

MERITOR INC
Form 10-K
November 21, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Fiscal Year Ended September 30, 2012
Commission file number 1-15983

MERITOR, INC.

(Exact name of registrant as specified in its charter)

Indiana

38-3354643

(State or other jurisdiction of incorporation
or organization)

(I.R.S. Employer
identification no)

2135 West Maple Road
Troy, Michigan

48084-7186

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: (248) 435-1000

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of each class

Name of each exchange on which registered

Common Stock, \$1 Par Value

New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: None

Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes ☐ No ☒

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding twelve months (or for such shorter period that the registrant was required to submit and post such files).

Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of "accelerated filer", "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐

Accelerated filer ☐

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

Smaller reporting
company ☐

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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ☐ No ☒

The aggregate market value of the registrant's voting and non-voting common equity held by non-affiliates of the registrant on March 30, 2012 (the last business day of the most recently completed second fiscal quarter) was approximately \$765,333,392.

96,524,636 shares of the registrant's Common Stock, par value \$1 per share, were outstanding on November 7, 2012.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information contained in the definitive Proxy Statement for the Annual Meeting of Shareowners of the registrant to be held on January 24, 2013 is incorporated by reference into Part III.

	Page No.
<u>PART I.</u>	
Item 1. <u>Business</u>	<u>1</u>
Item 1A. <u>Risk Factors</u>	<u>13</u>
Item 1B. <u>Unresolved Staff Comments</u>	<u>22</u>
Item 2. <u>Properties</u>	<u>23</u>
Item 3. <u>Legal Proceedings</u>	<u>23</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>25</u>
Item 4A. <u>Executive Officers of the Registrant</u>	<u>25</u>
<u>PART II.</u>	
Item 5. <u>Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	<u>26</u>
Item 6. <u>Selected Financial Data</u>	<u>28</u>
Item 7. <u>Management’s Discussion and Analysis of Financial Conditions and Results of Operations</u>	<u>30</u>
Item 7A. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>59</u>
Item 8. <u>Financial Statements and Supplementary Data</u>	<u>61</u>
Item 9. <u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	<u>128</u>
Item 9A. <u>Controls and Procedures</u>	<u>128</u>
Item 9B. <u>Other Information</u>	<u>130</u>
<u>PART III.</u>	
Item 10. <u>Directors, Executive Officers and Corporate Governance</u>	<u>130</u>
Item 11. <u>Executive Compensation</u>	<u>130</u>
Item 12. <u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>130</u>
Item 13. <u>Certain Relationships and Related Transactions, and Director Independence</u>	<u>131</u>
Item 14. <u>Principal Accountant Fees and Services</u>	<u>132</u>
<u>PART IV.</u>	
Item 15. <u>Exhibits and Financial Statement Schedules</u>	<u>133</u>
<u>Signatures</u>	<u>141</u>

PART I

Item 1. Business.

Overview

Meritor, Inc., (the "company" or "Meritor"), headquartered in Troy, Michigan, is a premier global supplier of a broad range of integrated systems and components to original equipment manufacturers ("OEMs") and the aftermarket for the commercial vehicle, transportation and industrial sectors. The company serves commercial truck, trailer, off-highway, military, bus and coach and other industrial OEMs and certain aftermarkets. Our principal products are axles, undercarriages, drivelines, brakes and braking systems.

Meritor was incorporated in Indiana in 2000 in connection with the merger of Meritor Automotive, Inc. ("Meritor Automotive") and Arvin Industries, Inc. ("Arvin"). On March 30, 2011, we announced that we officially changed the company name from ArvinMeritor, Inc. to Meritor, Inc. and on that date, began trading our common stock on the New York Stock Exchange under the ticker symbol MTOR. As used in this Annual Report on Form 10-K, the terms "company," "Meritor," "we," "us" and "our" include Meritor, its consolidated subsidiaries and its predecessors unless the context indicates otherwise.

Meritor serves a broad range of customers worldwide, including medium- and heavy-duty truck OEMs, specialty vehicle manufacturers, certain aftermarkets, and trailer producers. Our total sales from continuing operations in fiscal year 2012 were approximately \$4.4 billion. Our ten largest customers accounted for approximately 71 percent of fiscal year 2012 sales from continuing operations. Sales from operations outside the United States (U.S.) accounted for approximately 62 percent of total sales from continuing operations in fiscal year 2012. Our continuing operations also participated in 6 unconsolidated joint ventures, which we accounted for under the equity method of accounting and that generated revenues of approximately \$1.8 billion in fiscal year 2012.

The company's fiscal year ends on the Sunday nearest to September 30. Fiscal year 2012 ended on September 30, 2012, fiscal year 2011 ended on October 2, 2011, and fiscal year 2010 ended on October 3, 2010. All year and quarter references relate to our fiscal year and fiscal quarters unless otherwise stated. For ease of presentation, September 30 is utilized consistently throughout this report to represent the fiscal year end.

Whenever an item in this Annual Report on Form 10-K refers to information under specific captions in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations or Item 8. Financial Statements and Supplementary Data, the information is incorporated in that item by reference.

References in this Annual Report on Form 10-K to our belief that we are a leading supplier or the world's leading supplier, and other similar statements as to our relative market position are based principally on calculations we have made. These calculations are based on information we have collected, including company and industry sales data obtained from internal and available external sources as well as our estimates. In addition to such quantitative data, our statements are based on other competitive factors such as our technological capabilities, our engineering, research and development efforts, and our innovative solutions as well as the quality of our products and services, in each case relative to that of our competitors in the markets we address.

Recent Developments

On November 12, 2012, we announced a revised management reporting structure resulting in two business segments to drive efficiencies. Our new business segments are Commercial Truck & Industrial; and Aftermarket & Trailer. The discussion of our business set forth in this Report on Form 10-K will be of such business as it existed in fiscal year

2012 prior to this announcement.

Divestiture Activity

On January 2, 2012, we completed the sale of our Commercial Truck manufacturing facility located in St. Priest, France to Renault Trucks SAS, an affiliate of AB Volvo. This transaction did not have a significant impact on our sales as production was absorbed by our remaining manufacturing facilities in Europe. During fiscal year 2012, we recognized non-cash charges of \$19 million, including an asset impairment charge of \$17 million for the disposal group, in connection with the sale. In addition, other restructuring charges of approximately \$5 million associated with employee headcount reduction and plant rationalization costs were recorded during fiscal year 2012.

As a result of the divestiture of our light vehicle systems business ("LVS") prior to 2012, our company is now able to focus solely on commercial vehicle and industrial markets. See Note 3 of the Notes to Consolidated Financial Statements under Item 8. Financial Statements and Supplementary Data below for further information with respect to divestiture activity in 2011 and 2010 and changes in continuing and discontinued operations.

Our Business

Our reporting segments are as follows:

The Commercial Truck segment supplies drivetrain systems and components, including axles, drivelines and braking and suspension systems, primarily for medium- and heavy-duty trucks in North America, South America and Europe. The Industrial segment supplies drivetrain systems including axles, brakes, drivelines and suspensions for off-highway, military, construction, bus and coach, fire and emergency, and other industrial applications. This segment also includes all of our original equipment (OE) businesses in Asia Pacific, including all on- and off-highway activities.

The Aftermarket & Trailer segment supplies axles, brakes, drivelines, suspension parts and other replacement and remanufactured parts, including transmissions, to commercial vehicle and industrial aftermarket customers. This segment also supplies a wide variety of undercarriage products and systems for trailer applications in North America. See Note 23 of the Notes to Consolidated Financial Statements under Item 8. Financial Statements and Supplementary Data for financial information by segment for continuing operations for each of the three years ended September 30, 2012, including information on sales and assets by geographic area. The heading "Products" below includes information on certain product sales for each of the three fiscal years ended September 30, 2012.

Business Strategies

We are currently a global supplier of a broad range of integrated systems, modules and components to OEMs and the aftermarket for the commercial vehicle, transportation and industrial sectors, and we believe we have developed market positions as a leader in many of the markets we serve. The unprecedented challenges in the last few years in the credit markets, deterioration and then rapid upturn in the commercial vehicle market and a worldwide recession have forced us to sharpen our business and operating strategies to align to these new business conditions and to better position our company for the future. We are working to enhance our leadership positions and capitalize on our existing customer, product and geographic strengths.

We expect production volumes in North America and Europe to soften compared to the levels experienced in fiscal year 2012. Beginning in second quarter of fiscal year 2012, production volumes in South America declined significantly as the industry transitioned to tighter emission standard requirements for commercial vehicles. The recovery of production volumes has been slower than previously expected and we expect production volumes in South America to remain at such low levels during the first half of fiscal year 2013, with a modest improvement expected in the second half of fiscal year 2013. Production volumes in the Asia-Pacific region, more specifically China and India, have decreased compared to levels experienced in fiscal year 2011, and there is no certainty as to when these volumes will return to the levels previously experienced.

Sales for our primary military program were at their peak during the third quarter of fiscal year 2012. This program is expected to wind down over the next few years beginning in fiscal year 2013. We are working to secure our participation in new military programs with various OEMs. However, failure to secure new military contracts could have a longer-term negative impact on our Industrial Segment. In addition, even if sales of our military programs do return to historic levels, the levels of profitability on these sales could be lower than what we have recognized in recent periods.

Our business continues to address a number of other challenging industry-wide issues including the following:

Uncertainty around the global market outlook;

- Volatility in price and availability of steel, components and other commodities;

Disruptions in the financial markets and their impact on the availability and cost of credit;

Higher energy and transportation costs;

Impact of currency exchange rate volatility;

Consolidation and globalization of OEMs and their suppliers; and
Significant pension and retiree medical health care costs.

Other

Other significant factors that could affect our results and liquidity in fiscal year 2013:

- Significant contract awards or losses of existing contracts or failure to negotiate acceptable terms in contract renewal negotiations;
- Ability to manage possible adverse effects on our European operations, or financing arrangements related thereto, in the event one or more countries exit the European monetary union;
- Ability to work with our customers to manage rapidly changing production volumes;
- Ability to recover and timing of recovery of steel price and other cost increases from our customers;
- Any unplanned extended shutdowns or production interruptions by us, our customers or our suppliers (including those caused by financial distress of our customers and suppliers);
- A significant deterioration or slowdown in economic activity in the key markets in which we operate;
- Higher than planned price reductions to our customers;
- Potential price increases from our suppliers;
- Additional restructuring actions and the timing and recognition of restructuring charges;
- Higher than planned warranty expenses, including the outcome of known or potential recall campaigns;
- Our ability to implement planned productivity, cost reduction, and other margin improvement initiatives; and
- Restrictive government actions by foreign countries (such as restrictions on transfer of funds and trade protection measures, including export duties and quotas and customs duties and tariffs).

Our specific business strategies are influenced by these industry factors and trends as well as by the recent global economic and financial crisis and are focused on leveraging our resources to continue to develop and produce competitive product offerings. We believe the following strategies will allow us to maintain a balanced portfolio of commercial truck, industrial and aftermarket businesses covering key global markets. See Item 1A. Risk Factors below for information on certain risks that could have an impact on our business, financial condition or results of operations in the future.

Financial and Operational Excellence

Strive to Manage the Cycle. The industries in which we operate have been characterized historically by periodic fluctuations in overall demand for medium- and heavy-duty trucks, and other vehicles for which we supply products, resulting in corresponding fluctuations in demand for our products. The length and timing of the cyclical nature of the commercial vehicle industry cannot be predicted with certainty. To effectively manage the cyclical nature of our business, we are focused on cost management and maintaining sufficient balance sheet flexibility. In addition, we expect to balance the on-highway commercial vehicle cycles with complementary business lines, including aftermarket, military, construction and industrial supply. We also attempt to utilize flexible manufacturing processes and plant footprints in our effort to take advantage of industry upturns and effectively manage industry downturns.

Drive a Continuous Improvement Culture. The company implemented Performance Plus, a long-term profit improvement and cost reduction initiative, in fiscal year 2007 to improve operational performance and increase cash flow, earnings and shareowner value. The actions and programs that are part of the Performance Plus initiatives include delivering cost improvements by focusing on operational excellence (materials; manufacturing; and overhead) and enhancing revenue by focusing on commercial excellence (engineering, research and development; product strategy and growth; and aftermarket).

In fiscal year 2007, as part of Performance Plus, we implemented the Meritor Production System, a lean manufacturing initiative that guides our pursuit of operational excellence. Meritor Production System integrates several of our previous performance improvement initiatives into a set of actions that focus on improving systems, processes, behaviors and capabilities. Throughout our company, continuous improvement teams work to achieve significant cost savings, increase productivity and efficiency, improve design and quality, streamline operations and improve workplace safety. Maintaining a continuous improvement culture is important to our business operations and to maintaining and improving our operating results.

Profitable Growth

Focus on Organic Growth While Reviewing Strategic Opportunities. Our long term goal is to grow businesses that offer attractive returns and are core to our operations as well as to diversify through complementary product lines, geographic expansion, and initiatives in adjacent markets. We have identified the areas of our business that we believe have the most potential for leveraging into other industries, products, markets and technologies, and we are focusing our resources on these areas. We also continue to review and evaluate on an ongoing basis all of our existing businesses to determine whether we need to modify, restructure, sell or otherwise discontinue any one of the businesses.

We believe that commercial vehicle and industrial suppliers continue to consolidate into larger, more efficient and more capable companies and collaborate with each other in an effort to better serve the global needs of OEM customers by being where these customers need them. We regularly evaluate various strategic and business development opportunities, including licensing agreements, marketing arrangements, joint ventures, acquisitions and dispositions. We remain committed to selectively pursuing alliances and acquisitions that would allow us to leverage our capabilities, gain access to new customers and technologies, expand our global presence, enter complementary product market segments and implement our business strategies.

Strengthen our Presence in Emerging Global Markets. Geographic expansion to meet the global sourcing needs of customers and to enter new markets is an important element of our growth strategy. We currently have wholly-owned operations and regional joint ventures in South America. We also have joint ventures and wholly-owned subsidiaries in China, India and Turkey and participate in programs to support customers as they establish and expand operations in those markets.

We plan to continue to grow and expand globally, with a keen focus on South America and Asia-Pacific (primarily China and India) because we believe these regions offer the greatest profit potential. Sales in these regions represented approximately 23 percent, 30 percent and 29 percent of total sales from continuing operations in fiscal years 2012, 2011 and 2010, respectively.

Product and Technology Focus

Deliver High Quality Products for All Markets we Serve. We believe the quality of our core product lines and our ability to service our products through our aftermarket capabilities give us a competitive advantage. A key part of delivering high quality products is delivering service through the entire life cycle of the product. We continue to invest in new product development as we seek to keep our core product lines continually refreshed and in step with evolving market requirements and continue to grow our complimentary product lines. Building upon the strength of these core technologies, we intend to expand our presence globally, and continue our growth in complementary product lines, such as military vehicle and off-highway markets. Our strategy involves diversifying on a geographic and product line basis through the aftermarket, off- and on-highway and added adjacencies that we will explore. Through implementation of our technology roadmap, complementary technologies such as electronics, controls and mechatronics are expected to be applied to traditional product lines to provide enhanced performance and expanded

vehicle content.

Leverage Our Technology to Address Mobility, Safety and Environmental Provisions. In our opinion, another industry trend is the increasing amount of equipment required for changes in environmental and safety-related regulatory provisions. OEMs select suppliers based not only on the cost and quality of their products, but also on their ability to meet stringent environmental and safety requirements and to service and support the customer after the sale. We use our technological and market expertise to anticipate trends and to develop and engineer products that aim to address mobility, safety and environmental concerns.

To address safety, we have implemented a strategy of focusing on products and technologies that enhance overall vehicle braking performance. As part of this strategy, we are focusing on the integration of braking and stability products and suspension products as well as the development of electronic control capabilities. Through MeritorWabco, our joint venture with WABCO Holdings, Inc. ("WABCO"), we offer electronic braking systems that integrate anti-lock braking systems technology, automatic traction control, collision avoidance systems and other key vehicle control system components to improve braking performance and meet all required stopping distances for commercial vehicles.

Nurture Emerging Next-Generation Products. We continue to invest in advanced technologies and expanded product portfolios that address customer needs by improving fuel efficiency, optimizing products for specific vehicle applications, and enhancing driver/vehicle safety. Examples of these products being developed include:

SMARTandem single drive axle solution: Using technologies developed in house to enhance the traction and fuel economy of a conventional 6x2 axle configuration, we developed a system which achieves up to a five-percent fuel economy benefit for line haul operators over a 6x4, improved traction over a conventional 6x2, while still providing the weight savings of a 6x2 over a 6x4 configuration. This product serves as platform for additional technologies as well, such as LogixDrive and tire inflation.

- Meritor(R) LogixDrive(TM): This axle system is enabled by electronic controls that continuously monitor oil temperature, vehicle speed, braking and torque conditions in order to manage and optimize the amount of lubrication in the axle. The LogixDrive system addresses the two main areas of power loss in axles: gear and bearing friction and oil churning due to gear rotation.

Meritor Tire Inflation Systems: Meritor is utilizing a variant of its pneumatic control unit developed for SMARTandem to provide tire inflation capability to maintain tire pressures in on-highway applications. Properly maintained tire pressures not only provide fuel economy benefits, but also improve safety.

Next Generation Air Disk Brake: Building on the successful platform of our current Elsa disk brake, we are developing the next generation of brake targeted at more accurate performance characteristics, longer life, and increased efficiency. Simplification of internal mechanisms and a more robust manufacturing process will also drive increases in reliability and life.

New, more powerful front and rear brakes: We released more powerful front and rear brakes to deliver the new stopping distances mandated by the U.S. government's FMVSS 121, which took effect in August 2011. The next phase of the legislation is targeted for August 2013 applies to more severe applications. Development of the new brakes are focused on daily driving characteristics as well as the more demanding performance required in an emergency stopping scenario.

- Fuel economy modeling: Working with Oakridge National Labs, Meritor is developing models to predict and ultimately develop technologies aimed at providing significant improvements in drivetrain fuel economy.

Light Commercial Vehicle drive axle for India market: Launching in 2013 will be a new light commercial vehicle single-drive axle targeted at the 5-7 GVW weight class range. Leveraging proven technology from Meritor's medium and heavy duty axle range, this expands Meritor's portfolio for the India market.

Products

Meritor designs, develops, manufactures, markets, distributes, sells, services and supports a broad range of products for use in the transportation and industrial sectors. In addition to sales of original equipment systems and components, we provide our original equipment, aftermarket and remanufactured products to vehicle OEMs, their dealers (who in turn sell to motor carriers and commercial vehicle users of all sizes), independent distributors, and other end-users in certain aftermarkets.

The following chart sets forth, for each of the three fiscal years with the most recent ended September 30, 2012, information about product sales comprising more than 10% of consolidated revenue in any of those years. A narrative description of our principal products follows the chart.

Product Sales:

	Fiscal Year Ended September 30,					
	2012		2011		2010	
Axles, Undercarriage and Drivelines	75	%	78	%	73	%
Brakes and Braking Systems	23	%	21	%	24	%
Other	2	%	1	%	3	%
Total:	100	%	100	%	100	%

The three segments included in our continuing operations manufacture and supply the products set forth and described below.

Axles, Undercarriage & Drivelines

We believe we are one of the world's leading independent suppliers of axles for medium- and heavy-duty commercial vehicles, with the leading market position in axle manufacturing in North America, South America and Europe, and are one of the major axle manufacturers in the Asia-Pacific region. Our extensive truck axle product line includes a wide range of front steer axles and rear drive axles. Our front steer and rear drive axles can be equipped with our cam, wedge or air disc brakes, automatic slack adjusters, complete wheel-end equipment such as hubs, rotors and drums, and (through our WABCO joint venture) anti-lock braking systems ("ABS") and vehicle stability control systems.

We supply heavy-duty axles in certain global regions, for use in numerous off-highway vehicle applications, including construction, material handling, and mining. We also supply axles for use primarily in medium- and heavy-duty military tactical wheeled vehicles, principally in North America. These products are designed to tolerate high tonnage and operate under extreme geographical and climate conditions. In addition, we have other off-highway vehicle products that are currently in development for certain other regions. We also supply axles for use in buses, coaches and recreational vehicles, fire trucks and other specialty vehicles in North America, Asia Pacific and Europe, and believe we are the leading supplier of bus and coach axles in North America.

We are one of the major manufacturers of heavy-duty trailer axles in North America. Our trailer axles are available in more than 40 models in capacities from 20,000 to 30,000 pounds for virtually all heavy trailer applications and are available with our broad range of suspension modules, brake products, including drum brakes, disc brakes, anti-lock and trailer stability control systems, and ABS (through our WABCO joint venture).

We supply universal joints and driveline components, including our Permalube™ universal joint and RPL Permalube™ driveline, which are low maintenance, permanently lubricated designs used often in the high mileage on-highway market. We supply drivelines in a variety of global regions, for use in numerous on-highway vehicle applications, including construction, material handling and mining. We supply transfer cases and drivelines for use in medium- and heavy-duty military tactical wheeled vehicles, principally in North America. We also supply transfer cases for use in specialty vehicles in North America. Anti-lock brakes and stability control systems (which we supply through our WABCO joint venture) are also used in military vehicles and specialty vehicles. In addition, we supply trailer air suspension systems and products with an increasing market presence in North America. We also supply advanced suspension modules for use in light-, medium- and heavy-duty military tactical wheeled vehicles, principally in North America.

Through a joint venture, we develop, manufacture and sell truck suspensions, trailer axles and suspensions and related wheel-end products in the South American market. We believe this joint venture has a number one product position in suspension and trailer axles in the South American market.

Brakes and Braking Systems

We believe we are one of the leading independent suppliers of air brakes to medium- and heavy-duty commercial vehicle manufacturers in North America and Europe. In Brazil, one of the largest truck and trailer markets in the world, we believe that Master Sistemas Automotivos Limitada, our 49%-owned joint venture with Randon S. A. Veiculos e Implementos, is a leading supplier of brakes and brake-related products.

Through manufacturing facilities located in North America, Asia Pacific and Europe, we manufacture a broad range of foundation air brakes, as well as automatic slack adjusters for brake systems. Our foundation air brake products

include cam drum brakes, which offer improved lining life and tractor/trailer interchangeability; wedge drum brakes, which are lightweight and provide automatic internal wear adjustment; air disc brakes, which provide enhanced stopping distance and improved fade resistance for demanding applications; and wheel-end components such as hubs, drums and rotors.

Our brakes and brake system components also are used in medium- and heavy-duty military tactical wheeled vehicles, principally in North America. We also supply brakes for use in buses, coaches and recreational vehicles, fire trucks and other specialty vehicles in North America and Europe, and we believe we are the leading supplier of bus and coach brakes in North America, and also supply brakes for commercial vehicles, buses and coaches in Asia Pacific.