NAVISTAR INTERNATIONAL CORP
Form 10-Q
June 09, 2009
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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 April 30, 2009

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from To

Commission file number 1-9618

NAVISTAR INTERNATIONAL CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**36-3359573**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
4201 Winfield Road, P.O. Box 1488, Warrenville, Illinois	**60555**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code (630) 753-5000

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 ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the proceeding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

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 definition of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act.) Yes ¨ No x.

As of May 31, 2009, the number of shares outstanding of the registrant s common stock was 70,300,666, net of treasury shares.

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Disclosure Regarding Forward-Looking Statements

Information provided and statements contained in this report that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (Securities Act), Section 21E of the Securities Exchange Act of 1934, as amended (Exchange Act), and the Private Securities Litigation Reform Act of 1995. Such forward-looking statements only speak as of the date of this report and the Navistar International Corporation (the Company) assumes no obligation to update the information included in this report. Such forward-looking statements include information concerning our possible or assumed future results of operations, including descriptions of our business strategy. These statements often include words such as believe, expect, anticipate, intend, plan, estimate, or similar expressions. statements are not guarantees of performance or results and they involve risks, uncertainties, and assumptions. For a further description of these factors, see Item 1A, *Risk Factors*, included within our Form 10-K for the year ended October 31, 2008, which was filed on December 30, 2008, and Item 1A, *Risk Factors*, included in this report. Although we believe that these forward-looking statements are based on reasonable assumptions, there are many factors that could affect our actual financial results or results of operations and could cause actual results to differ materially from those in the forward-looking statements. All future written and oral forward-looking statements by us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to above. Except for our ongoing obligations to disclose material information as required by the federal securities laws, we do not have any obligations or intention to release publicly any revisions to any forward-looking statements to reflect events or circumstances in the future or to reflect the occurrence of unanticipated events.

Available Information

We are subject to the reporting and information requirements of the Exchange Act and as a result, are obligated to file periodic reports, proxy statements, and other information with the United States Securities and Exchange Commission (SEC). We make these filings available free of charge on our website (http://www.navistar.com) as soon as reasonably practicable after we electronically file them with, or furnish them to, the SEC. The SEC

maintains a website (http://www.sec.gov) that contains our annual, quarterly, and current reports, proxy and information statements, and other information we file electronically with the SEC. You can read and copy any materials we file with the SEC at the SEC s Public Reference Room at 100 F Street, N.E., Room 1850, Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Information on our website does not constitute part of this Quarterly Report on Form 10-Q.

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PART I

Item 1. Condensed Consolidated Financial Statements

Navistar International Corporation and Subsidiaries

Consolidated Statements of Operations

(Unaudited)

(in millions, except per share data)	Three Months Ended April 30, 2009	Three Months Ended April 30, 2008	Six Months Ended April 30, 2009	Six Months Ended April 30, 2008
Sales and revenues				
Sales of manufactured products, net	**$ 2,741**	$ 3,853	**$ 5,636**	$ 6,713
Finance revenues	**67**	96	**142**	190
Sales and revenues, net	**2,808**	3,949	**5,778**	6,903
Costs and expenses				
Costs of products sold	**2,295**	3,200	**4,618**	5,663
Restructuring charges	**(3)**		**55**	
Selling, general and administrative expenses	**300**	364	**676**	685
Engineering and product development costs	**130**	99	**238**	181
Interest expense	**57**	102	**150**	269
Other (income) expense, net	**22**	(4)	**(176)**	(5)
Total costs and expenses	**2,801**	3,761	**5,561**	6,793
Equity in income of non-consolidated affiliates	**14**	21	**31**	45
Income before income tax	**21**	209	**248**	155
Income tax benefit (expense)	**(9)**	2	**(2)**	(9)
Net income	**$ 12**	$ 211	**$ 246**	$ 146
Basic earnings per share	**$ 0.16**	$ 3.00	**$ 3.45**	$ 2.08
Diluted earnings per share	**$ 0.16**	$ 2.88	**$ 3.44**	$ 2.00
Weighted average shares outstanding				
Basic	**70.8**	70.3	**71.2**	70.3
Diluted	**71.3**	73.2	**71.5**	72.9

See Notes to Condensed Consolidated Financial Statements

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Navistar International Corporation and Subsidiaries

Consolidated Balance Sheets

(in millions, except per share data)	April 30, 2009 (Unaudited)	October 31, 2008
ASSETS		
Current assets		
Cash and cash equivalents	**$ 718**	$ 861
Marketable securities		2
Trade and other receivables, net	**794**	1,025
Finance receivables, net	**1,655**	1,789
Inventories	**1,646**	1,628
Deferred taxes, net	**75**	75
Other current assets	**161**	155
Total current assets	**5,049**	5,535
Restricted cash and cash equivalents	**651**	557
Trade and other receivables, net	**33**	31
Finance receivables, net	**1,713**	1,948
Investments in and advances to non-consolidated affiliates	**154**	156
Property and equipment (net of accumulated depreciation and amortization of $1,698 and $1,603, at the respective dates)	**1,419**	1,501
Goodwill	**287**	297
Intangible assets (net of accumulated amortization of $84 and $74, at the respective dates)	**211**	232
Deferred taxes, net	**46**	41
Other noncurrent assets	**94**	92
Total assets	**$ 9,657**	$ 10,390
LIABILITIES, REDEEMABLE EQUITY SECURITIES, AND STOCKHOLDERS DEFICIT		
Liabilities		
Current liabilities		
Notes payable and current maturities of long-term debt	**$ 579**	$ 665
Accounts payable	**1,525**	2,027
Other current liabilities	**1,160**	1,183
Total current liabilities	**3,264**	3,875
Long-term debt	**5,070**	5,409
Postretirement benefits liabilities	**1,995**	1,646
Deferred taxes, net	**97**	103
Other noncurrent liabilities	**664**	709
Total liabilities	**11,090**	11,742
Redeemable equity securities	**14**	143
Stockholders deficit		
Series D convertible junior preference stock	**4**	4
Common stock ($0.10 par value per share, 110.0 shares authorized, 75.4 shares issued at both dates)	**7**	7
Additional paid in capital	**2,104**	1,966
Accumulated deficit	**(2,146)**	(2,392)
Accumulated other comprehensive loss	**(1,252)**	(943)
Common stock held in treasury, at cost (5.1 and 4.1 shares, at the respective dates)	**(164)**	(137)

Total stockholders deficit		**(1,447)**		(1,495)
Total liabilities, redeemable equity securities, and stockholders deficit	**$**	**9,657**	$	10,390

See Notes to Condensed Consolidated Financial Statements

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Navistar International Corporation and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(in millions)	Six Months Ended April 30, 2009	2008
Cash flows from operating activities		
Net income	**$ 246**	$ 146
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation and amortization	**140**	156
Depreciation of equipment held for or under lease	**27**	30
Deferred taxes	**(2)**	5
Amortization of debt issuance costs	**8**	10
Stock-based compensation	**11**	2
Provision for doubtful accounts	**28**	18
Impairment of goodwill and intangibles	**7**	
Equity in income of non-consolidated affiliates	**(31)**	(45)
Dividends from non-consolidated affiliates	**47**	29
(Gain) loss on sales of affiliates	**1**	(4)
(Gain) loss on sale of property and equipment	**3**	(2)
Loss on sale and impairment of repossessed vehicle inventory	**15**	4
Loss on sale of finance receivables	**25**	7
Restructuring charges	**55**	
Changes in other assets and liabilities	**(93)**	(35)
Net cash provided by operating activities	**487**	321
Cash flows from investing activities		
Purchases of marketable securities	**(354)**	(42)
Sales or maturities of marketable securities	**356**	11
Net change in restricted cash and cash equivalents	**(96)**	(316)
Capital expenditures	**(77)**	(103)
Purchase of equipment leased to others	**(18)**	(14)
Proceeds from sales of property and equipment	**4**	19
Investments and advances to non-consolidated affiliates	**(14)**	(4)
Proceeds from sales of affiliates	**3**	19
Other investing activities		(1)
Net cash used in investing activities	**(196)**	(431)
Cash flows from financing activities		
Proceeds from issuance of securitized debt	**321**	815
Principal payments on securitized debt	**(658)**	(980)
Proceeds from issuance of non-securitized debt	**259**	74
Principal payments on non-securitized debt	**(362)**	(8)
Net increase in notes and debt outstanding under revolving credit facilities	**71**	162
Principal payments under financing arrangements and capital lease obligations	**(24)**	(51)
Debt issuance costs	**(2)**	(7)
Stock repurchase	**(29)**	

Net cash provided by (used in) financing activities	**(424)**	5
Effect of exchange rate changes on cash and cash equivalents	**(10)**	3
Decrease in cash and cash equivalents	**(143)**	(102)
Cash and cash equivalents at beginning of period	**861**	777
Cash and cash equivalents at end of the period	**$ 718**	$ 675

See Notes to Condensed Consolidated Financial Statements

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Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Summary of significant accounting policies

Organization and Description of the Business

Navistar International Corporation (NIC), incorporated under the laws of the state of Delaware in 1993, is a holding company whose principal operating subsidiaries are Navistar, Inc. and Navistar Financial Corporation (NFC). References herein to the Company, we, our, or us refer collectively to NIC, its subsidiaries, and certain variable interest entities (VIEs) of which we are the primary beneficiary. We operate in four principal industry segments: Truck, Engine, Parts (collectively called manufacturing operations), and Financial Services. The Financial Services segment consists of NFC and our foreign finance operations (collectively called financial services operations).

Basis of Presentation and Consolidation

The accompanying unaudited condensed consolidated financial statements include the assets, liabilities, and results of operations of our manufacturing operations, majority-owned dealers (Dealcors), wholly-owned financial services subsidiaries, and VIEs of which we are the primary beneficiary. The effects of transactions among consolidated entities have been eliminated to arrive at the consolidated amounts. Certain reclassifications were made to prior year s amounts to conform to the 2009 presentation.

We prepared the accompanying unaudited condensed consolidated financial statements in accordance with United States (U.S.) generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X issued by the SEC. Accordingly, they do not include all of the information and notes required by U.S. GAAP for comprehensive annual financial statements.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting policies described in our Annual Report on Form 10-K for the year ended October 31, 2008 and should be read in conjunction with the disclosures therein. In our opinion, these interim financial statements reflect all adjustments, consisting of normal recurring adjustments, necessary to present fairly the financial condition, results of operations, and cash flows for the periods presented. Operating results for interim periods are not necessarily indicative of annual operating results.

Variable Interest Entities

We are the primary beneficiary of several VIEs, primarily joint ventures, established to manufacture or distribute products and enhance our operational capabilities. Our determination that we are the primary beneficiary of these entities is based upon the characteristics of our variable interests, which absorb the majority of the VIE s expected gains and losses. Accordingly, we include in our consolidated financial statements the assets and liabilities and results of operations of those entities, even though we may not own a majority voting interest. The liabilities recognized as a result of consolidating these VIEs do not represent additional claims on our general assets; rather they represent claims against the specific assets of the consolidated entities. Assets recognized as a result of consolidating these entities are not available to satisfy claims against our general assets.

Our Financial Services segment consolidates several VIEs. As a result, our consolidated balance sheets include assets of $1.9 billion and $2.2 billion and liabilities of $1.7 billion and $2.0 billion as of April 30, 2009 and October 31, 2008, respectively, from securitizations by VIEs that are treated as borrowings. In addition, our consolidated balance sheets include assets of $751 million and $727 million and related liabilities of $633 million and $632 million as of April 30, 2009 and October 31, 2008, respectively, from structures in which we

Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

transferred assets to consolidated special purpose entities (SPEs) that are not VIEs, which in turn arranged securitizations. Investors that hold on-balance sheet securitization debt have a priority claim on the cash flows generated by their respective securitized assets to the extent required to repay principal and interest. Investors in securitizations with these VIEs and SPEs have no recourse to the general credit of NIC or any other consolidated entity.

Our Financial Services segment does not consolidate a qualifying special purpose entity (QSPE) that is outside the scope of Financial Accounting Standards Board (FASB) Interpretation (FIN) No. 46(R), *Consolidation of Variable Interest Entities An Interpretation of ARB No. 51,* and a conduit since we are not its primary beneficiary. We obtain funds from the QSPE and conduit through consolidated SPEs, which transfer assets to the QSPE and conduit in securitizations. Portions of the transferred assets are accounted for as sales and accordingly those portions are not carried on our consolidated balance sheets. Our consolidated SPEs retain residual economic interests in the future cash flows of the securitized assets that are owned by the QSPE and conduit. We carry these interests as an asset, included in *Finance receivables, net* on our consolidated balance sheets. Retained interests are subordinated to the priority claims of investors in each respective securitization; our maximum loss exposure to the activities of the QSPE and conduit is limited to our retained interests. See Note 4, *Finance receivables*, for further discussion.

We are also involved with other VIEs, which we do not consolidate because we are not the primary beneficiary. Our determination that we are not the primary beneficiary of these entities is based upon the characteristics of our variable interests, which do not absorb the majority of the VIE s expected gains and losses. Our financial support and maximum loss exposure relating to these non-consolidated VIEs is not material to our financial condition, results of operations, or cash flows.

We use the equity method to account for our investments in entities that we do not control under the voting interest or variable interest models, but where we have the ability to exercise significant influence over operating and financial policies. Consolidated net income includes our share of the net earnings of these entities. As of April 30, 2009, we use the equity method to account for investments in 18 partially-owned affiliates, in which NIC or one of its subsidiaries is a shareholder, general or limited partner, or venturer, as applicable, including our 49 percent interest in Blue Diamond Parts (BDP), a VIE which we do not consolidate because we are not the primary beneficiary. See Note 6, *Investments in and advances to non-consolidated affiliates*, for further discussion.

Out-Of-Period Adjustments

Included in the results of operations for the three months and six months ended April 30, 2009 are certain out-of-period adjustments which represent corrections of prior-period errors. These errors primarily relate to overstatements of *Accounts payable* of $9 million due to processing errors in our Truck segment that originated in the fourth quarter of 2008 and $10 million due to errors in self-insurance reserve calculations and related intercompany transaction eliminations between our financial services operations and our manufacturing operations that originated primarily in periods prior to 2008. Correcting these errors, which were not material to any of the related periods, resulted in a $19 million increase to net income for the three and six month periods ended April 30, 2009.

Recently Adopted Accounting Standards

As of January 31, 2009, we adopted FASB Staff Position (FSP) No. FAS 140-4 and FIN 46(R)-8, *Disclosures about Transfers of Financial Assets and Interests in Variable Interest Entities.* This FSP requires enhanced

Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

disclosures about a transferor s continuing involvement with transferred financial assets and an enterprise s involvement with VIEs and SPEs. We have complied with the disclosure requirements of this FSP as stated above and within Note 4, *Finance receivables*.

As of November 1, 2008, we adopted FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*. The statement permits entities to choose to measure many financial instruments and certain other items at fair value. We elected to not measure any of our financial assets or financial liabilities at fair value that were not previously required to be measured at fair value; therefore, the adoption of this statement did not impact our condensed consolidated financial statements.

As of November 1, 2008, we adopted FASB Statement No. 157, *Fair Value Measurements*. The statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. In February 2008, the FASB issued FSPs that (i) deferred the effective date of this statement for one year for certain nonfinancial assets and nonfinancial liabilities and (ii) removed certain leasing transactions from the scope of the statement. There was no adjustment to *Accumulated deficit* as a result of our adoption of FASB Statement No. 157. The disclosures required by this statement are included in Note 8, *Fair value measurements*.

In March 2008, the FASB issued FASB Statement No. 161, *Disclosures about Derivative Instruments and Hedging Activities*. The statement amends and expands the disclosure requirements of FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*. FASB Statement No. 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The disclosures required by this statement are included in Note 11, *Financial instruments and commodity contracts*.

Recently Issued Accounting Standards

Accounting pronouncements issued by various standard setting and governmental authorities that have not yet become effective with respect to our consolidated financial statements are described below, together with our assessment of the potential impact they may have on our consolidated financial statements:

In April 2009, the FASB issued FSP 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments*. This statement amends FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, to require disclosures about fair value of financial instruments for interim periods ending after June 15, 2009. Our effective date is July 31, 2009.

In April 2008, the FASB issued FSP No. FAS 142-3, *Determination of the Useful Life of Intangible Assets*, that amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement No. 142, *Goodwill and Other Intangible Assets*. It is effective for financial statements issued for fiscal years beginning after December 15, 2008 and interim periods within those fiscal years and should be applied prospectively to intangible assets acquired after the effective date. Early adoption is not permitted. The FSP also requires expanded disclosure related to the determination of useful lives for intangible assets and should be applied to all intangible assets recognized as of, and subsequent to, the effective date. Our effective date is November 1, 2009. The impact of FSP No. FAS 142-3 will depend on the size and nature of acquisitions on or after November 1, 2009.

In February 2008, the FASB issued FSP No. FAS 157-2, *Effective Date of FASB Statement No. 157*, that permits companies to partially defer the effective date of FASB Statement No. 157 for one year for nonfinancial assets

Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. FSP No. FAS 157-2 does not permit companies to defer recognition and disclosure requirements for financial assets and financial liabilities or for nonfinancial assets and nonfinancial liabilities that are remeasured at least annually. We have decided to defer adoption of FASB Statement No. 157 until November 1, 2009 for nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in our consolidated financial statements on a nonrecurring basis. Our significant nonfinancial assets and liabilities that could be impacted by this deferral include assets and liabilities measured at fair value in a business combination as well as goodwill, tangible assets, and intangible assets tested for impairment. We are evaluating the potential impact on our consolidated financial statements, if any.

In December 2008, the FASB issued FSP No. FAS 132(R)-1, *Employers Disclosures about Postretirement Benefit Plan Assets*, that provides guidance on an employer s disclosures about plan assets of a defined benefit pension or other postretirement plan. Our effective date is October 31, 2010.

In December 2007, the FASB issued FASB Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements An Amendment of ARB No. 51*, that clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity. It is effective for fiscal years and interim periods within those fiscal years, beginning on or after December 15, 2008. Our effective date is November 1, 2009. Upon adoption, our minority interests will be reported as a separate component of *Stockholders deficit*.

In December 2007, the FASB issued FASB Statement No. 141(R), *Business Combinations*, that substantially changes the accounting for and reporting of business combinations including (i) expanding the definition of a business and a business combination, (ii) requiring all assets and liabilities of the acquired business, including goodwill and contingent consideration to be recorded at fair value on the acquisition date, (iii) requiring acquisition-related transaction and restructuring costs to be expensed rather than accounted for as acquisition costs, and (iv) requiring reversals of valuation allowances related to acquired deferred tax assets and changes to acquired income tax uncertainties to be recognized in earnings. FASB Statement No. 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. An entity may not apply the statement before that date. Our effective date is November 1, 2009. This statement will generally apply prospectively to business combinations for which the acquisition date is on or after that date; however, adjustments made to deferred tax asset valuation allowances arising from business combinations before the effective date are subject to the provisions of FASB Statement No. 141(R).

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses. Significant estimates and assumptions are used for, but are not limited to, pension and other postretirement benefits, allowance for doubtful accounts, sales of receivables, income tax contingency accruals and valuation allowances, product warranty accruals, asbestos accruals, asset impairment, and litigation-related accruals. Actual results could differ from our estimates.

Concentration Risks

Our financial condition, results of operations, and cash flows are subject to concentration risks related to concentrations of union employees and two customers. As of April 30, 2009, approximately 6,000, or 63%, of

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Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

our hourly workers and approximately 760, or 10%, of our salaried workers are represented by labor unions and are covered by collective bargaining agreements. Our collective bargaining agreement with the National Automobile, Aerospace and Agricultural Implement Workers of Canada expires on June 30, 2009. As of April 30, 2009, approximately 800, or 8%, of our hourly workers and approximately 100, or 1%, of our salaried workers are covered by this collective bargaining agreement. See Note 16, *Segment reporting*, for discussion of customer concentrations. Additionally, our future operations may be affected by changes in governmental procurement policies, budget considerations, changing national defense requirements, and global, political, and economic developments in the U.S. and certain foreign countries (primarily Canada, Mexico, Brazil, and Argentina).

Product Warranty Liability

Accrued product warranty and deferred warranty revenue activity is as follows:

	Six Months Ended April 30,	
(in millions)	**2009**	**2008**
Balance, at beginning of period	**$ 602**	$ 677
Costs accrued and revenues deferred	**102**	100
Adjustments to pre-existing warranties[A]	**78**	5
Payments and revenues recognized	**(180)**	(174)
Warranty adjustment related to legal settlement[B]	**(75)**	
Balance, at end of period	**$ 527**	$ 608

(A) Adjustments to pre-existing warranties reflect changes in our estimate of warranty costs for products sold in prior periods. Such adjustments typically occur when claims experience deviates from historic and expected trends. The adjustments were $61 million and $78 million for the three months and six months ended April 30, 2009. The adjustments were $0.86 per diluted share and $1.09 per diluted share for the three months and six months ended April 30, 2009, respectively.

(B) See Note 2, *Ford settlement and related charges*, for a discussion regarding warranty adjustments related to the Ford Settlement.

The amount of deferred revenue related to extended warranty programs was $129 million at April 30, 2009 and October 31, 2008. Revenue recognized under our extended warranty programs was $10 million and $20 million for the three months and six months ended April 30, 2009, respectively, and $12 million and $23 million for the three months and six months ended April 30, 2008, respectively.

2. Ford settlement and related charges

In January 2009, we reached a settlement agreement with Ford Motor Company (Ford) where we agreed to settle our respective lawsuits against each other (the Ford Settlement). The result of the Ford Settlement resolves all prior warranty claims, resolves the selling price for our engines going forward and allows Ford to pursue a separate strategy related to diesel engines in its products. Additionally, both companies agreed to end their current North America supply agreement for diesel engines as of December 31, 2009 (the agreement was otherwise set to expire July 2012). For additional information on the Ford Settlement, see Note 12, *Commitments and contingencies*.

In the third and fourth quarters of 2008, the Engine segment recognized $395 million of charges for impairments of property and equipment and related charges associated with its asset groups in the VEE Business Unit. The

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Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

impairment charges were the result of a reduction in demand from Ford for diesel engines produced by the VEE Business Unit and the expectation that Ford s demand for diesel engines would continue to be below previously anticipated levels.

In the first quarter of 2009, in connection with the Ford Settlement we received a $200 million cash payment from Ford, which was recorded as a gain in *Other (income) expense, net,* and we reversed our previously recorded warranty liability of $75 million, which was recorded as a reduction of *Costs of products sold*. With the changes in Ford s strategy, we announced our intentions to close our Indianapolis Engine Plant (IEP) and our Indianapolis Casting Corporation foundry (ICC) and the Engine segment recognized $58 million of restructuring charges and $27 million of other related charges. The restructuring charges consisted of $21 million in personnel costs for employee termination and related benefits, $16 million of charges for pension and other postretirement benefit contractual termination benefits and a pension curtailment, and $21 million of other contractual costs. The other related charges consisted of $21 million related to inventory valuation and low volume adjustments in *Costs of products sold* and $6 million of indirect employee costs in *Selling, general and administrative expenses.* We expect the majority of the restructuring and other costs, excluding pension and other postretirement related costs, will be paid by the end of 2009, with the balance paid in 2010.

The following table summarizes the activity in the restructuring liability, which excludes $16 million of charges for pension and other postretirement benefits, contractual termination benefits, and the pension curtailment for 2009:

(in millions)	Balance at October 31, 2008	Additions	Payments	Adjustments	Balance at April 30, 2009
Employee termination charges	$	$ 21	$	$ (3)	**$ 18**
Other contractual costs		21			**21**
	$	$ 42	$	$ (3)	**$ 39**

In the second quarter of 2009, the Engine segment recognized an additional $41 million of other related charges primarily related to low volume adjustments of which $17 million were recognized in *Costs of products sold* and $24 million were recognized in *Other (income) expense, net*. In addition, $6 million of indirect employee costs were reversed from *Selling, general and administrative expenses* due to revisions to reflect our expected results.

Due to the loss of the business with Ford, we continue to resolve commercial disputes with certain suppliers and to evaluate alternatives to improve our ongoing cost structure. Such actions may subject us to additional discrete charges in future periods, which could be material. Additionally as a part of the Ford Settlement, we expect to increase our interest in our Blue Diamond Truck (BDT) and BDP joint ventures with Ford to 75%. We are currently evaluating the appropriate accounting treatment for the transaction as it relates to the expected increased ownership of BDT and BDP.

Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

3. Allowance for doubtful accounts

The activity related to our allowance for doubtful accounts for trade and other receivables and finance receivables is summarized as follows:

	Three Months Ended April 30,		Six Months Ended April 30,	
(in millions)	**2009**	**2008**	**2009**	**2008**
Balance, at beginning of period	**$ 109**	$ 107	**$ 113**	$ 101
Provision for doubtful accounts	**26**	6	**28**	18
Charge-off of accounts, net of recoveries	**(13)**	(20)	**(19)**	(26)
Balance, at end of period	**$ 122**	$ 93	**$ 122**	$ 93

Impaired finance receivables include accounts with specific loss reserves and accounts that are on non-accrual status. Most balances with specific loss reserves are also on a non-accrual status. In certain cases, we continue to collect payments on our impaired finance receivables.

Information regarding impaired finance receivables is as follows:

	As of	
(in millions)	**April 30, 2009**	**October 31, 2008**
Impaired finance receivables with specific loss reserves	**$ 59**	$ 56
Impaired finance receivables without specific loss reserves	**4**	4
Specific loss reserves on impaired finance receivables	**28**	21
Finance receivables on non-accrual status	**65**	61
Average balance of impaired finance receivables	**61**	47

Repossessions

We repossess sold and leased vehicles on defaulted finance receivables and leases, and place them into *Inventories*. We liquidate these repossessions to partially recover the credit losses in our portfolio. Losses recognized at the time of repossession and charged against the allowance for doubtful accounts were $11 million and $15 million for the three months and six months ended April 30, 2009, respectively, and $12 million and $16 million for the three months and six months ended April 30, 2008, respectively. Losses recognized upon the sale of repossessed vehicles were $1 million and $6 million for the three months and six months ended April 30, 2009, respectively, and $4 million for the three months and six months ended April 30, 2008.

A summary of the activity related to repossessed vehicles is as follows:

Three Months Ended April 30,	Six Months Ended April 30,

(in millions)	2009	2008	2009	2008
Repossessed vehicles, at beginning of period	**$ 37**	$ 31	**$ 45**	$ 25
Repossessions	**21**	42	**36**	62
Liquidations	**(24)**	(25)	**(41)**	(39)
Impairments	**(3)**		**(9)**	
Repossessed vehicles, at end of period	**$ 31**	$ 48	**$ 31**	$ 48

Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

4. Finance receivables

Finance receivables are receivables of our financial services operations, which generally can be repaid or refinanced without penalty prior to contractual maturity. Total finance receivables reported on the consolidated balance sheets are net of an allowance for doubtful accounts.

The primary business of our financial services operations is to provide wholesale, retail, and lease financing for new and used trucks sold by us and our dealers and, as a result, our finance receivables and leases are concentrated in the trucking industry. On a geographic basis, there is not a disproportionate concentration of credit risk in any area of the U.S. or other countries where we have financial service operations. We retain as collateral an ownership interest in the equipment associated with leases and, on our behalf and the behalf of the various trusts, we maintain a security interest in equipment associated with generally all finance receivables.

All of the assets of our financial services operations are restricted through security agreements to benefit the creditors of the respective finance subsidiary. Total on-balance sheet assets of our financial services operations are $4.6 billion and $4.9 billion at April 30, 2009 and October 31, 2008, respectively. Included in total assets are on-balance sheet finance receivables of $3.4 billion and $3.7 billion at April 30, 2009 and October 31, 2008, respectively.

Securitizations

Our financial services operations transfer wholesale notes, accounts receivable, retail notes, finance leases, and operating leases through SPEs which generally are only permitted to purchase these assets, issue asset-backed securities, and make payments on the securities. In addition to servicing receivables, our continued involvement in the SPEs includes an economic interest in the transferred receivables and managing exposure to interest rates using interest rate swaps, interest rate caps, and forward contracts. Certain sales of wholesale notes and accounts receivables are considered to be sales in accordance with FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, and are accounted for off-balance sheet. For sales that do qualify for off-balance sheet treatment, an initial gain (loss) is recorded at the time of the sale while servicing fees and excess spread income are recorded as revenue when earned over the life of the finance receivables.

We securitized finance receivables and investment in operating leases of $309 million and $321 million under secured borrowings for the three and six month periods ended April 30, 2009, respectively, and $305 million and $815 million for the three and six month periods ended April 30, 2008, respectively.

Off-Balance Sheet Securitizations

We use an SPE that has in place a revolving wholesale note trust, which is a QSPE, which provides for the funding of eligible wholesale notes through an investor certificate and a variable funding certificate. The SPE owned $738 million of wholesale notes and $54 million of marketable securities as of April 30, 2009, and $819 million of wholesale notes and $95 million of marketable securities as of October 31, 2008. The QSPE holds $99 million and $97 million of wholesale notes with our Dealcors as of April 30, 2009 and October 31, 2008, respectively.

Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Components of available wholesale note trust funding certificates were as follows:

(in millions)	Maturity	As of April 30, 2009	As of October 31, 2008
Investor certificate	February 2010	**$ 212**	$ 212
Variable funding certificate	October 2009	**750**	800
Total wholesale note funding		**$ 962**	$ 1,012

Unutilized funding related to the variable funding certificate was $300 million and $250 million at April 30, 2009 and October 31, 2008, respectively.

We use another SPE of which we are not the primary beneficiary. The SPE utilizes a $100 million conduit funding arrangement which provides for the funding of eligible accounts receivables. The conduit matures in August 2009. The trust owned $113 million of retail accounts and $21 million of marketable securities as of April 30, 2009, and $123 million of retail accounts and $23 million of marketable securities as of October 31, 2008. There was $86 million and $52 million of unutilized funding at April 30, 2009 and October 31, 2008, respectively.

For sold receivables, wholesale notes balances past due over 60 days were $3 million as of April 30, 2009 and October 31, 2008. There were no past due retail balances for the accounts receivable financing at either date. No credit losses on sold receivables were recorded for the three months and six months ended April 30, 2009 and 2008.

Retained Interests in Off-Balance Sheet Securitizations

The terms of receivable transfers generally require our financial services operations to provide credit enhancements in the form of excess seller s interests and/or cash reserves, which are owned by the trust and conduit. The maximum exposure under all credit enhancements was $239 million and $230 million as of April 30, 2009 and October 31, 2008, respectively.

Retained interests, which arise from the credit enhancements, represent the fair value of the excess of the cash flows from the assets held by the QSPE and conduit over the future payments of debt service to investors in the QSPE and conduit. The securitization agreements entitle us to these excess cash flows. Our retained interests are restricted assets that are subordinated to the interests of the investors in the QSPE and conduit. Our retained interests are recognized as an asset in *Finance receivables, net.*

The key economic assumptions and the sensitivity of the current fair values of residual cash flows comprising our retained interests to an immediate adverse change of 10 percent and 20 percent in each assumption are as follows:

(dollars in millions)	As of April 30, 2009	As of October 31, 2008	Fair Value Change at April 30, 2009 Adverse 10%	Fair Value Change at April 30, 2009 Adverse 20%

Discount rate	**14.1 to 26.9%**	14.6 to 23.0%	**$ 2.5**	**$ 4.9**
Estimated credit losses	**0.0 to 0.24%**	0.0 to 0.24%	**0.1**	**0.1**
Payment speed (percent of portfolio per month)	**6.8 to 69.1%**	8.8 to 75.7%	**0.5**	**0.9**

Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

The lower end of the discount rate assumption range and the upper end of the payment speed assumption range were used to value the retained interests in the retail account securitization. No percentage for estimated credit losses were assumed for retail account securitizations as no losses have been incurred to date. The upper end of the discount rate assumption range and the lower end of the payment speed assumption range were used to value the retained interests in the wholesale note securitization facility.

The effect of a variation of a particular assumption on the fair value of the retained interests is calculated based upon changing one assumption at a time. Oftentimes however, changes in one factor may result in changes in another, which in turn could magnify or counteract these reported sensitivities.

Finance Revenues

Finance revenues derived from receivables that are both on and off-balance sheet consist of the following:

	Three Months Ended April 30,		Six Months Ended April 30,	
(in millions)	**2009**	**2008**	**2009**	**2008**
Finance revenues from on-balance sheet receivables:				
Retail notes and finance leases revenue	**$ 62**	$ 92	**$ 126**	$ 172
Operating leases revenue	**5**	6	**11**	11
Wholesale notes interest	**3**	7	**11**	15
Retail and wholesale accounts interest	**5**	8	**10**	16
Other income (loss)	**2**	(3)	**2**	2
Total finance revenues from on-balance sheet receivables	**77**	110	**160**	216
Revenues from off-balance sheet securitization:				
Fair value adjustments	**10**	2	**29**	5
Excess spread income	**9**	6	**11**	11
Servicing fees revenue	**2**	3	**4**	6
Losses on sale of finance receivables	**(10)**	(4)	**(25)**	(7)
Investment revenue			**2**	2
Securitization Income	**11**	7	**21**	17
Gross revenue from off-balance sheet securitization	**88**	117	**181**	233
Less: Intercompany revenues	**(21)**	(21)	**(39)**	(43)
Finance revenues	**$ 67**	$ 96	**$ 142**	$ 190

Cash flows from off-balance sheet securitization transactions are as follows:

	Three Months Ended April 30,	Six Months Ended April 30,

(in millions)	2009	2008	2009	2008
Proceeds from finance receivables	**$ 898**	$ 1,006	**$ 1,940**	$ 1,817
Servicing fees	**2**	5	**4**	8
Cash from net excess spread	**8**	10	**10**	15
Investment income		3	**1**	4
Net cash from securitization transactions	**$ 908**	$ 1,024	**$ 1,955**	$ 1,844

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Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

5. Inventories

The components of inventories are as follows:

	As of	
	April 30, 2009	October 31, 2008
(in millions)		
Finished products	$ **952**	$ 998
Work in process	**265**	219
Raw materials	**386**	359
Supplies	**43**	52
Total inventories	$ **1,646**	$ 1,628

6. Investments in and advances to non-consolidated affiliates

Investments in and advances to non-consolidated affiliates is comprised of a 49 percent interest in BDP, a 51 percent interest in BDT, and sixteen other partially-owned affiliates. We do not control these affiliates, but have the ability to exercise significant influence over their operating and financial policies. Our ownership percentages in the sixteen other affiliates range from 10 percent to 51 percent. Our investment in these affiliates is an integral part of our operations, and we account for them using the equity method of accounting. As a part of the Ford Settlement, we expect to increase our interest in our BDT and BDP joint ventures with Ford to 75%. We are currently evaluating the appropriate accounting treatment for the transaction as it relates to the expected increase ownership of BDT and BDP.

Presented below is summarized financial information for BDP, which is considered a significant unconsolidated affiliate. BDP manages sourcing, merchandising, and distribution of various replacement parts.

	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
(in millions)				
Net service revenue	$ **52**	$ 57	$ **101**	$ 108
Net expenses	**7**	7	**10**	16
Income before tax expense	**45**	50	**91**	92
Net income	**47**	50	**92**	91

In April 2009, we entered into an agreement with Caterpillar Inc. (Caterpillar) for the purposes of establishing a joint venture to develop, manufacture, and distribute commercial trucks in regions outside of North America and India. Additionally, we expect to enter into a strategic alliance involving the development, design, manufacture, and sale of Caterpillar-branded heavy duty severe service trucks in North America. Upon completion of the joint venture agreement and formation of the joint venture, we expect to initially have a 50% ownership interest in the joint venture and expect to contribute approximately $46 million as an initial capital contribution. Furthermore, we expect to provide up to an additional $123 million of funding over the following three years. We did not make any capital contributions as of April 30, 2009.

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(Unaudited)

7. Debt

The following table summarizes our debt obligations:

(in millions)	As of April 30, 2009	October 31, 2008
Manufacturing operations:		
Facilities, due 2012	**$ 1,330**	$ 1,330
Debt of majority-owned dealerships	**145**	157
Financing arrangements and capital lease obligations	**287**	306
7.5% Senior Notes, due 2011, net of unamortized discount of less than $1 million at both dates	**15**	15
9.95% Senior Notes, due 2011	**5**	6
Other	**17**	20
Total manufacturing operations debt	**1,799**	1,834
Less: Current portion	**(199)**	(195)
Net long-term manufacturing operations debt	**$ 1,600**	$ 1,639
Financial services operations:		
Asset-backed debt issued by consolidated SPEs, at variable rates, due serially through 2016	**$ 1,732**	$ 2,076
Bank revolvers, at fixed and variable rates, due dates from 2009 through 2013	**1,416**	1,370
Revolving retail warehouse facility, at variable rates, due 2010	**500**	500
Commercial paper, at variable rates, due 2009	**69**	162
Borrowings secured by operating and finance leases, at various rates, due serially through 2016	**133**	132
Total financial services operations debt	**3,850**	4,240
Less: Current portion	**(380)**	(470)
Net long-term financial services operations debt	**$ 3,470**	$ 3,770

8. Fair value measurements

On November 1, 2008, we adopted FASB Statement No. 157, *Fair Value Measurements,* as amended by FSP No. FAS 157-3, for assets and liabilities measured at fair value on a recurring basis. FASB Statement No. 157:

defines fair value as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in an orderly transaction between market participants at the measurement date, and establishes a framework for measuring fair value,

establishes a hierarchy of fair value measurements based upon the observability of inputs used to value assets and liabilities,

requires consideration of nonperformance risk, and

expands disclosures about the methods used to measure fair value.

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Notes to Condensed Consolidated Financial Statements (Continued)

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FASB Statement No. 157 establishes a three-level hierarchy of measurements based upon the reliability of observable and unobservable inputs used to arrive at fair value. Observable inputs are independent market data, while unobservable inputs reflect our assumptions about valuation. Depending on the inputs, we classify each fair value measurement as follows:

Level 1 based upon quoted prices for *identical* instruments in active markets,

Level 2 based upon quoted prices for *similar* instruments, prices for identical or similar instruments in markets that are not active, or model-derived valuations all of whose significant inputs are observable, and

Level 3 based upon one or more significant unobservable inputs.

The following section describes key inputs and assumptions in our valuation methodologies:

Cash Equivalents and Restricted Cash Equivalents. We classify highly liquid investments, with a maturity of 90 days or less at the date of purchase, including U.S. Treasury bills, federal agency securities, and A-1 / P-1 (or higher) rated commercial paper, as cash equivalents. We use quoted prices where available and use a matrix of observable market-based inputs when quoted prices are unavailable.

Marketable Securities. Our marketable securities portfolios are classified as available-for-sale and include investments in U.S. government and, corporate obligations with a maturity of greater than 90 days at the date of purchase. We use quoted prices from active markets to determine their fair values.

Wholesale Notes. Wholesale notes are classified as held-for-sale and are valued at the lower of amortized cost or fair value on an aggregate basis. Amortized cost approximates fair values as a result of the short-term nature and variable interest terms inherent to wholesale notes.

Derivative Assets and Liabilities. We measure the fair value of derivatives assuming that the unit of account is an individual derivative transaction and that derivative could be sold or transferred on a stand-alone basis. We classify within Level 2 our derivatives that are traded over-the-counter and valued using internal models based on readily available observable market inputs. In certain cases, market data is not available and we estimate inputs such as in situations where trading in a particular commodity, or for instruments with notional amounts that fluctuate over time, is not active. Measurements based upon these unobservable assumptions are classified within Level 3. For more information regarding derivatives, see Note 11, *Financial instruments and commodity contracts*.

Retained Interests. We retain certain interests in receivables sold in off-balance sheet securitization transactions. We estimate the fair value of retained interests using internal valuation models that incorporate market inputs and our own assumptions about future cash flows. The fair value of retained interests is estimated based on the present value of monthly collections on the sold finance receivables in excess of amounts accruing to investors and other obligations arising in securitization transactions. In addition to the amount of debt and collateral held by the securitization vehicle, the three key inputs that affect the valuation of the retained interests include credit losses, payment speed, and the discount rate. We classify these assets within Level 3. For more information regarding retained interest, see Note 4, *Finance receivables*.

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Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

The following table presents the financial instruments measured at fair value on a recurring basis as of April 30, 2009:

(in millions)	Level 1	Level 2	Level 3	Total
Assets				
Derivative financial instruments	$	$ 2	$ 47	$ 49
Retained interests			239	239
Total assets	$	$ 2	$ 286	$ 288
Liabilities				
Derivative financial instruments	$	$ 50	$ 50	$ 100
Total liabilities	$	$ 50	$ 50	$ 100

The table below presents the changes for those financial instruments classified within Level 3 of the valuation hierarchy:

(in millions)	Derivative Assets and Liabilities	Retained Interests
Three Months Ended April 30, 2009		
Balance at February 1, 2009	$ (1)	$ 199
Total gains (losses) (realized/unrealized)		
Included in earnings[(A)]	(5)	
Purchases, issuances, and settlements	3	40
Balance at April 30, 2009	$ (3)	$ 239
Change in unrealized gains (losses) on assets and liabilities still held	$ (1)	$

(in millions)	Derivative Assets and Liabilities	Retained Interests
Six Months Ended April 30, 2009		
Balance at November 1, 2008	$ 1	$ 230
Total gains (losses) (realized/unrealized)		
Included in earnings[(A)]	(7)	5
Purchases, issuances, and settlements	3	4

Balance at April 30, 2009	**$**	**(3)**	**$**	**239**
Change in unrealized gains (losses) on assets and liabilities still held	$	(3)	$	5

(A) Net gains and (losses) on derivative assets for the three months and six months ended April 30, 2009, were ($1) million and $1 million, respectively, and are included in *Interest expense* and *Costs of products sold*. Losses on derivative liabilities for the three months and six months ended April 30, 2009 were $4 million and $8 million, respectively, and are included in *Interest expense* and *Costs of products sold*. For retained interests, gains recognized in the consolidated statement of operations are included in *Finance revenues*.

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The following table presents the financial instruments measured at fair value on a nonrecurring basis as of April 30, 2009:

(in millions)	Level 2
Finance receivables[A]	$ 31

(A) Certain impaired finance receivables are measured at fair value on a nonrecurring basis. An impairment charge is recorded for the amount by which the carrying value of the receivables exceeds the fair value of the underlying collateral, net of remarketing costs. As of April 30, 2009, impaired receivables with a carrying amount of $59 million had specific loss reserves of $28 million and a fair value of $31 million. Fair values of the underlying collateral are determined by reference to dealer vehicle value publications adjusted for certain market factors.

9. Postretirement benefits

Defined Benefit Plans

We provide postretirement benefits to a substantial portion of our employees. Costs associated with postretirement benefits include pension and postretirement health care expenses for employees, retirees, and surviving spouses and dependents. Generally, our pension plans are non-contributory. Our policy is to fund the pension plans in accordance with applicable U.S. and Canadian government regulations and to make additional contributions from time to time. For the three months and six months ended April 30, 2009, we contributed $9 million and $19 million, respectively, to our pension plans to meet regulatory minimum funding requirements. For the three months and six months ended April 30, 2008, we contributed $14 million and $21 million, respectively, to our pension plans to meet regulatory minimum funding requirements. We currently anticipate additional contributions of approximately $18 million during the remainder of 2009.

Other post-employment benefit (OPEB) obligations, such as retiree medical, are generally funded in accordance with a 1993 restructured health and life legal settlement, which requires us to fund a portion of the plans annual service cost. For the three months and six months ended April 30, 2009, we contributed $1 million and $2 million, respectively, to our OPEB plans to meet legal funding requirements. For the three months and six months ended April 30, 2008, we contributed $1 million and $2 million, respectively, to our OPEB plans to meet legal funding requirements. We currently anticipate additional contributions of approximately $1 million during the remainder of 2009.

As discussed in Note 2, *Ford settlement and related charges,* the Company committed to close IEP and ICC. Our commitment to close the plants resulted in a charge of $16 million during the first quarter of 2009 representing a plan curtailment and related contractual termination benefits. The plan curtailment also resulted in a plan remeasurement at January 31, 2009 increasing the Projected Benefit Obligation (PBO) by $241 million. The discount rate used to measure the PBO was 6.5% at January 31, 2009 compared to 8.4% at October 31, 2008. All other significant assumptions remained unchanged from the October 31, 2008 measurement date. Actuarial losses for the three months ended January 31, 2009 of $321 million, which were primarily due to the change in the discount rate and negative asset returns, were recognized as a charge to equity as a component of *Accumulated other comprehensive loss*.

In addition to the plan curtailment and related contractual termination benefits resulting from the Ford Settlement, the Company recognized an additional $2 million of contractual termination benefits in the first quarter of 2009 related to the terminations of certain salaried employees in December 2008.

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On December 16, 2007, the majority of Company employees represented by the United Automobile, Aerospace and Agriculture Implement Workers of America (UAW) voted to ratify a new contract that will run through September 30, 2010. Among the changes from the prior contract was the cessation of annual lump sum payments that had been made to certain retirees. Prior to December 16, 2007, we accounted for these payments as a defined benefit plan based on the historical substance of the underlying arrangement. The elimination of these payments and other changes resulted in a net settlement and curtailment of the plan resulting in income of $42 million, which is presented as a reduction of *Selling, general and administrative expenses* for the six months ended April 30, 2008.

Components of Net Postretirement Benefits Expense (Income)

Net postretirement benefits expense (income) included in our consolidated statements of operations is composed of the following:

	Three Months Ended April 30,				Six Months Ended April 30,			
	Pension Benefits		Health and Life Insurance Benefits		Pension Benefits		Health and Life Insurance Benefits	
(in millions)	2009	2008	2009	2008	2009	2008	2009	2008
Service cost for benefits earned during the period	**$ 4**	$ 6	**$ 1**	$ 3	**$ 8**	$ 12	**$ 3**	$ 6
Interest on obligation	**57**	56	**29**	28	**117**	112	**58**	57
Amortization of net cumulative losses	**19**	3			**34**	7	**(1)**	
Amortization of prior service cost (benefit)		1	**(1)**	(1)		1	**(2)**	(2)
Settlements and curtailments					**6**	(42)		(1)
Contractual termination benefits					**9**		**3**	
Premiums on pension insurance	**1**	1			**1**	1		
Less: Expected return on assets	**(46)**	(81)	**(10)**	(17)	**(94)**	(162)	**(20)**	(34)
Net postretirement benefits expense (income)	**$ 35**	$ (14)	**$ 19**	$ 13	**$ 81**	$ (71)	**$ 41**	$ 26

Defined Contribution Plans and Other Contractual Arrangements

Our defined contribution plans cover a substantial portion of domestic salaried employees and certain domestic represented employees. The defined contribution plans contain a 401(k) feature and provide most participants with a matching contribution from the Company. Many participants covered by the plan receive annual Company contributions to their retirement account based on an age-weighted percentage of the participant s eligible compensation for the calendar year. Defined contribution expense pursuant to these plans was $9 million and $15 million for the three months and six months ended April 30, 2009, respectively, and $6 million and $12 million for the three months and six months ended April 30, 2008, respectively.

In accordance with the 1993 restructured health care and life insurance plans, an independent Retiree Supplemental Benefit Trust (the Trust) was established. The Trust, and the benefits it provides to certain retirees, are not part of the Company s consolidated financial statements. The assets of the Trust arise from three sources: (i) the Company s 1993 contribution to the Trust of 25.5 million shares of our Class B common stock, which was subsequently sold by the Trust prior to 2000; (ii) contingent profit-sharing contributions made by the Company; and (iii) net investment gains on the Trust s assets, if any.

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(Unaudited)

The Company s contingent profit sharing obligations will continue until certain funding targets defined by the 1993 Settlement Agreement are met (Profit Sharing Cessation). Upon Profit Sharing Cessation, the Company would assume responsibility for (i) establishing the investment policy for the Trust, (ii) approving or disapproving of certain additional supplemental benefits to the extent such benefits would result in higher expenditures than those contemplated upon the Profit Sharing Cessation, and (iii) making additional contributions to the Trust as necessary to make up for investment and /or actuarial losses.

For the six months ended April 30, 2009 we have recorded profit sharing accruals of less than $1 million based on our estimate of 2009 results. For the three months ended April 30, 2009 we reversed $12 million due to revisions to reflect our expected results. There have been no profit sharing contributions to the Trust during the three years ended October 31, 2008.

10. Income taxes

Under Accounting Principles Board Opinion No. 28, *Interim Financial Reporting*, we compute on a quarterly basis an estimated annual effective tax rate considering ordinary income and related income tax expense. Ordinary income refers to income (loss) before income tax expense excluding significant, unusual, or infrequently occurring items. The tax effect of an unusual or infrequently occurring item is recorded in the interim period in which it occurs. To the extent the Company cannot reliably estimate annual projected taxes for a taxing jurisdiction, taxes on ordinary income for such a jurisdiction are reported in the period in which they are incurred, which is the case for our domestic and Canadian tax jurisdictions. Other items included in income tax expense in the periods in which they occur include the cumulative effect of changes in tax laws or rates, foreign exchange gains and losses, adjustments to uncertain tax positions, and adjustments to our valuation allowance due to changes in judgment in the realizability of deferred tax assets in future years.

We have evaluated the need to maintain a valuation allowance for deferred tax assets based on an assessment of whether it is more likely than not that deferred tax benefits will be realized through the generation of future taxable income. Appropriate consideration is given to all available evidence, both positive and negative, in assessing the need for a valuation allowance. Due to our recent history of U.S. and Canadian operating and taxable losses, the inconsistency of these profits, and the uncertainty of their financial outlook, we continue to maintain a full valuation allowance against our domestic and Canadian deferred tax assets.

On November 1, 2007, we adopted FIN No. 48 *Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 143*, which addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under FIN No. 48, we may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position should be measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement. FIN No. 48 also provides guidance on de-recognition, classification, interest and penalties on income taxes, and accounting in interim periods. As of April 30, 2009, the amount of the liability for unrecognized tax benefits was $97 million. If the unrecognized tax benefits are recognized, the entire amount would impact our effective tax rate. However, to the extent we continue to maintain a full valuation allowance against our deferred tax assets, the effect may be in the form of an increase in the deferred tax asset related to our net operating loss carry forward which would be offset by a full valuation allowance.

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(Unaudited)

We recognize interest and penalties related to uncertain tax positions as part of *Income tax benefit (expense)*. The net reduction in total interest and penalties during the three months and six months ended April 30, 2009 of $4 million and $6 million, respectively, was primarily related to an audit resolution. Cumulative interest and penalties included in *Other current liabilities* and *Other noncurrent liabilities* at April 30, 2009 was $2 million.

We have open tax years from 1993 to 2008 with significant tax jurisdictions in the U.S., Canada, Mexico, and Brazil. In connection with the examination of tax returns, contingencies may arise that generally result from differing interpretations of applicable tax laws and regulations as they relate to the amount, timing or inclusion of revenues or expenses in taxable income, or the sustainability of tax credits to reduce income taxes payable. We believe we have sufficient accruals for our contingent tax liabilities. Interim tax provisions include amounts considered sufficient to pay assessments that may result from examinations of prior year tax returns, although actual results may differ. While it is probable that the liability for unrecognized tax benefits may increase or decrease during the next twelve months, we do not expect any such change would have a material effect on our financial condition, results of operations, or cash flows.

11. Financial instruments and commodity contracts

Derivative Financial Instruments

We use derivative financial instruments as part of our overall interest rate, foreign currency, and commodity risk management strategies to reduce our interest rate exposure, to potentially increase the return on invested funds, to reduce exchange rate risk for transactional exposures denominated in currencies other than the functional currency, and to minimize commodity price volatility. From time to time, we use foreign currency forward and option contracts to manage the risk of exchange rate movements that would reduce the value of our foreign currency cash flows. Foreign currency exchange rate movements create a degree of risk by affecting the value of sales made and costs incurred in currencies other than the functional currency. From time to time, we also use commodity forward contracts to manage variability related to exposure to certain commodity price risk. We generally do not enter into derivative financial instruments for speculative or trading purposes and did not during the three months and six months ended April 30, 2009 and 2008. None of our derivatives qualified for hedge accounting treatment in 2009 or 2008.

Certain of our derivative contracts contain provisions that require us to provide collateral if certain thresholds are exceeded. At April 30, 2009, the amount of collateral provided was less than $1 million and no collateral was provided at October 31, 2008. Collateral is not required to be provided by our counter-parties for derivative contracts. We manage exposure to counter-party credit risk by entering into derivative financial instruments with various major financial institutions that can be expected to fully perform under the terms of such agreements. We do not anticipate nonperformance by any of the counter-parties. Our exposure to credit risk in the event of nonperformance by the counter-parties is limited to those gains that have been recorded, but have not yet been received in cash. At April 30, 2009 and October 31, 2008, our exposure to credit risk was $49 million and $46 million, respectively.

Our financial services operations manage exposure to fluctuations in interest rates by limiting the amount of fixed rate assets funded with variable rate debt. This is accomplished by funding fixed rate receivables utilizing a combination of fixed rate and variable rate debt and derivative financial instruments to convert variable rate debt to fixed. These derivative financial instruments may include interest rate swaps, interest rate caps, and forward contracts. The fair value of these instruments is estimated based on quoted market prices and is subject to market risk, as the instruments may become less valuable due to changes in market conditions or interest rates. Notional amounts of derivative financial instruments do not represent exposure to credit loss.

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The fair values of all derivatives are recorded as assets or liabilities on a gross basis in our consolidated balance sheets. At April 30, 2009 and October 31, 2008, the fair values of our derivatives and their respective balance sheet locations are presented in the following table:

	Asset Derivatives		Liability Derivatives	
(in millions)	Location in Consolidated Balance Sheets	Fair Value	Location in Consolidated Balance Sheets	Fair Value
As of April 30, 2009				
Interest rate swaps:				
Current portion	Other current assets	**$**	Other current liabilities	**$**
Noncurrent portion	Other noncurrent assets	**47**	Other noncurrent liabilities	**93**
Interest rate caps purchased	Other noncurrent assets	**2**	Other noncurrent liabilities	
Interest rate caps sold	Other noncurrent assets		Other noncurrent liabilities	**2**
Foreign currency contracts	Other current assets		Other current liabilities	**1**
Commodity contracts	Other current assets		Other current liabilities	**4**
Total fair value		**49**		**100**
Less: Current portion				**(5)**
Noncurrent portion		**$ 49**		**$ 95**
As of October 31, 2008				
Interest rate swaps:				
Current portion	Other current assets	$	Other current liabilities	$ 2
Noncurrent portion	Other noncurrent assets	39	Other noncurrent liabilities	80
Interest rate caps purchased	Other noncurrent assets		Other noncurrent liabilities	3
Interest rate caps sold	Other noncurrent assets	3	Other noncurrent liabilities	
Foreign currency contracts	Other current assets	3	Other current liabilities	3
Commodity contracts	Other current assets	1	Other current liabilities	
Total fair value		46		88
Less: Current portion		(4)		(5)
Noncurrent portion		$ 42		$ 83

The location and amount of gain (loss) recognized in income on derivatives are as follows for the periods ended April 30:

	Location in	Amount of Gain (Loss) Recognized	
(in millions)	Consolidated Statements of Operations	2009	2008
Three months ended April 30,			

Interest rate swaps	Interest expense	**$ (9)**	$ 1
Interest rate caps purchased	Interest expense	**1**	
Interest rate caps sold	Interest expense	**(1)**	
Foreign currency contracts	Other (income) expense, net		
Commodity forward contracts	Costs of products sold	**(3)**	
Total gain (loss)		**$ (12)**	$ 1

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Notes to Condensed Consolidated Financial Statements (Continued)

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(in millions)	Location in Consolidated Statements of Operations	Amount of Gain (Loss) Recognized 2009	2008
Six months ended April 30,			
Interest rate swaps	Interest expense	**$ (34)**	$ (39)
Interest rate caps purchased	Interest expense	**(1)**	
Interest rate caps sold	Interest expense	**1**	
Foreign currency contracts	Other (income) expense, net	**3**	
Commodity forward contracts	Costs of products sold	**(8)**	
Total loss		**$ (39)**	$ (39)

Interest Rate Swaps and Caps

In September 2008, we entered into two floating-to-floating interest rate swaps (basis swaps) to economically hedge a portion of the floating interest rate associated with our $1.5 billion five-year term loan facility and synthetic revolving facility. The basis swaps had an aggregate notional amount of $1.1 billion and became effective October 30, 2008. The basis swaps matured on January 30, 2009. For the six months ended April 30, 2009, we recognized a loss of $2 million, under these arrangements.

In June 2005, Truck Retail Instalment Paper Corporation (TRIP), a special purpose, wholly-owned subsidiary of NFC, entered into a $500 million revolving facility. Under the terms of this agreement, TRIP purchases and holds fixed rate retail notes and finance leases from NFC. TRIP finances such purchases with its revolving facility. TRIP purchased interest caps with a notional amount of $500 million to protect it against the potential of rising commercial paper interest rates. To offset the economic cost of these caps, NFC sold identical interest rate caps. The interest rate caps have a maturity date of June 30, 2016. For the three months and six months ended April 30, 2009, the amount of gains and (losses) under the purchased interest rate caps that were directly offset by the sold interest rate caps were $1 million and ($1) million, respectively. For the three months and six months ended April 30, 2008, the amount of gains and losses under the purchased interest rate caps that were directly offset by the sold interest rate caps were less than $1 million in both periods.

NFC has entered into interest rate swap agreements in connection with the sale of retail notes and lease receivables. The purpose and structure of these swaps is to convert the floating rate portion of the asset-backed securities into fixed rate swap interest to match the interest basis of the receivables pool sold to the owner trust in those periods, and to protect NFC from interest rate volatility. As of April 30, 2009 and October 31, 2008, the aggregate notional amount of the outstanding interest rate swaps was $4.7 billion and $5.1 billion, respectively. The interest rate swap agreements have several maturity dates ranging from May 2010 to October 2015. For the three months and six months ended April 30, 2009, losses under our interest rate swap agreements related to the sale and funding of retail notes and finance leases were $9 million and $ 32 million, respectively. For the three months and six months ended April 30, 2008, gains (losses) under our interest rate swap agreements related to the sale and funding of retail notes and finance leases were $2 million and ($39) million, respectively.

As of April 30, 2009 and October 31, 2008, our Mexican financial services operations had outstanding interest rate swaps with aggregate notional amounts of less than $1 million and $32 million, respectively, and interest rate caps with aggregate notional amounts of less than $1 million and $1 million, respectively. The purpose and structure of these swaps is to convert the floating rate of the peso-denominated debt into a fixed interest rate. We pay fixed interest of 8.71% and receive interest based on the Interbank Interest Equilibrium Rate. The swap agreements have maturity dates of December 2010 and October 2009. For the three months and six months ended April 30, 2009 and 2008, gains were less than $1 million.

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Foreign Currency Contracts

In 2008, we entered into forward exchange contracts as economic hedges of anticipated cash flows denominated in Indian rupees and South African rand. These contracts were entered into to protect against the risk that the eventual cash flows resulting from such transactions will be adversely affected by changes in exchange rates between the U.S. dollar and either the Indian rupee or South African rand. As of April 30, 2009 and October 31, 2008, we had outstanding Indian rupee forward exchange contracts with aggregate notional amounts of $36 million. As of October 31, 2008, we had outstanding South African rand forward exchange contracts with aggregate notional amounts of $13 million. The forward exchange contracts outstanding as of April 30, 2009 mature in October 2009. For the three months and six months ended April 30, 2009, gains and (losses) related to these contracts were less than ($1) million and $3 million, respectively.

Commodity Forward Contracts

In 2008, we entered into commodity forward contracts as economic hedges of exposure to variability of commodity prices for diesel fuel and lead. These contracts were entered into to protect against the risk that the eventual cash flows related to purchases of the commodities will be adversely affected by future changes in prices. As of April 30, 2009 and October 31, 2008, we had outstanding diesel fuel commodity forward contracts with aggregate notional amounts of $15 million and $9 million, respectively, and outstanding lead commodity forward contracts with aggregate notional amounts of $1 million and $2 million, respectively. The commodity forward contracts outstanding as of April 30, 2009 have several maturity dates ranging from May 2009 to January 2010. For the three months and six months ended April 30, 2009, losses related to these contracts were $3 million and $8 million, respectively.

12. Commitments and contingencies

Guarantees

We occasionally provide guarantees that could obligate us to make future payments if the primary entity fails to perform under its contractual obligations. As described below, we have recognized liabilities for some of these guarantees in our consolidated balance sheets as they meet the recognition and measurement provisions of FIN No. 45, *Guarantor s Accounting and Disclosure Requirements for Guarantees Including Indirect Guarantees of the Indebtedness of Others*. In addition to the liabilities that have been recognized as described below, we are contingently liable for other potential losses under various guarantees. We do not believe that claims that may be made under such guarantees would have a material effect on our financial condition, results of operations, or cash flows.

We have issued residual value guarantees in connection with various leases that extend through 2011. The amounts of the guarantees are estimated and recorded as liabilities as of April 30, 2009. Our guarantees are contingent upon the fair value of the leased assets at the end of the lease term.

We obtain certain stand-by letters of credit and surety bonds from third party financial institutions in the ordinary course of business when required under contracts or to satisfy insurance-related requirements. The amount of available stand-by letters of credit and surety bonds were $64 million at April 30, 2009.

We extend credit commitments to certain truck fleet customers, which allow them to purchase parts and services from participating dealers. The participating dealers receive accelerated payments from us with the result that we carry the receivables and absorb the credit risk related to these customers. At April 30, 2009, we have $35 million of unused credit commitments outstanding under this program.

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In addition, at April 30, 2009 we have entered into various purchase commitments of $166 million and contracts that have cancellation fees of $9 million with various expiration dates through 2013.

In the ordinary course of business, we also provide routine indemnifications and other guarantees, the terms of which range in duration and often are not explicitly defined. We do not believe these will result in claims that would have a material impact on our financial condition, results of operations, or cash flows.

The terms of the Ford Settlement require us to indemnify Ford with respect to intellectual property infringement claims, if any, that are brought against Ford or others that use the 6.0 liter or 6.4 liter engines on behalf of Ford. The maximum amount of future payments that we could potentially be required to pay under the indemnification would depend upon whether any such claims are alleged in the future and thus cannot currently be determined.

Environmental Liabilities

We have been named a potentially responsible party (PRP), in conjunction with other parties, in a number of cases arising under an environmental protection law, the Comprehensive Environmental Response, Compensation, and Liability Act, popularly known as the Superfund law. These cases involve sites that allegedly received wastes from current or former Company locations. Based on information available to us which, in most cases, consists of data related to quantities and characteristics of material generated at current or former Company locations, material allegedly shipped by us to these disposal sites, as well as cost estimates from PRPs and/or federal or state regulatory agencies for the cleanup of these sites, a reasonable estimate is calculated of our share, if any, of the probable costs and accruals are recorded in our condensed consolidated financial statements. These accruals are generally recognized no later than completion of the remedial feasibility study and are not discounted to their present value. We review all accruals on a regular basis and believe that, based on these calculations, our share of the potential additional costs for the cleanup of each site will not have a material effect on our financial condition, results of operations, or cash flows.

Three sites formerly owned by us, (i) Solar Turbines in San Diego, California, (ii) the West Pullman Plant in Chicago, Illinois, and (iii) the Canton Plant in Canton, Illinois, and one site partially owned by us, Wisconsin Steel in Chicago, Illinois, were identified as having soil and groundwater contamination. While investigations and cleanup activities continue at all sites, we believe that we have adequate accruals to cover costs to complete the cleanup of these sites.

We have accrued $17 million for these and other environmental matters that may arise, which are included within *Other current liabilities* and *Other noncurrent liabilities*, as of April 30, 2009 and October 31, 2008. The majority of these accrued liabilities are expected to be paid out during the period from 2009 through 2011.

Along with other vehicle manufacturers, we have been subject to an increase in the number of asbestos-related claims in recent years. In general, these claims relate to illnesses alleged to have resulted from asbestos exposure from component parts found in older vehicles, although some cases relate to the alleged presence of asbestos in our facilities. In these claims, we are not the sole defendant, and the claims name as defendants numerous manufacturers and suppliers of a wide variety of products allegedly containing asbestos. We have strongly disputed these claims, and it has been our policy to defend against them vigorously. Historically, the actual damages paid out to claimants have not been material in any year to our financial condition, results of operations, or cash flows. It is possible that the number of these claims will continue to grow, and that the costs for resolving asbestos related claims could become significant in the future.

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Legal Proceedings

Overview

We are subject to various claims arising in the ordinary course of business, and are parties to various legal proceedings that constitute ordinary, routine litigation incidental to our business. The majority of these claims and proceedings relate to commercial, product liability, and warranty matters. In our opinion, apart from the actions set forth below, the disposition of these proceedings and claims, after taking into account recorded accruals and the availability and limits of our insurance coverage, will not have a material adverse effect on our business or our financial condition, results of operations, or cash flows.

Settlement of Ford Litigation

In January 2007, a complaint was filed against us in Oakland County Circuit Court in Michigan by Ford claiming damages relating to warranty and pricing disputes with respect to certain engines purchased by Ford from us. While Ford s complaint did not quantify its alleged damages, we estimated that Ford may have been seeking in excess of $500 million, and that this amount might have increased (i) as we continued to sell engines to Ford at a price that Ford alleged was too high and (ii) as Ford paid its customers warranty claims, which Ford alleged were attributable to us. We disagreed with Ford s position and defended ourselves vigorously in the litigation. We filed an answer to the complaint denying Ford s allegations in all material respects. We also asserted affirmative defenses to Ford s claims, as well as counterclaims alleging that, among other things, Ford had materially breached contracts between it and us in several different respects.

In June 2007, we filed a separate lawsuit against Ford in the Circuit Court of Cook County, Illinois, for breach of contract relating to the manufacture of new diesel engines for Ford for use in vehicles including the F-150 pickup truck. In that case we sought unspecified damages. In September 2007, the judge dismissed our lawsuit against Ford, directing us to proceed with mediation. In February 2008, we re-filed the lawsuit against Ford because the parties were unable to resolve the dispute through mediation.

On January 13, 2009, we announced that we had reached an agreement with Ford to restructure our ongoing business relationship and settle all existing litigation between us and Ford. As part of the settlement agreement, both companies agreed to terminate their respective lawsuits and release each other from various actual and potential claims, including those brought in the lawsuits. We also received a cash payment from Ford and expect to increase our interest in our BDT and BDP joint ventures with Ford to 75%. Finally, we will end our current diesel engine supply agreement with Ford effective December 31, 2009. We will however continue our diesel engine supply arrangement with Ford in South America.

Securities and Exchange Commission Investigations

In October 2004, we received a request from the staff of the SEC to voluntarily produce certain documents and information related to our accounting practices with respect to defined benefit pension plans and other postretirement benefits. We fully cooperated with this request. On April 7, 2009, the SEC confirmed that the investigation into this matter has been completed and that the SEC did not intend to recommend any enforcement action related to this matter.

In January 2005, we announced that we would restate our financial results for 2002 and 2003 and the first three quarters of 2004. Our restated Annual Report on Form 10-K was filed in February 2005. The SEC notified us on

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February 9, 2005 that it was conducting an informal inquiry into our restatement. On March 17, 2005, we were advised by the SEC that the status of the inquiry had been changed to a formal investigation. On April 7, 2006, we announced that we would restate our financial results for 2002 through 2004 and for the first three quarters of 2005. We were subsequently informed by the SEC that it was expanding the investigation to include that restatement. Our 2005 Annual Report on Form 10-K, which included the restated financial statements, was filed in December 2007. We have been providing information to and fully cooperating with the SEC on this investigation. Based on the status of the investigation, we are not able to predict its final outcome.

Litigation Relating to Accounting Controls and Financial Restatement

In December 2007, a complaint was filed against us by Norfolk County Retirement System and Brockton Contributory Retirement System (collectively Norfolk). In March 2008, an additional complaint was filed by Richard Garza. Each of these matters is pending in the United States District Court, Northern District of Illinois.

The plaintiffs in the Norfolk case allege they are shareholders suing on behalf of themselves and a class of other shareholders who purchased shares of the Company s common stock between February 14, 2003 and July 17, 2006. The complaint alleges that the defendants, which include the Company, one of its executive officers, two of its former executive officers, and the Company s former independent accountants, Deloitte & Touche LLP, violated federal securities laws by making false and misleading statements about the Company s financial condition during that period. In March 2008, the court appointed Norfolk County Retirement System and the Plumbers Local Union 519 Pension Trust as joint lead plaintiffs. The plaintiffs in this matter seek compensatory damages and attorneys fees among other relief. We are currently awaiting the Court s decision on a motion to dismiss that we originally filed on July 7, 2008.

The plaintiff in the Garza case brought a derivative claim on behalf of the Company against one of the Company s executive officers, two of its former executive officers, and certain of its directors, alleging that (i) all of the defendants violated their fiduciary obligations under Delaware law by willfully ignoring certain accounting and financial reporting problems at the Company, thereby knowingly disseminating false and misleading financial information about the Company, (ii) certain of the defendants were unjustly enriched in connection with their sale of Company stock during the December 2002 to January 2006 period, and (iii) the defendants violated Delaware law by failing to hold an annual meeting of shareholders. In connection with this last allegation, the plaintiff seeks an order requiring defendants to schedule an annual meeting of shareholders. Otherwise, the plaintiffs in this matter seek compensatory damages, disgorgement of the proceeds of defendants profits from the sale of Company stock, attorneys fees, and other equitable relief.

We strongly dispute the allegations in these complaints and will vigorously defend ourselves.

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13. Comprehensive income (loss)

Total comprehensive income (loss) is summarized as follows:

(in millions)	Three Months Ended April 30, 2009	Three Months Ended April 30, 2008	Six Months Ended April 30, 2009	Six Months Ended April 30, 2008
Net income	**$ 12**	$ 211	**$ 246**	$ 146
Other comprehensive income (loss)				
Foreign currency translation adjustments	**24**	22	**(19)**	15
Postretirement and other postemployment benefits	**18**	2	**31**	(6)
Pension remeasurement			**(321)**	
Total other comprehensive income (loss)	**42**	24	**(309)**	9
Total comprehensive income (loss)	**$ 54**	$ 235	**$ (63)**	$ 155

14. Stockholders deficit

The following table summarizes the activity in stockholders deficit:

(in millions)	Series D Convertible Junior Preference Stock	Common Stock	Additional Paid in Capital	Compre-hensive Loss	Accumulated Deficit	Accumulated Other Comprehensive Loss	Common Stock Held in Treasury, at Cost	Total
Balance as of October 31, 2008	**$ 4**	**$ 7**	**$ 1,966**		**$ (2,392)**	**$ (943)**	**$ (137)**	**$ (1,495)**
Net income				$ 246	246			246
Other comprehensive loss:								
Foreign currency translation adjustments				(19)				(19)
Postretirement and other postemployment benefits				31				31
Pension remeasurement(A)				(321)				(321)
Total other comprehensive loss				(309)		(309)		
Total comprehensive loss				$ (63)				
Stock options recorded as redeemable equity securities			(5)					(5)
Redeemable equity securities modification			130					130

Transfer from redeemable equity securities upon exercise or expiration of stock options			4				4
Stock-based compensation			11				11
Treasury stock reissued			(2)			2	
Share repurchase program						(29)	(29)
Balance as of April 30, 2009	**$ 4**	**$ 7**	**$ 2,104**	**$ (2,146)**	**$ (1,252)**	**$ (164)**	**$ (1,447)**

(A) See Note 9, Postretirement benefits.

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Redeemable Equity Securities

In the first quarter of 2009, we modified the terms of certain outstanding stock options classified as mezzanine equity. The modification, which required the consent of plan participants, eliminated the feature that allowed for cash settlement in the event of a change in control when certain other conditions existed. As a result, the value of the modified award is no longer required to be presented as mezzanine equity under the provisions of Emerging Issues Task Force (EITF) Topic No. D-98, *Classification and Measurement of Redeemable Securities*. The modification has resulted in a reduction of $130 million of *Redeemable equity securities* and a corresponding increase to *Additional paid in capital.* As additional plan participants consent to the modification, additional amounts will be reclassified from *Redeemable equity securities* to *Additional paid in capital*.

Share Repurchase Program

In July 2008, our Board of Directors authorized a $36 million share repurchase program, which expires in July 2009. We initiated the share repurchase program in January 2009, and through April 30, 2009, repurchased 1,000,000 shares of our common stock at an average price of $28.89.

15. Earnings per share

The following table shows the information used in the calculation of our basic and diluted earnings (loss) per share:

	Three Months Ended April 30,		Six Months Ended April 30,	
(in millions, except per share data)	**2009**	**2008**	**2009**	**2008**
Numerator:				
Net income available to common stockholders	**$ 12**	$ 211	**$ 246**	$ 146
Denominator:				
Weighted average shares outstanding				
Basic	**70.8**	70.3	**71.2**	70.3
Effect of dilutive securities	**0.5**	2.9	**0.3**	2.6
Diluted	**71.3**	73.2	**71.5**	72.9
Basic earnings per share	**$ 0.16**	$ 3.00	**$ 3.45**	$ 2.08
Diluted earnings per share	**$ 0.16**	$ 2.88	**$ 3.44**	$ 2.00

Shares not included in the computation of diluted earnings per share, as they would be anti-dilutive, were 0.4 million for both the three months and six months ended April 30, 2009. There were no anti-dilutive shares in 2008.

16. Segment reporting

The following is a description of our four reporting segments:

Our *Truck* segment manufactures and distributes a full line of class 4 through 8 trucks and buses under the International® and IC Bus, LLC (IC bus   ) brands, and Navistar Defense, LLC military vehicles. Our Truck segment also produces chassis for motor homes and commercial step-van vehicles under the

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Workhorse Custom Chassis, LLC (WCC) brand. In an effort to strengthen and maintain our dealer network, this segment occasionally acquires and operates dealer locations for the purpose of transitioning ownership or providing temporary operational assistance.

Our *Engine* segment designs and manufactures diesel engines for use primarily in our class 6 and 7 medium trucks and buses and selected class 8 heavy truck models, and for sale to original equipment manufacturers (OEMs) primarily in North America. In addition, our Engine segment produces diesel engines in Brazil primarily for distribution in South America under the MWM brand for sale to OEMs.

Our *Parts* segment provides customers with proprietary products needed to support the International truck, IC bus, WCC chassis, Navistar Defense military vehicles, and the MaxxForce® engine lines. Our Parts segment also provides a wide selection of other standard truck, trailer, and engine aftermarket parts.

Our *Financial Services* segment provides retail, wholesale, and lease financing of products sold by the Truck segment and its dealers within the U.S. and Mexico as well as financing for wholesale accounts and selected retail accounts receivable.
Corporate contains those items that are not included in our four segments.

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Segment Profit (Loss)

We define segment profit (loss) as income (loss) before income tax. Our results for interim periods are not necessarily indicative of results for a full year. Effective November 1, 2008, we began allocating certain fees charged by our Financial Services segment to our manufacturing operations for unused funding facilities, surcharges on retail and wholesale account balances, and retail note and wholesale note balances for Dealcor dealers which were $6 million and $11 million for the three months and six months ended April 30, 2009. Selected financial information is as follows:

(in millions)	Truck	Engine(C)	Parts	Financial Services(A)	Corporate and Eliminations	Total
Three Months Ended April 30, 2009						
External sales and revenues, net	**$ 1,773**	**$ 434**	**$ 534**	**$ 67**	**$**	**$ 2,808**
Intersegment sales and revenues		**158**	**43**	**21**	**(222)**	
Total sales and revenues, net	**$ 1,773**	**$ 592**	**$ 577**	**$ 88**	**$ (222)**	**$ 2,808**
Depreciation and amortization	**$ 45**	**$ 32**	**$ 1**	**$ 6**	**$ 4**	**$ 88**
Interest expense				**38**	**19**	**57**
Equity in income (loss) of non-consolidated affiliates	**(10)**	**22**	**2**			**14**
Segment profit (loss)	**56**	**(84)**	**115**	**18**	**(84)**	**21**
Capital expenditures(B)	**19**	**14**	**3**	**1**	**2**	**39**
Three Months Ended April 30, 2008						
External sales and revenues, net	$ 2,717	$ 751	$ 385	$ 96	$	$ 3,949
Intersegment sales and revenues		188	53	21	(262)	
Total sales and revenues, net	$ 2,717	$ 939	$ 438	$ 117	$ (262)	$ 3,949
Depreciation and amortization	$ 45	$ 39	$ 2	$ 5	$ 6	$ 97
Interest expense				67	35	102
Equity in income (loss) of non-consolidated affiliates	(3)	23	1			21
Segment profit (loss)	209	51	56	19	(126)	209
Capital expenditures(B)	33	28	1	2	2	66
Six Months Ended April 30, 2009						
External sales and revenues, net	**$ 3,834**	**$ 783**	**$ 1,019**	**$ 142**	**$**	**$ 5,778**
Intersegment sales and revenues	**1**	**318**	**98**	**39**	**(456)**	
Total sales and revenues, net	**$ 3,835**	**$ 1,101**	**$ 1,117**	**$ 181**	**$ (456)**	**$ 5,778**
Depreciation and amortization	**$ 85**	**$ 59**	**$ 3**	**$ 12**	**$ 8**	**$ 167**
Interest expense				**102**	**48**	**150**
Equity in income (loss) of non-consolidated affiliates	**(17)**	**44**	**4**			**31**
Segment profit (loss)	**170**	**105**	**219**	**17**	**(263)**	**248**
Capital expenditures(B)	**33**	**34**	**6**	**1**	**3**	**77**
Six Months Ended April 30, 2008						
External sales and revenues, net	$ 4,600	$ 1,385	$ 728	$ 190	$	$ 6,903
Intersegment sales and revenues		340	111	43	(494)	

Total sales and revenues, net	$ 4,600	$ 1,725	$ 839	$ 233	$ (494)	$ 6,903
Depreciation and amortization	$ 86	$ 76	$ 4	$ 10	$ 10	$ 186
Interest expense				186	83	269
Equity in income (loss) of non-consolidated affiliates	(3)	46	2			45
Segment profit (loss)	218	85	105	(6)	(247)	155
Capital expenditures(B)	55	39	2	3	4	103
As of April 30, 2009						
Segment assets	**$ 2,585**	**$ 1,281**	**$ 700**	**$ 4,561**	**$ 530**	**$ 9,657**
As of October 31, 2008						
Segment assets	2,796	1,374	711	4,879	630	10,390

(A) Total sales and revenues in the Financial Services segment include interest revenues of $80 million and $163 million for the three months and six months ended April 30, 2009, respectively, and $108 million and $212 million for the same periods in 2008.

(B) Exclusive of purchase of equipment leased to others.

(C) See Note 2, *Ford settlement and related charges,* and Note 12, *Commitment and contingencies,* for further discussion.

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Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

The following is information about our two customers from which we derived more than 10% of our consolidated *Sales and revenues, net*:

Sales of vehicles and service parts to the U.S. government were 32% of consolidated sales and revenues for the three months and six months ended April 30, 2009 and 26% and 23% for the same periods in 2008 and were recorded in the Truck and Parts segments. U.S. government receivable balances related to sales of vehicles and service parts totaled $308 million and $314 million as of April 30, 2009 and October 31, 2008, respectively.

Sales of diesel engines to Ford were 8% and 6% of consolidated sales and revenues for the three months and six months ended April 30, 2009 and 10% and 11% for the same periods in 2008. Ford accounted for 45% and 37% of our diesel unit volume (including intercompany transactions) for the three months and six months ended April 30, 2009 and 54% for the same periods in 2008. Ford receivable balances totaled $96 million and $84 million as of April 30, 2009 and October 31, 2008, respectively.

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Navistar International Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Continued)

(Unaudited)

17. Condensed consolidating guarantor and non-guarantor financial information

The following tables set forth condensed consolidating balance sheets as of April 30, 2009 and October 31, 2008, and condensed consolidating statements of operations for the three months and six months ended April 30, 2009 and 2008, and condensed consolidating statements of cash flows for the six months ended April 30, 2009 and 2008. The information is presented as a result of Navistar, Inc. s guarantee, exclusive of its subsidiaries, of NIC s indebtedness under its 7.5% Senior Notes due 2011. Navistar, Inc. is a direct wholly-owned subsidiary of NIC. None of NIC s other subsidiaries guarantee any of these notes. The guarantee is full and unconditional. Separate financial statements and other disclosures concerning Navistar, Inc. have not been presented because management believes that such information is not material to investors. Within this disclosure only, NIC includes the consolidated financial results of the parent company only, with all of its wholly-owned subsidiaries accounted for under the equity method. Likewise, Navistar, Inc., for purposes of this disclosure only, includes the consolidated financial results of its wholly-owned subsidiaries accounted for under the equity method. Non-Guarantor Subsidiaries includes the combined financial results of all other non-guarantor subsidiaries. Eliminations and Other includes all eliminations and reclassifications to reconcile to the condensed consolidated financial statements. NIC files a consolidated U.S. federal income tax return that includes Navistar, Inc. and its U.S. subsidiaries. Navistar, Inc. has a tax allocation agreement (Tax Agreement) with NIC which requires Navistar, Inc. to compute its separate federal income tax liability and remit any resulting tax liability to NIC. Tax benefits that may arise from net operating losses of Navistar, Inc. are not refunded to Navistar, Inc. but may be used to offset future required tax payments under the Tax Agreement. The effect of the Tax Agreement is to allow NIC, the parent company, rather than Navistar, Inc., to realize the benefit of current U.S. taxable losses of Navistar, Inc. and all other direct or indirect subsidiaries of NIC. Certain previously reported amounts have been reclassified to conform to the current quarters financial statement presentation.