DELPHI CORP
Form 10-Q
July 17, 2003

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549-1004

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2003

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ________ to ________________.

Commission file No. 1-14787

DELPHI CORPORATION

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**38-3430473** (IRS employer identification number)
5725 Delphi Drive, Troy, Michigan (Address of principal executive offices)	**48098** (Zip code)

(248) 813-2000

(Registrant s telephone number, including area code)

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 X. No _.

As of June 30, 2003, there were 560,295,941 outstanding shares of the registrant s $0.01 par value common stock.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

DELPHI CORPORATION

CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
	(in millions, except per share amounts)			
Net sales:				
General Motors and affiliates	$ 4,313	$ 4,818	$ 8,868	$ 9,302
Other customers	2,781	2,504	5,408	4,708
Total net sales	7,094	7,322	14,276	14,010
Less operating expenses:				
Cost of sales, excluding items listed below	6,240	6,332	12,552	12,221
Selling, general and administrative	422	361	811	723
Depreciation and amortization	260	247	513	491
Restructuring (Note 2)				225
Total operating expenses	6,922	6,940	13,876	13,660
Operating income	172	382	400	350
Less: interest expense	45	47	90	95
Other income, net	2	8	4	18
Income before income taxes	129	343	314	273
Income tax expense	41	123	99	104
Net income	$ 88	$ 220	$ 215	$ 169
Basic and diluted earnings per share (Note 1)	$ 0.16	$ 0.39	$ 0.38	$ 0.30

See notes to consolidated financial statements.

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DELPHI CORPORATION

CONSOLIDATED BALANCE SHEETS

	June 30, 2003 (Unaudited)	December 31, 2002
	(in millions)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 730	$ 1,014
Accounts receivable, net:		
General Motors and affiliates	2,596	2,304
Other customers	1,295	1,712
Retained interests in receivables (Note 3)	543	
Inventories, net (Note 4)	1,833	1,769
Deferred income taxes	466	502
Prepaid expenses and other	205	241
Total current assets	7,668	7,542
Long-term assets:		
Property, net	6,023	5,944
Deferred income taxes	3,675	3,649
Goodwill, net	738	699
Other	1,526	1,482
Total assets	$ 19,630	$ 19,316
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Notes payable and current portion of long-term debt	$ 1,096	$ 682
Accounts payable	3,265	3,060
Accrued liabilities	1,747	2,118
Total current liabilities	6,108	5,860
Long-term liabilities:		
Long-term debt	1,533	2,084
Pension benefits	3,571	3,568
Postretirement benefits other than pensions	5,413	5,120
Other	1,352	1,405
Total liabilities	17,977	18,037
Stockholders equity (Note 6):		
Common stock, $0.01 par value, 1,350 million shares authorized, 565 million shares issued in 2003 and 2002	6	6
Additional paid-in capital	2,462	2,445
Retained earnings	1,666	1,530
Minimum pension liability	(2,098)	(2,098)
Accumulated other comprehensive loss, excluding minimum pension liability	(307)	(493)
Treasury stock, at cost (4.7 million and 6.9 million shares in 2003 and 2002, respectively)	(76)	(111)

Total stockholders equity	1,653	1,279
Total liabilities and stockholders equity	$ 19,630	$ 19,316

See notes to consolidated financial statements.

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DELPHI CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Six Months Ended June 30,	
	2003	2002
	(in millions)	
Cash flows from operating activities:		
Net income	$ 215	$ 169
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	513	491
Deferred income taxes	15	36
Restructuring		225
Changes in operating assets and liabilities:		
Accounts receivable and retained interests in receivables, net	(445)	(817)
Inventories, net	(68)	(87)
Prepaid expenses and other	(13)	11
Accounts payable	206	558
Restructuring obligations	(24)	(245)
Accrued liabilities	(328)	69
Other long-term liabilities	301	(74)
Other	3	(80)
Net cash provided by operating activities	375	256
Cash flows from investing activities:		
Capital expenditures	(462)	(461)
Other	23	38
Net cash used in investing activities	(439)	(423)
Cash flows from financing activities:		
Net proceeds from (repayments of) borrowings under credit facilities and other debt	(171)	309
Dividend payments	(79)	(78)
Issuance (purchases) of treasury stock, net	1	(12)
Net cash (used in) provided by financing activities	(249)	219
Effect of exchange rate fluctuations on cash and cash equivalents	29	(56)
Decrease in cash and cash equivalents	(284)	(4)
Cash and cash equivalents at beginning of period	1,014	757
Cash and cash equivalents at end of period	$ 730	$ 753

See notes to consolidated financial statements.

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DELPHI CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. BASIS OF PRESENTATION

General Delphi Corporation (Delphi) is a world-leading supplier of vehicle electronics, transportation components, integrated systems and modules and other electronic technology. The consolidated financial statements and notes thereto included in this report should be read in conjunction with our consolidated financial statements and notes thereto included in our 2002 Annual Report on Form 10-K filed with the Securities and Exchange Commission. The consolidated financial statements include the accounts of Delphi and its wholly-owned and majority-owned subsidiaries.

All significant intercompany transactions and balances between consolidated Delphi businesses have been eliminated. In the opinion of management, all adjustments, consisting of only normal recurring items, which are necessary for a fair presentation have been included. The results for interim periods are not necessarily indicative of results which may be expected from any other interim period or for the full year and may not necessarily reflect the consolidated results of operations, financial position and cash flows of Delphi in the future.

Certain prior period amounts have been reclassified to conform to current period presentation.

Earnings Per Share Basic earnings per share amounts were computed using weighted average shares outstanding for each respective period. Diluted earnings per share also reflect the weighted average impact from the date of issuance of all potentially dilutive securities, unless inclusion would have had an antidilutive effect. Actual weighted average shares outstanding used in calculating basic and diluted earnings per share were:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	**2002**	**2003**	**2002**
		(in thousands)		
Weighted average shares outstanding	560,291	560,650	559,928	560,550
Effect of dilutive securities	148	8,238	59	7,626
Diluted shares outstanding	560,439	568,888	559,987	568,176

The Board of Directors declared a dividend on Delphi common stock of $0.07 per share on June 18, 2003, payable on July 29, 2003, to holders of record on June 30, 2003. The dividend declared on March 26, 2003 was paid on May 5, 2003.

Stock-Based Compensation As allowed under Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation, Delphi accounts for stock-based compensation using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. Stock options granted during the three months ended June 30, 2003 were exercisable at prices equal to the fair market value of Delphi common stock on the dates the options were granted; accordingly, no compensation expense has been recognized for the stock options granted.

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If we accounted for stock-based compensation using the fair value recognition provisions of SFAS No. 123 and related amendments, our net income and basic and diluted earnings per share would have been as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
	(in millions, except per share amounts)			
Net income, as reported	$ 88	$ 220	$ 215	$ 169
Less: Total stock-based employee compensation expense determined under fair value method for all awards, net of related tax effects	4	11	7	21
Pro forma net income	$ 84	$ 209	$ 208	$ 148
Earnings per share:				
Basic and diluted as reported	$ 0.16	$ 0.39	$ 0.38	$ 0.30
Basic and diluted pro forma	$ 0.15	$ 0.37	$ 0.37	$ 0.26

During 1999, Delphi awarded certain employees approximately 3 million restricted stock units, which were delivered to them as stock during the first quarter of 2003 in accordance with the original award terms. During the first quarter of 2003, we also cancelled approximately 20 million shares available for future grants under the terms of certain of Delphi s stock option plans. In April 2003, we granted 12 million options at a weighted average exercise price of $8.43 per share and 3 million restricted stock units at a weighted average fair market value of $8.43 per share. As of June 30, 2003, there are 9 million shares available for future grants.

2. RESTRUCTURING AND PRODUCT LINE CHARGES

In the first quarter of 2002, Delphi approved restructuring plans to eliminate approximately 6,100 positions from our global workforce, comprised of 3,100 U.S. employees and 3,000 employees in non-U.S. locations, downsize more than 25 selected facilities in the United States and Europe, and exit certain other activities by the end of the first quarter of 2003. The restructuring charge totaled $231 million with $222 million of employee costs (including postemployment benefits and special termination pension benefits) and $9 million in other exit costs (lease and contract cancellation fees). This charge, when netted against a $6 million reversal for the 2001 restructuring reserve, resulted in a net restructuring charge of $225 million ($150 million after-tax) in the first quarter of 2002.

The restructuring actions were completed as planned in the first quarter of 2003. Total cash paid for restructuring was $200 million, with $191 million for employee costs and $9 million for other exit costs. The cash outflows for the first quarter of 2003 were $24 million, with $17 million for employee costs and $7 million for other exit costs.

During the second quarter of 2002, we began to wind down our generator product line. Of the total recorded loss of $231 million ($149 million after-tax) associated with the wind down of this product line, $37 million ($24 million after-tax) for contractually required payments (principally employee related) was recorded in cost of sales during the first quarter of 2002.

3. ASSET SECURITIZATION

In the first quarter of 2003, we entered into a $500 million domestic accounts receivable securitization facility agreement (Facility Agreement) under which we sell certain trade receivables. When we sell receivables, we retain a subordinated interest in the pool of receivables sold, which are considered to be retained interests in the securitized receivables. Losses on the sale of receivables depend in part on the previous carrying amount of the financial assets involved in the transfer, allocated between assets sold and the retained interests based upon their relative fair values at the date of transfer. We determine the fair

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value of the receivables sold and our retained interests using estimated discounted cash flows upon the sale of the receivables and, for the retained interests, at the end of each quarter. The valuation methodology considers historical and projected collections, the discount rate inherent in the Facility Agreement (currently approximately 1.6%) and estimated future credit losses arising from the sold receivables. Due to the short-term nature of trade receivables, the carrying amount approximates fair value of the retained interests. Variation in the credit and discount assumptions would not significantly impact fair value.

Under this Facility Agreement, we have agreed to sell certain accounts receivable to Delphi Receivables LLC (DR), a wholly-owned consolidated special purpose entity. DR may then sell, on a non-recourse basis (subject to certain exceptions relating to receivables that are reduced or cancelled for reasons unrelated to the creditworthiness of the obligor or customary write-offs, are disputed, or for which any representations and warranties are no longer true), an undivided interest in its receivables to certain third parties (the receivable conduits), which are unrelated to Delphi or DR and are expected to be multi-seller conduits that fund their purchase through the issuance of commercial paper, with back-up purchase commitments from the conduits financial institutions. The transfer qualifies for sale treatment under the provisions of SFAS No. 140, Accounting for the Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. The receivables are sold at fair market value and the loss on the sale is recorded in operating income at the time the undivided interest is sold to the third party. We do perform collections and administrative functions on the receivables sold. The nature of such activities and the terms of the Facility Agreement do not result in the recognition of a servicing asset or liability. At June 30, 2003, DR had sold $488 million of undivided interests in its receivables to the receivable conduits; these receivables have been excluded from our consolidated balance sheet. A loss on sale of $2 million was recorded for the three months ended June 30, 2003. During the quarter ended June 30, 2003, proceeds from new securitizations were $828 million and proceeds from reinvested collections were $561 million. As of June 30, 2003, the receivable conduits had a preferential interest in $543 million of the receivables held at DR to secure their interest under the Facility Agreement. The Facility Agreement which is between Delphi, DR, the receivable conduits, financial institutions and their agents, expires on March 31, 2004 and can be extended on an annual basis until March 31, 2006 based upon the mutual agreement of the parties. Additionally, the Facility Agreement contains financial and other covenants similar to our revolving credit facilities that, if not met, would result in a termination of the agreement. At June 30, 2003, we were in compliance with all such covenants.

4. INVENTORIES, NET

Inventories, net consisted of:

	June 30, 2003	December 31, 2002
	(in millions)	
Productive material, work-in-process and supplies	$ 1,534	$ 1,587
Finished goods	552	435
Total inventories at FIFO	2,086	2,022
Less: allowance to adjust the carrying value of certain inventories to LIFO	(253)	(253)
Total inventories, net	$ 1,833	$ 1,769

5. DERIVATIVES AND HEDGING ACTIVITIES

Delphi is exposed to market risk, such as fluctuations in foreign currency exchange rates, commodity prices and changes in interest rates. To manage the volatility relating to these exposures, we aggregate the exposures on a consolidated basis to take advantage of natural offsets. For exposures that are not offset within our operations, we enter into various derivative transactions pursuant to our risk management policies. Designation is performed on a transaction basis to support hedge accounting. The changes in fair value of these hedging instruments are offset in part or in whole by corresponding changes in the fair value

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or cash flows of the underlying exposures being hedged. We assess the initial and ongoing effectiveness of our hedging relationships in accordance with our documented policy. We do not hold or issue derivative financial instruments for trading purposes.

Gains and losses on derivatives qualifying as cash flow hedges are recorded in other comprehensive income (OCI) to the extent that hedges are effective until the underlying transactions are recognized in earnings. Net gains included in OCI as of June 30, 2003, were $18 million after-tax ($29 million pre-tax). Of this pre-tax total, a gain of approximately $20 million is expected to be included in cost of sales within the next 12 months and a gain of approximately $6 million is expected to be included in subsequent periods. A loss of approximately $2 million is expected to be included in depreciation and amortization expense over the lives of the related fixed assets and a gain of approximately $5 million is expected to be included in interest expense over the term of the related debt. The unrealized amounts in OCI will fluctuate based on changes in the fair value of open contracts at each reporting period. Cash flow hedges are discontinued when it is probable that the original forecasted transactions will not occur. The amount included in cost of sales related to hedge ineffectiveness and the time value of options was not material.

6. STOCKHOLDERS EQUITY

Changes in stockholders equity for the six months ended June 30, 2003 were:

	Common Stock		Additional		Accumulated Other Comprehensive Income (Loss)			Total
	Shares	Amount	Paid-in Capital	Retained Earnings	Minimum Pension Liability	Other	Treasury Stock	Stockholders Equity
				(in millions)				
Balance at January 1, 2003.	565	$ 6	$ 2,445	$ 1,530	$ (2,098)	$ (493)	$ (111)	$ 1,279
Net income				215				215
Currency translation adjustments and other, net of tax						159		159
Net change in unrecognized loss on derivative instruments, net of tax						27		27
Total comprehensive income								401
Shares issued for employee benefit plans			17				35	52
Dividends				(79)				(79)
Balance at June 30, 2003	565	$ 6	$ 2,462	$ 1,666	$ (2,098)	$ (307)	$ (76)	$ 1,653

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7. SEGMENT REPORTING

Selected information regarding Delphi s product sectors is as follows:

	Dynamics, Propulsion & Thermal	Electrical, Electronics, Safety & Interior	Automotive Holdings Group	Other(a)	Total
			(in millions)		
For the Three Months Ended:					
June 30, 2003					
Net sales to GM and affiliates	$ 1,920	$ 1,935	$ 458	$	$ 4,313
Net sales to other customers	1,092	1,588	101		2,781
Inter-sector net sales	212	105	206	(523)	
Total net sales	$ 3,224	$ 3,628	$ 765	$ (523)	$ 7,094
Sector operating income (loss)	$ 123	$ 267	$ (158)	$ (60)(c)	$ 172(c)
June 30, 2002(b)					
Net sales to GM and affiliates	$ 2,079	$ 2,159	$ 580	$	$ 4,818
Net sales to other customers	1,030	1,361	113		2,504
Inter-sector net sales	208	97	292	(597)	
Total net sales	$ 3,317	$ 3,617	$ 985	$ (597)	$ 7,322
Sector operating income (loss)	$ 140	$ 318	$ (57)	$ (19)	$ 382
For the Six Months Ended:					
June 30, 2003					
Net sales to GM and affiliates	$ 3,955	$ 3,949	$ 964	$	$ 8,868
Net sales to other customers	2,128	3,079	201		5,408
Inter-sector net sales	404	212	422	(1,038)	
Total net sales	$ 6,487	$ 7,240	$ 1,587	$ (1,038)	$ 14,276
Sector operating income (loss)	$ 243	$ 527	$ (296)	$ (74)(c)	$ 400(c)
June 30, 2002(b)					
Net sales to GM and affiliates	$ 4,041	$ 4,160	$ 1,101	$	$ 9,302
Net sales to other customers	1,955	2,534	219		4,708
Inter-sector net sales	400	188	561	(1,149)	
Total net sales	$ 6,396	$ 6,882	$ 1,881	$ (1,149)	$ 14,010
Sector operating income (loss)	$ 238(d)	$ 558(d)	$ (152)(d)	$ (32)(d)	$ 612(d)

(a) Other includes activity not allocated to the product sectors and elimination of inter-sector transactions.

(b) As previously disclosed, amounts have been reclassified from prior presentation to conform to our new sector alignment.

(c) Includes the second quarter 2003 legal settlement with a former supplier of $38 million.

(d) Excludes the first quarter 2002 net restructuring and generator product line charges of $262 million with $78 million for Dynamics, Propulsion & Thermal, $64 million for Electrical, Electronics, Safety & Interior, $104 million for Automotive Holdings Group (AHG) and $16 million for Other.

8. COMMITMENTS AND CONTINGENCIES

Delphi is from time to time subject to various legal actions and claims incidental to its business, including those arising out of alleged defects, breach of contracts, product warranties, intellectual property matters, environmental matters, and employment-related matters. In particular, as more fully discussed in Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

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Labor Matters, the International Union of Electronic, Electrical, Salaried, Machine & Furniture Workers-Communication Workers of America, AFL-CIO filed a grievance to protest certain planned layoffs at one of our manufacturing sites. The matter was submitted to binding arbitration and the arbitrator ruled that Delphi had assumed an enforceable contract obligation to maintain a minimum employment level at the site but that strict enforcement of that contract was not an appropriate remedy. Instead, the arbitrator ordered the parties to appear at a remedial hearing to discuss and present evidence as to the remedy. The hearing took place in June 2003. We expect a ruling in the second half of 2003.

As previously disclosed, with respect to environmental matters, Delphi received notices that it is a potentially responsible party (PRP) in proceedings at various sites, including the Tremont City Landfill Site located in Tremont, Ohio. The Tremont City Landfill Site proceeding, which is alleged to concern ground water contamination, is in the early stages of investigation and involves multiple other PRPs. Based on the information gathered to date, Delphi has been identified as the largest waste-generator PRP, however, we expect that other parties, including landfill operator and transporter PRPs, will ultimately have to share a significant portion of any overall site costs. In September 2002, Delphi and other PRPs entered into a Consent Order with the Environmental Protection Agency (EPA) to perform a Remedial Investigation and Feasibility Study concerning a portion of the site. The investigation is expected to be completed during 2005, as various EPA reviews are required through each phase of the study. We have reserved approximately $2 million for our share of the expected investigation costs. Current preliminary assessments indicate that a reasonably possible outcome of the investigative study is capping and future monitoring of this site, which would substantially limit future remediation costs. Based on cost estimates received to date, we have included an estimate of the potential costs of capping and future monitoring of the site in our overall reserve estimates. Because the scope of the investigation and the extent of the required remediation are still being determined, it is possible that the final resolution of this matter may require that we make material future expenditures for remediation, possibly over an extended period of time and possibly in excess of our existing reserves. As the investigation proceeds, we will periodically re-assess any potential remediation costs and, as appropriate, our overall environmental reserves.

With respect to warranty matters, as previously disclosed, a few customers have advised Delphi that they intend to pursue warranty claims vigorously. In particular, although in 2001 we settled or resolved most of our known pre-separation warranty claims with GM, as previously disclosed, GM requested that Delphi agree to reimburse GM for the anticipated costs of GM s voluntary recall campaign to repair certain 1996 to 1998 models which GM states could experience a failure of the power steering gear lower pinion bearing. GM may assert additional pre-separation claims in the future. As we have already informed GM, we believe that this claim and the remainder of known pre-separation warranty claims are adequately covered by commercial defenses or customer credits and that we have no further financial liability for such matters. Accordingly, although we cannot ensure that the future costs of warranty claims by GM or other customers will not be material, we believe our established reserves are adequate to cover potential warranty settlements. However, the final amounts determined to be due related to these matters could differ materially from our recorded estimates. Additionally, in connection with our separation from GM, we agreed to indemnify GM against substantially all losses, claims, damages, liabilities or activities arising out of or in connection with our business. Due to the nature of such indemnities we are not able to estimate the maximum amount.

As previously disclosed, the Ninth Circuit Court of Appeals affirmed the federal district court s decision to award one of Delphi s former suppliers approximately $38 million ($25 million after-tax), inclusive of accrued interest, in connection with a commercial dispute. The settlement was included in selling, general and administrative expenses and paid during the third quarter of 2003.

Litigation is subject to many uncertainties, and the outcome of individual litigated matters is not predictable with assurance. After discussions with counsel, it is the opinion of management that the outcome of such matters will not have a material adverse impact on the consolidated financial position, results of operations or cash flows of Delphi.

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On a worldwide basis, Delphi has a concentration of employees working under union collective bargaining agreements representing approximately 91% of its hourly workforce. A significant proportion of the U.S. union employees labor agreements expire beginning in September 2003. Certain suppliers and customers of Delphi also have union represented work forces. Future work stoppages by Delphi employees or employees of Delphi s suppliers or customers could disrupt Delphi s production of automotive components and systems. In addition, our ability to fix certain sites and businesses that have been placed in AHG depend, in part, on our ability to satisfactorily address any labor issues.

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ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations

The following management s discussion and analysis of financial condition and results of operations (MD&A) should be read in conjunction with the MD&A included in our Annual Report on Form 10-K for the year ended December 31, 2002.

Three Months Ended June 30, 2003 versus Three Months Ended June 30, 2002

Net Sales. Consolidated net sales by product sector and in total for the three months ended June 30, 2003 and 2002 were:

	Three Months Ended June 30,	
Product Sector	**2003**	**2002**
	(in millions)	
Dynamics, Propulsion & Thermal	$ 3,224	$ 3,317
Electrical, Electronics, Safety & Interior	3,628	3,617
Automotive Holdings Group	765	985
Other	(523)	(597)
Consolidated net sales	$ 7,094	$ 7,322

Consolidated net sales for the second quarter of 2003 were $7.1 billion compared to $7.3 billion for the same period of 2002. Our non-GM sales increased by $277 million principally due to $223 million of favorable currency exchange rates, increased production volumes and new business from diversifying our global customer base, partially offset by price decreases. As a percent of our net sales for the second quarter of 2003, our non-GM sales were 39%. Net sales to GM decreased by $505 million, due to $484 million of lost production in North America primarily resulting from the tornado stricken GM Oklahoma City facility, price decreases and our decision to exit certain businesses. Continued price pressures resulted in price reductions of approximately $98 million, or 1.3% for the second quarter of 2003 compared to approximately $147 million or 2.1% for the second quarter of 2002.

Gross Margin. Our gross margin was 12.0% for the second quarter of 2003 compared to gross margin of 13.5% for the second quarter of 2002. The decrease reflected approximately $189 million of higher wages and increased U.S. pension and healthcare expenses, lower volumes and price decreases and the acceleration of portfolio related actions, including costs associated with closure of a facility and voluntary early retirements, of approximately $27 million ($18 million after-tax).

Selling, General and Administrative. Selling, general and administrative expenses (SG&A) were $422 million, 5.9% of net sales for the second quarter of 2003, compared to $361 million or 4.9% of total net sales for the second quarter of 2002. SG&A was adversely impacted by a legal settlement to one of our former suppliers of approximately $38 million ($25 million after-tax), in connection with a commercial dispute. Excluding the legal settlement, SG&A was $384 million or 5.4% of net sales.

Depreciation and Amortization. Depreciation and amortization for the second quarter of 2003, which includes $8 million ($5 million after-tax) of portfolio related actions, principally facility closure costs, was consistent with amounts for the comparable period of 2002.

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Operating Income. Operating income was $172 million for the second quarter of 2003 compared to operating income of $382 million for the second quarter of 2002.

Product Sector	Three Months Ended June 30, 2003	Three Months Ended June 30, 2002
	(in millions)	
Dynamics, Propulsion & Thermal	$ 123	$ 140
Electrical, Electronics, Safety & Interior	267	318
Automotive Holdings Group	(158)	(57)
Other	(60)	(19)
Total operating income	$ 172	$ 382

The decrease in operating income from the second quarter of 2002 primarily reflected increased pension, healthcare and wages, lower pricing, the legal settlement in connection with a commercial dispute and the portfolio-related actions referred to above, partially offset by savings realized from our restructuring plans, material cost savings and manufacturing performance. The increase in net sales attributable to currency exchange rates did not significantly impact our operating income, as we manage our currency exposure through hedging techniques, including derivative instruments.

Taxes. Our effective tax rate for the second quarter of 2003 was between 31% and 32% compared to 36% for the second quarter of 2002. The rate for the second quarter of 2003 was affected by entity structuring, which allowed substantial earnings from the Asia-Pacific region to be considered indefinitely reinvested in foreign operations. As compared to our original expectations, during the first six months of 2003 we experienced higher than expected earnings in certain jurisdictions outside of the United States (where effective tax rates are lower than the effective U. S. tax rate), and lower than expected earnings in the United States. We expect that this shift may partially correct over the second six months of 2003. We will re-revaluate our full year tax rate at the end of the third quarter. If current trends continue, our tax rate for the full year may be in the 29%-30% range.

Net Income. As a result of the factors referred to above, our net income was $88 million for the second quarter of 2003 as compared to net income of $220 million for the second quarter of 2002.

Earnings Per Share. Basic and diluted earnings per share was $0.16 for the second quarter of 2003 compared to basic and diluted earnings per share of $0.39 for the second quarter 2002.

Six Months Ended June 30, 2003 versus Six Months Ended June 30, 2002

Net Sales. Consolidated net sales by product sector and in total for the six months ended June 30, 2003 and 2002 were:

Product Sector	Six Months Ended June 30, 2003	Six Months Ended June 30, 2002
	(in millions)	
Dynamics, Propulsion & Thermal	$ 6,487	$ 6,396
Electrical, Electronics, Safety & Interior	7,240	6,882
Automotive Holdings Group	1,587	1,881
Other	(1,038)	(1,149)
Consolidated net sales	$ 14,276	$ 14,010

Consolidated net sales for the first six months of 2003 were $14.3 billion compared to $14.0 billion for the same period of 2002. Our non-GM sales increased by $700 million principally due to $420 million of favorable currency exchange rates, increased production volumes and new business from diversifying our global customer base, partially offset by price decreases. As a percent of our net sales for the six months ended June 30, 2003, our non-GM sales were 38%. Net sales to GM decreased by $434 million, due to $321 million of lost production in North America primarily resulting from the tornado stricken GM Oklahoma City facility, price decreases and our decision to exit certain businesses, partially offset by favorable currency exchange rates. Our net sales also were impacted by continued price pressures that resulted in price reductions of approximately $209 million, or 1.5% for the first six months of 2003 compared to approximately $267 million or 2.0% for the first six months of 2002.

Gross Margin. Our gross margin was 12.1% for the first six months of 2003 compared to gross margin of 12.8% for the first six months of 2002. The decrease reflected approximately $371 million of higher wages and increased U.S. pension and healthcare and price decreases, partially offset by lower material costs, as well as manufacturing performance and savings realized from our restructuring plans. The gross margin for the first six months of 2002 included a charge of $37 million related to our generator product line.

Selling, General and Administrative. Selling, general and administrative expenses was $811 million, 5.7% of total net sales for the first six months of 2003, compared to $723 million or 5.2% of total net sales for the first six months of 2002. Selling, general and administrative expense was adversely impacted by a legal settlement to one of our former suppliers of approximately $38 million ($25 million after-tax), in connection with a commercial dispute. Excluding the legal settlement, selling, general and administrative expenses were $773 million or 5.4% of net sales.

Depreciation and Amortization. Depreciation and amortization for the first six months of 2003 was consistent with amounts for the comparable period of 2002.

Restructuring. In the first quarter of 2002, Delphi approved restructuring plans to eliminate approximately 6,100 positions from our global workforce, comprised of 3,100 U.S. employees and 3,000 employees in non-U.S. locations, downsize more than 25 selected facilities in the United States and Europe, and exit certain other activities by the end of the first quarter of 2003. The restructuring charge totaled $231 million with $222 million of employee costs (including postemployment benefits and special termination pension benefits) and $9 million in other exit costs (lease and contract cancellation fees). This charge, when netted against a $6 million reversal for the 2001 restructuring reserve, resulted in a net restructuring charge of $225 million ($150 million after-tax) in the first quarter of 2002.

The restructuring actions were completed as planned in the first quarter of 2003. Total cash paid for restructuring was $200 million, with $191 million for employee costs and $9 million for other exit costs. The cash outflows for the first quarter of 2003 were $24 million, with $17 million for employee costs and $7 million for other exit costs. We are currently realizing savings, principally payroll and related costs, associated with these restructuring actions and we expect these savings to grow to more than $125 million (after-tax) by early 2004 with reductions of approximately $90 million in cost of sales and approximately $35 million in selling, general and administrative expense. The after-tax breakdown of these savings by sector is expected to be approximately $43 million for Dynamics, Propulsion & Thermal, approximately $36 million for Electrical, Electronics, Safety & Interior, approximately $37 million for Automotive Holdings Group and approximately $9 million for Other.

Operating Income. Operating income was $400 million for the first six months of 2003 compared to operating income of $350 million for the first six months of 2002. To facilitate analysis of our operating

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income by product sector, we have excluded the 2002 net restructuring and product line charges of $262 million from the segment information presented below:

Product Sector	Six Months Ended June 30, 2003	Six Months Ended June 30, 2002(a)
	(in millions)	
Dynamics, Propulsion & Thermal	$ 243	$ 238
Electrical, Electronics, Safety & Interior	527	558
Automotive Holdings Group	(296)	(152)
Other	(74)	(32)
Total operating income	$ 400	$ 612

(a) Excludes the first quarter 2002 net restructuring and generator product line charges of $262 million with $78 million for Dynamics, Propulsion & Thermal, $64 million for Electrical, Electronics, Safety & Interior, $104 million for Automotive Holdings Group and $16 million for Other.

The decrease in operating income from the six months of 2002 primarily reflected increased pension, healthcare and wages, lower pricing, the legal settlement in connection with a commercial dispute and the portfolio-related actions referred to above, partially offset by savings realized from our restructuring plans, material cost savings and manufacturing performance. The increase in net sales attributable to currency exchange rates did not significantly impact our operating income, as we manage our currency exposure through hedging techniques, including derivative instruments.

Taxes. Our effective tax rate for the first six months of 2003 was between 31% and 32% compared to 38% for the comparable period of 2002. The rate for the first six months of 2003 was affected by entity structuring, which allowed substantial earnings from the Asia-Pacific region to be considered indefinitely reinvested in foreign operations. As compared to our original expectations, during the first six months of 2003 we experienced higher than expected earnings in certain jurisdictions outside of the United States (where effective tax rates are lower than the effective U. S. tax rate), and lower than expected earnings in the United States. We expect that this shift may partially correct over the second six months of 2003. We will re-revaluate our full year tax rate at the end of the third quarter. If current trends continue, our tax rate for the full year may be in the 29%-30% range. The rate for the six months of 2002 reflected our inability to fully tax effect our restructuring initiatives in certain jurisdictions. The effective tax rate for the full year 2002 was 35%.

Net Income. As a result of the factors referred to above, our net income was $215 million for the first six months of 2003 as compared to net income of $169 million for the first six months of 2002.

Earnings Per Share. Basic and diluted earnings per share was $0.38 for the six months of 2003 compared to basic and diluted earnings per share of $0.30, for the first six months of 2002.

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Our segment data shown above is based on our realigned sectors; for comparative purposes, the financial data for all the quarterly periods in 2002 is shown below:

	Dynamics, Propulsion & Thermal	Electrical, Electronics, Safety & Interior	Automotive Holdings Group	Other(a)	Total
			(in millions)		
For the Three Months Ended March 31, 2002					
Net sales to GM and affiliates	$ 1,962	$ 2,001	$ 521	$	