmental regulation and oversight of international trade. A

good reputation helps to develop practical working understandings that will assist in meeting security requirements while minimizing potential international trade obstacles, especially as governments promulgate new regulations and increase oversight and enforcement of new and existing laws. The Company considers its current working relationships with these entities to be satisfactory. The airline and ocean steamship line industries have incurred significant losses in recent years and many carriers are highly leveraged with debt. This situation has required the Company to be increasingly selective in determining which carriers to utilize. Further changes in the financial stability, operating capabilities and capacity of asset-based carriers, space allotments

available from carriers, governmental regulations, and/or trade accords could adversely affect the Company's business in unpredictable ways.

#### International Trade and Competition

The Company operates in 62 countries in the competitive global logistics industry and Company activities are closely tied to the global economy. International trade is influenced by many factors, including economic and political conditions in the United States and abroad, currency exchange rates, and laws and policies relating to tariffs, trade restrictions, foreign investments and taxation. Periodically, governments consider a variety of changes to current tariffs and trade restrictions and accords. The Company cannot predict which, if any, of these proposals may be adopted, or the effects the adoption of any such proposal will have on the Company's business. Doing business in foreign locations also subjects the Company to a variety of risks and considerations not normally encountered by domestic enterprises. In addition to being influenced by governmental policies concerning international trade, the Company's business may also be affected by political developments and changes in government personnel or policies, as well as economic turbulence, political unrest and security concerns in the nations in which it does business and the future impact that these events may have on international trade and oil prices.

The global logistics services industry is intensely competitive and is expected to remain so for the foreseeable future. Consistent with continuing uncertainty in global economic conditions, concerns over volatile fuel costs, rising costs in general, political unrest and fluctuating currency exchange rates, the Company's pricing and terms continue to be pressured by customers, carriers and service providers which has resulted in a compression of the Company's unitary margins. We expect these competitive conditions to continue.

The Company cannot predict what impact ongoing uncertainties in the global economy may have on its operating results, freight volumes, pricing, changes in consumer demand, carrier stability and capacity, customers' abilities to pay or on changes in competitors' behavior.

#### Seasonality

Historically, the Company's operating results have been subject to seasonal trends with the first quarter being the weakest and the third and fourth quarters being the strongest. This pattern has been the result of, or influenced by, numerous factors including weather patterns, national holidays, consumer demand, new product launches, economic conditions and a myriad of other similar and subtle forces. In addition, this historical quarterly trend has been influenced by the growth and diversification of the Company's international network and service offerings.

A significant portion of the Company's revenues are derived from customers in retail industries whose shipping patterns are tied closely to consumer demand, and from customers in industries whose shipping patterns are dependent upon just-in-time production schedules. Therefore, the timing of the Company's revenues are, to a large degree, impacted by factors out of the Company's control, such as a sudden change in consumer demand for retail goods, product launches and/or manufacturing production delays. Additionally, many customers ship a significant portion of their goods at or near the end of a quarter, and therefore, the Company may not learn of a shortfall in revenues until late in a quarter.

To the extent that a shortfall in revenues or earnings was not expected by securities analysts, any such shortfall from levels predicted by securities analysts could have an immediate and adverse effect on the trading price of the Company's stock. The Company cannot accurately forecast many of these factors or estimate accurately the relative influence of any particular factor and, as a result, there can be no assurance that historical patterns will continue in future periods.

#### Critical Accounting Estimates

The preparation of consolidated financial statements in accordance with accounting principles generally accepted in the United States requires that the Company make estimates and judgments. The Company bases its estimates on historical experience and on assumptions that it believes are reasonable. The Company's critical accounting estimates are discussed in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" section of the Company's annual report on Form 10-K for the year ended December 31, 2013, filed on February 27, 2014. There have been no material changes to the critical accounting estimates previously disclosed in that report.



## Results of Operations

The following table shows the total net revenues (a non-GAAP measure calculated as revenues less directly related operations expenses attributable to the Company's principal services) and the Company's expenses for the three and six-month periods ended June 30, 2014 and 2013, expressed as percentages of net revenues. Management believes that net revenues are a better measure than total revenues when analyzing and discussing management's effectiveness in managing the Company's principal services since total revenues earned by the Company as a freight consolidator include the carriers' charges to the Company for carrying the shipment, whereas revenues earned by the Company in its other capacities include primarily the commissions and fees actually earned by the Company. Net revenue is one of the Company's primary operational and financial measures that demonstrates the ability of the Company to manage sell rates to customers with its ability to concentrate and leverage its purchasing power through effective consolidation of shipments from multiple customers utilizing a variety of transportation carriers and optimal routings. Using net revenue also provides a commonality for comparison among various services.

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

	Three months ended June 30, 2014			2013			Six months ended June 30, 2014			2013		
	Amount	Percent of net revenues		Amount	Percent of net revenues		Amount	Percent of net revenues		Amount	Percent of net revenues	
(in thousands)												
Airfreight services:												
Revenues	\$667,257			\$642,969			\$1,314,395			\$1,263,343		
Expenses	503,213			483,016			986,095			947,935		
Net revenues	164,044	34 %		159,953	34 %		328,300	34 %		315,408	34 %	
Ocean freight services and ocean services:												
Revenues	536,438			492,007			1,005,662			937,486		
Expenses	423,716			380,727			791,091			725,650		
Net revenues	112,722	23		111,280	24		214,571	23		211,836	23	
Customs brokerage and other services:												
Revenues	395,446			368,248			770,729			715,603		
Expenses	187,498			167,609			364,300			322,968		
Net revenues	207,948	43		200,639	42		406,429	43		392,635	43	
Total net revenues	484,714	100		471,872	100		949,300	100		919,879	100	
Overhead expenses:												
Salaries and related costs	260,767	54		255,569	54		516,709	54		503,986	55	
Other	81,504	17		72,724	16		154,945	17		143,796	15	
Total overhead expenses	342,271	71		328,293	70		671,654	71		647,782	70	
Operating income	142,443	29		143,579	30		277,646	29		272,097	30	
Other income, net	5,954	1		7,395	2		8,370	1		12,169	1	
Earnings before income taxes	148,397	30		150,974	32		286,016	30		284,266	31	
Income tax expense	56,669	12		58,311	12		110,093	12		110,993	12	
Net earnings	91,728	18		92,663	20		175,923	18		173,273	19	
Less net earnings attributable to the noncontrolling interest	426	—		348	—		797	—		643	—	
	\$91,302	18 %		\$92,315	20 %		\$175,126	18 %		\$172,630	19 %	

Net earnings attributable to shareholders

Airfreight services:

Airfreight services revenues increased 4% for both the three and six-month periods ended June 30, 2014, as compared with the same periods for 2013, due to a 6% increase in tonnage for both the three and six months that was partially offset by the Company lowering sell rates in response to competitive market conditions in North America and Asia Pacific. Airfreight services expenses also increased 4% for both the three and six-month periods ended June 30, 2014 as the increase in tonnage was slightly offset by negotiating lower buy rates with carriers, primarily on exports from North America.

Airfreight services net revenues increased 3% for the three-month period ended June 30, 2014, as compared with the same period for 2013. This increase was primarily due to a 6% improvement in airfreight tonnage, partially offset by a 4% decrease in net revenue per kilo. North America export tonnage grew by 9% but net revenues increased by only 2% as the Company implemented sell rate reductions to customers, which on average outpaced buy rate reductions negotiated with carriers. Europe net revenues increased 22% primarily due to a 19% growth in export tonnage. Asia Pacific net revenues decreased 5% due to lowering sell rates in response to competitive market conditions while maintaining export tonnage comparable to the same period in 2013.

Airfreight services net revenues increased 4% for the six-month period ended June 30, 2014, as compared with the same period for 2013. This was primarily due to a 6% improvement in airfreight tonnage, partially offset by a 3% decrease in net revenue per kilo. For the same reasons described above, North America export tonnage grew by 11% but net revenues increased by only 6%, Europe net revenues increased 16% primarily due to a 14% growth in export tonnage, and Asia Pacific net revenues decreased 3%, while maintaining export tonnage comparable to the same period in 2013.

The global airfreight market continues to be affected by overcapacity and the timing of new product launches. Customers remain focused on improving supply-chain efficiency by utilizing deferred airfreight or ocean freight whenever possible. The Company expects these trends to continue in conjunction with carriers' efforts to manage available capacity, however, this could be affected by new product launches during periods that have historically experienced higher demands. These factors result in a higher degree of volatility in buy and sell rates and volumes.

Ocean freight services and ocean services:

Ocean freight and ocean services revenues increased 9% and 7%, respectively, for the three and six-month periods ended June 30, 2014, as compared with the same periods for 2013. Container volume increased 12% for both the three and six months as the Company lowered sell rates to maintain its existing customer base and grow market share. Ocean freight and ocean services expenses increased 11% and 9%, respectively, for the three and six-month periods ended June 30, 2014, as compared with the same periods for 2013, primarily resulting from higher volumes and higher costs in ocean freight consolidation and order management services. Container volume is measured in terms of forty-foot container equivalent units (FEUs).

Ocean freight and ocean services net revenues increased 1% for both the three and six-month periods ended June 30, 2014, as compared with the same periods for 2013. Ocean freight and ocean services net revenues are comprised of three basic services: ocean freight consolidation, direct ocean forwarding and order management. The largest component is ocean freight consolidation, which represented 44% of ocean freight net revenue for both the three and six-month periods ended June 30, 2014 and 48% and 47%, respectively, for the same periods ended in 2013.

Ocean freight consolidation net revenues decreased 7% for the three-month period ended June 30, 2014, as compared with the same period in 2013. The 12% increase in volume was more than offset by the effect of reducing sell rates to maintain customers and grow market share while incurring slightly higher average buy rates, primarily in North America and Asia Pacific. This resulted in a 17% decrease in net revenue per container. Ocean freight consolidation net revenues decreased 6% for the six-month period ended June 30, 2014, as compared with the same period in 2013. The 12% increase in volume was more than offset by the effect of reducing sell rates, which resulted in a 16% decrease in net revenue per container, primarily in North America and Asia Pacific.

Direct ocean freight forwarding net revenues increased 8% and 6%, respectively, for the three and six-month periods ended June 30, 2014, as compared with the same periods in 2013, as a result of higher volumes principally in Asia Pacific and Europe. Order management net revenues increased 11% and 9%, respectively, for the three and six-month periods ended June 30, 2014, as compared with the same periods in 2013, mostly due to higher volumes with new and

existing customers, primarily in North America. The overall margins in order management declined due to higher costs, primarily in Asia Pacific.

North America ocean freight and ocean services net revenues increased 1% and 2%, respectively, for the three and six-month periods ended June 30, 2014, primarily due to an increase in order management services, offset by a decline in ocean freight consolidation. Europe ocean freight and ocean services net revenues increased 5% and 4% for the three and six-month periods, primarily due to an increase in direct ocean forwarding, offset by a decline in ocean freight consolidation. Asia Pacific remained flat in the second quarter and decreased 1% in the first half of 2014 as compared with 2013, primarily due to an increase in direct ocean forwarding, offset by a decline in ocean freight consolidation.

Customs brokerage and other services:

Customs brokerage and other services revenues increased 7% and 8%, respectively, for the three and six-month periods ended June 30, 2014, as compared with the same periods for 2013, as a result of increased volumes from existing and new customers. Customs brokerage and other services expenses increased 12% and 13%, respectively, for the three and six-month periods ended June 30, 2014, as compared with the same periods for 2013 due to higher costs associated with import and delivery services.

Customs brokerage and other services net revenues increased 4% for both the three and six-month periods ended June 30, 2014, as compared with the same periods in 2013, primarily due to higher volumes from existing and new customers in North America. The margin percentage declined primarily as a result of higher import services costs and lower yields in domestic time-definite transportation services.

North America, Asia Pacific and Europe net revenues increased 4%, 2% and 5%, respectively, in the second quarter of 2014, as compared with the same period in 2013, primarily as a result of higher volumes from existing and new customers. North America and Europe net revenues increased 6% and 2%, respectively, in the first half of 2014, as compared with the same period in 2013, primarily as a result of higher volumes from existing and new customers. Asia Pacific net revenues declined 1%, primarily due to higher import services costs.

Overhead expenses:

Salaries and related costs increased 2% and 3%, respectively, for the three and six-month periods ended June 30, 2014, as compared with the same periods in 2013, primarily as a result of a higher average number of employees in North America. In the second quarter of 2014, the Company benefited from a \$5 million reduction in expense resulting from favorable claims experience in its healthcare insurance program.

Historically, the relatively consistent relationship between salaries and net revenues is the result of a compensation philosophy that has been maintained since the inception of the Company: offer a modest base salary and the opportunity to share in a fixed and determinable percentage of the operating profit of the business unit controlled by each key employee. Using this compensation model, changes in individual incentive compensation will occur in proportion to changes in Company operating income, creating a direct alignment between corporate performance and shareholder interests. Bonuses to management for the six-month period ended June 30, 2014 were up 1% as compared with the same period for 2013, primarily as a result of a 2% increase in operating income. The Company's management incentive compensation programs have always been incentive-based and performance driven and there is no built-in bias that favors or enriches management in a manner inconsistent with overall corporate performance.

Salaries and related costs as a percentage of net revenues remained constant and decreased 1%, respectively, for the three and six month periods ended June 30, 2014 as compared with the same periods for 2013.

Because the Company's management incentive compensation programs are also cumulative, no management bonuses can be paid unless the relevant business unit is, from inception, cumulatively profitable. Any operating losses must have been offset in their entirety by operating profits before current management is eligible for a bonus. Since the most significant portion of management compensation comes from the incentive bonus programs, the Company believes that this cumulative feature is a disincentive to excessive risk taking by its managers. Due to the nature of the Company's services, it has a short operating cycle. The outcome of any higher risk transactions, such as overriding established credit limits, would be known in a relatively short time frame. Management believes that when the potential and certain impact on the bonus is fully considered in light of this short operating cycle, the potential for short term gains that could be generated by engaging in risky business practices is sufficiently mitigated to discourage excessive and inappropriate risk taking. Management believes that both the stability and the long term growth in revenues, net revenues and net earnings are a result of the incentives inherent in the Company's compensation



program.

Other overhead expenses increased 12% and 8%, respectively, for the three and six-month periods ended June 30, 2014, as compared with the same periods in 2013. The increase in expenses in the second quarter of 2014 is primarily due to: (i) consulting fees and costs associated with the Company's strategic assessment and organizational changes; (ii) higher ongoing costs related to investments in software and systems; (iii) increased building, maintenance and warehousing costs; (iv) claims; and (v) the impact of the transition to a value added tax system in certain jurisdictions in the second quarter of 2013.

The increase in expenses in the first half of 2014 is primarily due to similar cost increases described above, partially offset by a recovery of bad debt expense. Other overhead expenses as a percentage of net revenues increased 1% and 2%, respectively, for the three and six-month periods ended June 30, 2014, as compared with the same periods in 2013.

Income tax expense:

The Company pays income taxes in the United States and other jurisdictions. The Company's consolidated effective income tax rate was 38.2% and 38.5% for the three and six-month periods ended June 30, 2014 and 38.6% and 39.0%, for the same periods in 2013. The decreases in the effective tax rates over the prior periods are principally the result of an increasingly higher proportion of the Company's total outstanding stock options being non-qualified grants. The tax benefit associated with non-qualified stock option grants is recorded when the related compensation expense is recognized while the tax benefits for incentive stock options and employee stock purchase plan shares cannot be anticipated and are recognized if and when a disqualifying disposition event occurs.

#### Currency and Other Risk Factors

The nature of the Company's worldwide operations necessitates the Company dealing with a multitude of currencies other than the U.S. dollar. This results in the Company being exposed to the inherent risks of volatile international currency markets and governmental interference. Some of the countries where the Company maintains offices and/or agency relationships have strict currency control regulations which influence the Company's ability to hedge foreign currency exposure. The Company tries to compensate for these exposures by accelerating international currency settlements among its offices or agents. The Company may enter into foreign currency hedging transactions where there are regulatory or commercial limitations on the Company's ability to move money freely around the world or the short-term financial outlook in any country is such that hedging is the most time-sensitive way to mitigate short-term exchange losses. Any such hedging activity during the three and six months ended June 30, 2014 and 2013 was insignificant. The Company had no foreign currency derivatives outstanding at June 30, 2014 and December 31, 2013. During the three and six months ended June 30, 2014, net foreign currency losses were less than \$1 million and approximately \$3 million, respectively. Net foreign currency gains were less than \$1 million in the second quarter of 2013. Net foreign currency losses were less than \$1 million in the first half of 2013.

International air and ocean freight forwarding and customs brokerage are intensively competitive and are expected to remain so for the foreseeable future. There are a large number of entities competing in the international logistics industry, many of which have significantly more resources than the Company; however, the Company's primary competition is confined to a relatively small number of companies within this group. The industry continues to experience consolidations into larger firms striving for stronger and more complete multinational and multi-service networks. However, regional and local brokers and forwarders remain a competitive force.

The primary competitive factors in the international logistics industry continue to be price and quality of service, including reliability, responsiveness, expertise, convenience, and scope of operations. The Company emphasizes quality customer service and believes that its prices are competitive with those of others in the industry. Customers regularly solicit bids from competitors in order to improve service, pricing and contractual terms such as seeking longer payment terms, higher or unlimited liability limits and performance penalties. Increased competition and competitors' acceptance of expanded contractual terms could result in reduced revenues, reduced margins, higher operating costs or loss of market share, any of which would damage the Company's results of operations and financial condition.

Larger customers utilize more sophisticated and efficient procedures for the management of their logistics supply chains by embracing strategies such as just-in-time inventory management. The Company believes that this trend has resulted in customers using fewer service providers with greater technological capacity and more consistent global

coverage. Accordingly, sophisticated computerized customer service capabilities and a stable worldwide network have become significant factors in attracting and retaining customers. Developing and maintaining these systems and a worldwide network has added a considerable indirect cost to the services provided to customers. Smaller and middle-tier competitors, in general, do not have the resources available to develop customized systems and a worldwide network.

#### Liquidity and Capital Resources

The Company's principal source of liquidity is cash and cash equivalents, short-term investments and cash generated from operating activities. Net cash provided by operating activities for the three and six months ended June 30, 2014, was approximately \$45 million and \$219 million, respectively, as compared with \$84 million and \$249 million for the same periods in 2013. The decreases of \$39 million and \$30 million for the three and six-month periods ended June 30, 2014 are primarily due to changes in working capital accounts. At June 30, 2014, working capital was \$1,348 million, including cash and cash equivalents and short-term investments of \$1,057 million. The Company had no long-term debt at June 30, 2014. Management believes that the Company's current cash position and operating cash flows will be sufficient to meet its capital and liquidity requirements for at least the next 12 months and thereafter for the foreseeable future, including meeting any contingent liabilities related to standby letters of credit and other obligations.

As a customs broker, the Company makes significant cash advances for a select group of its credit-worthy customers. These cash advances are for customer obligations such as the payment of duties and taxes to governmental authorities in various countries throughout the world. Cash advances are a "pass through" and are not recorded as a component of revenue and expense. The billings of such advances to customers are accounted for as a direct increase in accounts receivable from the customer and a corresponding increase in accounts payable to governmental customs authorities. As a result of these "pass through" billings, the conventional Days Sales Outstanding or DSO calculation does not directly measure collection efficiency. For customers that meet certain criteria, the Company has agreed to extend payment terms beyond its customary terms. Management believes that the Company has effective credit control procedures, and historically has experienced relatively insignificant collection problems.

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

Cash used in investing activities for the three and six months ended June 30, 2014 was \$38 million and \$105 million, respectively, as compared with \$106 million and \$116 million for the same periods in 2013. The Company received net proceeds from short-term investments of less than \$1 million and made a net investment of \$60 million for the three and six-month periods ended June 30, 2014, respectively, as compared with net short-term investments of \$90 million for the same periods in 2013. The Company had capital expenditures of \$10 million and \$18 million, respectively, for the three and six-month periods ended June 30, 2014, as compared with capital expenditures of \$17 million and \$27 million, for the same periods in 2013. Capital expenditures in the three and six months ended June 30, 2014 related primarily to investments in technology, office furniture and equipment and building and leasehold improvements. The Company does have need, on occasion, to purchase buildings to house staff and to facilitate the staging of customers' freight. During the second quarter of 2014, the Company deposited \$27 million in an escrow account for an expected land acquisition. Total capital expenditures in 2014 are estimated to be approximately \$50 million. This includes routine capital expenditures plus additional real estate development.

Cash used in financing activities during the three and six months ended June 30, 2014, was \$172 million and \$390 million as compared with \$75 million and \$89 million for the same periods in 2013. The Company uses the proceeds from stock option exercises and available cash to repurchase the Company's common stock on the open market to limit the growth in issued and outstanding shares. Also, during the three and six months ended June 30, 2014, the Company used cash to repurchase additional common stock of 2.0 million and 7.6 million shares to reduce the number of total outstanding shares.

The Company follows established guidelines relating to credit quality, diversification and maturities of its investments to preserve principal and maintain liquidity. The Company's investment portfolio has not been adversely impacted by the disruption in the credit markets. However, there can be no assurance that the Company's investment portfolio will

not be adversely affected in the future.

At June 30, 2014, the Company was contingently liable for \$77 million from standby letters of credit and guarantees. The standby letters of credit and guarantees relate primarily to obligations of the Company's foreign subsidiaries for credit extended in the ordinary course of business by direct carriers, primarily airlines, and for duty and tax deferrals available from governmental entities responsible for customs and value-added-tax (VAT) taxation. The total underlying amounts due and payable for transportation and governmental excises are properly recorded as obligations in the books of the respective foreign subsidiaries, and there would be no need to record additional expense in the unlikely event the parent company is required to perform.

The Company's foreign subsidiaries regularly remit dividends to the U.S. parent company after evaluating their working capital requirements and needs to finance local capital expenditures. In some cases, the Company's ability to repatriate funds from foreign operations may be subject to foreign exchange controls. At June 30, 2014, cash and cash equivalent balances of \$661 million were held by the Company's non-United States subsidiaries, of which \$57 million was held in banks in the United States. Earnings of the Company's foreign subsidiaries are not considered to be indefinitely reinvested outside of the United States and, accordingly, a deferred tax liability has been accrued for all undistributed earnings, net of foreign related tax credits that are available to be repatriated.

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

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

#### Foreign Exchange Risk

The Company conducts business in many different countries and currencies. The Company's business often results in billings issued in a country and currency which differs from that where the expenses related to the service are incurred. In the ordinary course of business, the Company creates numerous intercompany transactions and may have receivables, payables and currencies that are not denominated in the local functional currency. This brings foreign exchange risk to the Company's earnings. The principal foreign exchange risks to which the Company is exposed are in Chinese Yuan, Euro, Mexican Peso and Canadian Dollar.

Foreign exchange rate sensitivity analysis can be quantified by estimating the impact on the Company's earnings as a result of hypothetical changes in the value of the U.S. dollar, the Company's functional currency, relative to the other currencies in which the Company transacts business. All other things being equal, an average 10% weakening of the U.S. dollar, throughout the six months ended June 30, 2014, would have had the effect of raising operating income approximately \$19 million. An average 10% strengthening of the U.S. dollar, for the same period, would have the effect of reducing operating income approximately \$15 million. This analysis does not take into account changes in shipping patterns based upon this hypothetical currency fluctuation. For example, a weakening in the U.S. dollar would be expected to increase exports from the United States and decrease imports into the United States over some relevant period of time, but the exact effect of this change cannot be quantified without making speculative assumptions.

The Company currently does not use derivative financial instruments to manage foreign currency risk and only enters into foreign currency hedging transactions in limited locations where regulatory or commercial limitations restrict the Company's ability to move money freely. Any such hedging activity during the three and six months ended June 30, 2014 and 2013 was insignificant. During the three and six months ended June 30, 2014, net foreign currency losses were less than \$1 million and approximately \$3 million, respectively. Net foreign currency gains were less than \$1 million in the second quarter of 2013. Net foreign currency losses were less than \$1 million in the first half of 2013. The Company had no foreign currency derivatives outstanding at June 30, 2014 and December 31, 2013. The Company instead follows a policy of accelerating international currency settlements to manage foreign exchange risk relative to intercompany billings. As of June 30, 2014, the Company had approximately \$47 million of net unsettled intercompany transactions. The majority of intercompany billings are resolved within 30 days.

#### Interest Rate Risk

At June 30, 2014, the Company had cash and cash equivalents and short term investments of \$1,057 million, of which \$476 million was invested at various short-term market interest rates. The Company had no long-term debt at June 30, 2014. A hypothetical change in the interest rate of 10 basis points at June 30, 2014 would not have a significant impact on the Company's earnings.

In management's opinion, there has been no material change in the Company's interest rate risk exposure in the second quarter of 2014.

### Item 4. Controls and Procedures

#### Evaluation of Controls and Procedures

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

#### Changes in Internal Controls

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

over financial reporting.

The Company's management has confidence in the Company's internal controls and procedures. Nevertheless, the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, does not expect that the Company's disclosure controls and procedures or the Company's internal controls will prevent all errors or intentional fraud. An internal control system, no matter how well-conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of such internal controls are met. Further, the design of an internal control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all internal control systems, no evaluation of controls can provide absolute assurance that all the Company's control issues and instances of fraud, if any, have been detected.

The Company is developing a new accounting system which it plans to implement on a worldwide basis over the next several years. This system is expected to improve the efficiency of certain financial and transactional processes and reporting. This transition will affect the processes that constitute the Company's internal control over financial reporting and will require testing for operating effectiveness.

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

The Company is involved in claims, lawsuits, government investigations and other legal matters that arise in the ordinary course of business and are subject to inherent uncertainties. Currently, in management's opinion and based upon advice from legal advisors, none of these matters are expected to have a significant effect on the Company's operations or financial position. As of June 30, 2014, the amounts accrued for these claims, lawsuits, government investigations and other legal matters are not significant to the Company's operations or financial position. At this time the Company is unable to estimate any additional loss or range of reasonably possible losses, if any, beyond the amounts recorded, that might result from the resolution of these matters.

**Item 1A. Risk Factors**

There have been no material changes in the Company's risk factors from those disclosed in the Company's annual report on Form 10-K filed on February 27, 2014.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**  
**ISSUER PURCHASES OF EQUITY SECURITIES**

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number of shares that may yet be purchased under the plans or programs
April 1-30, 2014	2,627	\$39.33	2,627	21,294,193
May 1-31, 2014	1,498,387	45.61	1,498,387	20,000,468
June 1-30, 2014	1,372,966	45.85	1,372,966	18,476,691
Total	2,873,980	\$45.72	2,873,980	18,476,691

In November 1993, the Company's Board of Directors authorized a Non-Discretionary Stock Repurchase Plan for the purpose of repurchasing the Company's common stock in the open market with the proceeds received from the exercise of stock options. On February 9, 2009, the Plan was amended to increase the authorization to repurchase up to 40 million shares of the Company's common stock. This authorization has no expiration date. This plan was disclosed in the Company's annual report on Form 10-K filed on March 31, 1995. In the second quarter of 2014, 558,184 shares of common stock were repurchased under the Non-Discretionary Stock Repurchase Plan.

On November 13, 2001, the Company's Board of Directors announced a Discretionary Stock Repurchase Plan, which authorized the repurchase of the Company's common stock in the open market to reduce the issued and outstanding common stock to 200 million shares. On February 24, 2014, the Plan was amended to authorize management to reduce issued and outstanding stock to 190 million shares. The maximum number of shares available for repurchase under this plan will increase as the total number of outstanding shares increases. This authorization has no expiration date. In the second quarter of 2014, 2,315,796 shares of common stock were repurchased under the Discretionary Stock Repurchase Plan. These discretionary repurchases included 315,796 shares that were made to limit the growth in the number of issued and outstanding shares resulting from stock option exercises and 2,000,000 shares to reduce the number of total shares outstanding.

**Item 3. Defaults Upon Senior Securities**

Not applicable.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information**

(a) Not applicable.

(b) Not applicable.



Item 6. Exhibits

Exhibits required by Item 601 of Regulation S-K.

Exhibit Number	Description
10.1	The Company's 2014 Stock Option Plan (incorporated by reference to Appendix A of the Company's Notice of Annual Meeting of Shareholders and Proxy Statement pursuant to Regulation 14A filed on March 21, 2014)
10.2	Form of Stock Option Agreement used in connection with options granted under the Company's 2014 Stock Option Plan (incorporated by reference to Appendix B of the Company's Notice of Annual Meeting of Shareholders and Proxy Statement pursuant to Regulation 14A filed on March 21, 2014)
10.3	First Amendment to the Company's 2002 Employee Stock Purchase Plan (incorporated by reference to Appendix C of the Company's Notice of Annual Meeting of Shareholders and Proxy Statement pursuant to Regulation 14A filed on March 21, 2014)
10.4	The Company's 2014 Directors' Restricted Stock Plan (incorporated by reference to Appendix D of the Company's Notice of Annual Meeting of Shareholders and Proxy Statement pursuant to Regulation 14A filed on March 21, 2014)
10.5	Form of Restricted Stock Agreement used in connection with restricted stock granted under the Company's 2014 Directors' Restricted Stock Plan (incorporated by reference to Appendix E of the Company's Notice of Annual Meeting of Shareholders and Proxy Statement pursuant to Regulation 14A filed on March 21, 2014)
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32	Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
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



SIGNATURES

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

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.

August 7, 2014

/s/ JEFFREY S. MUSSER

Jeffrey S. Musser, President, Chief Executive Officer and Director

August 7, 2014

/s/ BRADLEY S. POWELL

Bradley S. Powell, Senior Vice President and Chief Financial Officer

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES  
Form 10-Q Index and Exhibits  
June 30, 2014

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32	Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
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
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