

## **ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

### **Results of Operations**

#### *FISCAL 2006 COMPARED TO FISCAL 2005*

##### Net Sales

Fiscal 2006 consolidated net sales were approximately \$2.5 billion, a decrease of \$113 million compared to the previous year. The decrease is driven primarily by lower sales volumes in both segments.

Engines Segment net sales were \$1.6 billion versus \$1.7 billion in the prior year, a decrease of \$91 million or 5%. The decrease is primarily the result of a 7% decrease in engine unit shipments between years. The shipment decline is attributable to softer retail demand for lawn and garden equipment and efforts by retailers and OEMs to control inventory levels in the wake of reduced demand. This unit shipment decline was partially offset by \$30 million from a price increase implemented in the beginning of the fiscal year, as well as a favorable mix of engine unit shipments.

Power Products net sales were \$1.2 billion in both fiscal 2006 and 2005. Lower volumes in fiscal 2006 of \$105 million for pressure washer and lawn and garden equipment sales were almost fully offset by \$75 million of increased volume and pricing on generators as well as \$23 million from a favorable mix of lawn and garden product. Management believes the decline in volume of lawn and garden and pressure washer sales is attributable to lower consumer discretionary spending, which resulted in lower demand at retailers.

##### Gross Profit

Consolidated gross profit decreased \$13 million in fiscal 2006. The decrease is primarily the result of the volume decreases noted above offset by pricing improvements in both segments.

Engines Segment margins increased from 21% in fiscal 2005 to 23% in fiscal 2006. The increase in margin is attributable to the price increase discussed above as well as \$13 million in gains on the sale of operating assets. In addition, ongoing cost reduction programs contributed \$8 million to the margin. These positive margin enhancers were enough to overcome the impact of a 4% production volume decline, a mix of product that favored lower margin units and other manufacturing cost increases.

The Power Products Segment margin decreased to 10% in fiscal 2006 from 11% in fiscal 2005. The decline is primarily attributable to \$19 million in losses associated with the wind down of operations at the Murray, Inc. operating facility and the write-off of excess inventory related to Murray product. Partially offsetting these losses was \$16 million in pricing improvements, primarily on generators.

##### Engineering, Selling, General and Administrative Costs

Engineering, selling, general and administrative costs increased \$2 million between years. Excluding the impact of the \$39 million write-off of the Murray, Inc. trade receivable that occurred in fiscal 2005 the category increased \$41 million between years.

Increases in this category in fiscal 2006 as compared to fiscal 2005 included: \$9 million from the expensing of stock based compensation in fiscal 2006, \$12 million in increased legal fees associated with litigation, \$9 million associated with increased information technology spending, and \$2 million from increased engineering costs associated with new product development in the Power Products Segment. Planned increases of \$9.0 million in selling and advertising costs also contributed to the year over year increase in this category.

##### Interest Expense

Interest expense increased \$5 million in fiscal 2006 compared to fiscal 2005. The increase is attributable to higher borrowings between years associated with the term notes used for the Murray, Inc. asset acquisition in February 2005.

##### Other Income

Other income decreased \$2 million in fiscal 2006 as compared to fiscal 2005. The decrease is attributed primarily to higher deferred financing expenses. Deferred financing expense increased as a result of the acceleration of debt repayments and the write-off of associated deferred financing costs.

##### Provision for Income Taxes

The effective tax rate was approximately 33% in both fiscal 2006 and fiscal 2005.

## *FISCAL 2005 COMPARED TO FISCAL 2004*

### Net Sales

Fiscal 2005 consolidated net sales were approximately \$2.7 billion, an increase of \$708 million, or 36% compared to the previous year. The increase is attributable almost entirely to growth within the Power Products Segment.

Engines Segment net sales were \$1.7 billion versus \$1.6 billion in the prior year, an improvement of \$122 million or 8%. The improvement was the result of a 10% engine unit shipment increase, which contributed \$148 million; and \$35 million from pricing and a favorable Euro exchange rate. The increase in engine unit shipments was driven by market share gains as well as \$119 million in increased shipments to our Power Products Segment, that were eliminated in consolidation. These favorable items were offset by: a mix of product that favored lower priced units and \$22 million of lower service and component sales.

Power Products net sales were \$1.2 billion versus \$489 million in the prior year, a \$704 million increase. The acquisition of Simplicity and Murray contributed \$389 and \$214 million respectively to the Segment's growth. In addition, increased generator demand sparked by unprecedented hurricane activity early in the year, as well as Florida legislation that provided for a tax holiday on purchases of hurricane related supplies late in the fiscal year, resulted in increased segment sales of \$102 million.

### Gross Profit

Consolidated gross profit increased \$65 million between years. The acquisition of Simplicity added \$69 million. The sales of Murray branded products and components added \$2 million. These increases along with other volume and price improvements in both segments were offset by significant cost increases, which led to margin percentage decreases in both segments.

Engines Segment margins decreased from 24% in fiscal 2004 to 21% in fiscal 2005. Pricing improvements, including the impact of the Euro, added \$35 million to the Engines Segment margin. Manufacturing cost reduction programs contributed an additional \$12 million. These positive margin enhancers were not enough to overcome a \$59 million increase in manufacturing costs, primarily overhead, raw materials and component costs, and a \$19 million decrease from a mix of lower margined product. Consistent with the prior year, the cost increases reflect initiatives by many vendors to pass along higher costs due to price pressures on scrap aluminum and steel.

The Power Products Segment margin decreased to 11% in fiscal 2005 from 12% in fiscal 2004. The acquisition of Simplicity contributed 9% gross margin in fiscal 2005 after the application of purchase accounting on acquired inventory. Murray sales were essentially at a zero margin after the application of purchase accounting, which reduced the overall segment margin by 3%. The margins on generators and pressure washers declined between years as the \$10 million impact of pricing improvements was offset by component and freight costs on expedited shipments to meet generator demand early in the year. In addition, Euro purchases reduced the gross margin of the Power Products Segment by \$4 million. Under the Company's foreign currency management program, this negative impact on margins was offset by the positive impact of the Euro discussed for the Engines Segment.

### Engineering, Selling, General and Administrative Costs

Engineering, selling, general and administrative costs increased \$108 million or 53% compared to fiscal 2004. The write-off of a trade receivable from Murray, Inc. accounts for \$39 million of the increase. The acquisition of Simplicity added another \$56 million to the category. The remaining increase is attributable to planned increases in advertising expenses, increased salaries and fringe benefits, and increased international variable selling costs, including \$1 million from the impact of a stronger Euro.

### Interest Expense

Interest expense decreased approximately \$1 million in fiscal 2005 compared to fiscal 2004. The decrease is attributable to lower borrowings between years.

### Other Income

Other income increased \$12 million between fiscal years 2005 and 2004. The increase is due to the receipt of \$12 million in cash dividends from an equity investment in preferred stock of Metal Technologies, Inc., the entity that acquired two ductile foundries from the Company in August of 1999. Refer to Note 9 of the Notes to Consolidated Financial Statements for the details of the components of other income.

### Provision for Income Taxes

The effective tax rate decreased from 34% in fiscal 2004 to 33% in fiscal 2005. The decrease is primarily attributable to a tax benefit on dividend income in the current year.

### Extraordinary Gain

The extraordinary gain represents the difference between the estimated fair value of the selected assets acquired from Murray and the cash paid, after all tax considerations. See Note 3 of the Notes to Consolidated Financial Statements for additional information on this acquisition.

### **Liquidity and Capital Resources**

#### *FISCAL YEARS 2006, 2005 AND 2004*

Cash flows from operating activities were \$155 million, \$149 million and \$50 million in fiscal 2006, 2005 and 2004 respectively.

The fiscal 2006 cash flows from operating activities were \$6 million higher than the prior year. The primary reason for the increase is lower working capital requirements in the current year. Lower fourth quarter sales in fiscal 2006 resulted in higher inventory levels offset by lower receivables and accrued liabilities including rebates, incentive compensation and income taxes. The reduction in net income between years was more than offset by a series of increased non-cash items in the current year including non-cash pension charges, stock compensation expense, gains on fixed asset sales, the deferred tax credit, and the elimination of the extraordinary gain in the current year.

The fiscal 2005 cash flows from operations were \$98 million higher than the prior year. Fiscal 2005 did not experience the significant increase in inventories experienced in 2004, resulting in a \$141 million improvement in cash flows in fiscal 2005. During fiscal 2004, inventories for engines and power products were increased to what management believes are a more normal level. Accordingly, no such incremental inventory build-up was required in fiscal 2005. Offsetting the favorable impact of inventory levels on cash flows was a \$27 million reduction in accounts payable and accrued liabilities between years. The decrease is primarily attributable to a \$19 million reduction in incentive compensation accruals between years and \$5 million in lower rebate accruals.

The fiscal 2004 cash flows from operating activities were \$123 million lower than the prior year. Fiscal 2004 experienced a significant increase in inventory levels, which reduced cash flows from operating activities by \$129 million in fiscal 2004 and \$117 million between years. Engine inventories increased \$76 million between years. This increase is attributable to strong production levels through the end of the fiscal year driven by a strong selling season at retail. In addition, we believed that the increased inventory was needed to meet our forecast for fiscal 2005. Our Power Products Segment also experienced an increase in inventory levels of \$53 million between years. This increase in inventory reflects strong production levels throughout the year in order to replenish depleted inventories after the demand creating events for generators in fiscal 2004. Pressure washer inventory levels reflected increasing demand for the product due to significant market growth in the category. Inventory on hand will always reflect demand and our ability to respond to market changes at our production facilities in a timely manner.

Also contributing to the lower cash flows from operating activities in fiscal 2004 were increased receivables growth between years of \$23 million, which reflects our sales growth at both Segments and timing of payments, lower payable increases between years of \$40 million and lower deferred tax provisions between years of \$11 million. Offsetting these reductions in cash flows in fiscal 2004 were increased earnings of \$55 million, a reduction in prepaid expenses between years of \$7 million and lower pension income of \$7 million.

Cash used in investing activities was \$55 million, \$437 million and \$47 million in fiscal 2006, 2005 and 2004, respectively. These cash flows include capital expenditures of \$70 million, \$86 million and \$53 million in fiscal 2006, 2005 and 2004, respectively. The capital expenditures relate primarily to reinvestment in equipment, capacity additions and new products.

In fiscal 2006, Briggs & Stratton received \$12 million in cash from the sale of certain operating assets. In addition, Briggs & Stratton received \$6 million as a refund of a portion of the cash paid for certain assets of Murray, Inc. in fiscal 2005.

In fiscal 2005, cash used in investing activities also includes \$232 million in cash paid for the Simplicity acquisition and \$123 million for the acquisition of certain Murray assets.

In fiscal 2004, Briggs & Stratton received \$6 million as a refund of a portion of the cash paid for the BSPPG acquisition in fiscal 2001. The amount was to adjust the original purchase price for the actual value received in acquired receivables and inventory.

Briggs & Stratton used cash of \$169 million through financing activities in fiscal 2006. Briggs & Stratton provided cash from financing activities of \$106 million, and \$13 million in fiscal 2005 and fiscal 2004, respectively.

In fiscal 2006 the company paid off \$104 million of its long term debt, including \$90 million of its term notes due in fiscal 2008. In addition, Briggs & Stratton re-purchased \$35 million of its common shares in fiscal 2006.

Early in fiscal 2005 the Company used its available cash to finance the acquisition of Simplicity. To finance the acquisition of the Murray assets the Company issued \$125 million in term notes in fiscal 2005. The Company incurred \$1 million in fees in fiscal 2005 negotiating the term notes and an amendment to its revolving credit facility. During fiscal 2004, Briggs & Stratton did not use its revolver to finance working capital needs.

During fiscal 2006, the Company received \$12 million from the exercise of stock options compared to \$20 million in fiscal 2005 and \$45 million in fiscal 2004. The stock and option activity is a direct reflection of the market value of the Company's stock and option strike prices that encourage the exercise of the options.

#### Future Liquidity and Capital Resources

Briggs & Stratton has a \$350 million revolving credit facility that expires in May 2009. This credit facility will be used to fund seasonal working capital requirements and other financing needs. This facility and Briggs & Stratton's other indebtedness contain certain restrictive covenants described in Note 8 of the Notes to Consolidated Financial Statements.

On August 10, 2006, Briggs & Stratton announced its intent to initiate repurchases of up to \$120 million of its common stock through open market transactions during fiscal 2007 and fiscal 2008. The timing and amount of actual purchases will depend upon the market price of the stock and certain governing loan covenants. As of August 31, 2006, approximately \$21 million of common stock has been repurchased under this plan.

Briggs & Stratton expects capital expenditures to be \$80 million in fiscal 2007. These anticipated expenditures reflect our plans to continue to reinvest in equipment, new products, and capacity enhancements.

Management believes that available cash, the credit facility, cash generated from future operations, existing lines of credit and access to debt markets will be adequate to fund Briggs & Stratton's capital requirements for the foreseeable future.

#### **Financial Strategy**

Management believes that the value of Briggs & Stratton is enhanced if the capital invested in operations yields a cash return that is greater than the cost of capital. Consequently, management's first priority is to reinvest capital into physical assets and products that maintain or grow the global cost leadership and market positions that Briggs & Stratton has achieved, and drive the economic value of the Company. Management's next financial objective is to identify strategic acquisitions or alliances that enhance revenues and provide a superior economic return. Several successful joint ventures and the acquisition of Generac Portable Products, Inc. and Simplicity are examples of our successful execution of this strategy. Finally, management believes that when capital cannot be invested for returns greater than the cost of capital, we should return capital to the capital providers through dividends and/or stock buy-backs.

#### **Off-Balance Sheet Arrangements**

Briggs & Stratton has no off-balance sheet arrangements or significant guarantees to third parties not fully recorded in our Balance Sheets or fully disclosed in our Notes to Consolidated Financial Statements. Briggs & Stratton's significant contractual obligations include our debt agreements and certain employee benefit plans.

Briggs & Stratton is subject to financial and operating restrictions in addition to certain financial covenants under its domestic debt agreements. As is fully disclosed in Note 8 of the Notes to Consolidated Financial Statements, these restrictions could limit our ability to: pay dividends; incur further indebtedness; create liens; enter into sale and/or leaseback transactions; consolidate, sell or lease all or substantially all of our assets; and dispose of assets or the proceeds of our assets. We believe we will remain in compliance with these covenants in fiscal 2007. Briggs & Stratton has obligations concerning certain employee benefits including its pension plans, post retirement benefit obligations and deferred compensation arrangements. All of these obligations are recorded on our Balance Sheets and disclosed more fully in the Notes to Consolidated Financial Statements.

## Contractual Obligations

A summary of the Company's expected payments for significant contractual obligations as of July 2, 2006 is as follows (in thousands):

	<u>Total</u>	<u>2007</u>	<u>2008-2009</u>	<u>2010-2011</u>	<u>Thereafter</u>
Long-Term Debt . . . . .	\$ 386,175	\$ -	\$ 116,175	\$270,000	\$ -
Interest on Long-Term Debt . . . . .	123,931	32,166	50,829	40,936	-
Capital Leases . . . . .	1,540	686	854	-	-
Operating Leases . . . . .	49,474	13,716	18,677	11,095	5,986
Consulting Agreement . . . . .	582	429	153	-	-
	<u>\$ 561,702</u>	<u>\$ 46,997</u>	<u>\$ 186,688</u>	<u>\$322,031</u>	<u>\$ 5,986</u>

As of July 2, 2006, the Company had no material purchase obligations other than those created in the ordinary course of business related to inventory and property, plant and equipment which generally have terms of less than 90 days.

## Other Matters

### Labor Agreement

Briggs & Stratton has collective bargaining agreements with its unions. These agreements expire at various times ranging from 2006-2008.

### Emissions

The U.S. Environmental Protection Agency (EPA) has developed national emission standards under a two phase process for small air cooled engines. Briggs & Stratton currently has a complete product offering which complies with the EPA's Phase I engine emission standards. The Phase II program imposes more stringent standards over the useful life of the engine and has been phased in for Class II (225 or greater cubic centimeter) displacement engines and will be phased in through 2008 for Class I (under 225 cubic centimeter) displacement engines. The majority of Briggs & Stratton's engines are certified to be compliant with the EPA's Phase II standards and all engines will be Phase II certified in the next year. Accordingly, Briggs & Stratton does not believe compliance with the new standards will have a material adverse effect on its financial position or results of operations.

The EPA is also evaluating the development of Phase III standards to further reduce engine exhaust emissions and to control evaporative emissions from small off-road engines and equipment they are used in. A draft regulation is scheduled for publication by the end of calendar year 2006. We cannot predict the scope of any proposal or of the final regulations that the EPA may ultimately adopt, and accordingly cannot estimate what, if any, impact such regulations could have on future financial performance.

The California Air Resources Board (CARB) adopted a Tier 3 regulation requiring additional reductions to engine exhaust emissions and also requiring new controls on evaporative emissions from small engines. The Tier 3 regulation is phased in between 2006 and 2008 depending upon the size of the engine and type of control. While Briggs & Stratton believes the cost of the regulation on a per engine basis may be significant, Briggs & Stratton does not believe the regulation will have a material effect on its financial condition or results of operations. This assessment is based on a number of factors, including federal regulation, which precludes other states from opting into the California standard, revisions the CARB made to its adopted regulation from the proposal published in September 2003 in response to recommendations from Briggs & Stratton and others in the regulated category, the fact that California represents a relatively small percentage of Briggs & Stratton's engine sales and our ability and intention to pass increased costs associated with the CARB regulation on to California consumers.

The European Commission adopted an engine emission Directive regulating exhaust emissions from engines manufactured by Briggs & Stratton. The Directive parallels the regulation previously promulgated by the U.S. EPA. Stage 1 was effective in February, 2004 and Stage 2 will be phased in from 2005 to 2007, with some limited extensions available for specific size and type engines until 2010. Briggs & Stratton's full European product line has been compliant with Stage 1 since 2004. Briggs & Stratton has certified the majority of its Class 2 engines to be compliant with the Stage 2 standards and intends to have a full European product line compliant with Stage 2 in 2007. Briggs & Stratton does not believe compliance with the Directive will have a material adverse effect on its financial position or results of operations.

## Critical Accounting Policies

Briggs & Stratton's critical accounting policies are more fully described in Note 2 and Note 14 of the Notes to Consolidated Financial Statements. As discussed in Note 2, the preparation of financial statements in conformity with accounting principles generally accepted in the U.S. ("GAAP") requires management to make estimates and assumptions about future events that affect the amounts reported in the financial statements and accompanying notes. Future events and their effects cannot be determined with absolute certainty. Therefore, the determination of estimates requires the exercise of judgment. Actual results inevitably will differ from those estimates, and such differences may be material to the financial statements.

The most significant accounting estimates inherent in the preparation of our financial statements include estimates as to the recovery of accounts receivable and inventory reserves, as well as those used in the determination of liabilities related to customer rebates, pension obligations, postretirement benefits, warranty, product liability, litigation and taxation.

The reserves for customer rebates, warranty, product liability, inventory and doubtful accounts are fact specific and take into account such factors as specific customer situations, historical experience, and current and expected economic conditions. Changes in these reserves may be required if actual experience differs from the original estimates.

The Company's estimate of income taxes payable, deferred income taxes, and the effective tax rate is based on a complex analysis of many factors including interpretations of Federal, state and foreign income tax laws, the difference between tax and financial reporting bases of assets and liabilities, estimates of amounts currently due or owed in various jurisdictions, and current accounting standards. We review and update our estimates on a quarterly basis as facts and circumstances change and actual results are known. In addition, Federal, state and foreign taxing authorities periodically review the Company's estimates and interpretation of income tax laws. Adjustments to the effective income tax rate and recorded tax related assets and liabilities may occur in future periods if actual results differ significantly from original estimates and interpretations.

The pension benefit obligation and related pension expense or income are calculated in accordance with Statement of Financial Accounting Standard (SFAS) No. 87, "Employer's Accounting for Pensions", and are impacted by certain actuarial assumptions, including the discount rate and the expected rate of return on plan assets. These rates are evaluated on an annual basis considering such factors as market interest rates and historical asset performance. Actuarial valuations at July 2, 2006 used a discount rate of 6.35% and an expected rate of return on plan assets of 8.75%. Our discount rate was selected using a methodology that matches plan cash flows with a selection of Moody's Aa or higher rated bonds, resulting in a discount rate that better matches a bond yield curve with comparable cash flows. A 0.25% decrease in the discount rate would increase annual pension expense by approximately \$0.4 million. A 0.25% decrease in the expected return on plan assets would increase our annual pension expense by approximately \$2.0 million. In estimating the expected return on plan assets, the Company considers the historical returns on plan assets, adjusted for forward looking considerations, including inflation assumptions and active management of the plan's invested assets. Changes in the discount rate and return on assets can have a significant effect on the funded status of our pension plans, stockholders' equity and expense. We cannot predict these changes in discount rates or investment returns and, therefore, cannot reasonably estimate whether the impact in subsequent years will be significant.

The Company uses a market-related value of assets that recognizes the difference between the expected return and the actual return on plan assets over a five year period. As of July 2, 2006 the Company had \$133.0 million of unrecognized asset gains associated with its market-related value of assets and subject to amortization in future periods.

The funded status of the Company's pension plan is the difference between the projected benefit obligation and the fair value of its plan assets. The projected benefit obligation is the actuarial present value of all benefits expected to be earned by the employees' service. At July 2, 2006 the projected benefit obligation exceeded the fair value of plan assets by \$4 million. Material differences may arise between the funded status of the plan and the recorded asset or liability as certain items that have an immediate impact on the projected benefit obligation are amortized over a longer period of time for balance sheet purposes using actuarial assumptions. As of July 2, 2006 there were \$136.7 million in actuarial losses not reflected in the recorded asset or liability.

The other postretirement benefits obligation and related expense or income are calculated in accordance with SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions" and are impacted by

certain actuarial assumptions, including the health care trend rate. An increase of one percentage point in health care costs would increase the accumulated postretirement benefit obligation by \$14.5 million and would increase the service and interest cost by \$1.5 million. A corresponding decrease of one percentage point, would decrease the accumulated postretirement benefit by \$13.5 million and decrease the service and interest cost by \$1.3 million.

For pension benefits and postretirement benefits, actuarial gains and losses are accounted for in accordance with GAAP. Accumulation of actuarial gains and losses results from differences in actual experience compared to original assumptions over several years for discount rates, health care cost trends, and other factors. Accumulated actuarial gains and losses are amortized over future periods, and as a result, will impact recognized expense and the recorded obligation in future periods. Refer to Note 14 for additional discussion.

#### New Accounting Pronouncements

In November 2004, the FASB issued SFAS No. 151, "Inventory Costs – an amendment of ARB No. 43, Chapter 4." SFAS No. 151 seeks to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs and wasted material (spoilage) in the determination of inventory carrying costs. The statement requires such costs to be treated as a current period expense. This statement became effective for the company on July 2, 2006. The adoption of SFAS No. 151 does not have a material impact on the Consolidated Financial Statements.

On July 13, 2006, the FASB issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109". Interpretation 48 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with Statement 109 and prescribes a standard methodology for financial statement disclosure of tax positions taken or expected to be taken on a tax return. Additionally, Interpretation 48 provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. Interpretation 48 is effective for fiscal years beginning after December 15, 2006, with early adoption permitted. At this time, the impact, if any, of adoption of Interpretation 48 on our consolidated financial position has not been made.

## ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Briggs & Stratton is exposed to market risk from changes in foreign exchange and interest rates. To reduce the risk from changes in foreign exchange rates, Briggs & Stratton uses financial instruments. Briggs & Stratton does not hold or issue financial instruments for trading purposes.

### Foreign Currency

Briggs & Stratton's earnings are affected by fluctuations in the value of the U.S. dollar against the Japanese Yen and the Euro. The Yen is used to purchase engines from Briggs & Stratton's joint venture. Briggs & Stratton purchases components in Euros from third parties and receives Euros for certain products sold to European customers. Briggs & Stratton's foreign subsidiaries' earnings are also influenced by fluctuations of the local currency against the U.S. dollar as these subsidiaries purchase inventory from the parent in U.S. dollars. Forward foreign exchange contracts are used to partially hedge against the earnings effects of such fluctuations. At July 2, 2006, Briggs & Stratton had the following forward foreign exchange contracts outstanding with the Fair Value (Gains) Losses shown (in thousands):

<u>Hedge Currency</u>	<u>Notional Value</u>	<u>Fair Market Value</u>	<u>Conversion Currency</u>	<u>(Gain) Loss at Fair Value</u>
Japanese Yen	1,650,000	\$ 14,615	U.S.	\$ (229)
Euro	81,000	\$ 104,802	U.S.	\$ 1,031
Australian Dollars	4,175	\$ 3,098	U.S.	\$ (71)

All of the above contracts expire within twelve months.

Fluctuations in currency exchange rates may also impact the shareholders' investment in Briggs & Stratton. Amounts invested in Briggs & Stratton's non-U.S. subsidiaries and joint ventures are translated into U.S. dollars at the exchange rates in effect at fiscal year-end. The resulting cumulative translation adjustments are recorded in Shareholders' Investment as Accumulated Other Comprehensive Income. The cumulative translation adjustments component of Shareholders' Investment increased \$1.8 million during the year. Using the year-end exchange rates, the total amount invested in non-U.S. subsidiaries on July 2, 2006 was \$89.1 million.

### Interest Rates

Briggs & Stratton is exposed to interest rate fluctuations on its borrowings, depending on general economic conditions.

On July 2, 2006, Briggs & Stratton had the following short-term loans outstanding (in thousands):

<u>Currency</u>	<u>Amount</u>	<u>Weighted Average Interest Rate</u>
U.S. Dollars	3,000	6.58%
Euro	338	5.00%

These loans carry variable interest rates. Assuming borrowings are outstanding for an entire year, an increase (decrease) of one percentage point in the weighted average interest rate, would increase (decrease) interest expense by \$34 thousand.

Long-term loans, net of unamortized discount, consisted of the following (in thousands):

<u>Description</u>	<u>Amount</u>	<u>Maturity</u>
7.25% Senior Notes	\$ 80,973	2007
8.875% Senior Notes	\$ 267,351	2011
Variable Rate Term Notes	\$ 35,000	2008

The Senior Notes carry fixed rates of interest and are therefore not subject to market fluctuation. The Variable Rate Term Note is subject to interest rate fluctuations, therefore an increase (decrease) of one percentage point in the weighted average interest rate would increase (decrease) interest expense by \$350 thousand.