

**Income from operations.** Income from operations increased 22.0 percent to \$509.7 million for 2007. This increase was primarily driven by the growth in our gross profits. Income from operations as a percentage of gross profits was 40.9 percent and 38.6 percent for 2007 and 2006.

**Investment and other income.** Investment and other income increased 16.8 percent to \$13.8 million in 2007. Our portfolio yield increased slightly in 2007 from 2006.

**Provision for income taxes.** Our effective income tax rate was 38.1 percent for 2007 and 37.9 percent for 2006. The effective income tax rate for both periods is greater than the statutory federal income tax rate primarily due to state income taxes, net of federal benefit.

**Net income.** Net income increased 21.5 percent to \$324.3 million for 2007. Basic net income per share increased 21.8 percent to \$1.90. Diluted income per share increased 21.6 percent to \$1.86 for 2007.

## **LIQUIDITY AND CAPITAL RESOURCES**

We have historically generated substantial cash from operations, which has enabled us to fund our growth while paying cash dividends and repurchasing stock. Cash and cash equivalents totaled \$494.7 million and \$338.9 million as of December 31, 2008 and 2007. Available-for-sale securities, consisting primarily of highly liquid investments, totaled \$2.6 million and \$115.8 million as of December 31, 2008 and 2007. Working capital at December 31, 2008 and 2007 was \$650.2 million and \$631.5 million.

Our first priority for our cash is growing the business, as we require some working capital and a relatively small amount of capital expenditures to grow. We are continually looking for acquisitions to redeploy our cash, but those acquisitions must fit our culture and enhance our growth opportunities.

If our cash balance continues to increase and there are no significant attractive acquisition opportunities, we expect to return more of the cash to our shareholders through future dividends and share repurchases.

**Cash from operating activities.** We generated \$447.6 million, \$308.4 million, and \$343.4 million of cash flow from operations in 2008, 2007, and 2006. During 2008, our cash flow from operations increased 45.1 percent compared to a 10.8 percent increase in net income. The primary factor that caused this increase in 2008 was the decrease in our accounts receivables balance of 9.1 percent to \$828.9 million in 2008 from \$911.8 million in 2007, as a result of declines in fuel prices and volumes at the end of 2008 compared to 2007.

**Cash used for investing activities.** We generated \$31.5 million cash in 2008, used cash of \$55.7 million in 2007, and used \$81.2 million cash in 2006 for investing activities. Our investing activities consist primarily of cash paid for acquisitions and our capital expenditures. During 2008, we exited nearly all of our available-for-sale securities, and invested in cash and cash equivalents which generated \$114.1 million of cash from investing activities.

We used cash of \$59.7 million, \$22.2 million, and \$39.7 million for acquisitions in 2008, 2007, and 2006. The amount paid in 2008 included \$50.2 million related to the closing of one acquisition and \$9.5 million related to earn-out payments and holdbacks from prior year acquisitions. The amount paid in 2007 included \$9.8 million related to the closing of one acquisition and \$12.4 million related to earn-out payments and holdbacks from prior year acquisitions. The amount paid in 2006 included \$29.5 million related to the closing of two acquisitions and \$10.2 million related to earn-out payments and holdbacks from prior year acquisitions.

We also used \$23.7 million, \$43.7 million, and \$43.3 million of net capital expenditures in 2008, 2007, and 2006. We spent \$5.6 million, \$21.1 million, and \$20.4 million in 2008, 2007, and 2006 on facilities on our new corporate campus in Eden Prairie, MN. This includes the spending to date on our new data center. The remaining capital expenditures of \$18.1 million, \$22.6 million, and \$22.9 million in 2008, 2007, and 2006 relate primarily to annual investments in information technology equipment to support our operating systems.

**Cash used for financing activities.** We used \$326.0 million, \$262.1 million, and \$145.8 million of cash flow for financing activities in 2008, 2007, and 2006. This was primarily quarterly dividends and share repurchases.

We used \$151.2 million, \$125.2 million, and \$90.8 million to pay cash dividends in 2008, 2007, and 2006, with the increase in 2008 due to a 22 percent increase in our quarterly dividend rate from \$0.18 per share in 2007 to \$0.22 per share in 2008.

We also used \$200.8 million, \$167.3 million, and \$85.3 million on share repurchases in 2008, 2007, and 2006. The increase in 2008 was due to a 13 percent increase in the number of shares repurchased and an increase in the average price paid per share. We will continue to use share repurchases as a variable way to return excess capital to shareholders. Our Board of

Directors has authorized a stock repurchase plan in 2007 of up to 10 million shares. We have used approximately 3.8 million shares of that authorization.

We have 3.5 million Euros available under a line of credit at an interest rate of 6.65 percent (Euribor plus 45 basis points) at December 31, 2008. This discretionary line of credit has no expiration date. Our credit agreement contains certain financial covenants, but does not restrict the payment of dividends. We were in compliance with all covenants of this agreement as of December 31, 2008.

Assuming no change in our current business plan, management believes that our available cash, together with expected future cash generated from operations and the amount available under our line of credit, will be sufficient to satisfy our anticipated needs for working capital, capital expenditures, and cash dividends in future periods. We also believe we could obtain funds under additional lines of credit on short notice, if needed.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Our consolidated financial statements include accounts of the company and all majority-owned subsidiaries. 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, those estimates and assumptions can affect amounts reported in the accompanying consolidated financial statements and related footnotes. In preparing our financial statements, we have made our best estimates and judgments of certain amounts included in the financial statements, giving due consideration to materiality. We do not believe there is a great likelihood that materially different amounts would be reported related to the accounting policies described below. 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. Note 1 of the Notes to Consolidated Financial Statements includes a summary of the significant accounting policies and methods used in the preparation of our consolidated financial statements. The following is a brief discussion of our critical accounting policies and estimates.

**Revenue recognition.** Gross revenues consist of the total dollar value of goods and services purchased from us by customers. Gross profits are gross revenues less the direct costs of transportation, products, and handling. We act principally as the service provider for these transactions and recognize revenue as these services are rendered or goods are delivered. At that time, our obligations to the transactions are completed and collection of receivables is reasonably assured. Emerging Issues Task Force (EITF) Issue No. 99-19, Reporting Revenue Gross as a Principal versus Net as an Agent, establishes the criteria for recognizing revenues on a gross or net basis. Most transactions in our Transportation and Sourcing businesses are recorded at the gross amount we charge our customers for the service we provide and goods we sell. In these transactions, we are the primary obligor, we are a principal to the transaction, we have all credit risk, we maintain substantially all risks and rewards, we have discretion to select the supplier, and we have latitude in pricing decisions.

Additionally, in our Sourcing business, we take loss of inventory risk during shipment and have general inventory risk. Certain transactions in customs brokerage, transportation management, and all transactions in Information Services are recorded at the net amount we charge our customers for the service we provide because many of the factors stated above are not present.

**Valuations for accounts receivable.** Our allowance for doubtful accounts is calculated based upon the aging of our receivables, our historical experience of uncollectible accounts, and any specific customer collection issues that we have identified. The allowance of \$29.3 million as of December 31, 2008, increased compared to the allowance of \$28.0 million as of December 31, 2007. We believe that the recorded allowance is sufficient and appropriate based on our customer aging trends, the exposures we have identified, and our historical loss experience.

**Goodwill.** We manage and report our operations as one operating segment. Our branches represent a series of components that are aggregated for the purpose of evaluating goodwill for impairment on an enterprise-wide basis. In the case where we have an acquisition that we feel has not yet become integrated into our branch network component, we will evaluate the impairment of any goodwill related to that specific acquisition and its results. Based on our annual analysis in accordance with SFAS No. 142, we have determined that there is no indication of goodwill impairment as of December 31, 2008.

**Stock-based compensation.** We account for share-based compensation in accordance with SFAS No. 123R, Share Based Payment. Under this standard, the fair value of each share-based payment award is established on the date of grant. For grants of restricted shares and restricted units, the fair value is established based on the market price on the date of the grant, discounted for post-vesting holding restrictions. The discounts have varied from 12 to 22 percent and are calculated using the Black-Scholes option pricing model. Increased stock price volatility is the primary factor that has caused the change in the discount applied. For grants of options, we use the Black-Scholes option pricing model to estimate the fair value of share-based payment awards. The determination of the fair value of share-based awards is affected by our stock price and a number of assumptions, including expected volatility, expected life, risk-free interest rate, and expected dividends.