INVACARE CORP
Form 10-Q
November 09, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2006

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 0-12938

Invacare Corporation
(Exact name of registrant as specified in its charter)

Ohio	95-2680965
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No)

One Invacare Way, P.O. Box 4028, Elyria, Ohio	44036
(Address of principal executive offices)	(Zip Code)

(440)329-6000 (Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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 (the "Exchange Act") during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No__

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act (Check One). Large accelerated filer X Accelerated filer __ Non-accelerated filer __

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

As of October 31, 2006, the Company had 30,778,125 Common Shares and 1,111,565 Class B Common Shares outstanding.

INVACARE CORPORATION

INDEX

2

Part I. FINANCIAL INFORMATION
Item 1. Financial Statements.

INVACARE CORPORATION AND SUBSIDIARIES
Condensed Consolidated Balance Sheets

	September 30, 2006 (unaudited)
ASSETS	(

CURRENT ASSETS	
..........Cash and cash equivalents	$ 9,31
..........Marketable securities	19
..........Trade receivables, net	281,88
..........Installment receivables, net	6,09
..........Inventories, net	200,39
..........Deferred income taxes	27,25
..........Other current assets	66,52
.... TOTAL CURRENT ASSETS	591,65
OTHER ASSETS	67,209
OTHER INTANGIBLES	108,588
PROPERTY AND EQUIPMENT, NET	174,124
GOODWILL	758,702
.... TOTAL ASSETS	$1,700,27
LIABILITIES AND SHAREHOLDERS' EQUITY	
CURRENT LIABILITIES	
..........Accounts payable	$172,98
..........Accrued expenses	141,38
..........Accrued income taxes	4,99
..........Short-term debt and current maturities of long-term obligations	78,68
.... TOTAL CURRENT LIABILITIES	398,05
LONG-TERM DEBT	392,909
OTHER LONG-TERM OBLIGATIONS	89,780
SHAREHOLDERS' EQUITY	
..........Preferred shares	
..........Common shares	7,98
..........Class B common shares	27
..........Additional paid-in-capital	144,63
..........Retained earnings	616,68
..........Accumulated other comprehensive earnings	92,52
..........Treasury shares	(42,57
.... TOTAL SHAREHOLDERS' EQUITY	819,53
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$1,700,276

See notes to condensed consolidated financial statements.

INVACARE CORPORATION AND SUBSIDIARIES

Condensed Consolidated Statement of Earnings - (unaudited)

(In thousands except per share data)	Three Months Ended September 30, 2006	2005
Net sales	$379,462	$395,270
Cost of products sold	267,925	276,583

Gross profit	111,537	118,687
Selling, general and administrative expense	88,844	86,631
Charge related to restructuring activities	2,356	2,760
Interest expense	8,829	7,523
Interest income	(685)	(719)
Earnings before Income Taxes	12,193	22,492
Income taxes	2,500	7,175
NET EARNINGS	$ 9,693	$ 15,317
DIVIDENDS DECLARED PER COMMON SHARE	.0125	.0125
Net Earnings per Share - Basic	$ 0.31	$ 0.48
Weighted Average Shares Outstanding - Basic	31,813	31,632
Net Earnings per Share - Assuming Dilution	$ 0.30	$ 0.47
Weighted Average Shares Outstanding - Assuming Dilution	31,890	32,450

See notes to condensed consolidated financial statements.

INVACARE CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statement of Cash Flows - (unaudited)

OPERATING ACTIVITIES
Net earnings
Adjustments to reconcile net earnings to
net cash provided by operating activities:
Depreciation and amortization
Provision for losses on trade and installment receivables
Provision for other deferred liabilities
Provision for deferred income taxes
Loss on disposals of property and equipment
Changes in operating assets and liabilities:
Trade receivables
Installment sales contracts, net
Inventories
Other current assets
Accounts payable
Accrued expenses
Other deferred liabilities

NET CASH PROVIDED BY OPERATING
ACTIVITIES

INVESTING ACTIVITIES
Purchases of property and equipment
Proceeds from sale of property and equipment
Other long term assets
Business acquisitions, net of cash acquired
Other

NET CASH USED FOR INVESTING ACTIVITIES

FINANCING ACTIVITIES
Proceeds from revolving lines of credit, securitization facility and long-term borrowings
Payments on revolving lines of credit, securitization facility and long-term debt and capital lease obligations
Proceeds from exercise of stock options
Payment of dividends

NET CASH REQUIRED BY FINANCING ACTIVITIES
Effect of exchange rate changes on cash

Decrease in cash and cash equivalents
Cash and cash equivalents at beginning of period

Cash and cash equivalents at end of period $

See notes to condensed consolidated financial statements.

INVACARE CORPORATION AND SUBSIDIARIES
Notes to Condensed Consolidated
Financial Statements
(Unaudited)
September 30, 2006

Nature of Operations - Invacare Corporation and its subsidiaries ("Invacare" or the "Company") is the leading home medical equipment manufacturer in the world based on its distribution channels, the breadth of its product line and net sales. The Company designs, manufactures and distributes an extensive line of medical equipment for the home health care, retail and extended care markets. The Company's products include standard manual wheelchairs, motorized and lightweight prescription wheelchairs, seating and positioning systems, motorized scooters, patient aids, home care beds, low air loss therapy products, respiratory products and distributed products.

Principles of Consolidation - The consolidated financial statements include the accounts of the Company, its majority owned subsidiaries and a variable interest entity for which the Company is the primary beneficiary and include all adjustments, which were of a normal recurring nature, necessary to present fairly the financial position of the Company as of September 30, 2006, the results of its operations for the three months and nine months ended September 30, 2006 and 2005, respectively, and changes in its cash flows for the nine months ended September 30, 2006 and 2005, respectively. Certain foreign subsidiaries, represented by the European segment, are consolidated using an August 31 quarter-end in order to meet filing deadlines. No material subsequent events have occurred related to the European segment, which would require disclosure or adjustment to the Company's financial statements. The results of operations for the three and nine months ended September 30, 2006, are not necessarily indicative of the results to be expected for the full year. All significant intercompany transactions are eliminated.

Reclassifications - Certain reclassifications have been made to the prior years' consolidated financial statements to conform to the presentation used for the period ended September 30, 2006.

Use of Estimates - The consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States, which require management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from these estimates.

Business Segments - The Company reports its results of operations through three primary business segments based on geographical area: North America, Europe and Asia/Pacific. The three reportable segments represent operating groups that sell products in different geographic regions.

The North America segment sells each of the Company's five primary product lines, which include: standard, rehab, distributed, respiratory, and continuing care products. Europe and Asia/Pacific sell the same product lines, with the exception of distributed products. Each business segment sells to the home health care, retail and extended care markets.

6

The Company evaluates performance and allocates resources based on profit or loss from operations before income taxes for each reportable segment. The accounting policies of each segment are the same as those described in the summary of significant accounting policies for the Company's consolidated financial statements. Intersegment sales and transfers are based on the costs to manufacture plus a reasonable profit element. Therefore, intercompany profit or loss on intersegment sales and transfers is not considered in evaluating segment performance.

The information by segment is as follows (in thousands):

	Three Months Ended September 30,	
	2006	2005
Revenues from external customers		
North America	$248,294	$260,448
Europe	113,908	111,909
Asia/Pacific	17,260	22,913
Consolidated	$379,462	$395,270
Intersegment Revenues		
North America	$12,087	$11,786
Europe	3,600	1,810
Asia/Pacific	12,122	10,286
Consolidated	$27,809	$23,882
Charge related to restructuring before income taxes		
North America	$ 1,914	$ 2,211

Europe	848	252
Asia/Pacific	166	297
Consolidated	$ 2,928	$ 2,760
Earnings (loss) before income taxes		
North America	$ 5,798	$17,042
Europe	11,433	10,548
Asia/Pacific	(2,061)	(815)
All Other *	(2,977)	(4,283)
Consolidated	$12,193	$22,492

* Consists of unallocated corporate selling, general and administrative costs and intercompany profits, which do not meet the quantitative criteria for determining reportable segments.

7

Net Earnings Per Common Share - The following table sets forth the computation of basic and diluted net earnings per common share for the periods indicated.

	Three Months Ended September 30, 2006	2005
	(In thousands, except	
Basic		
Average common shares outstanding	31,813	31,632
Net earnings	$9,693	$15,317
Net earnings per common share	$ .31	$ .48
Diluted		
Average common shares outstanding	31,813	31,632
Stock options and awards	77	818
Average common shares assuming dilution	31,890	32,450
Net earnings	$9,693	$15,317
Net earnings per common share	$ .30	$ .47

At September 30, 2006, 3,988,371 and 2,463,255 shares were excluded from the average common shares assuming dilution for the three and nine months ended September 30, 2006, respectively, as they were anti-dilutive. For the three and nine months ended September 30, 2006, the majority of the anti-dilutive shares were granted at an exercise prices of $25.13 and $41.87, respectively, which was higher than the average fair market value prices of $23.18 and $28.04, respectively. At September 30, 2005, 782,466 and 632,218 shares were excluded from the average common shares assuming dilution for the three and nine months ended September 30, 2005, respectively, as they were anti-dilutive. For the three and nine months ended September 30, 2005, the majority of the anti-dilutive shares were granted at exercise prices of $41.87 and $44.30, respectively, which was higher than the average fair market value prices of $40.66 and $43.57, respectively.

Concentration of Credit Risk - The Company manufactures and distributes durable medical equipment and supplies to the home health care, retail and extended care markets. The Company performs credit evaluations of its customers' financial condition. De Lage Landen Inc (DLL), a third party financing company, provides the majority of the lease financing to Invacare's customers. The Company's agreement with DLL provides for direct leasing between DLL and the Invacare customer. The Company retains a limited recourse obligation ($44,483,000 at September 30, 2006) to DLL for events of default under the contracts (total balance outstanding of $111,203,000 at September 30, 2006). Financial Accounting Standards Board (FASB) Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, requires the Company to record a guarantee liability as it relates to the limited recourse obligation. As such, the Company has recorded a liability for this guarantee obligation. The Company monitors the collections status of these contracts and has provided amounts for estimated losses in its allowances for doubtful accounts in accordance with FASB Statement No. 5, Accounting for Contingencies. Credit losses are provided for in the financial statements.

Substantially all of the Company's receivables are due from health care, medical equipment dealers and long term care facilities located throughout the United States, Australia, Canada, New Zealand and Europe. A significant portion of products sold to dealers, both foreign and domestic, is ultimately funded through government reimbursement programs such as Medicare and Medicaid. In addition, the Company also has seen a significant shift in reimbursement to customers from managed care entities. As a consequence, changes in these programs can have an adverse impact on dealer liquidity and profitability. In addition, reimbursement guidelines in the home health care industry have a substantial impact on the nature and type of equipment an end user can obtain as well as the timing of reimbursement and, thus, affect the product mix, pricing and payment patterns of the Company's customers.

The Medicare reimbursement changes for power wheelchairs resulting in a 35%-40% reduction in reimbursement for providers, effective November 15, 2006, are so dramatic that, if they are implemented in their current form, there will be customers who will not be able to change their infrastructure quickly enough to survive. As the industry's largest creditor, the Company would likely encounter increased bankruptcies in its customer base if there are no meaningful adjustments to these Medicare changes. Invacare intends to monitor this situation carefully, and if the new fee schedule is implemented in substantially its current form, the Company will assess the adequacy of its reserves for bad debt based upon its judgment as to how effectively providers will adapt to the changing reimbursement climate. While the Company believes its allowance for doubtful accounts is appropriately stated as of September 30, 2006, based on the current reimbursement levels, there is no way to predict the potential consequences to our provider customers if the new fee schedule is implemented in its present form. In the short-term, this uncertainty has caused providers to reduce their purchases and lower their inventory levels.

Goodwill and Other Intangibles - The change in goodwill reflected on the balance sheet from December 31, 2005 to September 30, 2006 was entirely the result of currency translation.

All of the Company's other intangible assets have definite lives and are amortized over their useful lives, except for $32,617,000 related to trademarks, which have indefinite lives.

As of September 30, 2006 and December 31, 2005, other intangibles consisted of the following (in thousands):

	September 30, 2006		December 3
	Historical Cost	Accumulated Amortization	Historical Cost
Customer lists	$67,914	$12,744	$64,218
Trademarks	32,617	-	30,246
License agreements	8,126	6,249	7,564
Developed technology	6,658	825	6,260
Patents	12,719	3,572	12,414
Other	7,906	3,962	7,876
	$135,940	$27,352	$128,578

Amortization expense related to other intangibles was $6,892,000 in the first nine months of 2006 and is estimated to be $8,912,000 in 2007, $8,487,000 in 2008, $8,272,000 in 2009, $7,859,000 in 2010 and $7,650,000 in 2011.

Investment in Affiliated Company - FASB Interpretation No. 46, Consolidation of Variable Interest Entities (FIN 46), requires consolidation of an entity if the Company is subject to a majority of the risk of loss from the variable interest entity's (VIE) activities or is entitled to receive a majority of the entity's residual returns, or both. A company that consolidates a VIE is known as the primary beneficiary of that entity.

The Company consolidates NeuroControl, a development stage company, which is currently pursuing FDA approval to market a product focused on the treatment of post-stroke shoulder pain in the United States. The Company owns a substantial minority equity interest in NeuroControl and is NeuroControl's largest secured lender. Certain of the Company's officers and directors (or their affiliates) have small minority equity ownership positions in NeuroControl. Based on the provisions of FIN 46 and the Company's analysis, the Company determined that it was the primary beneficiary of this VIE as of January 1, 2005 due to the Company board of directors' approval of additional funding in 2005. Accordingly, the Company has consolidated this investment on a prospective basis since January 1, 2005 and recorded an intangible asset for patented technology of $7,003,000. The other beneficial interest holders have no recourse against the Company.

Accounting for Stock-Based Compensation - Prior to the Company's adoption of Statement of Financial Accounting Standard No. 123 (Revised 2004), Share Based Payment ("SFAS 123R"), the Company accounted for options under its stock-based compensation plans using the intrinsic value method proscribed in Accounting Principles Board Opinion (APBO) No. 25, Accounting for Stock Issued to Employees, and related Interpretations. Only compensation cost related to restricted stock awards granted without cost was reflected in net income, as all other options awarded were granted at exercise prices equal to the market value of the underlying stock on the date of grant.

Effective January 1, 2006, the Company adopted SFAS 123R using the modified prospective application method. Under the modified prospective method, compensation cost was recognized for the nine months ended September 30, 2006 for: 1) all stock-based payments granted subsequent to January 1, 2006 based upon the grant-date fair value calculated in accordance with SFAS 123R, and 2) all stock-based payments granted prior to, but not vested as of, January 1, 2006 based upon grant-date fair value as calculated for previously presented pro forma footnote disclosures in accordance with the original provisions of SFAS No. 123, Accounting for Stock Based Compensation.

The amounts of stock-based compensation expense recognized were as follows (in thousands):

	Three Months Ended September 30, 2006	2005
Stock-based compensation expense recognized as part of selling, general and administrative expense	$ 404	$ 223

The 2006 amounts above reflect compensation expense related to restricted stock awards and nonqualified stock options awarded under the 2003 Performance Plan. The 2005 amounts reflect compensation expense recognized for restricted stock awards only, before SFAS 123R was adopted. Stock-based compensation is not allocated to the business segments, but is reported as part of All Other as shown in the Company's Business Segment Note to the Consolidated Financial Statements.

10

Pursuant to the modified prospective application method, results for periods prior to January 1, 2006 have not been restated to reflect the effects of adopting SFAS 123R. The pro forma information below is presented for comparative purposes, as required by SFAS No. 148, Accounting for Stock-Based Compensation - Transition and Disclosure, an amendment of FASB Statement No. 123, to illustrate the pro forma effect on net earnings and related earnings per share for the periods ended September 30, 2005, as if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock-based compensation for that period (in thousands):

	Three Mon Ended September 2005
Net earnings, as reported	$ 15,317
Add: Stock-based compensation expense included in reported income, net of tax ($78 and $230, respectively)	145
Deduct: Total stock-based compensation expense determined under fair value-based method for all awards, net of tax ($609 and $1,946, respectively)	(1,131
Adjusted net earnings	$ 14,331
Net earnings per share:	
Basic - as reported	$ 0.48
Basic - as adjusted for stock-based compensation expense	$ 0.45
Diluted - as reported	$ 0.47
Diluted - as adjusted for stock-based compensation expense	$ 0.44

Stock Incentive Plans - The 2003 Performance Plan (the "2003 Plan") allows the Compensation, Management Development and Corporate Governance Committee of the Board of Directors (the "Committee") to grant up to 3,800,000 Common Shares in connection with incentive stock options, non-qualified stock options, stock appreciation rights and stock awards (including the use of restricted stock). The Committee has the authority to determine which employees and directors will receive awards, the amount of the awards and the other terms and conditions of the awards. During the first nine months of 2006 and 2005, the Committee granted 496,475 and 586,475 non-qualified stock options for a term of ten years at the fair market value of the Company's Common Shares on the date of grant under the 2003 Plan.

Restricted stock awards of 115,932 and 21,304 shares were granted in the first nine months of 2006 and 2005, respectively, without cost to the recipients. Under the terms of the restricted stock awards, all of the shares granted vest ratably over the four years after the award date. Unearned restricted stock compensation of $2,879,188 for the shares granted in the first nine months of 2006 and $1,016,200 for the shares granted in the first nine months of 2005, determined as the market value of the shares at the date of grant, is being amortized on a straight-line basis over the vesting period. Compensation expense of $716,000 and $658,000 was recognized in the first nine months of 2006 and 2005, respectively, related to restricted stock awards granted since 2001. As of September 30, 2006, restricted stock awards totaling 150,535 were not yet vested.

On December 21, 2005, the Board of Directors of Invacare Corporation, based on the recommendation of the Committee, approved the acceleration of the vesting of all of the Company's unvested stock options, which were then underwater. The Board of Directors decided to approve the acceleration of the vesting of these stock options primarily to partially offset certain reductions in other benefits made by the Company and to provide additional incentive to those employees critical to the Company's cost reduction efforts.

The decision, which was effective as of December 21, 2005, accelerated the vesting for a total of 1,368,307 options on the Company's common shares; including 646,100 shares underlying options held by the Company's named executive officers. The stock options accelerated equated to 29% of the Company's total outstanding stock options. Vesting was not accelerated for the restricted awards granted under the Company's stock-based compensation plans and no other modifications were made to the awards that were accelerated. The exercise prices of the accelerated options, all of which were underwater, were unchanged by the acceleration of the vesting schedules.

All of the Company's outstanding unvested options under plans which were accelerated, had exercise prices ranging from $30.91 to $47.80 which were greater than the Company's stock market price of $30.75 as of the effective date of the acceleration.

Stock option activity during the nine months ended September 30, 2006 was as follows:

		Weighted Average Exercise Price
Options outstanding at January 1, 2006	4,776,162	$31.57
Granted	496,475	24.04
Exercised	(219,448)	24.93
Canceled	(246,025)	36.47
Options outstanding at September 30, 2006	4,807,164	$30.72
Options price range at September 30, 2006	$16.03 to $47.80	
Options exercisable at September 30, 2006	4,283,250	
Options available for grant at September 30, 2006*	1,766,635	

* Options available for grant as of September 30, 2006 reduced by net restricted stock award activity of 245,949.

The following table summarizes information about stock options outstanding at September 30, 2006:

		Options Outstanding		Opt
Exercise Prices	Number Outstanding At 9/30/06	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Numbe Exercis At 9/30
$16.03 - $19.50	394,505	2.9 years	$18.53	394,
$20.06 - $24.75	1,387,971	4.9	$23.27	946,
$25.13 - $29.85	667,083	2.7	$25.35	660,
$30.02 - $34.54	614,130	6.0	$32.67	543,
$36.10 - $39.67	675,712	6.5	$37.25	675,
$40.07 - $47.80	1,063,170	8.4	$43.18	1,063,
Total	4,807,164	5.6	$30.72	4,283,

The stock options awarded provided a four-year vesting period whereby options vest equally in each year. Options granted with graded vesting are accounted for as single options.

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

	2006	2005
Expected dividend yield	1.24%	.67%
Expected stock price volatility	28.7%	26.7%
Risk-free interest rate	4.80%	4.38%
Expected life (years)	5.6	5.6

The assumed expected life used is based on the Company's historical analysis of option history. The expected volatility used is also based on actual historical volatility, and expected dividend yield used is based on historical dividends as the Company has no current intention of changing its dividend policy.

The weighted-average fair value of options granted during the first nine months of 2006 and 2005 was $9.11 and $12.41, respectively. The plans provide that shares granted come from the Company's authorized but unissued Common Shares or treasury shares. In addition, the Company's stock-based compensation plans allow participants to exchange shares for withholding taxes, which results in the Company acquiring treasury shares. The weighted-average remaining contractual life of options outstanding at September 30, 2006 and 2005 was 5.6 years for both periods, respectively. The total instrinsic value of stock awards exercised during the nine months ended September 30, 2006 and 2005 were $1,732,000 and $7,223,000, respectively. As of September 30, 2006, all options outstanding and all options exercisable had no intrinsic value as all options had exercisable prices greater than the Company's closing stock price as of September 30, 2006. The exercise of stock awards in the first nine months of 2006 and 2005 resulted in cash received by the Company totaling $2,220,000 and $2,552,000 for each period, respectively and tax benefits of $926,000 and $4,475,000, respectively.

As of September 30, 2006, there was $8,136,000 of total unrecognized compensation cost from stock-based compensation arrangements granted under the plans, which is related to non-vested shares, and includes $3,856,000 related to restricted stock awards. The Company expects the compensation expense to be recognized over a weighted-average period of approximately 2 years.

Prior to the adoption of SFAS 123R, the Company presented all tax benefit deductions resulting from the exercise of stock options as a component of operating cash flows in the Consolidated Statement of Cash Flows. In accordance with SFAS 123R, tax benefits resulting from tax deductions in excess of the compensation expense recognized for those options is classified as a component of financing cash flows. The impact of this change was not material in the first nine months of 2006.

13

Warranty Costs - Generally, the Company's products are covered by warranties against defects in material and workmanship for periods up to six years from the date of sale to the customer. Certain components carry a lifetime warranty. A provision for estimated warranty cost is recorded at the time of sale based upon actual experience. The Company continuously assesses the adequacy of its product warranty accrual and makes adjustments as needed. Historical analysis is primarily used to determine the Company's warranty reserves. Claims history is reviewed and provisions are adjusted as needed. However, the Company does consider other events, such as a product recall, which could warrant additional warranty reserve provision. No material adjustments to warranty reserves were necessary in the first nine months of 2006.

The following is a reconciliation of the changes in accrued warranty costs for the reporting period (in thousands):

Balance as of January 1, 2006	$ 15,583
Warranties provided during the period	6,316
Settlements made during the period	(7,165)
Changes in liability for pre-existing warranties during the period, including expirations	454
Balance as of September 30, 2006	$ 15,188

Charge Related to Restructuring Activities - In the second half of 2005, the Company initiated multi-year cost reduction plans which include: global headcount reductions, transferring production to the Company's Chinese manufacturing facilities, increased sourcing of products and components in Asia, shifting resources from product development to manufacturing cost reduction activities and product rationalization, and exiting facilities.

The restructuring was necessitated by the continued decline in reimbursement by the U.S. government as well as similar reimbursement pressures abroad and continued pricing pressures faced by the Company as a result of outsourcing by competitors to lower cost locations.

To date, the Company has made substantial progress on its restructuring activities, including exiting four facilities and eliminating approximately 535 positions through September 30, 2006, including 235 positions in the first nine months of 2006. Restructuring charges of $9,997,000 were incurred in the first nine months of 2006, of which $1,644,000 is recorded in cost of products sold, since it relates to inventory markdowns, and the remaining charge amount is included in the Charge Related to Restructuring Activities in the Condensed Consolidated Statement of Earnings. There have been no material changes in accrued balances related to the charge, either as a result of revisions in the Company's restructuring plans or changes in estimates, and the Company expects to utilize the accruals recorded through September 30, 2006 during the next twelve months.

A progression of the accruals by segment recorded as a result of the restructuring is as follows (in thousands):

	Balance at 12/31/05	Accruals	Payments
North America			
Severance	$ 2,242	$ 4,758	$ (5,749)
Contract terminations	165	801	(894)
Product line discontinuance	-	1,220	(658)
Total	$ 2,407	$ 6,779	$ (7,301)
Europe			
Severance	$ 799	$ 925	$ (1,615)
Product line discontinuance	-	455	(455)
Other	-	906	(906)
Total	$ 799	$ 2,286	$ (2,976)
Asia/Pacific			
Severance	$ 63	$ 254	$ (317)
Contract terminations	-	393	(344)
Product line discontinuance	-	279	(279)
Other	-	6	(6)
Total	$ 63	$ 932	$ (946)
Consolidated			
Severance	$ 3,104	$ 5,937	$ (7,681)
Contract terminations	165	1,194	(1,238)
Product line discontinuance	-	1,954	(1,392)
Other	-	912	(912)
Total	$ 3,269	$ 9,997	$ (11,223)

Comprehensive Earnings - Total comprehensive earnings were as follows (in thousands):

	Three Months Ended September 30, 2006	2005
Net earnings	$ 9,693	$ 15,317
Foreign currency translation gain (loss)	3,945	7,457
Unrealized gain (loss) on available for sale securities	(2)	39
Current period unrealized gain (loss) on cash flow hedges	272	2,105

Total comprehensive earnings	$13,908	$24,918

Inventories - Inventories determined under the first in, first out method consist of the following components (in thousands):

	September 30, 2006	December 31, 2005
Raw materials	$ 64,074	$59,888
Work in process	26,338	16,700
Finished goods	109,982	100,337
	$200,394	$176,925

Property and Equipment - Property and equipment consist of the following (in thousands):

	September 30, 2006	December 31, 2005
Machinery and equipment	$268,480	$252,545
Land, buildings and improvements	88,895	84,031
Furniture and fixtures	27,959	28,788
Leasehold improvements	15,394	15,194
	400,728	380,558
Less allowance for depreciation	(226,604)	(204,352)
	$174,124	$176,206

Financing Arrangements - On September 28, 2006, the Company extended the termination date of its Receivables Purchase Agreement until November 30, 2006.

Acquisitions - In the first nine months of 2006, the Company made no acquisitions. On September 9, 2004, the Company acquired 100% of the shares of WP Domus GmbH (Domus), a European-based holding Company that manufactures several complementary product lines to Invacare's product lines, including power add-on products, bath lifts and walking aids, from WP Domus LLC. Domus has three divisions: Alber, Aquatec and Dolomite. The Company recorded accruals of $5,954,000 in accordance with EITF Issue No. 95-3, Recognition of Liabilities in Connection with a Purchase Business Combination, of which $3,833,000 is outstanding as of September 30, 2006.

A progression of the accruals balances for the first nine months of 2006 is as follows (in thousands):

	Balance at 12/31/05	Additional Accruals	Adjustments	Payment
Severance	$ 3,049	$ -	$ 118	$ (2

Exit of product lines	897	-	37	
Total	$ 3,946	$ -	$ 155	$ (2

The adjustments above represent the impact of currency translation. The Company anticipates all of the remaining reserves to be utilized or reversed in 2006.

16

Income Taxes - The Company had an effective tax rate of 25.0% for the nine month period ended September 30, 2006 compared with 31.9% for the same period a year ago. The effective tax rate declined due to a change in estimate in the mix of earnings and permanent deductions. The Company's effective tax rate is lower than the U.S. federal statutory rate primarily due to tax credits and earnings abroad being taxed at rates lower than the U.S. federal statutory rate.

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

The following discussion and analysis should be read in conjunction with our Condensed Consolidated Financial Statements and related notes thereto included elsewhere in this Quarterly Report on Form 10-Q and in our Current Report on Form 8-K as furnished to the Securities and Exchange Commission on October 26, 2006.

OUTLOOK

The domestic market for the Company's products has become seriously disrupted due to recently announced changes to Medicare reimbursement rules and policies for power wheelchairs and oxygen. Changes announced by the Centers for Medicare and Medicaid Services (CMS), effective November 15, 2006, impact Power Mobility Devices (PMD), by stipulating that the maximum fees that Medicare will reimburse suppliers for these products will be approximately 35% to 40% less than what they currently receive. If these fees are implemented, access to the medically appropriate PMD and customized mobility solutions designed for the mobility needs of disabled consumers will be dramatically reduced.

On November 1, 2006, the CMS posted the final rule to implement oxygen and capped rental provisions of the Deficit Reduction Act of 2005. The final rule requires medical equipment providers to transfer title of oxygen equipment to the beneficiary after 36 months for equipment placed in service after January 2, 2006. CMS also established a payment class for new technology such as portable oxygen transfilling equipment and portable oxygen concentrators. The final rule encourages the use of new oxygen technologies like the Invacare(R) HomeFill(TM) Oxygen System as it will receive higher reimbursement than traditional portable modalities.

The reimbursement changes and uncertainties affecting the core North American home medical equipment businesses make forecasting the Company's financial results for the remainder of 2006 difficult. Aside from the revenue slowdown, the Medicare changes are so dramatic that, if they are implemented in their current form, there will be customers who will not be able to change their infrastructure quickly enough to survive. As the industry's largest creditor, the Company would likely encounter increased bankruptcies in its customer base if there are no meaningful adjustments to these Medicare changes. Invacare intends to monitor this situation carefully, and if the new fee schedule is implemented in substantially its current form, the Company will assess the adequacy of its reserves for bad debt based upon its judgment as to how effectively providers will adapt to the changing reimbursement climate. While the Company believes its allowance for doubtful accounts is appropriately stated as of September 30, 2006, based on the current reimbursement levels, there is no way to predict the potential consequences to our provider customers if the new fee schedule is implemented in its present form. In the short-term, this uncertainty has caused providers to reduce their purchases and lower their inventory levels.

As a result of these conditions, the Company has lowered its full year earnings per share guidance to between $1.10 and $1.25, excluding restructuring charges, from its previous guidance of $1.45 to $1.65. This guidance excludes the impact of any one-time credit risks that arise resulting from the significant reduction in PMD reimbursement levels. In addition, the Company undertakes its annual impairment test of goodwill and intangible assets in accordance with SFAS No. 142, Goodwill and Other Intangible Assets, in the fourth quarter of each year. As a result of the reduced earnings guidance and one-time credit risks, there is the potential for an impairment charge related to these assets. The Company will complete this analysis during the fourth quarter. The impact of this potential impairment charge is excluded from the guidance. The net sales change for the year is expected to be between negative 2% and negative 4%. This new guidance excludes any fourth quarter impact from foreign currency and acquisitions.

This earnings per share range includes the impact from the stock option accounting Statement of Financial Accounting Standards No. 123 (Revised 2004), Share Based Payment ("SFAS 123R") issued by the Financial Accounting Standards Board. The impact of SFAS 123R on earnings per share for 2006 is estimated to be $0.03.

The Company anticipates operating cash flows of between $57 million and $67 million and net purchases of property, plant and equipment of approximately $22 million, down from our previous guidance in which operating cash flows were anticipated to be between $70 to $85 million and net purchases of property, plant and equipment was approximated to be $30 million. This outlook is subject to the potential impact from the previously mentioned PMD fee reductions and related one-time credit risks.

In light of the reimbursement changes, the Company has already begun to aggressively plan for further adjustments to our manufacturing strategy and rationalization of our product offerings and will undertake additional restructuring initiatives to adjust our costs and expenses and product assortments within the Medicare environment to mitigate the adverse consequences from these changes. The following previously communicated initiatives continue to be on track:

- >> Shifting substantial resources from product development to manufacturing cost reduction activities, engineered product cost reductions and product rationalization;
- >> Manufacturing cost reduction activities including headcount reductions;
- >> Transferring additional manufacturing to China and increasing the Asian sourcing of products. We expect the total cost of products coming from Asia to exceed $200 million in 2006, an increase of over 40% compared to 2005; and
- >> Continue to cost reduce the design and engineering of our products to address the reimbursement and pricing realities.

As a result of the dramatic reductions of 35%-40% in Medicare power wheelchair reimbursement, the Company will aggressively initiate further cost reductions and also work with providers to assist them in adjusting their business models for success under the changing reimbursement environment. The industry has never been more energized and coordinated to bring these reimbursement challenges to a favorable conclusion for providers and consumers.

In addition to these actions, the Company is progressing on its global manufacturing and distribution strategy to exit a number of manufacturing and distribution locations and reduce costs by $30 million annually by 2008.

As a result of the unstable reimbursement environment created by the U.S. government, external sales forecasting is meaningless. The Company will not attempt to make a public forecast for 2007 until 1) future oxygen and motorized wheelchair reimbursement is further understood and 2) November elections results are known and the new Congressional legislative agenda is communicated.

RESULTS OF OPERATIONS

NET SALES

Net sales for the three months ended September 30, 2006 were $379,462,000, compared to $395,270,000 for the same period a year ago, representing a 4% decrease. Foreign currency translation increased net sales by one percentage point. For the nine months ended September 30, 2006, net sales decreased 4% to $1,112,930,000, compared to $1,162,481,000 for the same period a year ago. Acquisitions contributed one percentage point to net sales, while foreign currency translation resulted in a decrease of one percentage point.

Excluding the impact of foreign currency and acquisitions, the net sales decline in the third quarter and first nine months was negatively impacted by Medicare reimbursement policies, which have been most disruptive to the power wheelchair and oxygen markets, including the most recent changes impacting PMDs announced by the CMS.

North American Operations

North American net sales decreased 5% for the quarter to $248,294,000 as compared to $260,448,000 for the same period a year ago with foreign currency accounting for an increase of less than one percentage point while acquisitions did not impact results for the quarter. For the first nine months of 2006, net sales decreased 3% to $748,375,000 as compared to $774,716,000 for the same period a year ago, with foreign currency and acquisitions each contributing less than one percentage point to net sales. These sales consist of Rehab (power wheelchairs, custom manual wheelchairs, personal mobility and seating and positioning), Standard (manual wheelchairs, personal care, home care beds, low air loss therapy and patient transport), Continuing Care (beds and furniture), Respiratory (oxygen concentrators, aerosol therapy, sleep, homefill and associated respiratory) and Distributed (ostomy, incontinence, diabetic, wound care and other medical supplies) products.

The decrease for the quarter was principally due to net sales decreases in Respiratory products (15%), Rehab products (9%) and Standard products (4%), which were partially offset by net sales increases in Continuing Care products (7%) and Distributed products (3%).

The Respiratory products net sales decline for the quarter was largely due to slower demand in the HomeFillTM oxygen system product line. Sales to small providers and independents declined 34% in the quarter. While the Company's proprietary technology continues to build share in the ambulatory oxygen market, providers have slowed purchases of HomeFillTM until they have a clearer view of future oxygen reimbursement levels. The Deficit Reduction Act passed earlier this year included the enactment of a 36-month capped rental period as compared to previously uncapped oxygen payments. In September, the Office of Inspector General issued a study suggesting $3.2 billion in savings over five years from a further reduction to a 13-month capped rental period. The uncertainty created by these announcements continues to negatively impact the oxygen market, particularly those providers considering changing to the HomeFill oxygen system.

The decline in net sales of Standard products for the quarter was due to particular weakness in manual wheelchairs and patient aids (canes, walkers, bath aids) due to low-cost Asian imports negatively impacting volumes. Unit volumes compared to prior year are stable to improved in many categories, excluding patient aids, with sales declines as a result of lower average sales prices. Standard Products revenues improved sequentially over the first and second quarters, by 5% and 2% respectively, as a result of pricing and product line adjustments, which have been facilitated by the acceleration of our Asian sourcing program.

Rehab product net sales decline was due primarily to continued Medicare and Medicaid related reimbursement pressures. Sales of consumer power wheelchairs were down 17% and custom power sales were down 12% and continue to be acutely impacted by these reimbursement issues.

Distributed product sales increase was primarily as a result of growth in sales to the retail sector and continuing increases in revenues from Invacare branded product for the quarter. Invacare Continuing Care Group sales increased in the quarter due to refinements to the channel strategy and sales investments resulting in increased unit volumes in its core bed products along with increases in other offerings such as bathing products and an injury reduction program for long-term caregivers.

European Operations

European net sales increased 2% for the quarter to $113,908,000 as compared to $111,909,000 for the same period a year ago, with foreign currency accounting for four percentage points of the net sales decrease, while acquisitions did not impact results for the quarter. European net sales for the first nine months decreased 3% to $314,141,000 as compared to $324,331,000 for the same period a year ago, with foreign currency accounting for three percentage points of the net sales decrease, while acquisitions contributed one percentage point for the nine-month period. Reimbursement challenges continue to impact our German business in the Invacare wheelchair product lines though these pressures have significantly moderated.

Asia/Pacific Operations

The Company's Asia/Pacific operations consist of Invacare Australia, which imports and distributes the Invacare range of products and manufactures and distributes the Rollerchair range of custom power wheelchairs and Pro Med lifts, DecPac ramps and Australian Healthcare Equipment beds, furniture and pressure care products; Dynamic Controls, a New Zealand manufacturer of electronic operating components used in power wheelchairs and scooters; Invacare New Zealand, a distributor of a wide range of home medical equipment; and Invacare Asia Sales, which imports and distributes home medical equipment to the Asia markets.

Asia/Pacific net sales decreased 25% in the quarter to $17,260,000 from $22,913,000 in the third quarter of 2005 and decreased 21% year to date to $50,414,000 from $63,434,000 for the same period a year ago. For the quarter, foreign currency accounted for three percentage points of the net sales decline, while acquisitions did not impact results for the quarter. For the first nine months of the year, foreign currency translation contributed five percentage points to the decrease while acquisitions contributed less than one percentage point. Performance in this region continues to be negatively impacted by U.S.

reimbursement uncertainty in the consumer power wheelchair market, resulting in decreased sales of microprocessor controllers by Invacare's Dynamic Controls subsidiary.

GROSS PROFIT

Gross profit as a percentage of net sales for the three and nine-month periods ended September 30, 2006 were 29.4% and 28.7%, respectively, compared to 30.0% and 29.4%, respectively, in the same periods last year. However, gross margin improved by .9 percentage points in the third quarter compared to the second quarter of 2006 as a result of cost reduction initiatives. Margins continue to be negatively impacted by lower volumes, high freight costs and a change in sales mix toward lower margin products.

For the first nine months, North American margins as a percentage of net sales declined to 27.0% compared with 29.0% in the same period last year principally due to reduced volumes of higher margin product, largely as a result of government reimbursement uncertainties primarily in Rehab and Respiratory products and to a lesser extent by pricing reductions in Standard products. In Europe, gross margin as a percentage of net sales improved year to date by 2.0 percentage points due to continued cost reduction activities. Gross margin, as a percentage of net sales in Asia/Pacific, decreased year to date by .9 percentage points, largely due to a change in sales mix toward lower margin products.

SELLING, GENERAL AND ADMINISTRATIVE

Selling, general and administrative ("SG&A") expense as a percentage of net sales for the three and nine months ended September 30, 2006 was 23.4% and 23.5%, respectively, compared to 21.9% and 22.4%, respectively, for the same periods a year ago. The dollar increases were $2,213,000 and $1,712,000, or 2.6% and 0.7%, respectively, for the quarter and first nine months of the year. Acquisitions did not have an impact on these expenses for the quarter but increased the first nine months expenses by $2,408,000, while foreign currency translation increased these expenses by $931,000 in the quarter and decreased these expenses by $3,690,000 in the first nine months compared to the same periods a year ago. Excluding the impact of foreign currency translation and acquisitions, selling, general and administrative expense increased 1.5% for the quarter and 1.2% compared to the same period a year ago.

North American SG&A cost increased $2,471,000, or 4.5%, for the quarter and $6,922,000, or 4.3%, in the first nine months compared to the same periods a year ago. Acquisitions did not impact the spending and accounted for 1.0% of the increase in the first nine months, respectively, while foreign currency translation accounted for approximately 0.6% of the increase in each period, respectively. The increase in spending is primarily attributable to increased depreciation as a result of ERP implementation and higher distribution costs.

European SG&A expense increased $171,000, or 0.6%, for the quarter and decreased $3,727,000 or 4.5% for the first nine months compared to the same periods a year ago. For the quarter, acquisitions did not have an impact on the results, and foreign currency translation increased SG&A by $853,000 or 3.2%. For the first nine months of 2006, acquisitions increased SG&A expense by $594,000 or 0.7%, and foreign currency translation decreased SG&A by $3,712,000 or 4.4%.

Asia/Pacific SG&A expense decreased $429,000, or 8.7%, for the quarter and $1,483,000, or 10.5%, in the first nine months of the year compared to the same periods a year ago. For the quarter, foreign currency translation decreased SG&A expense by $241,000, or 4.9%, while acquisitions had no impact. For the first nine months of 2006, acquisitions increased SG&A expense by $158,000, or 1.1%, and foreign currency translation decreased SG&A by $927,000, or 6.6%.

CHARGE RELATED TO RESTRUCTURING ACTIVITIES

On July 28, 2005, the Company announced cost reductions and profit improvement actions, which included: reducing global headcount, outsourcing improvements utilizing the Company's Chinese manufacturing capability and third parties, shifting substantial resources from product development to manufacturing cost reduction activities and product rationalization, reducing freight exposure through freight auctions and changing the freight policy, reducing general expenses, and exiting four facilities.

The restructuring was necessitated by the continued decline in reimbursement by the U.S. government as well as similar reimbursement pressures abroad and continued pricing pressures faced by the Company as a result of outsourcing by competitors to lower cost locations.

To date, the Company has made substantial progress on its restructuring activities, including exiting four facilities and eliminating approximately 535 positions through September 30, 2006, including 235 positions in the first nine months of 2006. Restructuring charges of $2,928,000 and $9,997,000 were incurred in the three and nine month periods ending September 30, 2006, of which $572,000 and $1,644,000, respectively, is recorded in cost of products sold as it relates to inventory markdowns and the remaining charge amount is included on the Charge Related to Restructuring Activities in the Condensed Consolidated Statement of Earnings as part of operations. Restructuring charges of $2,760,000 were incurred in the quarter ending September 30, 2005, principally for severance, of which $2,211,000 was incurred in North America, $297,000 in Asia/Pacific and $252,000 in Europe.

The restructuring charge for the quarter included charges of $1,914,000 in North America, which were incurred principally for severance; $848,000 in Europe primarily related to product line discontinuations and severance and other; and $166,000 in Asia/Pacific mostly related to exited contracts. Restructuring charges for the first nine months included charges of $6,779,000 in North America, which were incurred principally for severance; $2,286,000 in Europe primarily related to severance; and $932,000 in Asia/Pacific related to contract terminations.

With additional actions to be undertaken during the remainder of 2006, the Company anticipates recognizing restructuring charges of approximately $12,500,000 for the year pre-tax, which includes the incurrence of additional charges, primarily in Europe. The Company is assessing further cost reductions as a result of the dramatic reduction in Medicare reimbursement for power wheelchairs in the U.S. In addition, the Company continues to further refine its global manufacturing and distribution strategy, which is expected to result in additional annualized pre-tax savings of up to $30 million annually by 2008 once all plans have been executed.

INTEREST

Interest expense increased $1,306,000 and $4,595,000 for the third quarter and first nine months of 2006, respectively, compared to the same periods last year, primarily due to higher average borrowing rates. Interest income for the third quarter and first nine months of 2006 decreased $34,000 and $523,000, respectively, compared to the same periods last year, primarily due to extended financing terms provided to our customers.

INCOME TAXES

The Company had an effective tax rate of 20.5% for the three-month period and 25.0% for the nine-month period ended September 30, 2006, compared with 31.9% for each of the same periods a year ago. The effective tax rate declined due to a change in estimate in the mix of earnings and permanent deductions. The Company's effective tax rate is lower than the U.S. federal statutory rate primarily due to tax credits and earnings abroad being taxed at rates lower than the U.S. federal statutory rate.

LIQUIDITY AND CAPITAL RESOURCES

The Company's reported level of debt decreased by $66,387,000 from December 31, 2005 to $471,594,000 at September 30, 2006, as cash generated from operations and cash made available due to better cash management was used to pay down debt.

As of September 30, 2006, the Company had approximately $448,600,000 available under its lines of credit, excluding debt covenant restrictions. The Company's borrowing arrangements contain covenants with respect to maximum amount of debt, minimum loan commitments, interest coverage, net worth, dividend payments, working capital, and funded debt to capitalization, as defined in the Company's bank agreements and agreements with its note holders. As of September 30, 2006, the Company was in compliance with all covenant requirements. Under the most restrictive covenant of the Company's borrowing arrangements, the Company has the capacity to borrow up to an additional $4,659,000 as of September 30, 2006.

On September 28, 2006, the Company extended the termination date of its Receivables Purchase Agreement until November 30, 2006.

On November 6, 2006, the Company determined that it was in violation of a financial covenant contained in three Note Purchase Agreements between the Company and various institutional lenders (the "Note Purchase Agreements"). The Note Purchase Agreements relate to an aggregate principal amount of $330 million in long-term debt of the Company. The financial covenant limits the ratio of consolidated debt to consolidated operating cash flow. The Company believes the limits were exceeded as a result of borrowings by the Company in early October, 2006 under its $500 million credit facility dated January 14, 2005 with various banks (the "Credit Facility"). The violation of the covenant under the Note Purchase Agreements also may constitute a default under both the Credit Facility and the Company's separate $100 million trade receivables securitization facility (collectively, all of these loan facilities are referred to as the "Loan Facilities"). The Company has commenced discussions with its lenders and is confident that it can obtain the necessary waivers of the covenants that have been violated. However, there can be no assurance that these waivers can be secured, in which event the lenders have the right to prohibit additional borrowings under the Credit Facility, accelerate the Company's indebtedness under each of the Loan Facilities and take other actions as provided in the Loan Facilities. Any such action by the lenders would have a material adverse effect on the Company's liquidity and/or its financial position

CAPITAL EXPENDITURES

The Company had no individually material capital expenditure commitments outstanding as of September 30, 2006. The Company estimates that capital investments for 2006 will approximate $22,000,000 as compared to $31,517,000 in

2005. The Company believes that its balances of cash and cash equivalents, together with funds generated from operations and existing borrowing facilities will be sufficient to meet its operating cash requirements and to fund required capital expenditures for the foreseeable future.

CASH FLOWS

Cash flows provided by operating activities were $37,281,000 for the first nine months of 2006 compared to $63,123,000 in the first nine months of 2005. The decrease in operating cash flows for the first nine months of 2006 compared to the same period a year ago was primarily the result of lower earnings principally offset by change in inventories, which were less of a drain on cash.

Cash used for investing activities was $16,965,000 for the first nine months of 2006 compared to $81,078,000 in the first nine months of 2005. The decrease in cash used for investing is the result of no acquisitions being completed in the first nine months of 2006 compared to the first nine months of 2005 and reduced purchases of property and equipment in the first nine months of 2006 compared to the first nine months of 2005.

Cash required by financing activities was $35,843,000 for the first nine months of 2006 compared to $11,918,000 in the first nine months of 2005. Financing activities for the first nine months of 2006 were impacted by a decrease in the Company's net long-term borrowings as operating cash flows were used to decrease borrowings compared to the same period a year ago.

The effect of foreign currency translation and acquisitions may result in amounts being shown for cash flows in the Condensed Consolidated Statement of Cash Flows that are different from the changes reflected in the respective balance sheet captions.

During the first nine months of 2006, the Company generated free cash flow of $29,499,000 compared to free cash flow of $44,045,000 in the first nine months of 2005. The decrease was primarily attributable to lower earnings partially offset by fewer purchases of property, plant & equipment and lower inventory increases than in the prior year. Free cash flow is a non-GAAP financial measure that is comprised of net cash provided by operating activities, excluding net cash impact related to restructuring activities, less net purchases of property and equipment, net of proceeds from sales of property and equipment. Management believes that this financial measure provides meaningful information for evaluating the overall financial performance of the Company and its ability to repay debt or make future investments (including, for example, acquisitions). The non-GAAP financial measure is reconciled to the GAAP measure as follows (in thousands):

	Nine Months Ended September 30, 2006	2005
Net cash provided by operating activities	$ 37,281	$63,123
Net cash impact related to restructuring activities	7,707	335
Less: Purchases of property and equipment - net	(15,489)	(19,413)
Free Cash Flow	$ 29,499	$44,045

24

DIVIDEND POLICY

On August 23, 2006, the Company's Board of Directors declared a quarterly cash dividend of $0.0125 per Common Share to shareholders of record as of October 2, 2006, which was paid on October 13, 2006. At the current rate, the cash dividend will amount to $0.05 per Common Share on an annual basis.

CRITICAL ACCOUNTING POLICIES

The Consolidated Financial Statements included in the report include accounts of the Company, all majority-owned subsidiaries and a variable interest entity for which the Company is the primary beneficiary. The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions in certain circumstances that affect amounts reported in the accompanying Consolidated Financial Statements and related footnotes. In preparing these financial statements, management has made its best estimates and judgments of certain amounts included in the financial statements, giving due consideration to materiality. However, application of these accounting policies involves the exercise of judgment and use of assumptions as to future uncertainties and, as a result, actual results could differ from these estimates.

Revenue Recognition
Invacare's revenues are recognized when products are shipped to unaffiliated customers. The SEC's Staff Accounting Bulletin (SAB) No. 101, Revenue Recognition, as updated by SAB No. 104, provides guidance on the application of generally accepted accounting principles (GAAP) to selected revenue recognition issues. The Company has concluded that its revenue recognition policy is appropriate and in accordance with GAAP and SAB No. 101.

Sales are only made to customers with whom the Company believes collection is reasonably assured based upon a credit analysis, which may include obtaining a credit application, a signed security agreement, personal guarantee and/or a cross corporate guarantee depending on the credit history of the customer. Credit lines are established for new customers after an evaluation of their credit report and/or other relevant financial information. Existing credit lines are regularly reviewed and adjusted with consideration given to any outstanding past due amounts.

The Company offers discounts and rebates, which are accounted for as reductions to revenue in the period in which the sale is recognized. Discounts offered include: cash discounts for prompt payment, base and trade discounts based on contract level for specific classes of customers. Volume discounts and rebates are given based on large purchases and the achievement of certain sales volumes. Product returns are accounted for as a reduction to reported sales with estimates recorded for anticipated returns at the time of sale. The Company does not sell any goods on consignment.

Distributed products sold by the Company are accounted for in accordance with EITF 99-19 Reporting Revenue Gross as a Principal versus Net as an Agent. The Company records distributed product sales gross as a principal since the Company takes title to the products and has the risks of loss for collections, delivery and returns.

Product sales that give rise to installment receivables are recorded at the time of sale when the risks and rewards of ownership are transferred. DLL, a third party financing company, provides the majority of the lease financing to Invacare customers. As such, interest income is recognized based on the terms of the installment agreements. Installment accounts are monitored and if a customer defaults on payments, interest income is no longer recognized. All installment

25

accounts are accounted for using the same methodology, regardless of duration of the installment agreements.

Allowance for Uncollectible Accounts Receivable
Accounts receivable are reduced by an allowance for amounts that may become uncollectible in the future. Substantially all of the Company's receivables are

due from health care, medical equipment dealers and long term care facilities located throughout the United States, Australia, Canada, New Zealand and Europe. A significant portion of products sold to dealers, both foreign and domestic, is ultimately funded through government reimbursement programs such as Medicare and Medicaid. In addition, the Company has seen a significant shift in reimbursement to customers from managed care entities. As a consequence, changes in these programs can have an adverse impact on dealer liquidity and profitability. The estimated allowance for uncollectible amounts is based primarily on management's evaluation of the financial condition of the customer. In addition, as a result of the third party financing arrangement with DLL, management monitors the collection status of these contracts in accordance with the Company's limited recourse obligations and provides amounts necessary for estimated losses in the allowance for doubtful accounts.

Inventories and Related Allowance for Obsolete and Excess Inventory

Inventories are stated at the lower of cost or market with cost determined for manufacturing inventories by the first-in, first-out (FIFO) method.

Inventories have been reduced by an allowance for excess and obsolete inventories. The estimated allowance is based on management's review of inventories on hand compared to estimated future usage and sales. A provision for excess and obsolete inventory is recorded as needed based upon the discontinuation of products, redesigning of existing products, new product introductions, market changes and safety issues. Both raw materials and finished goods are reserved for on the balance sheet.

In general, we review inventory turns as an indicator of obsolescence or slow moving product as well as the impact of new product introductions. Depending on the situation, the individual item may be partially or fully reserved for. No inventory that was reserved for has been sold at prices above their new cost basis. The Company continues to increase its overseas sourcing efforts, increase its emphasis on the development and introduction of new products, and decrease the cycle time to bring new product offerings to market. These initiatives are sources of inventory obsolescence for both raw material and finished goods.

Goodwill, Intangible and Other Long-Lived Assets

Property, equipment, intangibles and certain other long-lived assets are amortized over their useful lives. Useful lives are based on management's estimates of the period that the assets will generate revenue. As a result of the adoption of SFAS No. 142, Goodwill and Other Intangible Assets in 2002, goodwill and intangible assets deemed to have indefinite lives are subject to annual impairment tests. Furthermore, goodwill and other long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Company completes its annual impairment tests in the fourth quarter of each year. The results of these analyses indicated no impairment of goodwill through 2005. Interest rates have a significant impact upon the discounted cash flow methodology utilized in our annual impairment testing. Increasing interest rates decrease the fair value estimates used in our testing.

26

Product Liability

The Company's captive insurance company, Invatection Insurance Co., currently has a policy year that runs from September 1 to August 31 and insures annual policy losses of $10,000,000 per occurrence and $13,000,000 in the aggregate of the Company's North American product liability exposure. The Company also has additional layers of external insurance coverage insuring up to $75,000,000 in annual aggregate losses arising from individual claims anywhere in the world that exceed the captive insurance company policy limits or the limits of the Company's per country foreign liability limits as applicable. There can be no assurance that Invacare's current insurance levels will continue to be adequate or available at affordable rates.

Product liability reserves are recorded for individual claims based upon historical experience, industry expertise and indications from a third-party actuary. Additional reserves, in excess of the specific individual case reserves, are provided for incurred but not reported claims based upon third-party actuarial valuations at the time such valuations are conducted. Historical claims experience and other assumptions are taken into consideration by the third-party actuary to estimate the ultimate reserves. For example, the

actuarial analysis assumes that historical loss experience is an indicator of future experience, the distribution of exposures by geographic area and nature of operations for ongoing operations is expected to be very similar to historical operations with no dramatic changes and that the government indices used to trend losses and exposures are appropriate. Estimates made are adjusted on a regular basis and can be impacted by actual loss awards or settlements on claims. While actuarial analysis is used to help determine adequate reserves, the Company is responsible for the determination and recording of adequate reserves in accordance with accepted loss reserving standards and practices.

Warranty
Generally, the Company's products are covered from the date of sale to the customer by warranties against defects in material and workmanship for various periods depending on the product. Certain components carry a lifetime warranty. A provision for estimated warranty cost is recorded at the time of sale based upon actual experience. The Company continuously assesses the adequacy of its product warranty accrual and makes adjustments as needed. Historical analysis is primarily used to determine the Company's warranty reserves. Claims history is reviewed and provisions are adjusted as needed. However, the Company does consider other events, such as a product recall, which could warrant additional warranty reserve provision. No material adjustments to warranty reserves were necessary in the current year. See Warranty Costs in the Notes to the Consolidated Financial Statements included in this report for a reconciliation of the changes in the warranty accrual.

Accounting for Stock-Based Compensation
Prior to January 1, 2006, the Company accounted for options under its stock-based compensation plans using the intrinsic value method proscribed in Accounting Principles Board Opinion (APBO) No. 25, Accounting for Stock Issued to Employees, and related Interpretations. Effective January 1, 2006, the Company adopted SFAS 123R using the modified prospective application method. Under the modified prospective method, compensation cost was recognized for the nine months ended September 30, 2006 for: 1) all stock-based payments granted subsequent to January 1, 2006 based upon the grant-date fair value calculated in accordance with SFAS 123R, and 2) all stock-based payments granted prior to, but not vested as of, January 1, 2006 based upon grant-date fair value previously calculated for previously presented pro forma footnote disclosures in accordance with the original provisions of SFAS No. 123, Accounting for Stock Based Compensation. Results for periods prior to January 1, 2006 have not been restated.

On December 21, 2005, the Board of Directors of Invacare Corporation, based on the recommendation of the Compensation, Management Development and Corporate Governance Committee (the "Committee"), approved the acceleration of the vesting for substantially all of the Company's unvested stock options, which were then underwater. The Board of Directors decided to approve the acceleration of the vesting of these stock options primarily to partially offset certain reductions in other benefits made by the Company and to provide additional incentive to those employees critical to the Company's cost reduction efforts.

The decision, which was effective as of December 21, 2005, accelerated the vesting for a total of 1,368,307 options on the Company's common shares, including 646,100 shares underlying options held by the Company's named executive officers. The stock options accelerated equated to 29% of the Company's total outstanding stock options. Vesting was not accelerated for the restricted stock awards granted under the Company's stock-based compensation plans and no other modifications were made to the awards that were accelerated. The exercise prices of the accelerated options, all of which were underwater, were unchanged by the acceleration of the vesting schedules.

All of the Company's outstanding unvested options under its stock-based compensation plans which were accelerated, had exercise prices ranging from $30.91 to $47.80 which were greater than the Company's stock market price of $30.75 as of the effective date of the acceleration.

Upon adoption of SFAS 123R, the Company did not make any other modifications to the terms of any previously granted options. However, the terms of new awards granted have been modified so that the vesting periods are deemed to be substantive for those who may be retiree eligible. No changes were made regarding the valuation methodologies or assumptions used to determine the fair value of options granted and the Company continues to use a Black-Scholes valuation model. As of September 30, 2006, there was $8,136,000 of total unrecognized compensation cost from stock-based compensation arrangements granted under the plans, which is related to non-vested shares, and includes $3,856,000 related to restricted stock awards. The Company expects the compensation expense to be recognized over a weighted-average period of approximately 2 years. The impact on earnings per share for 2006 is estimated to be $0.03.

The majority of the options awarded have been granted at exercise prices equal to the market value of the underlying stock on the date of grant; thus, no compensation was reflected in the Consolidated Statement of Earnings for these options prior to January 1, 2006. However, restricted stock awards granted without cost to the recipients were and continue to be expensed on a straight-line basis over the vesting periods.

Income Taxes

As part of the process of preparing its financial statements, the Company is required to estimate income taxes in various jurisdictions. The process requires estimating the Company's current tax exposure, including assessing the risks associated with tax audits, as well as estimating temporary differences due to the different treatment of items for tax and accounting policies. The temporary differences are reported as deferred tax assets and/or liabilities. The Company also must estimate the likelihood that its deferred tax assets will be recovered from future taxable income and whether or not valuation allowances should be established. In the event that actual results differ from its estimates, the Company's provision for income taxes could be materially impacted.

The Company does not believe that there is a substantial likelihood that materially different amounts would be reported related to its critical accounting policies.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109 ("FIN 48"). FIN 48 prescribes recognition and measurement of a tax position taken or expected to be taken in a tax return as well as guidance regarding derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006, thus January 1, 2007 for Invacare. The Company will adopt the standard as of the effective date and is currently analyzing the requirements and thus is unable to estimate the impact to the Company's reported results at this time.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R) ("FAS 148"). FAS 158, among other things, requires the recognition of the overfunded or underfunded status of a defined benefit postretirement plan as an asset or a liability on the Condensed Consolidated Balance Sheet and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. The Company is required to adopt and will adopt FAS 158 for its December 31, 2006 financial statements and is currently analyzing the requirements and thus is unable to estimate the impact to the Company's reported results at this time.

QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

The Company is exposed to market risk through various financial instruments, including fixed rate and floating rate debt instruments. The Company uses interest rate swap agreements to mitigate its current and future exposure to interest rate fluctuations. Based on the Company's September 30, 2006 debt levels, a 1.0% change in interest rates would impact interest expense by approximately $1,787,000 over the next twelve months. Additionally, the Company operates internationally and as a result is exposed to foreign currency fluctuations. Specifically, the exposure includes intercompany loans and third party sales or payments. In an attempt to reduce this exposure, foreign currency forward contracts are utilized. The Company does not believe that any potential loss related to these financial instruments would have a material adverse effect on the Company's financial condition or results of operations.

FORWARD-LOOKING STATEMENTS

This Form 10-Q contains forward-looking statements within the meaning of the "Safe Harbor" provisions of the Private Securities Litigation Reform Act of 1995. Terms such as "will," "should," "plan," "intend," "expect," "continue," "forecast," "believe," "anticipate" and "seek," as well as similar comments, are forward-looking in nature. Actual results and events may differ significantly from those expressed or anticipated as a result of risks and uncertainties which include, but are not limited to, the following: pricing pressures, the success of the Company's ongoing efforts to reduce costs, increasing raw material costs, the consolidations of health care customers and competitors, government budgetary and reimbursement issues at both the federal and state level (including those that affect the sales of and margins on product, along with the viability of customers), provider credit risks and possible goodwill impairment arising out of announced reimbursement changes, the ongoing implementation of

29

the Company's North American enterprise resource planning system, the ability to develop and sell new products with higher functionality and lower costs, the effect of offering customers competitive financing terms, the ability to successfully identify, acquire and integrate strategic acquisition candidates, the difficulties in managing and operating businesses in many different foreign jurisdictions, the orderly completion of facility consolidations, the vagaries of any litigation or regulatory investigations that the Company may be or become involved in at any time, the difficulties in acquiring and maintaining a proprietary intellectual property ownership position, the overall economic, market and industry growth conditions, foreign currency and interest rate risks, Invacare's ability to improve financing terms and reduce working capital, as well as the risks described from time to time in Invacare's reports as filed with the Securities and Exchange Commission. We undertake no obligation to review or update these forward-looking statements or other information contained herein.

Item 3. Quantitative and Qualitative Disclosure of Market Risk.

The information called for by this item is provided under the same caption under Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations.

Item 4. Controls and Procedures.

As of September 30, 2006, an evaluation was performed, under the supervision and with the participation of the Company's 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 Rules 13a-15(e) and 15d-15(e)). Based on that evaluation, the Company's management, including the Chief Executive Officer and Chief Financial Officer, concluded that the Company's disclosure controls and procedures were effective as of September 30, 2006, in ensuring that information required to be disclosed by the Company in the reports it files and submits under the Exchange Act is (1) recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms and (2) accumulated and communicated to the Company's management, including the Chief Executive Officer and the Chief Financial Officer, as appropriate to allow for timely decisions regarding required disclosure. There were no changes in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Part II. OTHER INFORMATION

Item 1A. Risk Factors.

In addition to the other information set forth in this report, you should carefully consider the risk factors disclosed in Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005.

30

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds (c) The following table presents information with respect to repurchases of common shares made by the Company during the three months ended September 30, 2006. All of the repurchased shares were surrendered to the Company by employees for tax withholding purposes in conjunction with the vesting of restricted shares held by the employees under the Company's 2003 Performance Plan.

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs
7/1/2006-7/31/2006	-	-	-
8/1/2006-8/31/2006 (1)	1,125	$ 22.13	-
9/1/2006-9/30/2006	-	-	-
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Total	1,125	$ 22.13	-
	=====	=====	=====

(1) Represents common shares surrendered to the Company for tax withholding purposes in conjunction with the vesting of restricted shares under the Company's 2003 Performance Plan.

On August 17, 2001, the Board of Directors authorized the company to purchase up to 2,000,000 Common Shares. To date, the company has purchased 637,100 shares with authorization remaining to purchase 1,362,900 more shares. The company purchased no shares pursuant to this Board authorized program during the third quarter of 2006.

Item 5. Other Information.

On November 6, 2006, the Company determined that it was in violation of a financial covenant contained in three Note Purchase Agreements between the Company and various institutional lenders (the "Note Purchase Agreements"). The Note Purchase Agreements relate to an aggregate principal amount of $330 million in long-term debt of the Company. The financial covenant limits the ratio of consolidated debt to consolidated operating cash flow. The Company believes the limits were exceeded as a result of borrowings by the Company in early October, 2006 under its $500 million credit facility dated January 14, 2005 with various banks (the "Credit Facility"). The violation of the covenant under the Note Purchase Agreements also may constitute a default under both the Credit Facility and the Company's separate $100 million trade receivables securitization facility (collectively, all of these loan facilities are referred to as the "Loan Facilities"). The Company has commenced discussions with its lenders and is confident that it can obtain the necessary waivers of the covenants that have been violated. However, there can be no assurance that these waivers can be secured, in which event the lenders have the right to prohibit additional borrowings under the Credit Facility, accelerate the Company's indebtedness under each of the Loan Facilities and take other actions as provided in the Loan Facilities. Any such action by the lenders would have a material adverse effect on the Company's liquidity and/or its financial position.

31

Item 6. Exhibits.

Exhibit No.	
31.1	Chief Executive Officer Rule 13a-14(a)/15d-14(a) Certification (filed herewith).
31.2	Chief Financial Officer Rule 13a-14(a)/15d-14(a) Certification (filed herewith).
32.1	Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).
32.2	Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).

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.

INVACARE CORPORATION

By:/s/ Gregory C. Thompson

Gregory C. Thompson
Chief Financial Officer
(As Principal Financial and Accounting
Officer and on behalf of the registrant)

Date: November 9, 2006