

Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies

a. Basis of Presentation

Expeditors International of Washington, Inc. ("the Company") is a global logistics company operating through a worldwide network of offices, international service centers and exclusive or non-exclusive agents. The Company's customers include retailing and wholesaling, electronics, and manufacturing companies around the world. The Company grants credit upon approval to customers.

International trade is influenced by many factors, including economic and political conditions in the United States and abroad, currency exchange rates, and United States and foreign laws and policies relating to tariffs, trade restrictions, foreign investments and taxation. Periodically, governments consider a variety of changes to current tariffs and trade restrictions. The Company cannot predict which, if any, of these proposals may be adopted, nor can the Company predict the effects adoption of any such proposal will have on the Company's business. Doing business in foreign locations also subjects the Company to a variety of risks and considerations not normally encountered by domestic enterprises. In addition to being affected by governmental policies concerning international trade, the Company's business may also be affected by political developments and changes in government personnel or policies in the nations in which it does business.

The consolidated financial statements include the accounts of the Company and its subsidiaries. In addition, the accounts of exclusive agents have been consolidated in those circumstances where the Company maintains unilateral control over the agents' assets and operations, notwithstanding a lack of technical majority ownership of the agents' common stock.

All significant intercompany accounts and transactions have been eliminated in consolidation.

All dollar amounts in the notes are presented in thousands except for share data.

b. Short-term Investments

Short-term investments are designated as available-for-sale and cost approximates market at December 31, 1999 and 1998.

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c. Long-Lived Assets, Depreciation and Amortization

Property and equipment are recorded at cost, including interest capitalized for the construction of certain facilities, and are depreciated or amortized on the straight-line method over the shorter of the assets' estimated useful lives or lease terms. Useful lives for major categories of property and equipment are as follows:

Buildings	28 to 40 years
Furniture, fixtures and equipment	3 to 5 years
Vehicles	3 to 5 years

No interest was capitalized in 1999. Interest capitalized in 1998 was \$193.

Expenditures for maintenance, repairs, and renewals of minor items are charged to earnings as incurred. Major renewals and improvements are capitalized. Upon disposition, the cost and related accumulated depreciation are removed from the accounts and the resulting gain or loss is included in income for the period.

The excess of the cost over the fair value of the net assets of acquired businesses (included in other assets, net) is amortized on the straight-line method over periods up to 40 years.

In accordance with Statement of Financial Accounting Standards (SFAS) No. 121, "Accounting for the Impairment of Long-Lived Assets and for Assets to Be Disposed Of", long-lived assets (property and equipment) and certain identifiable intangible assets (excess costs over the fair value of the net assets of acquired businesses) are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of long-term assets is measured by a comparison of the carrying amount of such assets against the undiscounted future cash flows expected to be generated by the assets. If such assets are determined to be impaired, the impairment to be recognized is measured by the amount by which the assets' carrying amounts exceeds the assets' discounted future cash flows.

d. Revenues and Revenue Recognition

Airfreight revenues include the charges to the Company for carrying the shipments when the Company acts as a freight consolidator. Ocean freight revenues include the charges to the Company for carrying the shipments when the Company acts as a Non-Vessel Operating Common Carrier (NVOCC). Revenues realized in other capacities include only the commissions and fees earned.

Revenues related to shipments are recognized at the time the freight is tendered to a direct carrier at origin. All other revenues, including breakbulk services, local transportation, customs formalities, distribution services and logistics management, are recognized upon performance.

The Securities and Exchange Commission recently issued Staff Accounting Bulletin (SAB) No. 101, "Revenue Recognition", to be effective the first quarter of 2000. The Company does not anticipate that compliance with SAB No. 101 will result in any material change to the Company's revenue recognition policies.

e. Income Taxes

Income taxes are accounted for under the asset and liability method of accounting. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributed to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and tax credit carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

f. Net Earnings per Common Share

Diluted earnings per share is computed using the weighted average number of common shares and dilutive potential common shares outstanding. Dilutive potential common shares represent outstanding stock options. Basic earnings per share is calculated using the weighted average of common shares outstanding without taking into consideration dilutive potential common shares outstanding.

g. Foreign Currency

Foreign currency amounts attributable to foreign operations have been translated into U.S. Dollars using year-end exchange rates for assets and liabilities, historical rates for equity, and average annual rates for revenues and expenses. Unrealized gains or losses arising from fluctuations in the year-end exchange rates are generally recorded as components of other comprehensive income as adjustments from foreign currency translation. Currency fluctuations are a normal operating factor in the conduct of the Company's business and exchange transaction gains and losses are generally included in freight consolidation expenses.

SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" establishes accounting standards for derivative and hedging transactions and is effective for fiscal years beginning after June 15, 2000. The Company follows a policy of accelerating international currency settlements to manage its foreign exchange exposure. Accordingly, the Company enters into foreign currency hedging transactions only in limited locations where there are regulatory or commercial limitations on the Company's ability to move money freely around the world. Any such hedging activity during 1999, 1998 and 1997 was insignificant. Net foreign currency gains realized during 1999 were \$196. Net foreign currency losses realized in 1998 were \$534. Net foreign currency gains realized in 1997 were \$1,065.

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h. Cash Equivalents

All highly liquid investments with a maturity of three months or less at date of purchase are considered to be cash equivalents.

i. Comprehensive Income

Comprehensive income consists of net income and other gains and losses affecting shareholders' equity that, under generally accepted accounting principles, are excluded from net income. For the Company, these consist of foreign currency translation gains and losses, net of related income tax effects.

j. Segment Reporting

SFAS No. 131, "Disclosure about Segments of an Enterprise and Related Information" establishes standards for the way that public companies report selected information about segments in their financial statements.

The Company is organized functionally in geographic operating segments. Accordingly, management focuses its attention on revenues, net revenues, operating income, identifiable assets, capital expenditures, depreciation and amortization and equity generated by or allocated to each of these geographical areas when evaluating effectiveness of geographic management.

k. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of the assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

l. Reclassification

Certain 1997 amounts have been reclassified to conform with the 1998 and 1999 presentation.

Note **2. Credit Arrangements**

The Company has a \$50,000 United States bank line of credit extending through June 30, 2000. Borrowings under the line bear interest at LIBOR +0.75% (6.57% at December 31, 1999) and are unsecured. As of December 31, 1999, the Company had \$18,000 of borrowings under this line.

The majority of the Company's foreign subsidiaries maintain bank lines of credit for short-term working capital purposes. These credit lines are supported by standby letters of credit issued by a United States bank, or guarantees issued by the Company to the foreign banks issuing the credit line. Lines of credit bear interest at .5% to 1.5% over the foreign banks' equivalent prime rates. At December 31, 1999 and 1998, the Company was liable for \$1,442 and \$1,245, respectively, of borrowings under these lines, and at December 31, 1999 was contingently liable for approximately \$19,163 under outstanding standby letters of credit and guarantees related to these lines of credit and other obligations.

In addition, at December 31, 1999 the Company had a \$8,096 credit facility with a United Kingdom bank (U.K. facility), secured by a corporate guarantee. The Company was contingently liable under the U.K. facility at December 31, 1999 for \$8,096 used to secure customs bonds issued by foreign governments.

At December 31, 1999, the Company was in compliance with all restrictive covenants of these credit lines and the associated credit facilities, including maintenance of certain minimum asset, working capital and equity balances and ratios.

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Note 3. Income Taxes

Income tax expense for 1999, 1998 and 1997 includes the following components:

	Federal	State	Foreign	Total
1999				
Current	\$ 3,823	1,331	14,149	19,303
Deferred	14,098	2,069	-	16,167
	<u>\$17,921</u>	<u>3,400</u>	<u>14,149</u>	<u>35,470</u>
1998				
Current	\$ 9,526	2,071	13,009	24,606
Deferred	2,726	971	-	3,697
	<u>\$ 12,252</u>	<u>3,042</u>	<u>13,009</u>	<u>28,303</u>
1997				
Current	\$ 9,993	1,669	10,246	21,908
Deferred	1,420	833	-	2,253
	<u>\$ 11,413</u>	<u>2,502</u>	<u>10,246</u>	<u>24,161</u>

Income tax expense differs from amounts computed by applying the U.S. Federal income tax rate of 35% to earnings before income taxes as a result of the following:

	1999	1998	1997
Computed "expected" tax expense	\$ 33,126	26,452	21,900
Increase (reduction) in income taxes resulting from:			
State and local income taxes, net of Federal income tax benefit	2,210	1,977	1,626
Decrease in valuation allowance for deferred tax assets	(147)	(207)	(85)
Other, net	281	81	720
	<u>\$35,470</u>	<u>28,303</u>	<u>24,161</u>

The components of earnings before income taxes are as follows:

	1999	1998	1997
United States	\$ 30,403	28,542	22,799
Foreign	64,242	47,035	39,773
	<u>\$94,645</u>	<u>75,577</u>	<u>62,572</u>

The tax effects of temporary differences, tax credits and operating loss carryforwards that give rise to significant portions of deferred tax assets and deferred tax liabilities at December 31, 1999 and 1998 are as follows:

Years ended December 31,	1999	1998
Deferred tax assets		
Foreign tax credits related to unremitted foreign earnings	\$ 29,044	21,453
Accrued intercompany and third party charges, deductible for taxes upon economic performance (i.e. actual payment)	2,998	2,844
Foreign currency translation adjustment	2,952	2,183
Provision for doubtful accounts receivable	2,194	1,575
Excess of financial statement over tax depreciation	2,181	1,703
Other	943	1,286
	<u>40,312</u>	<u>31,044</u>
Less valuation allowance	(76)	(223)
	<u>40,236</u>	<u>30,821</u>
Deferred tax liabilities		
Unremitted foreign earnings	(33,823)	(23,108)
Other	(4,061)	(3,103)
	<u>\$(37,884)</u>	<u>(26,211)</u>
Net deferred tax assets	\$ 2,352	4,610
Plus (less) current deferred tax liabilities (assets)	\$ 601	(2,427)
Noncurrent deferred tax assets	<u>\$ 2,953</u>	<u>2,183</u>

At December 31, 1999, the Company has net operating loss carryforwards for foreign income tax purposes of \$218 which are available over an indefinite period to offset future foreign taxable income.

The Company has not provided U.S. Federal income taxes on undistributed earnings of foreign subsidiaries accumulated through December 31, 1992 since the Company

intends to reinvest such earnings indefinitely or to distribute them in a manner in which no significant additional taxes would be incurred. Such undistributed earnings are approximately \$41,900 and the additional Federal and state taxes payable in a hypothetical distribution of such accumulated earnings would approximate \$10,100. Since 1993, the Company has been providing for Federal and state income tax expense on foreign earnings without regard to whether such earnings will be permanently reinvested outside the United States.

Note **4. Shareholders' Equity**

a. Dividends

On May 5, 1999, the Board of Directors declared a 2-for-1 stock split, effected in the form of a stock dividend of one share of common stock for every share outstanding, and increased the authorized common stock to 160,000,000 shares. The stock dividend was distributed on May 31, 1999 to shareholders of record on May 17, 1999. All share and per share information, except par value, has been adjusted for all years to reflect the stock split.

b. Non-Discretionary Stock Repurchase Plan

The Company has a Non-Discretionary Stock Repurchase Plan under which management is authorized to repurchase up to 2,200,000 shares of the Company's common stock in the open market with the proceeds received from the exercise of Employee and Director Stock Options. As of December 31, 1999, the Company had repurchased and retired 1,858,566 shares of common stock at an average price of \$12.97 over the period from 1994 through 1999.

c. Stock Option Plans

The Company has two stock option plans (the "1985 Plan" and the "1997 Plan") for employees under which the Board of Directors may grant officers and key employees options to purchase common stock at prices equal to or greater than market value on the date of grant. The 1985 Plan provides for non-qualified grants at exercise prices equal to or greater than the market value on the date of grant. Outstanding options generally vest and become exercisable over periods up to five years from the date of grant and expire no more than 10 years from the date of grant. The 1997 Plan provides for qualified and non-qualified grants of options to purchase shares, limited to not more than 100,000 per person per year. Grants less than or equal to 20,000 shares in any fiscal year, are granted at or above common stock prices on the date of grant. Any 1997 Plan grants in excess of the initial 20,000 shares granted per person per year (Excess Grants) require an exercise price of not less than 120% of the common stock price on the date of grant. Excess Grants expire no later than 5 years from the date of grant. Excess Grants in 1997 vest completely 3 years from the date of grant.

The Company also has a stock option plan (Directors Plan) under which non-employee directors elected at each annual meeting are granted non-qualified options to purchase 8,000 shares of common stock on the first business day of the month following the meeting.

Upon the exercise of non-qualified stock options, the Company derives a tax deduction measured by the excess of the market value over the option price at the date of exercise. The related tax benefit is credited to additional paid-in capital.

Details regarding the plans are as follows:

	Unoptioned Shares			Outstanding Options	
	1985 Plan	1997 Plan	Directors' Plan	Number of Shares	Weighted Average Price Per Share
Balance at December 31, 1996	236,328	–	128,000	5,322,680	\$ 4.18
Options authorized	–	4,000,000	–	–	–
Options granted	(30,000)	(832,900)	(24,000)	886,900	\$ 13.08
Options exercised	–	–	–	(470,720)	\$ 3.36
Options canceled	195,000	7,400	–	(202,400)	\$ 5.73
Balance at December 31, 1997	401,328	3,174,500	104,000	5,536,460	\$ 5.65
Options granted	(210,000)	(863,400)	(24,000)	1,097,400	\$ 21.78
Options exercised	–	–	–	(318,100)	\$ 4.54
Options canceled	66,250	52,400	–	(118,650)	\$ 4.27
Balance at December 31, 1998	257,578	2,363,500	80,000	6,197,110	\$ 8.49
Options granted	(100,000)	(908,900)	(24,000)	1,032,900	\$ 31.98
Options exercised	–	–	–	(1,323,405)	\$ 3.47
Options canceled	43,750	138,000	–	(181,750)	\$ 20.04
Balance at December 31, 1999	201,328	1,592,600	56,000	5,724,855	\$13.47

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The Company applies APB Opinion No. 25 and related interpretations in accounting for its stock option and its employee stock purchase rights plans. Accordingly, no compensation cost has been recognized for its fixed stock option or employee stock purchase rights plans. Had compensation cost for the Company's three stock based compensation and employee stock purchase rights plans been determined consistent with SFAS No. 123, the Company's net earnings, basic earnings per share and diluted earnings per share would have been decreased to the pro forma amounts indicated as follows:

	1999	1998	1997
Net earnings - as reported	\$59,175	47,274	38,411
Net earnings - pro forma	\$52,111	42,697	36,216
Basic earnings per share – as reported	\$ 1.18	.96	.79
Basic earnings per share – pro forma	\$ 1.05	.87	.74
Diluted earnings per share – as reported	\$ 1.10	.89	.73
Diluted earnings per share – pro forma	\$.98	.82	.70

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

	1999	1998	1997
Dividend yield	.23%	0.3%	0.5%
Volatility	47%	45%	39%
Risk-free interest rates	5.1 – 5.9%	4.6 – 5.7%	5.5 – 6.7%
Expected life (years) – stock option plans	5.5 - 7	7	7
Expected life (years) – stock purchase rights plan	1	1	1
Weighted average fair value of stock options granted during the year	\$17.55	\$11.49	\$5.98
Weighted average fair value of stock purchase rights	\$ 8.98	\$ 6.25	\$4.88

The following table summarizes information about fixed-price stock options outstanding at December 31, 1999:

Range of Exercise Price	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$ 2.66 – 3.29	1,066,755	1.6 years	\$ 2.98	1,066,755	\$ 2.98
\$ 3.47 – 5.69	1,571,300	4.9 years	\$ 5.17	1,260,550	\$ 5.06
\$ 6.04 – 14.66	924,000	7.0 years	\$10.74	174,500	\$ 8.31
\$15.04 – 21.94	1,178,000	7.4 years	\$20.73	24,000	\$19.38
\$27.50 – 32.09	984,800	9.3 years	\$31.98	24,000	\$29.25
\$ 2.66 – 32.09	5,724,855	5.9 years	\$13.47	2,549,805	\$ 4.77

d. Basic and Diluted Earnings Per Share

The following table reconciles the numerator and the denominator of the basic and diluted per share computations for earnings per share in 1999, 1998 and 1997.

	Net Earnings	Weighted Average Shares	Earnings Per Share
1999			
Basic earnings per share	\$ 59,175	50,137,045	\$ 1.18
Effect of dilutive potential common shares	-	3,690,772	-
Diluted earnings per share	<u>\$59,175</u>	<u>53,827,817</u>	<u>\$1.10</u>
1998			
Basic earnings per share	\$ 47,274	49,234,438	\$.96
Effect of dilutive potential common shares	-	3,823,946	-
Diluted earnings per share	<u>\$ 47,274</u>	<u>53,058,384</u>	<u>\$.89</u>
1997			
Basic earnings per share	\$ 38,411	48,857,858	\$.79
Effect of dilutive potential common shares	-	3,789,186	-
Diluted earnings per share	<u>\$ 38,411</u>	<u>52,647,044</u>	<u>\$.73</u>

e. Stock Purchase Plan

The Company's 1988 Employee Stock Purchase Plan provides for 2,800,000 shares of the Company's common stock to be reserved for issuance upon exercise of purchase rights granted to employees who elect to participate through regular payroll deductions beginning August 1 of each year. The purchase rights are exercisable on July 31 of the following year at a price equal to the lesser of (1) 85% of the fair market value of the Company's stock on July 31 or (2) 85% of the fair market value of the Company's stock on the preceding August 1. At December 31, 1999, 1998 and 1997, an aggregate of 2,169,235 shares, 1,917,844 shares and 1,692,290 shares, respectively, had been issued under the plan, and at December 31, 1999, \$2,753 had been withheld in connection with the plan year ending July 31, 2000.

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Note 5. Fair Value of Financial Instruments

The Company's financial instruments, other than cash, consist primarily of cash equivalents, short-term investments, accounts receivable, short-term borrowings, accounts payable and accrued expenses, and stock purchase rights. The fair values of these financial instruments, excluding stock purchase rights, approximate their carrying amounts based upon market interest rates or their short term nature. The fair value of the stock purchase rights, which have a carrying value of zero, has been determined using market prices for the related stock, and is approximately \$5,862 as of December 31, 1999.

Note 6. Commitments

a. Leases

The Company occupies office and warehouse facilities under terms of operating leases expiring up to 2005. At December 31, 1999, future minimum annual lease payments under all leases are as follows:

2000	\$19,370
2001	12,282
2002	10,463
2003	8,503
2004	4,727
Thereafter	2,479
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	\$57,824

b. Employee Benefits

The Company has employee savings plans under which the Company provides a discretionary matching contribution. In 1999, 1998 and 1997, the Company's contributions under the plans were \$2,663, \$2,219, and \$1,119, respectively.

Note 7. Contingencies

The Company is ordinarily involved in claims and lawsuits which arise in the normal course of business, none of which currently, in management's opinion, will have a significant effect on the Company's financial condition.

Note 8. Business Segment Information

Financial information regarding the Company's 1999, 1998, and 1997 operations by geographic area are as follows:

	United States	Other North America	Far East	Europe	Australia / New Zealand	Latin America	Middle East	Eliminations	Consolidated
1999									
Revenues from unaffiliated customers	\$ 358,454	21,407	821,977	175,794	12,995	8,224	45,724	–	1,444,575
Transfers between geographic areas	18,150	1,049	3,347	7,364	3,227	2,001	1,950	(37,088)	–
Total revenues	\$376,604	22,456	825,324	183,158	16,222	10,225	47,674	(37,088)	1,444,575
Net revenues	\$ 206,198	14,699	101,790	89,043	10,974	4,983	14,799	–	442,486
Operating income	\$ 30,747	2,279	37,779	17,535	2,127	442	2,414	–	93,323
Identifiable assets at year end	\$ 270,760	14,280	94,652	98,030	9,183	7,587	17,288	–	511,780
Capital expenditures	\$ 14,109	1,347	3,740	3,733	693	272	2,688	–	26,582
Depreciation and amortization	\$ 11,511	618	3,429	3,302	614	251	1,094	–	20,819
Equity	\$ 282,385	2,814	81,956	24,888	6,558	(179)	2,931	(118,968)	282,385
1998									
Revenues from unaffiliated customers	\$ 311,897	12,361	562,500	143,925	10,160	3,172	19,692	–	1,063,707
Transfers between geographic areas	13,116	765	3,061	6,558	2,400	1,482	1,029	(28,411)	–
Total revenues	\$ 325,013	13,126	565,561	150,483	12,560	4,654	20,721	(28,411)	1,063,707
Net revenues	\$ 170,748	8,492	82,025	74,199	8,589	3,604	5,793	–	353,450
Operating income	\$ 27,214	906	29,343	13,945	1,384	(264)	844	–	73,372
Identifiable assets at year end	\$ 220,786	12,511	70,465	84,112	6,987	3,547	8,188	–	406,596
Capital expenditures	\$ 40,053	592	5,998	3,686	748	570	808	–	52,455
Depreciation and amortization	\$ 8,225	459	2,481	2,957	511	251	663	–	15,547
Equity	\$ 217,198	1,184	71,012	17,283	4,874	(865)	1,556	(95,044)	217,198
1997									
Revenues from unaffiliated customers	\$ 285,166	6,929	526,878	112,726	9,611	2,594	10,098	–	954,002
Transfers between geographic areas	11,819	436	3,044	4,688	1,847	1,109	788	(23,731)	–
Total revenues	\$ 296,985	7,365	529,922	117,414	11,458	3,703	10,886	(23,731)	954,002
Net revenues	\$ 140,150	4,315	76,637	55,354	7,847	2,675	3,546	–	290,524
Operating income	\$ 22,934	351	25,709	10,104	1,125	(172)	(136)	–	59,915
Identifiable assets at year end	\$ 170,999	7,739	80,458	70,979	5,850	2,991	5,090	–	344,106
Capital expenditures	\$ 20,695	813	2,642	4,142	980	189	846	–	30,307
Depreciation and amortization	\$ 5,755	289	1,749	2,319	449	202	396	–	11,159
Equity	\$ 171,854	1,032	62,204	10,410	4,278	(1,258)	995	(77,661)	171,854

The Company charges its subsidiaries and affiliates for services rendered in the United States on a cost recovery basis.

Note 9. Quarterly Results (Unaudited)

	1st	2nd	3rd	4th
1999				
Revenues	\$283,712	331,980	406,139	422,743
Net revenues	94,413	104,230	119,719	124,124
Net earnings	9,521	13,229	17,839	18,587
Basic earnings per share	.19	.26	.35	.37
Diluted earnings per share	.18	.25	.33	.34
1998				
Revenues	\$223,349	241,970	289,675	308,713
Net revenues	75,764	82,374	92,890	102,422
Net earnings	8,034	11,080	14,217	13,943
Basic earnings per share	.16	.23	.29	.28
Diluted earnings per share	.15	.21	.27	.26

Net revenues are determined by deducting freight consolidation costs from total revenues. The sum of quarterly per share data may not equal the per share total reported for the year.

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