

NAVISTAR INTERNATIONAL CORP  
Form 10-Q  
June 07, 2016

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

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Form 10-Q

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(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended April 30, 2016

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

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NAVISTAR INTERNATIONAL CORPORATION  
(Exact name of registrant as specified in its charter)

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Delaware 36-3359573  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

2701 Navistar Drive, Lisle, Illinois 60532  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code (331) 332-5000

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes  No   
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 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  Accelerated filer

Non-accelerated filer  Smaller reporting company

(Do not check if a 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

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As of May 31, 2016, the number of shares outstanding of the registrant's common stock was 81,601,786, 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 the federal securities laws. Such forward-looking statements only speak as of the date of this report and Navistar International Corporation assumes no obligation to update the information included in this report.

Such forward-looking statements include, but are not limited to, statements concerning:

- estimates we have made in preparing our financial statements;
- our development of new products and technologies;
- anticipated sales, volume, demand, markets for our products, and financial performance;
- anticipated performance and benefits of our products and technologies;
- our business strategies relating to, and our ability to meet, federal and state regulatory heavy-duty diesel emissions standards applicable to certain of our engines, including the timing and costs of compliance and consequences of noncompliance with such standards, as well as our ability to meet other federal, state and foreign regulatory requirements;
- our business strategies and long-term goals, and activities to accomplish such strategies and goals;
- our ability to implement our new strategy focused on establishing a leading market position based on uptime advantage and a customer-centric culture, leading with connected vehicle offerings, providing customers with meaningful innovation and tailored solutions, and developing effective leaders at every level, as well as the results we expect to achieve from the implementation of our new strategy;
- our expectations related to new product launches;
- anticipated results from the realignment of our leadership and management structure;
- anticipated benefits from acquisitions, strategic alliances, and joint ventures we complete;
- our expectations and estimates relating to restructuring activities, including restructuring and integration charges and timing of cash payments related thereto, and operational flexibility, savings, and efficiencies from such restructurings;
- our expectations relating to the possible effects of anticipated divestitures and closures of businesses;
- our expectations relating to our cost-reduction actions and actions to reduce discretionary spending;
- our expectations relating to our ability to service our long-term debt;
- our expectations relating to our retail finance receivables and retail finance revenues;
- our expectations and estimates relating to our used truck inventory;
- our anticipated costs relating to the implementation of our emissions compliance strategy and other product modifications that may be required to meet other federal, state, and foreign regulatory requirements;
- liabilities resulting from environmental, health and safety laws and regulations;
- our anticipated capital expenditures;
- our expectations relating to payments of taxes;
- our expectations relating to warranty costs;
- our expectations relating to interest expense;
- our expectations relating to impairment of goodwill and other assets;
- costs relating to litigation and similar matters;
- estimates relating to pension plan contributions and unfunded pension and postretirement benefits;
- trends relating to commodity prices; and
- anticipated trends, expectations, and outlook relating to matters affecting our financial condition or results of operations.

These statements often include words such as "believe," "expect," "anticipate," "intend," "plan," "estimate," or similar expressions. These statements are not guarantees of performance or results and they involve risks, uncertainties, and assumptions. Although we believe that these forward-looking statements are based on reasonable assumptions, there are many factors that could affect our results of operations and could cause actual results to differ materially from those in the forward-looking statements. Factors that could cause or contribute to differences in our future financial results include those discussed in Item 1A, Risk Factors, included within (i) our Annual Report on Form 10-K for the year ended October 31, 2015, which was filed on December 17, 2015, as well as those factors discussed elsewhere in this report. 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 herein 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 annual, quarterly, and current reports, proxy statements, and other information with the United States ("U.S.") 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. Information on our website does not constitute part of this Quarterly Report on Form 10-Q. In addition, 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 electronically file with, or furnish to, the SEC. Any materials we file with, or furnish to, the SEC may also be read and/or copied at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330.

## PART I—Financial Information

## Item 1. Financial Statements

Navistar International Corporation and Subsidiaries  
Consolidated Statements of Operations  
(Unaudited)

| (in millions, except per share data)  | Three Months            |           | Six Months              |           |
|---|-------------------------|-----------|-------------------------|-----------|
|   | Ended April 30,<br>2016 | 2015      | Ended April 30,<br>2016 | 2015      |
| Sales and revenues  |                         |           |                         |           |
| Sales of manufactured products, net   | \$2,164                 | \$2,658   | \$3,894                 | \$5,043   |
| Finance revenues  | 33                      | 35        | 68                      | 71        |
| Sales and revenues, net   | 2,197                   | 2,693     | 3,962                   | 5,114     |
| Costs and expenses  |                         |           |                         |           |
| Costs of products sold  | 1,845                   | 2,360     | 3,311                   | 4,405     |
| Restructuring charges   | 3                       | 6         | 6                       | 9         |
| Asset impairment charges  | 3                       | 1         | 5                       | 8         |
| Selling, general and administrative expenses                                    | 202                     | 243       | 407                     | 484       |
| Engineering and product development costs                                       | 61                      | 76        | 119                     | 155       |
| Interest expense  | 81                      | 75        | 162                     | 152       |
| Other income, net   | (25 )                   | (28 )     | (47 )                   | (31 )     |
| Total costs and expenses  | 2,170                   | 2,733     | 3,963                   | 5,182     |
| Equity in income of non-consolidated affiliates                                 | 2                       | 1         | 1                       | 3         |
| Income (loss) from continuing operations before income taxes                    | 29                      | (39 )     | —                       | (65 )     |
| Income tax expense  | (16 )                   | (18 )     | (11 )                   | (25 )     |
| Income (loss) from continuing operations  | 13                      | (57 )     | (11 )                   | (90 )     |
| Income (loss) from discontinued operations, net of tax                          | —                       | —         | —                       | —         |
| Net income (loss)   | 13                      | (57 )     | (11 )                   | (90 )     |
| Less: Net income attributable to non-controlling interests                      | 9                       | 7         | 18                      | 16        |
| Net income (loss) attributable to Navistar International Corporation            | \$4                     | \$(64 )   | \$(29 )                 | \$(106 )  |
| Amounts attributable to Navistar International Corporation common shareholders: |                         |           |                         |           |
| Income (loss) from continuing operations, net of tax                            | \$4                     | \$(64 )   | \$(29 )                 | \$(106 )  |
| Income (loss) from discontinued operations, net of tax                          | —                       | —         | —                       | —         |
| Net income (loss)   | \$4                     | \$(64 )   | \$(29 )                 | \$(106 )  |
| Income (loss) per share:  |                         |           |                         |           |
| Basic:  |                         |           |                         |           |
| Continuing operations   | \$0.05                  | \$(0.78 ) | \$(0.35 )               | \$(1.30 ) |
| Discontinued operations   | —                       | —         | —                       | —         |
|   | \$0.05                  | \$(0.78 ) | \$(0.35 )               | \$(1.30 ) |
| Diluted:  |                         |           |                         |           |
| Continuing operations   | \$0.05                  | \$(0.78 ) | \$(0.35 )               | \$(1.30 ) |
| Discontinued operations   | —                       | —         | —                       | —         |
|   | \$0.05                  | \$(0.78 ) | \$(0.35 )               | \$(1.30 ) |
| Weighted average shares outstanding:  |                         |           |                         |           |
| Basic   | 81.7                    | 81.6      | 81.7                    | 81.5      |
| Diluted   | 82.0                    | 81.6      | 81.7                    | 81.5      |

See Notes to Consolidated Financial Statements

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Navistar International Corporation and Subsidiaries  
 Consolidated Statements of Comprehensive Income (Loss)  
 (Unaudited)

| (in millions)  | Three<br>Months<br>Ended<br>April 30, |        | Six Months<br>Ended April<br>30, |         |
|--|---------------------------------------|--------|----------------------------------|---------|
|  | 2016                                  | 2015   | 2016                             | 2015    |
| Net income (loss)  | \$13                                  | \$(57) | \$(11)                           | \$(90)  |
| Other comprehensive income (loss):   |                                       |        |                                  |         |
| Foreign currency translation adjustment  | 50                                    | (27)   | 17                               | (86)    |
| Defined benefit plans (net of tax)   | 15                                    | 33     | 48                               | 65      |
| Total other comprehensive income (loss)  | 65                                    | 6      | 65                               | (21)    |
| Comprehensive income (loss)  | 78                                    | (51)   | 54                               | (111)   |
| Less: Net income attributable to non-controlling interests                           | 9                                     | 7      | 18                               | 16      |
| Total comprehensive income (loss) attributable to Navistar International Corporation | \$69                                  | \$(58) | \$36                             | \$(127) |

See Notes to Consolidated Financial Statements

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Navistar International Corporation and Subsidiaries  
Consolidated Balance Sheets

|  | April 30,<br>2016 | October 31,<br>2015 |
|--|-------------------|---------------------|
| (in millions, except per share data)   |                   |                     |
| ASSETS   | (Unaudited)       |                     |
| Current assets   |                   |                     |
| Cash and cash equivalents  | \$ 589            | \$ 912              |
| Marketable securities  | 228               | 159                 |
| Trade and other receivables, net   | 369               | 429                 |
| Finance receivables, net   | 1,552             | 1,779               |
| Inventories, net   | 1,220             | 1,135               |
| Deferred taxes, net  | —                 | 36                  |
| Other current assets   | 172               | 172                 |
| Total current assets   | 4,130             | 4,622               |
| Restricted cash  | 139               | 121                 |
| Trade and other receivables, net   | 14                | 13                  |
| Finance receivables, net   | 209               | 216                 |
| Investments in non-consolidated affiliates   | 66                | 66                  |
| Property and equipment (net of accumulated depreciation and amortization of \$2,586 and \$2,546, respectively) | 1,281             | 1,345               |
| Goodwill   | 38                | 38                  |
| Intangible assets (net of accumulated amortization of \$128 and \$120, respectively)                           | 53                | 57                  |
| Deferred taxes, net  | 164               | 128                 |
| Other noncurrent assets  | 94                | 86                  |
| Total assets   | \$ 6,188          | \$ 6,692            |
| LIABILITIES and STOCKHOLDERS' DEFICIT  |                   |                     |
| Liabilities  |                   |                     |
| Current liabilities  |                   |                     |
| Notes payable and current maturities of long-term debt   | \$ 1,251          | \$ 1,110            |
| Accounts payable   | 1,146             | 1,301               |
| Other current liabilities  | 1,223             | 1,377               |
| Total current liabilities  | 3,620             | 3,788               |
| Long-term debt   | 3,974             | 4,188               |
| Postretirement benefits liabilities  | 2,945             | 2,995               |
| Deferred taxes, net  | —                 | 14                  |
| Other noncurrent liabilities   | 770               | 867                 |
| Total liabilities  | 11,309            | 11,852              |
| Stockholders' deficit  |                   |                     |
| Series D convertible junior preference stock   | 2                 | 2                   |
| Common stock (86.8 shares issued, and \$0.10 par value per share and 220 shares authorized, all at both dates) | 9                 | 9                   |
| Additional paid-in capital   | 2,498             | 2,499               |
| Accumulated deficit  | (4,895)           | (4,866)             |
| Accumulated other comprehensive loss   | (2,536)           | (2,601)             |
| Common stock held in treasury, at cost (5.2 and 5.3 shares, respectively)                                      | (206)             | (210)               |
| Total stockholders' deficit attributable to Navistar International Corporation                                 | (5,128)           | (5,167)             |
| Stockholders' equity attributable to non-controlling interests   | 7                 | 7                   |
| Total stockholders' deficit  | (5,121)           | (5,160)             |
| Total liabilities and stockholders' deficit  | \$ 6,188          | \$ 6,692            |

See Notes to Consolidated Financial Statements

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Navistar International Corporation and Subsidiaries  
Condensed Consolidated Statements of Cash Flows  
(Unaudited)

| (in millions)   | Six Months<br>Ended April<br>30, |         |
|---|----------------------------------|---------|
|   | 2016                             | 2015    |
| Cash flows from operating activities  |                                  |         |
| Net loss  | \$(11 )                          | \$(90 ) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: |                                  |         |
| Depreciation and amortization   | 74                               | 118     |
| Depreciation of equipment leased to others  | 37                               | 35      |
| Deferred taxes, including change in valuation allowance                                   | (3 )                             | (7 )    |
| Asset impairment charges  | 5                                | 8       |
| Loss on sales of investments and businesses, net  | 2                                | —       |
| Amortization of debt issuance costs and discount  | 17                               | 19      |
| Stock-based compensation  | 7                                | 8       |
| Provision for doubtful accounts, net of recoveries  | 8                                | (3 )    |
| Equity in income of non-consolidated affiliates, net of dividends                         | —                                | 5       |
| Other non-cash operating activities   | (8 )                             | (20 )   |
| Changes in other assets and liabilities, exclusive of the effects of businesses disposed  | (232 )                           | (310 )  |
| Net cash used in operating activities   | (104 )                           | (237 )  |
| Cash flows from investing activities  |                                  |         |
| Purchases of marketable securities  | (283 )                           | (162 )  |
| Sales of marketable securities  | 177                              | 431     |
| Maturities of marketable securities   | 37                               | 63      |
| Net change in restricted cash and cash equivalents  | (19 )                            | 53      |
| Capital expenditures  | (53 )                            | (45 )   |
| Purchases of equipment leased to others   | (78 )                            | (20 )   |
| Proceeds from sales of property and equipment   | 17                               | 5       |
| Proceeds from sales of affiliates   | 36                               | 7       |
| Net cash provided by (used in) investing activities                                       | (166 )                           | 332     |
| Cash flows from financing activities  |                                  |         |
| Proceeds from issuance of securitized debt  | 75                               | 250     |
| Principal payments on securitized debt  | (19 )                            | (199 )  |
| Net change in secured revolving credit facilities   | 38                               | 30      |
| Proceeds from issuance of non-securitized debt  | 110                              | 84      |
| Principal payments on non-securitized debt  | (162 )                           | (146 )  |
| Net increase (decrease) in notes and debt outstanding under revolving credit facilities   | (105 )                           | 5       |
| Principal payments under financing arrangements and capital lease obligations             | (1 )                             | (1 )    |
| Debt issuance costs   | (1 )                             | (7 )    |
| Proceeds from financed lease obligations  | 12                               | 20      |
| Proceeds from exercise of stock options   | —                                | 1       |
| Dividends paid by subsidiaries to non-controlling interest                                | (19 )                            | (20 )   |
| Other financing activities  | 1                                | —       |
| Net cash provided by (used in) financing activities                                       | (71 )                            | 17      |
| Effect of exchange rate changes on cash and cash equivalents                              | 18                               | (26 )   |
| Increase (decrease) in cash and cash equivalents  | (323 )                           | 86      |
| Cash and cash equivalents at beginning of the period                                      | 912                              | 497     |
| Cash and cash equivalents at end of the period  | \$589                            | \$583   |

See Notes to Consolidated Financial Statements

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Navistar International Corporation and Subsidiaries  
Consolidated Statements of Stockholders' Deficit  
(Unaudited)

| (in millions)   | Series<br>D<br>Convertible<br>Junior<br>Preference<br>Stock | Common<br>Stock | Additional<br>Paid-in<br>Capital | Accumulated<br>Deficit | Accumulated<br>Other<br>Comprehensive<br>Income<br>(Loss) | Common<br>Stock<br>Held in<br>Treasury<br>at cost | Stockholders'<br>Equity<br>Attributable<br>to<br>Non-controlling<br>Interests | Total     |
|---|---|-----------------|----------------------------------|------------------------|---|---|---|-----------|
| Balance as of October 31, 2015  | \$ 2  | \$ 9            | \$ 2,499                         | \$ (4,866 )            | \$ (2,601 )   | \$ (210 )   | \$ 7  | \$(5,160) |
| Net income (loss)   | —   | —               | —                                | (29 )                  | —   | —   | 18  | (11 )     |
| Total other comprehensive income  | —   | —               | —                                | —                      | 65  | —   | —   | 65        |
| Stock-based compensation  | —   | —               | 2                                | —                      | —   | —   | —   | 2         |
| Stock ownership programs  | —   | —               | (4 )                             | —                      | —   | 4   | —   | —         |
| Cash dividends paid to<br>non-controlling interest  | —   | —               | —                                | —                      | —   | —   | (19 )   | (19 )     |
| Acquisition of remaining ownership<br>interest from non-controlling<br>interest holder        | —   | —               | 1                                | —                      | —   | —   | —   | 1         |
| Other   | —   | —               | —                                | —                      | —   | —   | 1   | 1         |
| Balance as of April 30, 2016  | \$ 2  | \$ 9            | \$ 2,498                         | \$ (4,895 )            | \$ (2,536 )   | \$ (206 )   | \$ 7  | \$(5,121) |
| Balance as of October 31, 2014  | \$ 3  | \$ 9            | \$ 2,500                         | \$ (4,682 )            | \$ (2,263 )   | \$ (221 )   | \$ 34   | \$(4,620) |
| Net income (loss)   | —   | —               | —                                | (106 )                 | —   | —   | 16  | (90 )     |
| Total other comprehensive loss  | —   | —               | —                                | —                      | (21 )   | —   | —   | (21 )     |
| Transfer from redeemable equity<br>securities upon exercise or<br>expiration of stock options | —   | —               | 1                                | —                      | —   | —   | —   | 1         |
| Stock-based compensation  | —   | —               | 6                                | —                      | —   | —   | —   | 6         |
| Stock ownership programs  | —   | —               | (9 )                             | —                      | —   | 8   | —   | (1 )      |
| Cash dividends paid to<br>non-controlling interest  | —   | —               | —                                | —                      | —   | —   | (20 )   | (20 )     |
| Balance as of April 30, 2015  | \$ 3  | \$ 9            | \$ 2,498                         | \$ (4,788 )            | \$ (2,284 )   | \$ (213 )   | \$ 30   | \$(4,745) |

See Notes to Consolidated Financial Statements

Navistar International Corporation and Subsidiaries

Notes to 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 entities are Navistar, Inc. and Navistar Financial Corporation ("NFC").

References herein to the "Company," "we," "our," or "us" refer collectively to NIC and its consolidated subsidiaries, including certain variable interest entities ("VIEs") of which we are the primary beneficiary. We operate in four principal industry segments: Truck, Parts, Global Operations (collectively called "Manufacturing operations"), and Financial Services, which consists of NFC and our foreign finance operations (collectively called "Financial Services operations"). These segments are discussed in Note 12, Segment Reporting.

Our fiscal year ends on October 31. As such, all references to 2016 and 2015 contained within this Quarterly Report on Form 10-Q relate to the fiscal year, unless otherwise indicated.

Basis of Presentation and Consolidation

The accompanying unaudited consolidated financial statements include the assets, liabilities, and results of operations of our Manufacturing operations, which include majority-owned dealers ("Dealcors"), and our Financial Services operations, including VIEs of which we are the primary beneficiary. The effects of transactions among consolidated entities have been eliminated to arrive at the consolidated amounts.

Reclassifications were made to present the net change in secured revolving credit facilities as a separate line rather than within proceeds from issuance of securitized debt and principal payments on securitized debt in the Condensed Consolidated Statements of Cash Flows. This reclassification did not have an impact on the amount of net cash from financing activities as reported in our Condensed Consolidated Statements of Cash Flows.

We prepared the accompanying unaudited consolidated financial statements in accordance with United States ("U.S.") generally accepted accounting principles ("U.S. GAAP") for interim financial information and the instructions to the Quarterly Report on Form 10-Q and Article 10 of Regulation S-X issued by the U.S. Securities and Exchange Commission ("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 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, 2015, which should be read in conjunction with the disclosures therein. In our opinion, these interim consolidated 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 have an interest in several VIEs, primarily joint ventures, established to manufacture or distribute products and enhance our operational capabilities. We have determined for certain of our VIEs that we are the primary beneficiary because we have the power to direct the activities of the VIE that most significantly impact its economic performance and we have the obligation to absorb losses of, or the right to receive benefits from, the VIE that could potentially be significant to the VIE. 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 these VIEs. Assets of these entities are not readily available to satisfy claims against our general assets.

We are the primary beneficiary of our Blue Diamond Parts ("BDP") joint venture with Ford Motor Company ("Ford"). As a result, our Consolidated Balance Sheets include assets of \$49 million and \$50 million and liabilities of \$9 million and \$7 million as of April 30, 2016 and October 31, 2015, respectively, including \$2 million and \$7 million of cash and cash equivalents, at the respective dates, which are not readily available to satisfy claims against our general assets. The creditors of BDP do not have recourse to our general credit.



Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

Our Financial Services segment consolidates several VIEs. As a result, our Consolidated Balance Sheets include secured assets of \$1.0 billion and \$1.1 billion as of April 30, 2016 and October 31, 2015, respectively, and liabilities of \$870 million and \$844 million as of April 30, 2016 and October 31, 2015, respectively, all of which are involved in securitizations that are treated as asset-backed debt. In addition, our Consolidated Balance Sheets include secured assets of \$277 million and \$235 million as of April 30, 2016 and October 31, 2015, respectively, and corresponding liabilities of \$171 million and \$107 million, at the respective dates, which are related to other secured transactions that do not qualify for sale accounting treatment, and therefore, are treated as borrowings secured by operating and finance leases. Investors that hold securitization debt have a priority claim on the cash flows generated by their respective securitized assets to the extent that the related VIEs are required to make principal and interest payments. Investors in securitizations of these entities have no recourse to our general credit.

We also have an interest in other VIEs, which we do not consolidate because we are not the primary beneficiary. Our financial support and maximum loss exposure relating to these non-consolidated VIEs are 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. Equity in income of non-consolidated affiliates includes our share of the net income of these entities.

#### Product Warranty Liability

The following table presents accrued product warranty and deferred warranty revenue activity:

| (in millions)   | Six Months<br>Ended April<br>30, |         |
|---|----------------------------------|---------|
|   | 2016                             | 2015    |
| Balance at beginning of period                                    | \$994                            | \$1,197 |
| Costs accrued and revenues deferred                               | 69                               | 116     |
| Currency translation adjustment                                   | 1                                | (5 )    |
| Adjustments to pre-existing warranties <sup>(A)</sup>             | 51                               | (39 )   |
| Payments and revenues recognized                                  | (208 )                           | (210 )  |
| Balance at end of period  | 907                              | 1,059   |
| Less: Current portion   | 429                              | 496     |
| Noncurrent accrued product warranty and deferred warranty revenue | \$478                            | \$563   |

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. Our (A) warranty liability is generally affected by component failure rates, repair costs, and the timing of failures. Future events and circumstances related to these factors could materially change our estimates and require adjustments to our liability. In addition, new product launches require a greater use of judgment in developing estimates until historical experience becomes available.

In the second quarter of 2016, we recorded a charge for adjustments to pre-existing warranties of \$46 million or \$0.56 per diluted share. The pre-existing charges primarily relate to increases in both claim frequency and cost of repair across both the Medium Duty and Big Bore engine families. These charges increase the reserve for Navistar's standard warranty obligations as well as the loss positions related to our Big Bore extended service contracts. In the first quarter of 2015, we recorded a benefit for adjustments to pre-existing warranties of \$57 million or \$0.70 per diluted share. The impact of income taxes on the adjustments are not material due to our deferred tax valuation allowances on our U.S. deferred tax assets.

#### Extended Warranty Programs



The amount of deferred revenue related to extended warranty programs was \$367 million and \$401 million at April 30, 2016 and October 31, 2015, respectively. Revenue recognized under our extended warranty programs was \$38 million and \$76 million, in the three and six months ended April 30, 2016, respectively, and \$38 million and \$75 million for the three and six months ended April 30, 2015, respectively.

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 for the periods presented. Significant estimates and assumptions are used for, but are not limited to, pension and other postretirement benefits, allowance for doubtful accounts, income tax contingency accruals and valuation allowances, product warranty accruals, used truck inventory valuations, asbestos and other product liability accruals, asset impairment charges, restructuring charges and litigation-related accruals. Actual results could differ from our estimates.

Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

#### Concentration Risks

Our financial condition, results of operations, and cash flows are subject to concentration risks related to our significant unionized workforce. As of April 30, 2016, approximately 5,300, or 79%, of our hourly workers and approximately 300, or 5%, of our salaried workers, are represented by labor unions and are covered by collective bargaining agreements. Our future operations may be affected by changes in governmental procurement policies, budget considerations, changing national defense requirements, and political, regulatory and economic developments in the U.S. and certain foreign countries (primarily Canada, Mexico, and Brazil).

#### Inventories

Inventories are valued at the lower of cost or market. Our gross used truck inventory increased to approximately \$448 million at April 30, 2016 from \$390 million at October 31, 2015, offset by reserves of \$168 million and \$110 million, respectively. During the three and six months ended April 30, 2016, additional reserves of \$23 million and \$58 million, respectively, were recorded primarily in Costs of products sold.

In valuing our used truck inventory, we are required to make assumptions regarding the level of reserves required to value inventories at their net realizable value ("NRV"). Our judgments and estimates for used truck inventory are based on an analysis of current and forecasted sales prices, aging of and demand for used trucks, and the mix of sales through various market channels. The NRV is subject to change based on numerous conditions, including age, specifications, mileage, timing of sales, market mix and current and forecasted pricing. While calculations are made after taking these factors into account, significant management judgment regarding expectations for future events is involved. Future events that could significantly influence our judgment and related estimates include general economic conditions in markets where our products are sold, actions of our competitors, and the ability to sell used trucks in a timely manner.

#### Recently Adopted Accounting Standards

In the six months ended April 30, 2016, we have not adopted any new accounting guidance that has had a material impact on our consolidated financial statements.

#### Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers" (Topic 606), which supersedes the revenue recognition requirements in ASC 605, "Revenue Recognition." This ASU is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. In August 2015, the FASB issued ASU No. 2015-14, which postponed the effective date of ASU No. 2014-09 to fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017, with early adoption permitted on the original effective date for fiscal years beginning after December 15, 2016. Our effective date for this ASU is November 1, 2018. We are currently evaluating the method of adoption and the impact of this ASU on our consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases" (Topic 842). This ASU requires lessees to recognize, on the balance sheet, assets and liabilities for the rights and obligations created by leases of greater than twelve months. The accounting by lessors will remain largely unchanged. The ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, with early adoption permitted. Our effective date for this ASU is November 1, 2019. Adoption will require a modified retrospective transition. We are currently evaluating the method of adoption and the impact of this ASU on our consolidated financial statements.



Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

## 2. Restructurings and Impairments

Restructuring charges are recorded based on restructuring plans that have been committed to by management and are, in part, based upon management's best estimates of future events. Changes to the estimates may require future adjustments to the restructuring liabilities.

### Restructuring Liability

The following tables summarize the activity in the restructuring liability, which includes amounts related to discontinued operations and excludes pension and other postretirement contractual termination benefits:

| (in millions)                | Balance<br>at<br>October<br>31, 2015 | Additions | Payments | Adjustments | Balance<br>at April<br>30,<br>2016 |
|------------------------------|--------------------------------------|-----------|----------|-------------|------------------------------------|
| Employee termination charges | \$ 62                                | \$ 6      | \$ (49 ) | \$          | —\$ 19                             |
| Lease vacancy                | 5                                    | —         | (3 )     | —           | 2                                  |
| Other                        | 1                                    | —         | —        | —           | 1                                  |
| Restructuring liability      | \$ 68                                | \$ 6      | \$ (52 ) | \$          | —\$ 22                             |

| (in millions)                | Balance at<br>October 31, 2014 | Additions | Payments | Adjustments | Balance<br>at April<br>30,<br>2015 |
|------------------------------|--------------------------------|-----------|----------|-------------|------------------------------------|
| Employee termination charges | \$ 8                           | \$ 7      | \$ (4 )  | \$ (1 )     | \$ 10                              |
| Lease vacancy                | 11                             | —         | (4 )     | —           | 7                                  |
| Other                        | 1                              | —         | —        | —           | 1                                  |
| Restructuring liability      | \$ 20                          | \$ 7      | \$ (8 )  | \$ (1 )     | \$ 18                              |

### North American Manufacturing Restructuring Activities

We continue to focus on our core Truck and Parts businesses and evaluate our portfolio of assets to validate their strategic and financial fit. This allows us to close or divest non-core/non-strategic businesses, and identify opportunities to restructure our business and rationalize our Manufacturing operations in an effort to optimize our cost structure. For those areas that fall outside our core businesses, we are evaluating alternatives which could result in additional restructuring and other related charges in the future, including but not limited to: (i) impairments, (ii) costs for employee and contractor termination and other related benefits, and (iii) charges for pension and other postretirement contractual benefits and curtailments. These charges could be significant.

### Chatham restructuring activities

In the third quarter of 2011, we committed to close our Chatham, Ontario heavy truck plant, which had been idled since June 2009. At that time, we recognized curtailment and contractual termination charges related to postretirement plans. Based on a ruling regarding pension benefits received from the Financial Services Tribunal in Ontario, Canada, in the third quarter of 2014, we recognized additional charges of \$14 million related to the 2011 closure of the Chatham, Ontario plant. We appealed this ruling, but it was upheld in a July 3, 2015 decision issued by the Divisional Court of Ontario. On July 23, 2015, we filed a notice of motion for leave to appeal to the Court of Appeal for Ontario, which was perfected on August 25, 2015 through an additional filing. On December 21, 2015, the Ontario Court of Appeal denied the motion for leave to appeal. On April 25, 2016, we filed a qualified partial wind-up report for approval by the Financial Services Commission of Ontario. Potential charges in future periods could range from \$0 million to \$60 million, primarily related to pension, postretirement costs and termination benefits, which are subject to governmental approval, employee negotiation, acceptance rates and the resolution of disputes related thereto. In addition, we are evaluating the impact of the ruling on prior plan administration practices and it is probable that additional charges will be recognized, but those charges are currently not estimable.

### Foundry Facilities

In December 2014, we announced the closure of our Indianapolis, Indiana foundry facility and on June 30, 2015, we closed this foundry. In addition, on April 30, 2015, we sold our Waukesha, Wisconsin foundry operations. As a result, the Truck segment recognized charges of \$13 million and \$12 million in the first and second quarter of 2015, respectively, for the acceleration of depreciation of certain assets related to foundry and engine facilities. These charges are reported within Costs of products sold in our Consolidated Statements of Operations.

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Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

### Asset Impairments

In the six months ended April 30, 2016, we recorded \$5 million of Asset impairment charges in our Consolidated Statements of Operations, primarily due to \$3 million of asset impairment charges recorded in the Truck segment related to the sale of Pure Power Technologies ("PPT"), a components business focused on air and fuel systems, in February 2016.

In the six months ended April 30, 2015, we recorded \$8 million of Asset impairment charges in our Consolidated Statements of Operations, primarily due to \$7 million of asset impairment charges recorded in the Truck segment in the first quarter of 2015, resulting from a triggering event related to certain equipment leased to others.

### 3. Finance Receivables

Finance receivables are receivables of our Financial Services operations. Finance receivables generally consist of wholesale notes and accounts, as well as retail notes, finance leases and accounts. Total finance receivables reported on the Consolidated Balance Sheets are net of an allowance for doubtful accounts. Total assets of our Financial Services operations net of intercompany balances are \$2.3 billion and \$2.5 billion as of April 30, 2016 and October 31, 2015, respectively. Included in total assets of our Financial Services operations are finance receivables of \$1.8 billion and \$2.0 billion as of April 30, 2016 and October 31, 2015, respectively. We have two portfolio segments of finance receivables that we distinguish based on the type of customer and nature of the financing inherent to each portfolio. The retail portfolio segment represents loans or leases to end-users for the purchase or lease of vehicles. The wholesale portfolio segment represents loans to dealers to finance their inventory.

Our Finance receivables, net consist of the following:

| (in millions)                             | April 30, October 31, |        |
|---|-----------------------|--------|
|   | 2016                  | 2015   |
| Retail portfolio                          | \$ 506                | \$ 554 |
| Wholesale portfolio                       | 1,280                 | 1,467  |
| Total finance receivables                 | 1,786                 | 2,021  |
| Less: Allowance for doubtful accounts     | 25                    | 26     |
| Total finance receivables, net            | 1,761                 | 1,995  |
| Less: Current portion, net <sup>(A)</sup> | 1,552                 | 1,779  |
| Noncurrent portion, net                   | \$ 209                | \$ 216 |

The current portion of finance receivables is computed based on contractual maturities. Actual cash collections (A) typically vary from the contractual cash flows because of prepayments, extensions, delinquencies, credit losses, and renewals.

### Securitizations

Our Financial Services operations transfer wholesale notes, retail accounts receivable, retail notes, finance leases, and operating leases to special purpose entities ("SPEs"), which generally are only permitted to purchase these assets, issue asset-backed securities, and make payments on the securities issued. In addition to servicing receivables, our continued involvement in the SPEs may include an economic interest in the transferred receivables and, in some cases, managing exposure to interest rate changes on the securities using interest rate swaps or interest rate caps. There were no transfers of finance receivables that qualified for sale accounting treatment as of April 30, 2016 and October 31, 2015, and as a result, the transferred finance receivables are included in our Consolidated Balance Sheets and the related interest earned is included in Finance revenues.

We transfer eligible finance receivables into retail note owner trusts or wholesale note owner trusts in order to issue asset-backed securities. These trusts are VIEs of which we are determined to be the primary beneficiary and, therefore, the assets and liabilities of the trusts are included in our Consolidated Balance Sheets. The outstanding balance of finance receivables transferred into these VIEs was \$965 million and \$1.0 billion as of April 30, 2016 and October 31, 2015, respectively. Other finance receivables related to secured transactions that do not qualify for sale accounting

treatment were \$133 million and \$96 million as of April 30, 2016 and October 31, 2015, respectively. For more information on assets and liabilities of consolidated VIEs and other securitizations accounted for as secured borrowings by our Financial Services segment, see Note 1, Summary of Significant Accounting Policies.

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Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

Finance Revenues

The following table presents the components of our Finance revenues:

| (in millions)                           | Three Months Ended April 30, 2016 |       | Six Months Ended April 30, 2015 |       |
|---|-----------------------------------|-------|---------------------------------|-------|
|   | 2016                              | 2015  | 2016                            | 2015  |
| Retail notes and finance leases revenue | \$9                               | \$12  | \$19                            | \$25  |
| Wholesale notes interest                | 26                                | 24    | 52                              | 48    |
| Operating lease revenue                 | 16                                | 15    | 32                              | 30    |
| Retail and wholesale accounts interest  | 7                                 | 9     | 14                              | 17    |
| Gross finance revenues                  | 58                                | 60    | 117                             | 120   |
| Less: Intercompany revenues             | (25 )                             | (25 ) | (49 )                           | (49 ) |
| Finance revenues                        | \$33                              | \$35  | \$68                            | \$71  |

4. Allowance for Doubtful Accounts

Our two finance receivables portfolio segments, retail and wholesale, each consist of one class of receivable based on: (i) initial measurement attributes of the receivables, and (ii) the assessment and monitoring of risk and performance of the receivables. For more information, see Note 3, Finance Receivables.

The following tables present the activity related to our allowance for doubtful accounts for our retail portfolio segment, wholesale portfolio segment, and trade and other receivables:

| (in millions)   | Three Months Ended April 30, 2016 |                     |                             |       | Three Months Ended April 30, 2015 |                     |                             |       |
|---|-----------------------------------|---------------------|-----------------------------|-------|-----------------------------------|---------------------|-----------------------------|-------|
|   | Retail Portfolio                  | Wholesale Portfolio | Trade and Other Receivables | Total | Retail Portfolio                  | Wholesale Portfolio | Trade and Other Receivables | Total |
| Allowance for doubtful accounts, at beginning of period | \$19                              | \$ 4                | \$ 23                       | \$46  | \$23                              | \$ 3                | \$ 32                       | \$58  |
| Provision for doubtful accounts, net of recoveries      | 1                                 | —                   | 1                           | 2     | 3                                 | —                   | —                           | 3     |
| Charge-off of accounts <sup>(A)</sup>                   | (1 )                              | —                   | —                           | (1 )  | —                                 | —                   | —                           | —     |
| Other <sup>(B)</sup>                                    | 2                                 | —                   | 2                           | 4     | (1 )                              | —                   | (2 )                        | (3 )  |
| Allowance for doubtful accounts, at end of period       | \$21                              | \$ 4                | \$ 26                       | \$51  | \$25                              | \$ 3                | \$ 30                       | \$58  |

| (in millions)   | Six Months Ended April 30, 2016 |                     |                             |       | Six Months Ended April 30, 2015 |                     |                             |       |
|---|---------------------------------|---------------------|-----------------------------|-------|---------------------------------|---------------------|-----------------------------|-------|
|   | Retail Portfolio                | Wholesale Portfolio | Trade and Other Receivables | Total | Retail Portfolio                | Wholesale Portfolio | Trade and Other Receivables | Total |
| Allowance for doubtful accounts, at beginning of period | \$22                            | \$ 4                | \$ 22                       | \$48  | \$24                            | \$ 3                | \$ 38                       | \$65  |
| Provision for doubtful accounts, net of recoveries      | 3                               | —                   | 4                           | 7     | 5                               | —                   | —                           | 5     |
| Charge-off of accounts <sup>(A)</sup>                   | (4 )                            | —                   | (1 )                        | (5 )  | (1 )                            | —                   | (3 )                        | (4 )  |
| Other <sup>(B)</sup>                                    | —                               | —                   | 1                           | 1     | (3 )                            | —                   | (5 )                        | (8 )  |
| Allowance for doubtful accounts, at end of period       | \$21                            | \$ 4                | \$ 26                       | \$51  | \$25                            | \$ 3                | \$ 30                       | \$58  |

(A) We repossess sold and leased vehicles on defaulted finance receivables and leases, and place them into Inventories. Losses recognized at the time of repossession and charged against the allowance for doubtful accounts were less than \$1 million in both the three and six months ended April 30, 2016, as well as the three and six



months ended April 30, 2015.

(B) Amounts include impact from currency translation.

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Navistar International Corporation and Subsidiaries  
 Notes to Consolidated Financial Statements—(Continued)  
 (Unaudited)

The accrual of interest income is discontinued on certain impaired finance receivables. Impaired finance receivables include accounts with specific loss reserves and certain accounts that are on non-accrual status. In certain cases, we continue to collect payments on our impaired finance receivables.

The following table presents information regarding impaired finance receivables:

| (in millions)   | April 30, 2016   |                     |       | October 31, 2015 |                     |       |
|---|------------------|---------------------|-------|------------------|---------------------|-------|
|   | Retail Portfolio | Wholesale Portfolio | Total | Retail Portfolio | Wholesale Portfolio | Total |
| Impaired finance receivables with specific loss reserves    | \$21             | \$—                 | \$21  | \$21             | \$—                 | \$21  |
| Impaired finance receivables without specific loss reserves | —                | —                   | —     | —                | —                   | —     |
| Specific loss reserves on impaired finance receivables      | 11               | —                   | 11    | 9                | —                   | 9     |
| Finance receivables on non-accrual status                   | 21               | —                   | 21    | 21               | —                   | 21    |

The average balances of the impaired finance receivables in the retail portfolio were \$21 million and \$25 million during the six months ended April 30, 2016 and 2015, respectively.

We use the aging of our receivables as well as other inputs when assessing credit quality. The following table presents the aging analysis for finance receivables:

| (in millions)                       | April 30, 2016   |                     |         | October 31, 2015 |                     |         |
|-------------------------------------|------------------|---------------------|---------|------------------|---------------------|---------|
|                                     | Retail Portfolio | Wholesale Portfolio | Total   | Retail Portfolio | Wholesale Portfolio | Total   |
| Current, and up to 30 days past due | \$435            | \$ 1,276            | \$1,711 | \$486            | \$ 1,461            | \$1,947 |
| 30-90 days past due                 | 52               | 3                   | 55      | 48               | 4                   | 52      |
| Over 90 days past due               | 19               | 1                   | 20      | 20               | 2                   | 22      |
| Total finance receivables           | \$506            | \$ 1,280            | \$1,786 | \$554            | \$ 1,467            | \$2,021 |

5. Inventories

The following table presents the components of Inventories:

| (in millions)          | April 30, 2016 | October 31, 2015 |
|------------------------|----------------|------------------|
| Finished products      | \$ 859         | \$ 837           |
| Work in process        | 49             | 34               |
| Raw materials          | 312            | 264              |
| Total inventories, net | \$ 1,220       | \$ 1,135         |

Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

## 6. Debt

| (in millions)  | April 30,<br>2016 | October 31,<br>2015 |
|--|-------------------|---------------------|
| Manufacturing operations   |                   |                     |
| Senior Secured Term Loan Credit Facility, as amended, due 2020, net of unamortized discount of \$15 and \$17, respectively | \$ 1,022          | \$ 1,023            |
| 8.25% Senior Notes, due 2022, net of unamortized discount of \$17 and \$18, respectively                                   | 1,183             | 1,182               |
| 4.50% Senior Subordinated Convertible Notes, due 2018, net of unamortized discount of \$12 and \$14, respectively          | 188               | 186                 |
| 4.75% Senior Subordinated Convertible Notes, due 2019, net of unamortized discount of \$28 and \$32, respectively          | 383               | 379                 |
| Debt of majority-owned dealerships   | 13                | 28                  |
| Financing arrangements and capital lease obligations   | 46                | 49                  |
| Loan Agreement related to 6.5% Tax Exempt Bonds, due 2040  | 225               | 225                 |
| Financed lease obligations   | 75                | 111                 |
| Other  | 16                | 15                  |
| Total Manufacturing operations debt  | 3,151             | 3,198               |
| Less: Current portion  | 83                | 103                 |
| Net long-term Manufacturing operations debt  | \$ 3,068          | \$ 3,095            |
| (in millions)  | April 30,<br>2016 | October 31,<br>2015 |
| Financial Services operations  |                   |                     |
| Asset-backed debt issued by consolidated SPEs, at fixed and variable rates, due serially through 2021                      | \$ 933            | \$ 870              |
| Bank credit facilities, at fixed and variable rates, due dates from 2016 through 2021                                      | 947               | 1,063               |
| Commercial paper, at variable rates, program matures in 2017   | 88                | 86                  |
| Borrowings secured by operating and finance leases, at various rates, due serially through 2021                            | 106               | 81                  |
| Total Financial Services operations debt   | 2,074             | 2,100               |
| Less: Current portion  | 1,168             | 1,007               |
| Net long-term Financial Services operations debt   | \$ 906            | \$ 1,093            |

## Financial Services Operations

## Asset-backed Debt

In April 2016, Truck Retail Accounts Corporation ("TRAC"), one of our consolidated SPEs, renewed its \$100 million revolving facility for one year, to April 2017. Borrowings under this facility are secured by eligible retail accounts receivable.

In February 2016, the maximum capacity of NFC's wholesale variable funding notes ("VFN") facility was increased from \$375 million to \$500 million. The VFN facility is secured by assets of the wholesale note owner trust. In May 2016, the maturity date of the VFN facility was extended from October 2016 to May 2017.

Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

#### Bank Credit Facilities

In May 2016, NFC amended and extended its 2011 bank credit facility which was originally due in December 2016. The 2016 amendment extends the maturity date to June 2018 and initially reduces the revolving portion of the facility from \$500 million to \$400 million. The revolving portion will be further reduced to approximately \$275 million effective in December 2016. The amendment also provides for a reduction in the term loan facility, which was previously \$229 million, to approximately \$82 million, effective in December 2016, at which time the quarterly principal payments are reduced from \$9 million to \$2 million. The amendment allows NFC to increase revolving or term loan commitments, subject to obtaining commitments from existing or new lenders to provide additional or increased revolving commitments and/or additional term loans, to permit a maximum total facility size of \$700 million after giving effect to any such increase and without taking into account the non-extended loans and commitments. The portion of the outstanding amount as of April 30, 2016 that matures in June 2018 is classified as Long-term debt on our Consolidated Balance Sheets.

In March 2016, NFC paid \$30 million in cash dividends to Navistar, Inc. Dividends and certain affiliate loans are subject to the restricted payment covenants set forth in the NFC bank credit facility.

#### 7. Postretirement Benefits

##### Defined Benefit Plans

We provide postretirement benefits to a substantial portion of our employees and retirees. Costs associated with postretirement benefits include pension and postretirement health care expenses for employees, retirees, surviving spouses and dependents.

Generally, the 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 and six months ended April 30, 2016, we contributed \$21 million and \$40 million, respectively, and for the three and six months ended April 30, 2015, we contributed \$32 million and \$62 million, respectively, to our pension plans to meet regulatory funding requirements. We expect to contribute approximately \$57 million to our pension plans during the remainder of 2016.

We primarily fund other post-employment benefit ("OPEB") obligations, such as retiree medical, in accordance with a 1993 Settlement Agreement (the "1993 Settlement Agreement"), which requires us to fund a portion of the plans' annual service cost to a retiree benefit trust (the "Base Trust"). The 1993 Settlement Agreement resolved a class action lawsuit originally filed in 1992 regarding the restructuring of our then applicable retiree health care and life insurance benefits. Contributions for the three and six months ended April 30, 2016 and 2015, as well as anticipated contributions for the remainder of 2016, are not material.

##### Components of Net Periodic Benefit Expense

Net periodic benefit expense included in our Consolidated Statements of Operations is comprised of the following:

|  | Three Months Ended |          | Health and |          | Six Months Ended |          | Health and |          |
|--|--------------------|----------|------------|----------|------------------|----------|------------|----------|
|  | April 30,          |          | Life       |          | April 30,        |          | Life       |          |
|  | Pension            | Benefits | Insurance  | Benefits | Pension          | Benefits | Insurance  | Benefits |
| (in millions)                                      | 2016               | 2015     | 2016       | 2015     | 2016             | 2015     | 2016       | 2015     |
| Service cost for benefits earned during the period | \$3                | \$3      | \$2        | \$2      | \$5              | \$6      | \$3        | \$3      |
| Interest on obligation                             | 29                 | 35       | 15         | 18       | 59               | 71       | 30         | 36       |
| Amortization of cumulative loss                    | 26                 | 24       | 8          | 9        | 52               | 49       | 16         | 19       |
| Amortization of prior service benefit              | —                  | —        | (1)        | (1)      | —                | —        | (1)        | (2)      |
| Contractual termination benefits                   | 2                  | (1)      | —          | (1)      | 2                | (1)      | —          | (1)      |
| Premiums on pension insurance                      | 4                  | 4        | —          | —        | 8                | 5        | —          | —        |

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|                              |       |       |      |      |       |       |       |       |
|------------------------------|-------|-------|------|------|-------|-------|-------|-------|
| Expected return on assets    | (42 ) | (48 ) | (7 ) | (8 ) | (84 ) | (97 ) | (13 ) | (15 ) |
| Net periodic benefit expense | \$22  | \$17  | \$17 | \$19 | \$42  | \$33  | \$35  | \$40  |

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Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

In 2016, we changed the approach utilized to estimate the service cost and interest cost components of net periodic benefit cost for our major defined benefit postretirement plans. Historically, we estimated the service cost and interest cost components using a single weighted average discount rate derived from the yield curve used to measure the benefit obligation at the beginning of the period. In 2016, we are using a spot rate approach for the estimation of service and interest cost for our major plans by applying specific spot rates along the yield curve to the relevant projected cash flows, to provide a better estimate of service and interest costs. Interest on the obligation as reported above is \$9 million and \$4 million lower in the three months ended April 30, 2016 for pension and for health and life insurance, respectively, and \$18 million and \$8 million lower in the six months ended April 30, 2016 for pension and for health and life insurance, respectively, as a result of using the spot rate approach compared to the historical approach.

#### 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. We deposit the matching contribution annually. Many participants covered by the plans receive annual Company contributions to their retirement accounts based on an age-weighted percentage of the participant's eligible compensation for the calendar year. Defined contribution expense pursuant to these plans was \$8 million and \$15 million in the three and six months ended April 30, 2016, respectively, and \$8 million and \$17 million in the three and six months ended April 30, 2015, respectively.

In accordance with the 1993 Settlement Agreement, an independent Retiree Supplemental Benefit Trust (the "Supplemental Trust") was established. The Supplemental Trust, and the benefits it provides to certain retirees pursuant to a certain Retiree Supplemental Benefit Program under the 1993 Settlement Agreement ("Supplemental Benefit Program"), is not part of our consolidated financial statements.

Our contingent profit sharing obligations under a certain Supplemental Benefit Trust Profit Sharing Plan ("Supplemental Benefit Trust Profit Sharing Plan") will continue until certain funding targets defined by the 1993 Settlement Agreement are met. We have recorded no profit sharing accruals based on the operating performance of the entities that are included in the determination of qualifying profits. For more information on pending arbitration regarding the Supplemental Benefit Trust Profit Sharing Plan, see Note 11, Commitments and Contingencies.

#### 8. Income Taxes

We compute, on a quarterly basis, an estimated annual effective tax rate considering ordinary income and related income tax expense. For all periods presented, U.S. and certain foreign results are excluded from ordinary income due to ordinary losses for which no benefit can be recognized. Ordinary income refers to income (loss) before income tax expense excluding significant unusual or infrequently occurring items. The tax effect of a significant unusual or infrequently occurring item is recorded in the interim period in which the item occurs. Items included in income tax expense in the periods in which they occur include the tax effects of material restructurings, impairments, 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 regarding the ability to realize deferred tax assets in future years.

In the first quarter of 2016, we reviewed the impact of recently enacted U.S. tax legislation, the most significant of which is the Protecting Americans from Tax Hikes Act of 2015 ("PATH Act of 2015"), which extended the rules allowing us to forego bonus depreciation in exchange for refunds of previously paid Alternative Minimum Tax ("AMT"). This change resulted in the likely realization of our deferred AMT credits, on a more likely than not basis, which supports the release of the associated valuation allowance. In addition, the PATH Act of 2015 extended the "look-through rule," under subpart F of the U.S. Internal Revenue Code, which had expired for us on September 30, 2015. The "look-through rule" had provided an exception to the U.S. taxation of certain income generated by foreign subsidiaries. The rule was extended in December 2015 with retroactive effect to the beginning of our 2016 fiscal year, and the rule will remain in place through our 2020 fiscal year. This rule extension allowed us to reverse recently

recognized deferred tax liabilities associated with earnings in foreign jurisdictions. However, since the reversal of this deferred tax liability also had an associated and completely offsetting valuation allowance effect, there was no impact to total deferred taxes due to this change.

Also in the first quarter of 2016, we elected to early adopt the provisions of ASU 2015-17, "Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes." This ASU requires the offset of all deferred tax assets and liabilities, including valuation allowances, for each tax-paying jurisdiction within each tax-paying component. The net deferred tax must be presented as a single noncurrent amount for each jurisdiction. In accordance with the adoption provisions of ASU 2015-17 we have chosen to apply this change prospectively, and as a result, prior year amounts are maintained as originally filed.

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We have evaluated the need to maintain a valuation allowance for deferred tax assets based on our 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. As mentioned above, we have concluded that the valuation allowance on our U.S. deferred AMT credits is no longer necessary due to the enactment of the PATH Act of 2015. This partial valuation allowance release resulted in an income tax benefit of \$13 million. We continue to maintain a valuation allowance on our remaining U.S. deferred tax assets, as well as certain foreign deferred tax assets, that we believe, on a more-likely-than-not basis, will not be realized. For all remaining deferred tax assets, while we believe at April 30, 2016 that it is more likely than not that they will be realized, it is reasonably possible that additional deferred tax asset valuation allowances could be required in the next twelve months.

We 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 consolidated financial statements from such a position are measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement. As of April 30, 2016, the amount of liability for uncertain tax positions was \$42 million. The liability at April 30, 2016 has a recorded offsetting tax benefit associated with various issues that total \$12 million. If the unrecognized tax benefits are recognized, all would impact our effective tax rate. However, to the extent we continue to maintain a full valuation allowance against certain deferred tax assets, the effect may be in the form of an increase in the deferred tax asset related to our net operating loss carryforward, which would be offset by a full valuation allowance.

We recognize interest and penalties related to uncertain tax positions as part of Income tax expense. For the three and six months ended April 30, 2016, total interest and penalties related to our uncertain tax positions resulted in an income tax expense of less than \$1 million for both periods.

We have open tax years back to 2001 with various significant taxing jurisdictions including 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. Annual 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.



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9. Fair Value Measurements

For assets and liabilities measured at fair value on a recurring and nonrecurring basis, a three-level hierarchy of measurements based upon observable and unobservable inputs is used to arrive at fair value. Observable inputs are developed based on market data obtained from independent sources, while unobservable inputs reflect our assumptions about valuation based on the best information available in the circumstances. 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 an original maturity of 90 days or less, including U.S. Treasury bills, federal agency securities, and commercial paper, as cash equivalents. The carrying amounts of cash and cash equivalents and restricted cash approximate fair value because of the short-term maturity and highly liquid nature of these instruments.

**Marketable Securities**—Our marketable securities portfolios are classified as available-for-sale and primarily include investments in U.S. government securities and commercial paper with an original maturity greater than 90 days. We use quoted prices from active markets to determine fair value.

**Derivative Assets and Liabilities**—We measure the fair value of derivatives assuming that the unit of account is an individual derivative transaction and that each 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 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 is not active. Measurements based upon these unobservable inputs are classified within Level 3. For more information regarding derivatives, see Note 10, Financial Instruments and Commodity Contracts.

**Guarantees**—We provide certain guarantees of payments and residual values to specific counterparties. Fair value of these guarantees is based upon internally developed models that utilize current market-based assumptions and historical data. We classify these liabilities within Level 3. For more information regarding guarantees, see Note 11, Commitments and Contingencies.

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The following table presents the financial instruments measured at fair value on a recurring basis:

| (in millions)                              | April 30, 2016 |             |              |              | October 31, 2015 |             |              |              |
|--|----------------|-------------|--------------|--------------|------------------|-------------|--------------|--------------|
|  | Level 1        | Level 2     | Level 3      | Total        | Level 1          | Level 2     | Level 3      | Total        |
| <b>Assets</b>                              |                |             |              |              |                  |             |              |              |
| <b>Marketable securities:</b>              |                |             |              |              |                  |             |              |              |
| U.S. Treasury bills                        | \$41           | \$ —        | \$ —         | \$41         | \$53             | \$ —        | \$ —         | \$53         |
| Other                                      | 187            | —           | —            | 187          | 106              | —           | —            | 106          |
| <b>Derivative financial instruments:</b>   |                |             |              |              |                  |             |              |              |
| Commodity forward contracts <sup>(A)</sup> | —              | 6           | —            | 6            | —                | —           | —            | —            |
| Foreign currency contracts <sup>(A)</sup>  | —              | —           | —            | —            | —                | 1           | —            | 1            |
| <b>Total assets</b>                        | <b>\$228</b>   | <b>\$ 6</b> | <b>\$ —</b>  | <b>\$234</b> | <b>\$159</b>     | <b>\$ 1</b> | <b>\$ —</b>  | <b>\$160</b> |
| <b>Liabilities</b>                         |                |             |              |              |                  |             |              |              |
| <b>Derivative financial instruments:</b>   |                |             |              |              |                  |             |              |              |
| Commodity forward contracts <sup>(B)</sup> | \$—            | \$ 2        | \$ —         | \$2          | \$—              | \$ 2        | \$ —         | \$2          |
| Foreign currency contracts <sup>(B)</sup>  | —              | 5           | —            | 5            | —                | 2           | —            | 2            |
| Guarantees                                 | —              | —           | 19           | 19           | —                | —           | 10           | 10           |
| <b>Total liabilities</b>                   | <b>\$—</b>     | <b>\$ 7</b> | <b>\$ 19</b> | <b>\$26</b>  | <b>\$—</b>       | <b>\$ 4</b> | <b>\$ 10</b> | <b>\$14</b>  |

(A) The asset value of commodity forward contracts and foreign currency contracts is included in other current assets as of April 30, 2016 and October 31, 2015 in the accompanying Consolidated Balance Sheets.

(B) The liability value of commodity forward contracts and foreign currency contracts is included in other current liabilities as of April 30, 2016 and October 31, 2015 in the accompanying Consolidated Balance Sheets.

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

| (in millions)   | Three Months Ended April 30, |       | Six Months Ended April 30, |       |
|---|------------------------------|-------|----------------------------|-------|
|   | 2016                         | 2015  | 2016                       | 2015  |
| Guarantees, at beginning of period                            | \$(10)                       | \$(8) | \$(10)                     | \$(8) |
| Transfers out of Level 3                                      | —                            | —     | —                          | —     |
| Issuances   | (10)                         | —     | (11)                       | —     |
| Settlements   | 1                            | 1     | 2                          | 1     |
| Guarantees, at end of period                                  | \$(19)                       | \$(7) | \$(19)                     | \$(7) |
| Change in unrealized gains on assets (liabilities) still held | \$—                          | \$—   | \$—                        | \$—   |

The following table presents the financial instruments measured at fair value on a nonrecurring basis:

| (in millions)   | April 30, October 31, |              |
|---|-----------------------|--------------|
|   | 2016                  | 2015         |
| <b>Level 2 financial instruments</b>                          |                       |              |
| Carrying value of impaired finance receivables <sup>(A)</sup> | \$ 21                 | \$ 21        |
| Specific loss reserve   | (11)                  | (9)          |
| <b>Fair value</b>   | <b>\$ 10</b>          | <b>\$ 12</b> |

(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. Fair values of the underlying collateral are determined by reference to dealer vehicle value publications adjusted for certain market factors.

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In addition to the methods and assumptions we use for the financial instruments recorded at fair value as discussed above, we use the following methods and assumptions to estimate the fair value for our other financial instruments that are not marked to market on a recurring basis. The carrying amounts of Cash and cash equivalents, Restricted cash, and Accounts payable approximate fair values because of the short-term maturity and highly liquid nature of these instruments. Finance receivables generally consist of retail and wholesale accounts and retail and wholesale notes. The carrying amounts of Trade and other receivables and retail and wholesale accounts approximate fair values as a result of the short-term nature of the receivables. The carrying amounts of wholesale notes approximate fair values as a result of the short-term nature of the wholesale notes and their variable interest rate terms. Due to the nature of the aforementioned financial instruments, they have been excluded from the fair value amounts presented in the table below.

The fair values of our retail notes are estimated by discounting expected cash flows at estimated current market rates. The fair values of our retail notes are classified as Level 3 financial instruments.

The fair values of our debt instruments classified as Level 1 were determined using quoted market prices. The 6.5% Tax Exempt Bonds, due 2040, are traded, but the trading market is illiquid, and as a result, the Loan Agreement underlying the Tax Exempt Bonds is classified as Level 2. The fair values of our Level 3 debt instruments are generally determined using internally developed valuation techniques such as discounted cash flow modeling. Inputs such as discount rates and credit spreads reflect our estimates of assumptions that market participants would use in pricing the instrument and may be unobservable.

The following tables present the carrying values and estimated fair values of financial instruments:

| (in millions)   | As of April 30, 2016 |         |         |                |
|---|----------------------|---------|---------|----------------|
|   | Estimated Fair Value |         |         | Carrying Value |
|   | Level 1              | Level 2 | Level 3 |                |
| <b>Assets</b>   |                      |         |         |                |
| Retail notes  | \$—                  | \$—     | \$146   | \$ 145         |
| Notes receivable  | —                    | 1       | 1       | 1              |
| <b>Liabilities</b>  |                      |         |         |                |
| <b>Debt:</b>  |                      |         |         |                |
| <b>Manufacturing operations</b>   |                      |         |         |                |
| Senior Secured Term Loan Credit Facility, as Amended, due 2020                                  | —                    | 986     | 986     | 1,022          |
| 8.25% Senior Notes, due 2022  | 872                  | —       | 872     | 1,183          |
| 4.50% Senior Subordinated Convertible Notes, due 2018 <sup>(A)</sup>                            | —                    | 141     | 141     | 188            |
| 4.75% Senior Subordinated Convertible Notes, due 2019 <sup>(A)</sup>                            | —                    | 276     | 276     | 383            |
| Debt of majority-owned dealerships  | —                    | 13      | 13      | 13             |
| Financing arrangements  | —                    | 15      | 15      | 40             |
| Loan Agreement related to 6.50% Tax Exempt Bonds, due 2040                                      | —                    | 227     | 227     | 225            |
| Financed lease obligations  | —                    | 75      | 75      | 75             |
| Other   | —                    | 16      | 16      | 16             |
| <b>Financial Services operations</b>  |                      |         |         |                |
| Asset-backed debt issued by consolidated SPEs, at various rates, due serially through 2021      | —                    | 929     | 929     | 933            |
| Bank credit facilities, at fixed and variable rates, due dates from 2016 through 2021           | —                    | 930     | 930     | 947            |
| Commercial paper, at variable rates, program matures in 2017                                    | 88                   | —       | 88      | 88             |
| Borrowings secured by operating and finance leases, at various rates, due serially through 2021 | —                    | 106     | 106     | 106            |



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| (in millions)   | As of October 31, 2015 |         |         |                |
|---|------------------------|---------|---------|----------------|
|   | Estimated Fair Value   |         |         | Carrying Value |
|   | Level 1                | Level 2 | Level 3 |                |
| Assets  |                        |         |         |                |
| Retail notes  | \$—                    | \$—     | \$170   | \$ 166         |
| Notes receivable  | —                      | 3       | 3       | 3              |
| Liabilities   |                        |         |         |                |
| Debt:   |                        |         |         |                |
| Manufacturing operations  |                        |         |         |                |
| Senior Secured Term Loan Credit Facility, as Amended, due 2020                                  | —                      | 1,014   | 1,014   | 1,023          |
| 8.25% Senior Notes, due 2022  | 998                    | —       | 998     | 1,182          |
| 4.50% Senior Subordinated Convertible Notes, due 2018 <sup>(A)</sup>                            | —                      | 148     | 148     | 186            |
| 4.75% Senior Subordinated Convertible Notes, due 2019 <sup>(A)</sup>                            | —                      | 289     | 289     | 379            |
| Debt of majority-owned dealerships  | —                      | 28      | 28      | 28             |
| Financing arrangements  | —                      | 17      | 17      | 43             |
| Loan Agreement related to 6.50% Tax Exempt Bonds, due 2040                                      | —233                   | —       | 233     | 225            |
| Financed lease obligations  | —                      | 111     | 111     | 111            |
| Other   | —                      | 17      | 17      | 15             |
| Financial Services operations   |                        |         |         |                |
| Asset-backed debt issued by consolidated SPEs, at various rates, due serially through 2018      | —                      | 865     | 865     | 870            |
| Bank credit facilities, at fixed and variable rates, due dates from 2016 through 2020           | —                      | 1,048   | 1,048   | 1,063          |
| Commercial paper, at variable rates, program matures in 2017                                    | 86                     | —       | 86      | 86             |
| Borrowings secured by operating and finance leases, at various rates, due serially through 2020 | —                      | 80      | 80      | 81             |

The carrying value represents the consolidated financial statement amount of the debt which excludes the (A) allocation of the conversion feature to equity, while the fair value is based on internally developed valuation techniques such as discounted cash flow modeling for Level 3 convertible notes which include the equity feature.

#### 10. 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, reduce exchange rate risk for transactional exposures denominated in currencies other than the functional currency, and minimize the effect of 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 affect 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. In addition, we also use commodity forward contracts to manage our exposure to variability in certain commodity prices.

We generally do not enter into derivative financial instruments for speculative or trading purposes and did not during the three and six months ended April 30, 2016 and 2015. None of our derivatives qualified for hedge accounting treatment during the three and six months ended April 30, 2016 and 2015.



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The majority of our derivative contracts are transacted under International Swaps and Derivatives Association ("ISDA") master agreements. Each agreement permits the net settlement of amounts owed in the event of default or certain other termination events. For derivative financial instruments, we have elected not to offset derivative positions in the balance sheet with the same counterparty under the same agreement. Collateral is generally not required to be provided by our counter-parties for derivative contracts. However, certain of our derivative contracts contain provisions that require us to provide collateral if certain loss thresholds are exceeded. Collateral of \$2 million was provided as of April 30, 2016 and \$1 million of collateral was provided as of October 31, 2015. 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 instruments. 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 assets that have been recorded, but have not yet been received in cash. At April 30, 2016 and October 31, 2015, our exposure to the credit risk of others was \$6 million and \$1 million, respectively.

The following table presents the location and amount of loss (gain) recognized in our Consolidated Statements of Operations related to derivatives:

| (in millions)               | Location in Consolidated Statements of Operations | Three Months Ended April 30, 2016 |       | Six Months Ended April 30, 2015 |      |
|-----------------------------|---|-----------------------------------|-------|---------------------------------|------|
|                             |   | 2016                              | 2015  | 2016                            | 2015 |
| Cross currency swaps        | Other income, net                                 | \$—                               | \$ 1  | \$—                             | \$ 3 |
| Foreign currency contracts  | Other income, net                                 | 5                                 | —     | 4                               | 1    |
| Commodity forward contracts | Costs of products sold                            | (7 )                              | (5 )  | (2 )                            | 5    |
| Total (income) loss         |   | \$(2)                             | \$(4) | \$ 2                            | \$ 9 |

Foreign Currency Contracts

During 2016 and 2015, we entered into foreign exchange forward and option contracts as economic hedges of anticipated cash flows denominated in Brazilian Reais, Euros, Canadian Dollars, and Mexican Pesos. All contracts were entered into to protect against the risk that the eventual cash flows resulting from certain transactions would be affected by changes in exchange rates between the U.S. Dollar and the respective foreign currency.

The following table presents the outstanding foreign currency contracts as of April 30, 2016 and October 31, 2015:

| (in millions)             | Currency | Notional Amount | Maturity                                    |
|---------------------------|----------|-----------------|---|
| As of April 30, 2016      |          |                 |   |
| Forward exchange contract | EUR      | € 19            | April 2016 - October 2016 <sup>(A)</sup>    |
| Forward exchange contract | CAD      | C\$75           | April 2016 - September 2016 <sup>(B)</sup>  |
| Forward exchange contract | MXN      | 868             | April 2016 - May 2016 <sup>(C)</sup>        |
| As of October 31, 2015    |          |                 |   |
| Forward exchange contract | EUR      | € 30            | November 2015 - October 2016 <sup>(D)</sup> |
| Forward exchange contract | CAD      | C\$25           | November 2015                               |
| Forward exchange contract | MXN      | 1,270           | November 2015                               |

(A) Forward exchange contracts of €3 million matured in April 2016 but settled in May 2016, €4 million matured in May 2016, €4 million mature in June 2016, and €2 million mature each month from July 2016 through October 2016.

(B) Forward exchange contracts of C\$15 million matured in April 2016 but settled in May 2016, C\$15 million matured in May 2016, C\$15 million mature in June and July 2016, C\$10 million mature in August 2016, and C\$5 million mature in September 2016.



(C) Forward exchange contracts of 436 million matured in April 2016 but settled in May 2016 and 432 million matured in May 2016.

(D) Forward exchange contracts of €2 million settled in November 2015, €3 million matured in November 2015, €3 million matured in December 2015, €4 million matured in January 2016, and €2 million mature each month from February 2016 through October 2016.

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#### Commodity Forward Contracts

During 2016 and 2015, we entered into commodity forward contracts as economic hedges of our exposure to variability in commodity prices for diesel fuel and steel. As of April 30, 2016, we had outstanding diesel fuel contracts with aggregate notional values of \$18 million and outstanding steel contracts with aggregate notional values of \$18 million. The commodity forward contracts have various maturity dates through March 31, 2017. As of October 31, 2015, we had outstanding diesel fuel contracts with aggregate notional values of \$24 million and outstanding steel contracts with aggregate notional values of \$6 million. All of these contracts were entered into to protect against the risk that the eventual cash flows related to purchases of the commodities will be affected by changes in prices.

#### Interest-Rate Contracts

From time to time, we enter into various interest-rate contracts, interest rate caps, and cross currency swaps. As of both April 30, 2016 and October 31, 2015, there were no outstanding cross currency swaps. We are exposed to interest rate and exchange rate risk as a result of our borrowing activities. The objective of these contracts is to mitigate fluctuations in earnings, cash flows, and fair value of borrowings. Our Mexican financial services operation uses interest rate caps and cross currency swaps to protect against the potential of rising interest rates as required by the terms of its variable-rate asset-backed securities, and fluctuations in the value of the peso, as required under our Mexican bank credit facilities. As of April 30, 2016 and October 31, 2015, the notional amount of our outstanding interest rate caps at our Mexican financial services operation was \$141 million and \$108 million, respectively.

#### 11. 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. We have recognized liabilities for some of these guarantees in our Consolidated Balance Sheets as they meet the recognition and measurement provisions of U.S. GAAP. In addition to the liabilities that have been recognized, 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.

In March 2010, we entered into an operating agreement with GE Capital which contains automatic extensions and is subject to early termination provisions (the "Navistar Capital Operating Agreement"). Effective December 1, 2015, GE Capital assigned the Navistar Capital Operating Agreement to BMO Financial Group and its wholly-owned subsidiary BMO Harris Bank N.A. (together "BMO") as part of General Electric's sale of its GE Transportation Finance business. Under the terms of the Navistar Capital Operating Agreement, GE Capital was, and now BMO is, our third-party preferred source of retail customer financing for equipment offered by us and our dealers in the U.S. We refer to this alliance as "Navistar Capital." The Navistar Capital Operating Agreement contains a loss sharing arrangement for certain credit losses. Under the loss sharing arrangement, as amended, we generally reimburse our financing partner for credit losses in excess of the first 10% of the financed value of a contract; for certain leases we reimburse our financing partner for credit losses up to a maximum of the first 9.5% of the financed value of those lease contracts. Our exposure to loss is mitigated because contracts under the Navistar Capital Operating Agreement are secured by the financed equipment. There were \$1.5 billion and \$1.4 billion of outstanding loan principal and operating lease payments receivable at April 30, 2016 and October 31, 2015, respectively, financed through the Navistar Capital Operating Agreement and subject to the loss sharing arrangements in the U.S. The related financed values of these outstanding contracts were \$2.4 billion and \$2.3 billion at April 30, 2016 and October 31, 2015, respectively. Generally, we do not carry the contracts under the Navistar Capital Operating Agreement on our Consolidated Balance Sheets. However, for certain Navistar Capital financed contracts which we have accounted for as borrowings, we have recognized equipment leased to others of \$70 million and financed lease obligations of \$75 million in our Consolidated Balance Sheets as of April 30, 2016.

Based on our historic experience of losses on similar contracts and the nature of the loss sharing arrangement, we do not believe our share of losses related to balances currently outstanding will be material.

We also have issued limited residual value guarantees in connection with various leases. The amounts of the guarantees are estimated and recorded. Our guarantees are contingent upon the fair value of the leased assets at the end of the lease term. The amount of losses related to these arrangements has not been material to our Consolidated Statements of Operations or Condensed Consolidated Statements of Cash Flows and the value of the guarantees and accruals recorded are not material to our Consolidated Balance Sheets.

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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. As of April 30, 2016, the amount of stand-by letters of credit and surety bonds was \$91 million.

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. As of April 30, 2016, the total credit limit under this program was \$12 million of which \$8 million was unused.

In addition, as of April 30, 2016, we have entered into various purchase commitments of \$15 million and contracts that have cancellation fees of \$60 million with various expiration dates through 2020.

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.

#### 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 of the probable costs, if any, and accruals are recorded in our consolidated financial statements. These accruals are generally recognized no later than upon 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. Two sites formerly owned by us, Solar Turbines in San Diego, California, and the Canton Plant in Canton, Illinois, were identified as having soil and groundwater contamination. Two sites in Sao Paulo, Brazil, one at which we are currently operating and one where we formerly operated, were identified as having soil and groundwater contamination. While investigations and cleanup activities continue at these and other sites, we believe that we have adequate accruals to cover costs to complete the cleanup of all sites.

We have accrued \$20 million for these and other environmental matters, which are included within Other current liabilities and Other noncurrent liabilities, as of April 30, 2016. The majority of these accrued liabilities are expected to be paid subsequent to 2017.

Along with other vehicle manufacturers, we have been subject to an increased 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 generally 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.

#### Legal Proceedings

##### Overview

We are subject to various claims arising in the ordinary course of business, and are party 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 addition, from time to time we are subject to various

claims and legal proceedings related to employee compensation, benefits, and benefits administration including, but not limited to, compliance with the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), and Department of Labor requirements. 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.

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Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
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Profit Sharing Disputes

Pursuant to the 1993 Settlement Agreement, the program administrator and named fiduciary of the Supplemental Benefit Program is the Supplemental Benefit Program committee (the "Committee"), comprised of non-Company individuals. In August 2013, the Committee filed a motion for leave to amend its February 2013 complaint (which sought injunctive relief for the Company to provide certain information to which it was allegedly entitled under the Supplemental Benefit Trust Profit Sharing Plan) and a proposed amended complaint (the "Profit Sharing Complaint") in the U.S. District Court for the Southern District of Ohio (the "Court"). Leave to file the Profit Sharing Complaint was granted by the Court in October 2013. In its Profit Sharing Complaint, the Committee alleged the Company breached the 1993 Settlement Agreement and violated ERISA by failing to properly calculate profit sharing contributions due under the Supplemental Benefit Trust Profit Sharing Plan. The Committee seeks damages in excess of \$50 million, injunctive relief and reimbursement of attorneys' fees and costs. In October 2013, the Company filed a Motion to Dismiss the Profit Sharing Complaint and to compel the Committee to comply with the dispute resolution procedures set forth in the Supplemental Benefit Trust Profit Sharing Plan. In March 2014, the Court denied the Company's Motion to Dismiss and ruled, among other things, that the Company waived its right to compel the Committee to comply with the dispute resolution provisions set forth in the Supplemental Benefit Trust Profit Sharing Plan. In April 2014, the Company appealed the Court's refusal to compel the Committee to comply with the dispute resolution process to the Court of Appeals for the 6th Circuit. The Company also filed a motion with the Court to stay all proceedings pending the appeal. In May 2014, the Court granted the motion to stay all proceedings, including discovery, pending the appeal. In March 2015, the 6<sup>th</sup> Circuit Court of Appeals remanded the case to the Court with instructions that the Committee's claims in the Profit Sharing Complaint be arbitrated. In May 2015, the Court ordered that the claims in the Profit Sharing Complaint be arbitrated pursuant to the dispute resolution procedures in the Supplemental Benefit Trust Profit Sharing Plan. In November 2015, the Company and the Committee selected an arbitrator. The discovery process has commenced.

In addition, various local bargaining units of the United Automobile, Aerospace and Agricultural Implement Workers of America ("UAW") have filed separate grievances pursuant to the profit sharing plans under various collective bargaining agreements in effect between the Company and the UAW that may have similar legal and factual issues as the Profit Sharing Complaint.

Based on our assessment of the facts underlying the claims in the above actions, we are unable to provide meaningful quantification of how the final resolution of these claims may impact our future consolidated financial condition, results of operations, or cash flows.

FATMA Notice

International Indústria de Motores da América do Sul Ltda. ("IIAA"), formerly known as Maxion International Motores S/A ("Maxion"), now a wholly owned subsidiary of the Company, received a notice in July 2010 from the State of Santa Catarina Environmental Protection Agency ("FATMA") in Brazil. The notice alleged that Maxion had sent wastes to a facility owned and operated by a company known as Natureza and that soil and groundwater contamination had occurred at the Natureza facility. The notice asserted liability against Maxion and assessed an initial penalty in the amount of R\$2 million (the equivalent of approximately less than US\$1 million at April 30, 2016), which is not due and final until all administrative appeals are exhausted. Maxion was one of numerous companies that received similar notices. IIAA filed an administrative defense in August 2010 and has not yet received a decision following that filing. IIAA disputes the allegations in the notice and intends to vigorously defend itself.

Sao Paulo Groundwater Notice

In March 2014, IIAA, along with other nearby companies, received from the Sao Paulo District Attorney a notice and proposed Consent Agreement relating to alleged neighborhood-wide groundwater contamination at or around its Sao Paulo manufacturing facility. The proposed Consent Agreement seeks certain groundwater investigations and other technical relief and proposes sanctions in the amount of R\$3 million (the equivalent of approximately US\$1 million at April 30, 2016). In November 2014, IIAA extended a settlement offer. Currently, the parties remain in settlement

discussions concerning the sanctions amount and the provisions of a Consent Agreement.

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Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
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MaxxForce Engine EGR Warranty Litigation

On June 24, 2014, N&C Transportation Ltd. filed a putative class action lawsuit against Navistar International Corporation, Navistar, Inc., Navistar Canada Inc., and Harbour International Trucks (collectively, "Navistar") in Canada in the Supreme Court of British Columbia (the "N&C Action"). Subsequently, six additional, similar putative class action lawsuits have been filed in Canada (together with the N&C Action, the "Canadian Actions"). A certification hearing is scheduled in the N&C Action starting on June 13, 2016. The plaintiff submitted application materials for the certification motion, and Navistar's responding materials were filed on December 4, 2015. There are no court dates scheduled in any of the other Canadian Actions at this time.

On July 7, 2014, Par 4 Transport, LLC filed a putative class action lawsuit against Navistar, Inc. in the United States District Court for the Northern District of Illinois (the "Par 4 Action"). Subsequently, seventeen additional putative class action lawsuits were filed in various United States district courts, including the Northern District of Illinois, the Eastern District of Wisconsin, the Southern District of Florida, the Middle District of Pennsylvania, the Southern District of Texas, the Western District of Kentucky, the District of Minnesota, the District of Alabama, and the District of New Jersey (together with the Par 4 Action, the "U.S. Actions"). Some of the U.S. Actions name both Navistar International Corporation and Navistar, Inc. The U.S. Actions allege matters substantially similar to the Canadian Actions. More specifically, the Canadian Actions and the U.S. Actions (collectively, the "EGR Class Actions") seek to certify a class of persons or entities in Canada or the United States who purchased and/or leased a ProStar or other Navistar vehicle equipped with a model year 2008-2013 MaxxForce Advanced EGR engine. In substance, the EGR Class Actions allege that the MaxxForce Advanced EGR engines are defective and that the Company and Navistar, Inc. failed to disclose and correct the alleged defect. The EGR Class Actions assert claims based on theories of contract, breach of warranty, consumer fraud, unfair competition, misrepresentation and negligence. The EGR Class Actions seek relief in the form of monetary damages, punitive damages, declaratory relief, interest, fees, and costs.

On October 3, 2014, Navistar International Corporation and Navistar, Inc. filed a motion before the United States Judicial Panel on Multidistrict Litigation (the "MDL Panel") seeking to transfer and consolidate before Judge Joan B. Gottschall of the United States District Court for the Northern District of Illinois all of the then-pending U.S. Actions, as well as certain non-class action MaxxForce Advanced EGR engine lawsuits pending in various federal district courts.

On December 17, 2014, Navistar's motion to consolidate the U.S. Actions and certain other non-class action lawsuits was granted. The MDL Panel issued an order consolidating all of the U.S. Actions that were pending on the date of Navistar's motion before Judge Gottschall in the United States District Court for the Northern District of Illinois (the "MDL Action"). The MDL Panel also consolidated into the MDL Action certain non-class action MaxxForce Advanced EGR engine lawsuits pending in the various federal district courts, with the exception of one matter. For putative class action lawsuits filed subsequent to Navistar's original motion, we continue to request that the MDL Panel similarly transfer and consolidate these U.S. Actions.

At the request of the various law firms representing the plaintiffs in the MDL Action, on March 5, 2015, Judge Gottschall entered an order in the MDL Action appointing interim lead counsel and interim liaison counsel for the plaintiffs. On May 11, 2015, lead counsel for the plaintiffs filed a First Master Consolidated Class Action Complaint ("Consolidated Complaint"). The parties to the MDL Action exchanged initial disclosures on May 29, 2015. The Company answered the Consolidated Complaint on July 13, 2015. On May 27, 2016, Judge Gottschall entered a Case Management Order setting a July 13, 2017, date for plaintiffs' class certification motion. The Court also set a further status conference on July 27, 2016.

Based on our assessment of the facts underlying the claims in the above actions, we are unable to provide meaningful quantification of how the final resolution of these claims may impact our future consolidated financial condition, results of operations, or cash flows.

EPA Clean Air Act Litigation



In February 2012, Navistar, Inc. received a Notice of Violation ("NOV") from the United States Environmental Protection Agency (the "EPA") pertaining to certain heavy-duty diesel engines which, according to EPA, were not completely assembled by Navistar, Inc. until calendar year 2010 and, therefore, were not covered by Navistar, Inc.'s model year 2009 certificates of conformity. The NOV concluded that Navistar, Inc.'s introduction into commerce of each of these engines violated the Federal Clean Air Act.

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Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
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On July 14, 2015, the Department of Justice ("DOJ"), on behalf of the EPA, filed a lawsuit against Navistar International Corporation and Navistar, Inc. in the U.S. District Court for the Northern District of Illinois. Similar to the NOV, the lawsuit alleges that NIC and Navistar, Inc. introduced into commerce approximately 7,749 heavy-duty diesel engines that were not covered by model year 2009 certificates of conformity because those engines were not completely assembled until calendar year 2010, resulting in violations of the Federal Clean Air Act. On July 16, 2015, the DOJ filed an Amended Complaint clarifying the amount of civil penalties being sought. The lawsuit requests injunctive relief and the assessment of civil penalties of up to \$37,500 for each violation. On September 14, 2015, NIC and Navistar, Inc. each filed an Answer and Affirmative Defenses to the Amended Complaint. On December 1, 2015, the Court entered an order setting a discovery schedule. Discovery in the matter will proceed in two phases. Fact discovery for the liability phase commenced on December 9, 2015, and is scheduled to be completed on August 9, 2016, followed by expert discovery. The deadline for dispositive motions is January 20, 2017. After completion of the first phase, the Court will, if necessary, set further dates for a remedy phase. NIC and Navistar, Inc. dispute the allegations in the lawsuit. On May 13, 2016, the DOJ filed a motion for summary judgment on liability against NIC and Navistar, Inc. The court set a ruling date of September 1, 2016 on the DOJ's motion.

Based on our assessment of the facts underlying the complaint above, we are unable to provide meaningful quantification of how the final resolution of this matter may impact our future consolidated financial condition, results of operations or cash flows.

#### Shareholder Litigation

In March 2013, a putative class action complaint, alleging securities fraud, was filed against us by the Construction Workers Pension Trust Fund - Lake County and Vicinity, on behalf of itself and all other similarly situated purchasers of our common stock between the period of November 3, 2010 and August 1, 2012. A second class action complaint was filed in April 2013 by the Norfolk County Retirement System, individually and on behalf of all other similarly situated purchasers of our common stock between the period of June 9, 2010 and August 1, 2012. A third class action complaint was filed in April 2013 by Jane C. Purnell FBO Purnell Family Trust, on behalf of itself and all other similarly situated purchasers of our common stock between the period of November 3, 2010 and August 1, 2012. Each complaint named us as well as Daniel C. Ustian, our former President and Chief Executive Officer, and Andrew J. Cederoth, our former Executive Vice President and Chief Financial Officer as defendants. These complaints (collectively, the "10b-5 Cases") contain similar factual allegations which include, among other things, that we violated the federal securities laws by knowingly issuing materially false and misleading statements concerning our financial condition and future business prospects and that we misrepresented and omitted material facts in filings with the U.S. Securities Exchange Commission ("SEC") concerning the timing and likelihood of EPA certification of our EGR technology to meet 2010 EPA emission standards. The plaintiffs in these matters seek compensatory damages and attorneys' fees, among other relief.

In May 2013, an order was entered transferring and consolidating all 10b-5 Cases before one judge sitting in the U.S. District Court for the Northern District of Illinois and in July 2013, the Court appointed a lead plaintiff and lead plaintiff's counsel. The lead plaintiff filed a Consolidated Amended Complaint in October 2013. The Consolidated Amended Complaint enlarged the proposed class period to June 9, 2009 through August 1, 2012, and named fourteen additional current and former directors and officers as defendants. On December 17, 2013, defendants filed a motion to dismiss the Consolidated Amended Complaint. On July 22, 2014, the Court granted the defendants' Motion to Dismiss, denied the lead plaintiff's Motion to Strike as moot, and gave the lead plaintiff leave to file a second consolidated amended complaint by August 22, 2014.

On August 22, 2014, the plaintiff filed a Second Amended Complaint, which narrowed the claims in two ways. First, the plaintiff abandoned its claims against the majority of the defendants. The Second Amended Complaint brought claims against only Navistar, Dan Ustian, A.J. Cederoth, Jack Allen, and Eric Tech. The plaintiff also shortened the putative class period. In the prior complaint, the class period began on June 9, 2009. In the Second Amended Complaint, it begins on March 10, 2010. Defendants filed their Motion to Dismiss the Second Amended Complaint on

September 23, 2014. In November 2014, the plaintiff voluntarily dismissed Eric Tech as a defendant. On July 10, 2015, the Court issued its Opinion and Order on our Motion to Dismiss the Second Amended Complaint. The Motion to Dismiss was granted in part and denied in part. Specifically, the Court (i) dismissed all of plaintiff's claims against the Company, Andrew J. Cederoth and Jack Allen and (ii) dismissed all of plaintiff's claims against Daniel C. Ustian, the only remaining defendant, except for claims regarding two of Mr. Ustian's statements. Further, all of the dismissed claims were dismissed with prejudice except for claims based on statements made subsequent to the lead plaintiff's last purchase of the Company's stock (the "Post-Purchase Claims"). The Court determined the lead plaintiff lacked standing to assert the Post-Purchase Claims and dismissed those claims without prejudice. At a December 1, 2015 status conference, the parties reported that a settlement in principle had been reached, subject to, among other things, final documentation, confirmatory discovery and Court approval, and the Court filed a minute entry reflecting such report. On May 25, 2016, the Court entered an order preliminarily approving the settlement, as well as the class notice to be sent in connection with the settlement. The Court scheduled the Final Approval Hearing for October 25, 2016.

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Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
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In March 2013, James Gould filed a derivative complaint in the U.S. District Court for the Northern District of Illinois on behalf of the Company against us and certain of our current and former directors and former officers. The complaint alleges, among other things, that certain of our current and former directors and former officers committed a breach of fiduciary duty, waste of corporate assets and were unjustly enriched in relation to similar factual allegations made in the 10b-5 Cases. The plaintiff in this matter seeks compensatory damages, certain corporate governance reforms, certain injunctive relief, disgorgement of the proceeds of certain defendants' profits from the sale of Company stock, and attorneys' fees, among other relief. On May 3, 2013, the court entered a Stipulation and Order to Stay Action, staying the case pending further order of the court or entry of an order on the motion to dismiss the Consolidated Amended Complaint in the 10b-5 Cases. On July 31, 2014, after the amended complaint was dismissed, the parties filed a status report, and the court entered an order on August 27, 2014 continuing the stay pending a ruling on defendants' motion to dismiss the Second Amended Complaint in the 10b-5 Cases. In November 2015, the existing stay order in this derivative action was further extended through March 22, 2016 and in March 2016, it was again extended through July 6, 2016.

In August 2013, Abbie Griffin filed a derivative complaint in the State of Delaware Court of Chancery, on behalf of the Company against us and certain of our current and former directors and former officers. The complaint alleges, among other things, that certain of our current and former directors and former officers committed a breach of fiduciary duty, in relation to similar factual allegations made in the 10b-5 Cases. The plaintiff in this matter seeks compensatory damages, certain corporate governance reforms, certain injunctive relief, and attorneys' fees, among other relief. On August 29, 2013, the court entered an order staying the case pending resolution of the defendant's motion to dismiss the Consolidated Amended Complaint in the 10b-5 Cases. On August 5, 2014, the parties filed a status report with the court requesting that the August 2013 stay order remain in place pending a ruling on the motion to dismiss the Second Amended Complaint in the 10b-5 Cases and on November 9, 2014, the court entered an order continuing the stay pending a ruling on defendants' motion to dismiss the Second Amended Complaint in the 10b-5 Cases. In August 2015, the court further extended the stay of this derivative action through December 3, 2015. In November 2015, the court further extended the stay through March 23, 2016 and in March 2016, the court further extended the stay until June 6, 2016.

Based on our assessment of the facts underlying these matters described above, we are unable to provide meaningful quantification of how the final resolution of these matters may impact our future consolidated financial condition, results of operations, or cash flows.

#### Brazil Truck Dealer Disputes

In January 2014, IIAA initiated an arbitration proceeding under the International Chamber of Commerce rules seeking payment for goods sold and unpaid, in the amount of R\$64 million (approximately US\$18 million as of April 30, 2016), including penalties and interest, from a group of affiliated truck dealers in Brazil. The truck dealers are affiliated with each other, but not with us, and are collectively referred to as Navitrucks. In the proceeding, IIAA also seeks a declaration of fault against Navitrucks related to the termination of the truck dealer agreements between IIAA and Navitrucks. Navitrucks responded in part by submitting counterclaims against IIAA seeking the amount of R\$128 million (approximately US\$37 million as of April 30, 2016) for damages related to alleged unfulfilled promises and injury to Navitrucks' reputation. In October 2014, Navitrucks amended their counterclaims by increasing the amount of damages. During a preliminary hearing before the arbitral tribunal on March 24, 2015, the parties agreed to submit all of the pending claims between the parties to the exclusive jurisdiction of the arbitral tribunal. Pursuant to the timetable issued in the arbitration proceeding, IIAA presented its complaint in July 2015, Navitrucks filed its answer and counterclaims on August 24, 2015, and IIAA filed its rebuttal and answer to Navitrucks' counterclaims on October 22, 2015. On December 7, 2015, Navitrucks filed its rebuttal to IIAA's answer to counterclaims. The arbitral tribunal has set hearing dates for presenting witnesses and evidence of June 13-15, 2016. As of April 30, 2016, the approximate amount of the IIAA claim against Navitrucks is R\$124 million (approximately US\$35 million as of April 30, 2016), of which Navitrucks has acknowledged that IIAA is entitled to a credit in the approximate amount of R\$69 million

(approximately US\$20 million as of April 30, 2016), and the approximate amount of the Navitrucks claim against IIAA is R\$132 million (approximately US\$38 million as of April 30, 2016).

Based on our assessment of the facts underlying the claims in the above actions, we are unable to provide meaningful quantification of how the final resolution of these claims may impact our future consolidated financial condition, results of operations, or cash flows.

In addition, two other truck dealers and two truck fleet owners in Brazil have separate adversarial proceedings pending against IIAA that may have similar legal and factual issues as the Navitrucks claim. These other claims are not material either individually or in the aggregate.

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(Unaudited)

IC Bus Civil RICO Litigation

On June 1, 2016, plaintiffs Polar Express School Bus and Lakeview Bus Lines filed a lawsuit against Navistar International Corporation, Navistar, Inc., and IC Bus, LLC in the U.S. District Court for the Northern District of Illinois. The lawsuit alleges that the forty (40) IC brand buses owned or operated by plaintiffs contain defective ABS braking systems and also engines with defective emissions control systems. Plaintiffs claim that NIC, its subsidiaries, and their authorized dealers deliberately concealed the alleged defects, and the lawsuit seeks to plead causes of action under the Racketeer Influenced and Corrupt Organizations Act (RICO) and common law fraud. Plaintiffs seek compensatory damages in the amount of \$6.7 million, treble damages, punitive damages in the amount of \$50 million, and attorneys' fees and costs. NIC, Navistar, Inc., and IC Bus dispute the allegations in the lawsuit.

Based on our assessment of the facts underlying the claims in the above actions, we are unable to provide meaningful quantification of how the final resolution of these claims may impact our future consolidated financial condition, results of operations, or cash flows.

Other

U.S. Securities and Exchange Administrative Order

In June 2012, Navistar received an informal inquiry from the Chicago Office of the Enforcement Division of the SEC seeking a number of categories of documents for the periods dating back to November 1, 2010, relating to various accounting and disclosure issues. We received a formal order of private investigation in July 2012. We have received subsequent subpoenas from the staff of the SEC in connection with their inquiry. In December 2014, the SEC filed an application in the United States District Court for the Northern District of Illinois seeking an order compelling the production of certain documents withheld by Navistar from its responses to the administrative subpoenas on the basis of attorney-client privilege and/or the work product doctrine. The discovery dispute involved a small number of documents in relation to the number of documents already produced by Navistar. On June 30, 2015, following an in camera review of some of the documents at issue, the Court entered an Order sustaining the privilege claims in part and overruling the claims in part. The Court also entered related orders dated August 31, 2015 and October 21, 2015. Pursuant to those Orders, Navistar completed the production of those documents, or portions of documents, for which its privilege claims were denied, as well as other documents subject to the SEC's December 2014 application that the Company determined were not privileged under the reasoning of the Court's June 30, 2015 Order.

On August 13 and 17, 2015, the SEC staff transmitted "Wells Notices" in connection with the formal order of investigation from July 2012 described above. The Notices stated that the staff has made a preliminary determination to recommend that the SEC file an enforcement action against the Company and its former chief executive officer, Daniel Ustian, alleging violations of the Securities Exchange Act of 1934, certain related regulations, the Securities Act of 1933, and an August 5, 2010 Order Instituting Cease-and-Desist Proceedings against the Company. On September 17, 2015, Navistar submitted to the SEC a response to its Wells Notices. On October 13, 2015, Navistar met with the SEC to further respond to the Wells Notices, subsequent discussions followed, and the Company made an offer of settlement. On March 31, 2016, the SEC accepted the Company's offer and issued an administrative cease-and-desist order reflecting the terms of the settlement. The Company neither admitted nor denied wrongdoing. The order includes negligence-based charges pertaining to periodic filing requirements and material misstatements or omissions related to three applications in 2011 and 2012 by Navistar to the EPA for certification of heavy-duty diesel engines emitting 0.2g of nitrogen oxide ("NOx"). The order also requires the Company to pay a civil penalty in the amount of \$7.5 million, which the Company has paid and which it previously accrued for on its Consolidated Balance Sheets as of October 31, 2015.

12. Segment Reporting

The following is a description of our four reporting segments:

Our Truck segment manufactures and distributes Class 4 through 8 trucks, buses, and military vehicles under the International and IC Bus ("IC") brands, and produces engines under our proprietary brand name and parts required to support the military truck lines. This segment sells its products in the U.S., Canada, and Mexico markets, as well as

through our export truck business. In an effort to strengthen and maintain our dealer network, this segment occasionally acquires and operates dealer locations for the purpose of transitioning ownership. Our Parts segment provides customers with proprietary products needed to support the International commercial truck, IC Bus, proprietary engine lines, and export parts business, as well as our other product lines. Our Parts segment also provides a wide selection of other standard truck, trailer, and engine aftermarket parts. Also included in the Parts segment are the operating results of BDP, which manages the sourcing, merchandising, and distribution of certain service parts we sell to Ford in North America.

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Our Global Operations segment primarily consists of the IIAA (formerly MWM International Industria De Motores Da America Do Sul Ltda. ("MWM")) engine and truck operations in Brazil. The IIAA engine operations produce diesel engines, primarily under contract manufacturing arrangements, as well as under the MWM brand, for sale to OEMs in South America. In addition, our Global Operations segment includes the operating results of our joint venture in China with Anhui Jianghuai Automobile Co ("JAC").

Our Financial Services segment provides retail, wholesale, and lease financing of products sold by the Truck and Parts segments and their 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.

Segment Profit (Loss)

We define segment profit (loss) as Net income (loss) from continuing operations attributable to Navistar International Corporation excluding Income tax benefit (expense). Selected financial information is as follows:

| (in millions)  | Truck   | Parts | Global Operations | Financial Services <sup>(A)</sup> | Corporate and Eliminations | Total   |
|--|---------|-------|-------------------|-----------------------------------|----------------------------|---------|
| Three Months Ended April 30, 2016  |         |       |                   |                                   |                            |         |
| External sales and revenues, net   | \$1,459 | \$640 | \$ 64             | \$ 33                             | \$ 1                       | \$2,197 |
| Intersegment sales and revenues  | 21      | 7     | 13                | 25                                | (66)                       | —       |
| Total sales and revenues, net  | \$1,480 | \$647 | \$ 77             | \$ 58                             | \$ (65)                    | \$2,197 |
| Income (loss) from continuing operations attributable to NIC, net of tax | \$(23)  | \$176 | \$(1)             | \$ 25                             | \$(173)                    | \$4     |
| Income tax expense   | —       | —     | —                 | —                                 | (16)                       | (16)    |
| Segment profit (loss)  | \$(23)  | \$176 | \$(1)             | \$ 25                             | \$(157)                    | \$20    |
| Depreciation and amortization  | \$29    | \$4   | \$ 4              | \$ 12                             | \$ 4                       | \$53    |
| Interest expense   | —       | —     | —                 | 19                                | 62                         | 81      |
| Equity in income of non-consolidated affiliates                          | 1       | 1     | —                 | —                                 | —                          | 2       |
| Capital expenditures <sup>(C)</sup>                                      | 19      | 1     | 1                 | —                                 | 3                          | 24      |
| (in millions)  | Truck   | Parts | Global Operations | Financial Services <sup>(A)</sup> | Corporate and Eliminations | Total   |
| Three Months Ended April 30, 2015  |         |       |                   |                                   |                            |         |
| External sales and revenues, net   | \$1,933 | \$607 | \$ 115            | \$ 35                             | \$ 3                       | \$2,693 |
| Intersegment sales and revenues <sup>(B)</sup>                           | 33      | 6     | 15                | 25                                | (79)                       | —       |
| Total sales and revenues, net  | \$1,966 | \$613 | \$ 130            | \$ 60                             | \$ (76)                    | \$2,693 |
| Income (loss) from continuing operations attributable to NIC, net of tax | \$(51)  | \$133 | \$ 1              | \$ 22                             | \$(169)                    | \$(64)  |
| Income tax expense   | —       | —     | —                 | —                                 | (18)                       | (18)    |
| Segment profit (loss)  | \$(51)  | \$133 | \$ 1              | \$ 22                             | \$(151)                    | \$(46)  |
| Depreciation and amortization  | \$47    | \$4   | \$ 5              | \$ 12                             | \$ 6                       | \$74    |
| Interest expense   | —       | —     | —                 | 18                                | 57                         | 75      |
| Equity in income (loss) of non-consolidated affiliates                   | 1       | 1     | (1)               | —                                 | —                          | 1       |
| Capital expenditures <sup>(C)</sup>                                      | 24      | —     | 1                 | 2                                 | 1                          | 28      |





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| (in millions)  | Truck   | Parts   | Global<br>Operations | Financial<br>Services <sup>(A)</sup> | Corporate<br>and<br>Eliminations | Total    |
|--|---------|---------|----------------------|--------------------------------------|----------------------------------|----------|
| Six Months Ended April 30, 2016  |         |         |                      |                                      |                                  |          |
| External sales and revenues, net   | \$2,540 | \$1,202 | \$ 148               | \$ 68                                | \$ 4                             | \$3,962  |
| Intersegment sales and revenues  | 72      | 15      | 21                   | 49                                   | (157 )                           | —        |
| Total sales and revenues, net  | \$2,612 | \$1,217 | \$ 169               | \$ 117                               | \$ (153 )                        | \$3,962  |
| Income (loss) from continuing operations attributable to NIC, net of tax | \$(74 ) | \$326   | \$ (14 )             | \$ 51                                | \$ (318 )                        | \$(29 )  |
| Income tax expense   | —       | —       | —                    | —                                    | (11 )                            | (11 )    |
| Segment profit (loss)  | \$(74 ) | \$326   | \$ (14 )             | \$ 51                                | \$ (307 )                        | \$(18 )  |
| Depreciation and amortization  | \$63    | \$7     | \$ 9                 | \$ 24                                | \$ 8                             | \$111    |
| Interest expense   | —       | —       | —                    | 38                                   | 124                              | 162      |
| Equity in income (loss) of non-consolidated affiliates                   | 2       | 2       | (3 )                 | —                                    | —                                | 1        |
| Capital expenditures <sup>(C)</sup>                                      | 44      | 2       | 2                    | —                                    | 5                                | 53       |
| (in millions)  | Truck   | Parts   | Global<br>Operations | Financial<br>Services <sup>(A)</sup> | Corporate<br>and<br>Eliminations | Total    |
| Six Months Ended April 30, 2015  |         |         |                      |                                      |                                  |          |
| External sales and revenues, net   | \$3,564 | \$1,221 | \$ 253               | \$ 71                                | \$ 5                             | \$5,114  |
| Intersegment sales and revenues <sup>(B)</sup>                           | 72      | 18      | 29                   | 49                                   | (168 )                           | —        |
| Total sales and revenues, net  | \$3,636 | \$1,239 | \$ 282               | \$ 120                               | \$ (163 )                        | \$5,114  |
| Income (loss) from continuing operations attributable to NIC, net of tax | \$(69 ) | \$278   | \$ (14 )             | \$ 46                                | \$ (347 )                        | \$(106 ) |
| Income tax expense   | —       | —       | —                    | —                                    | (25 )                            | (25 )    |
| Segment profit (loss)  | \$(69 ) | \$278   | \$ (14 )             | \$ 46                                | \$ (322 )                        | \$(81 )  |
| Depreciation and amortization  | \$99    | \$7     | \$ 12                | \$ 24                                | \$ 11                            | \$153    |
| Interest expense   | —       | —       | —                    | 38                                   | 114                              | 152      |
| Equity in income (loss) of non-consolidated affiliates                   | 3       | 2       | (2 )                 | —                                    | —                                | 3        |
| Capital expenditures <sup>(C)</sup>                                      | 38      | —       | 3                    | 2                                    | 2                                | 45       |
| (in millions)  | Truck   | Parts   | Global<br>Operations | Financial<br>Services                | Corporate<br>and<br>Eliminations | Total    |
| Segment assets, as of:   |         |         |                      |                                      |                                  |          |
| April 30, 2016   | \$1,887 | \$645   | \$ 370               | \$ 2,284                             | \$ 1,002                         | \$6,188  |
| October 31, 2015   | 1,876   | 641     | 409                  | 2,455                                | 1,311                            | 6,692    |

Total sales and revenues in the Financial Services segment include interest revenues of \$42 million and \$84 (A) million for the three and six months ended April 30, 2016, respectively, and \$44 million and \$89 million for the three and six months ended April 30, 2015, respectively.

During the second quarter of 2015, we identified a \$35 million adjustment related to the first quarter of 2015 Intersegment sales and revenues. As a result, the Truck segment and Corporate and Eliminations should have (B) reported Intersegment sales and revenues of \$39 million and \$(89) million, respectively, and reported Total sales and revenues, net, of \$1,670 million and \$(87) million, respectively, for the three months ended January 31, 2015.

The adjustment did not impact the consolidated results for the first or second quarter of 2015.

(C) Exclusive of purchases of equipment leased to others.



Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
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## 13. Stockholders' Deficit

## Accumulated Other Comprehensive Loss

Changes in Accumulated other comprehensive loss, net of tax, included in the Consolidated Statements of Stockholders' Deficit, consisted of the following:

| (in millions)  | Unrealized<br>Gain on<br>Marketable<br>Securities | Foreign<br>Currency<br>Translation<br>Adjustments | Defined<br>Benefit<br>Plans | Total     |
|--|---|---|-----------------------------|-----------|
| Balance as of January 31, 2016                                   | \$ 1  | \$ (320 )   | \$(2,282)                   | \$(2,601) |
| Other comprehensive income (loss) before reclassifications       | —   | 50  | (18 )                       | 32        |
| Amounts reclassified out of accumulated other comprehensive loss | —   | —   | 33                          | 33        |
| Net current-period other comprehensive income                    | —   | 50  | 15                          | 65        |
| Balance as of April 30, 2016                                     | \$ 1  | \$ (270 )   | \$(2,267)                   | \$(2,536) |

| (in millions)  | Unrealized<br>Gain on<br>Marketable<br>Securities | Foreign<br>Currency<br>Translation<br>Adjustments | Defined<br>Benefit<br>Plans | Total     |
|--|---|---|-----------------------------|-----------|
| Balance as of October 31, 2015                                   | \$ 1  | \$ (287 )   | \$(2,315)                   | \$(2,601) |
| Other comprehensive income (loss) before reclassifications       | —   | 17  | (18 )                       | (1 )      |
| Amounts reclassified out of accumulated other comprehensive loss | —   | —   | 66                          | 66        |
| Net current-period other comprehensive income                    | —   | 17  | 48                          | 65        |
| Balance as of April 30, 2016                                     | \$ 1  | \$ (270 )   | \$(2,267)                   | \$(2,536) |

| (in millions)  | Unrealized<br>Gain on<br>Marketable<br>Securities | Foreign<br>Currency<br>Translation<br>Adjustments | Defined<br>Benefit<br>Plans | Total     |
|--|---|---|-----------------------------|-----------|
| Balance as of January 31, 2015                                   | \$ 1  | \$ (186 )   | \$(2,105)                   | \$(2,290) |
| Other comprehensive loss before reclassifications                | —   | (27 )   | —                           | (27 )     |
| Amounts reclassified out of accumulated other comprehensive loss | —   | —   | 33                          | 33        |
| Net current-period other comprehensive income (loss)             | —   | (27 )   | 33                          | 6         |
| Balance as of April 30, 2015                                     | \$ 1  | \$ (213 )   | \$(2,072)                   | \$(2,284) |

| (in millions)  | Unrealized<br>Gain on<br>Marketable<br>Securities | Foreign<br>Currency<br>Translation<br>Adjustments | Defined<br>Benefit<br>Plans | Total     |
|--|---|---|-----------------------------|-----------|
| Balance as of October 31, 2014                                   | \$ 1  | \$ (127 )   | \$(2,137)                   | \$(2,263) |
| Other comprehensive loss before reclassifications                | —   | (86 )   | —                           | (86 )     |
| Amounts reclassified out of accumulated other comprehensive loss | —   | —   | 65                          | 65        |
| Net current-period other comprehensive income (loss)             | —   | (86 )   | 65                          | (21 )     |
| Balance as of April 30, 2015                                     | \$ 1  | \$ (213 )   | \$(2,072)                   | \$(2,284) |

Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
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The following table displays the amounts reclassified from Accumulated other comprehensive loss and the affected line item in the Consolidated Statements of Operations:

|  | Location in Consolidated Statements of Operations | Three Months Ended April 30, |        | Six Months Ended April 30, |        |
|--|---|------------------------------|--------|----------------------------|--------|
|  |   | 2016                         | 2015   | 2016                       | 2015   |
| Defined benefit plans                              |   |                              |        |                            |        |
| Amortization of prior service benefit              | Selling, general and administrative expenses      | \$(1 )                       | \$(1 ) | \$(1 )                     | \$(2 ) |
| Amortization of actuarial loss                     | Selling, general and administrative expenses      | 34                           | 34     | 67                         | 68     |
|  | Total before tax                                  | 33                           | 33     | 66                         | 66     |
|  | Tax expense                                       | —                            | —      | —                          | (1 )   |
| Total reclassifications for the period, net of tax |   | \$33                         | \$33   | \$66                       | \$65   |

14. Earnings (Loss) Per Share Attributable to Navistar International Corporation

The following table presents the information used in the calculation of our basic and diluted income (loss) per share for continuing operations, discontinued operations, and net income (loss), all attributable to Navistar International Corporation:

| (in millions, except per share data)  | Three Months Ended April 30, |          | Six Months Ended April 30, |          |
|---|------------------------------|----------|----------------------------|----------|
|   | 2016                         | 2015     | 2016                       | 2015     |
| Numerator:  |                              |          |                            |          |
| Amounts attributable to Navistar International Corporation common stockholders: |                              |          |                            |          |
| Income (loss) from continuing operations, net of tax                            | \$4                          | \$(64 )  | \$(29 )                    | \$(106 ) |
| Income (loss) from discontinued operations, net of tax                          | —                            | —        | —                          | —        |
| Net income (loss)   | \$4                          | \$(64 )  | \$(29 )                    | \$(106 ) |
| Denominator:  |                              |          |                            |          |
| Weighted average shares outstanding:  |                              |          |                            |          |
| Basic   | 81.7                         | 81.6     | 81.7                       | 81.5     |
| Effect of dilutive securities   | 0.3                          | —        | —                          | —        |
| Diluted   | 82.0                         | 81.6     | 81.7                       | 81.5     |
| Income (loss) per share attributable to Navistar International Corporation:     |                              |          |                            |          |
| Basic:  |                              |          |                            |          |
| Continuing operations   | \$0.05                       | \$(0.78) | \$(0.35)                   | \$(1.30) |
| Discontinued operations   | —                            | —        | —                          | —        |
| Net income (loss)   | \$0.05                       | \$(0.78) | \$(0.35)                   | \$(1.30) |
| Diluted:  |                              |          |                            |          |
| Continuing operations   | \$0.05                       | \$(0.78) | \$(0.35)                   | \$(1.30) |
| Discontinued operations   | —                            | —        | —                          | —        |
| Net income (loss)   | \$0.05                       | \$(0.78) | \$(0.35)                   | \$(1.30) |



Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
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The conversion rate on our 4.50% senior subordinated convertible notes due 2018 ("2018 Convertible Notes") is 17.1233 shares of common stock per \$1,000 principal amount of 2018 Convertible Notes, equivalent to an initial conversion price of approximately \$58.40 per share of common stock. The 2018 Convertible Notes have an anti-dilutive effect when calculating diluted earnings per share when our average stock price is less than \$58.40. The conversion rate on our 4.75% senior subordinated convertible notes due April 2019 ("2019 Convertible Notes") is 18.4946 shares of common stock per \$1,000 principal amount of 2019 Convertible Notes, equivalent to an initial conversion price of approximately \$54.07 per share of common stock. The 2019 Convertible Notes have an anti-dilutive effect when calculating diluted earnings per share when our average stock price is less than \$54.07. The computation of diluted earnings per share also excludes outstanding options and other common stock equivalents in periods where inclusion of such potential common stock instruments would be anti-dilutive.

For the three months ended April 30, 2016, certain outstanding options and other common stock equivalents were excluded from the computation of diluted earnings per share, as our average stock price during the period was less than their respective exercise prices. The aggregate options and other common stock equivalents not included were 14.9 million.

For the six months ended April 30, 2016, no dilutive shares were included in the computation of diluted earnings per share because they would have been anti-dilutive due to the net loss attributable to Navistar International Corporation. The aggregate shares not included were 14.8 million.

For both the three and six months ended April 30, 2015, no dilutive shares were included in the computation of diluted earnings per share because they would have been anti-dilutive due to the net loss attributable to Navistar International Corporation. The aggregate shares not included were 16.0 million.

For both the three and six months ended April 30, 2016 and both the three and six months ended April 30, 2015, the aggregate shares not included in the computation of earnings per share were primarily comprised of 3.4 million shares related to the 2018 Convertible Notes and 7.6 million shares related to the 2019 Convertible Notes.

#### 15. Condensed Consolidating Guarantor and Non-guarantor Financial Information

The following tables set forth condensed consolidating balance sheets as of April 30, 2016 and October 31, 2015, and condensed consolidating statements of operations and comprehensive income (loss) for the three and six months ended April 30, 2016 and 2015, and condensed consolidating statements of cash flows for the six months ended April 30, 2016 and 2015.

The information is presented as a result of Navistar, Inc.'s guarantee, exclusive of its subsidiaries, of NIC's indebtedness under our 8.25% Senior Notes, due 2021, and obligations under our Loan Agreement related to the 6.5% Tax Exempt Bonds, due 2040. Navistar, Inc. is a direct wholly-owned subsidiary of NIC. None of NIC's other subsidiaries guarantee any of these notes or bonds. The guarantees are "full and unconditional", as those terms are used in Regulation S-X Rule 3-10, except that the guarantees will be automatically released in certain customary circumstances, such as when the subsidiary is sold or all of the assets of the subsidiary are sold, the capital stock is sold, when the subsidiary is designated as an "unrestricted subsidiary" for purposes of the respective indentures for each of the 8.25% Senior Notes, due 2021, and the 6.5% Tax Exempt Bonds, due 2040, upon liquidation or dissolution of the subsidiary or upon legal or covenant defeasance, or satisfaction and discharge of the notes or bonds. 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 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 and its operating units accounted for on a consolidated basis. "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 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 utilize current U.S. taxable losses of Navistar, Inc. and all other direct or indirect subsidiaries of NIC.

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Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
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## Condensed Consolidating Statement of Operations for the Three Months Ended April 30, 2016

| (in millions)  | NIC  | Navistar, Inc. | Non-Guarantor Subsidiaries | Eliminations and Other | Consolidated |
|--|------|----------------|----------------------------|------------------------|--------------|
| Sales and revenues, net  | \$ — | \$ 1,702       | \$ 1,423                   | \$ (928 )              | \$ 2,197     |
| Costs of products sold   | —    | 1,548          | 1,208                      | (911 )                 | 1,845        |
| Restructuring charges  | —    | 3              | —                          | —                      | 3            |
| Asset impairment charges   | —    | 2              | 1                          | —                      | 3            |
| All other operating expenses (income)                                | 38   | 233            | 66                         | (18 )                  | 319          |
| Total costs and expenses   | 38   | 1,786          | 1,275                      | (929 )                 | 2,170        |
| Equity in income (loss) of affiliates                                | 42   | 68             | —                          | (108 )                 | 2            |
| Income (loss) before income taxes                                    | 4    | (16 )          | 148                        | (107 )                 | 29           |
| Income tax expense   | —    | (2 )           | (14 )                      | —                      | (16 )        |
| Earnings (loss) from continuing operations                           | 4    | (18 )          | 134                        | (107 )                 | 13           |
| Income (loss) from discontinued operations, net of tax               | —    | —              | —                          | —                      | —            |
| Net income (loss)  | 4    | (18 )          | 134                        | (107 )                 | 13           |
| Less: Net income attributable to non-controlling interests           | —    | —              | 9                          | —                      | 9            |
| Net income (loss) attributable to Navistar International Corporation | \$ 4 | \$ (18 )       | \$ 125                     | \$ (107 )              | \$ 4         |

## Condensed Consolidating Statement of Comprehensive Income (Loss) for the Three Months Ended April 30, 2016

| (in millions)  | NIC   | Navistar, Inc. | Non-Guarantor Subsidiaries | Eliminations and Other | Consolidated |
|--|-------|----------------|----------------------------|------------------------|--------------|
| Net income (loss)  | \$ 4  | \$ (18 )       | \$ 134                     | \$ (107 )              | \$ 13        |
| Other comprehensive income (loss):   |       |                |                            |                        |              |
| Foreign currency translation adjustment  | 50    | —              | 50                         | (50 )                  | 50           |
| Defined benefit plans (net of tax)   | 15    | 31             | (16 )                      | (15 )                  | 15           |
| Total other comprehensive income (loss)  | 65    | 31             | 34                         | (65 )                  | 65           |
| Comprehensive income (loss)  | 69    | 13             | 168                        | (172 )                 | 78           |
| Less: Net income attributable to non-controlling interests                           | —     | —              | 9                          | —                      | 9            |
| Total comprehensive income (loss) attributable to Navistar International Corporation | \$ 69 | \$ 13          | \$ 159                     | \$ (172 )              | \$ 69        |

Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

Condensed Consolidating Statement of Operations for the Six Months Ended April 30, 2016

| (in millions)  | NIC    | Navistar,<br>Inc. | Non-Guarantor<br>Subsidiaries | Eliminations<br>and Other | Consolidated |
|--|--------|-------------------|-------------------------------|---------------------------|--------------|
| Sales and revenues, net  | \$—    | \$ 3,044          | \$ 2,623                      | \$ (1,705 )               | \$ 3,962     |
| Costs of products sold   | —      | 2,752             | 2,231                         | (1,672 )                  | 3,311        |
| Restructuring charges  | —      | 4                 | 2                             | —                         | 6            |
| Asset impairment charges   | —      | 2                 | 3                             | —                         | 5            |
| All other operating expenses (income)                                | 57     | 446               | 174                           | (36 )                     | 641          |
| Total costs and expenses   | 57     | 3,204             | 2,410                         | (1,708 )                  | 3,963        |
| Equity in income (loss) of affiliates                                | 28     | 55                | (1 )                          | (81 )                     | 1            |
| Income (loss) before income taxes                                    | (29 )  | (105 )            | 212                           | (78 )                     | —            |
| Income tax benefit (expense)   | —      | 11                | (22 )                         | —                         | (11 )        |
| Earnings (loss) from continuing operations                           | (29 )  | (94 )             | 190                           | (78 )                     | (11 )        |
| Income (loss) from discontinued operations, net of tax               | —      | —                 | —                             | —                         | —            |
| Net income (loss)  | (29 )  | (94 )             | 190                           | (78 )                     | (11 )        |
| Less: Net income attributable to non-controlling interests           | —      | —                 | 18                            | —                         | 18           |
| Net income (loss) attributable to Navistar International Corporation | \$(29) | \$(94 )           | \$ 172                        | \$ (78 )                  | \$( 29 )     |

Condensed Consolidating Statement of Comprehensive Income (Loss) for the Six Months Ended April 30, 2016

| (in millions)  | NIC    | Navistar,<br>Inc. | Non-Guarantor<br>Subsidiaries | Eliminations<br>and Other | Consolidated |
|--|--------|-------------------|-------------------------------|---------------------------|--------------|
| Net income (loss)  | \$(29) | \$(94 )           | \$ 190                        | \$ (78 )                  | \$( 11 )     |
| Other comprehensive income (loss):   |        |                   |                               |                           |              |
| Foreign currency translation adjustment  | 17     | —                 | 17                            | (17 )                     | 17           |
| Defined benefit plans (net of tax)   | 48     | 63                | (15 )                         | (48 )                     | 48           |
| Total other comprehensive income (loss)  | 65     | 63                | 2                             | (65 )                     | 65           |
| Comprehensive income (loss)  | 36     | (31 )             | 192                           | (143 )                    | 54           |
| Less: Net income attributable to non-controlling interests                           | —      | —                 | 18                            | —                         | 18           |
| Total comprehensive income (loss) attributable to Navistar International Corporation | \$36   | \$(31 )           | \$ 174                        | \$ (143 )                 | \$ 36        |

Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

## Condensed Consolidating Balance Sheet as of April 30, 2016

| (in millions)   | NIC              | Navistar,<br>Inc. | Non-Guarantor<br>Subsidiaries | Eliminations<br>and Other | Consolidated   |
|---|------------------|-------------------|-------------------------------|---------------------------|----------------|
| <b>Assets</b>   |                  |                   |                               |                           |                |
| Cash and cash equivalents   | \$228            | \$24              | \$337                         | \$—                       | \$589          |
| Marketable securities   | 47               | —                 | 181                           | —                         | 228            |
| Restricted cash   | 16               | 5                 | 118                           | —                         | 139            |
| Finance and other receivables, net  | 3                | 101               | 2,145                         | (105)                     | 2,144          |
| Inventories   | —                | 812               | 421                           | (13)                      | 1,220          |
| Investments in non-consolidated affiliates  | (7,585)          | 6,215             | 63                            | 1,373                     | 66             |
| Property and equipment, net   | —                | 691               | 597                           | (7)                       | 1,281          |
| Goodwill  | —                | —                 | 38                            | —                         | 38             |
| Deferred taxes, net   | —                | 15                | 149                           | —                         | 164            |
| Other   | 33               | 125               | 162                           | (1)                       | 319            |
| <b>Total assets</b>   | <b>\$(7,258)</b> | <b>\$7,988</b>    | <b>\$4,211</b>                | <b>\$1,247</b>            | <b>\$6,188</b> |
| <b>Liabilities and stockholders' equity (deficit)</b>                             |                  |                   |                               |                           |                |
| <b>Debt</b>   |                  |                   |                               |                           |                |
| Debt  | \$1,979          | \$1,141           | \$2,108                       | \$(3)                     | \$5,225        |
| Postretirement benefits liabilities   | —                | 2,839             | 198                           | —                         | 3,037          |
| Amounts due to (from) affiliates  | (7,820)          | 10,584            | (2,936)                       | 172                       | —              |
| Other liabilities   | 3,711            | 1                 | (595)                         | (70)                      | 3,047          |
| <b>Total liabilities</b>  | <b>(2,130)</b>   | <b>14,565</b>     | <b>(1,225)</b>                | <b>99</b>                 | <b>11,309</b>  |
| Stockholders' equity attributable to non-controlling interest                     | —                | —                 | 7                             | —                         | 7              |
| Stockholders' equity (deficit) attributable to Navistar International Corporation | (5,128)          | (6,577)           | 5,429                         | 1,148                     | (5,128)        |
| <b>Total liabilities and stockholders' equity (deficit)</b>                       | <b>\$(7,258)</b> | <b>\$7,988</b>    | <b>\$4,211</b>                | <b>\$1,247</b>            | <b>\$6,188</b> |

Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

## Condensed Consolidating Statement of Cash Flows for the Six Months Ended April 30, 2016

| (in millions)   | NIC     | Navistar, Inc. | Non-Guarantor Subsidiaries | Eliminations and Other | Consolidated |
|---|---------|----------------|----------------------------|------------------------|--------------|
| Net cash provided by (used in) operations                       | \$(293) | \$ (297 )      | \$ 218                     | \$ 268                 | \$ (104 )    |
| Cash flows from investment activities                           |         |                |                            |                        |              |
| Net change in restricted cash and cash equivalents              | —       | 2              | (21 )                      | —                      | (19 )        |
| Net sales (purchases) of marketable securities                  | 65      | —              | (134 )                     | —                      | (69 )        |
| Capital expenditures and purchase of equipment leased to others | —       | (34 )          | (97 )                      | —                      | (131 )       |
| Other investing activities                                      | —       | —              | 53                         | —                      | 53           |
| Net cash provided by (used in) investing activities             | 65      | (32 )          | (199 )                     | —                      | (166 )       |
| Cash flows from financing activities                            |         |                |                            |                        |              |
| Net borrowings (repayments) of debt                             | —       | 259            | (26 )                      | (298 )                 | (65 )        |
| Other financing activities                                      | —       | 13             | (49 )                      | 30                     | (6 )         |
| Net cash provided by (used in) financing activities             | —       | 272            | (75 )                      | (268 )                 | (71 )        |
| Effect of exchange rate changes on cash and cash equivalents    | —       | —              | 18                         | —                      | 18           |
| Decrease in cash and cash equivalents                           | (228 )  | (57 )          | (38 )                      | —                      | (323 )       |
| Cash and cash equivalents at beginning of the period            | 456     | 81             | 375                        | —                      | 912          |
| Cash and cash equivalents at end of the period                  | \$228   | \$ 24          | \$ 337                     | \$ —                   | \$ 589       |

## Condensed Consolidating Statement of Operations for the Three Months Ended April 30, 2015

| (in millions)  | NIC    | Navistar, Inc. | Non-Guarantor Subsidiaries | Eliminations and Other | Consolidated |
|--|--------|----------------|----------------------------|------------------------|--------------|
| Sales and revenues, net  | \$—    | \$ 2,009       | \$ 1,943                   | \$ (1,259 )            | \$ 2,693     |
| Costs of products sold   | —      | 1,864          | 1,735                      | (1,239 )               | 2,360        |
| Restructuring charges  | —      | —              | 6                          | —                      | 6            |
| Asset impairment charges   | —      | 1              | —                          | —                      | 1            |
| All other operating expenses (income)                                | 27     | 282            | 79                         | (22 )                  | 366          |
| Total costs and expenses   | 27     | 2,147          | 1,820                      | (1,261 )               | 2,733        |
| Equity in income (loss) of affiliates                                | (37 )  | 64             | —                          | (26 )                  | 1            |
| Income (loss) before income taxes                                    | (64 )  | (74 )          | 123                        | (24 )                  | (39 )        |
| Income tax expense   | —      | (1 )           | (17 )                      | —                      | (18 )        |
| Earnings (loss) from continuing operations                           | (64 )  | (75 )          | 106                        | (24 )                  | (57 )        |
| Income (loss) from discontinued operations, net of tax               | —      | —              | —                          | —                      | —            |
| Net income (loss)  | (64 )  | (75 )          | 106                        | (24 )                  | (57 )        |
| Less: Net income attributable to non-controlling interests           | —      | —              | 7                          | —                      | 7            |
| Net income (loss) attributable to Navistar International Corporation | \$(64) | \$(75 )        | \$ 99                      | \$ (24 )               | \$( 64 )     |

Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

Condensed Consolidating Statement of Comprehensive Income (Loss) for the Three Months Ended April 30, 2015

| (in millions)  | NIC    | Navistar, Inc. | Non-Guaranteed Subsidiaries | Eliminations and Other | Consolidated |
|--|--------|----------------|-----------------------------|------------------------|--------------|
| Net income (loss)  | \$(64) | \$(75)         | \$ 106                      | \$ (24)                | \$(57)       |
| Other comprehensive income (loss):   |        |                |                             |                        |              |
| Foreign currency translation adjustment  | (27)   | —              | (27)                        | 27                     | (27)         |
| Defined benefit plans (net of tax)   | 33     | 31             | 2                           | (33)                   | 33           |
| Total other comprehensive income (loss)  | 6      | 31             | (25)                        | (6)                    | 6            |
| Comprehensive income (loss)  | (58)   | (44)           | 81                          | (30)                   | (51)         |
| Less: Net income attributable to non-controlling interests                           | —      | —              | 7                           | —                      | 7            |
| Total comprehensive income (loss) attributable to Navistar International Corporation | \$(58) | \$(44)         | \$ 74                       | \$ (30)                | \$(58)       |

Condensed Consolidating Statement of Operations for the Six Months Ended April 30, 2015

| (in millions)  | NIC     | Navistar, Inc. | Non-Guaranteed Subsidiaries | Eliminations and Other | Consolidated |
|--|---------|----------------|-----------------------------|------------------------|--------------|
| Sales and revenues, net  | \$—     | \$3,619        | \$ 3,711                    | \$(2,216)              | \$ 5,114     |
| Costs of products sold   | —       | 3,273          | 3,305                       | (2,173)                | 4,405        |
| Restructuring charges  | —       | 3              | 6                           | —                      | 9            |
| Asset impairment charges   | —       | 8              | —                           | —                      | 8            |
| All other operating expenses (income)                                | 50      | 546            | 204                         | (40)                   | 760          |
| Total costs and expenses   | 50      | 3,830          | 3,515                       | (2,213)                | 5,182        |
| Equity in income (loss) of affiliates                                | (56)    | 79             | 1                           | (21)                   | 3            |
| Income (loss) before income taxes                                    | (106)   | (132)          | 197                         | (24)                   | (65)         |
| Income tax expense   | —       | (2)            | (23)                        | —                      | (25)         |
| Earnings (loss) from continuing operations                           | (106)   | (134)          | 174                         | (24)                   | (90)         |
| Income (loss) from discontinued operations, net of tax               | —       | —              | —                           | —                      | —            |
| Net income (loss)  | (106)   | (134)          | 174                         | (24)                   | (90)         |
| Less: Net income attributable to non-controlling interests           | —       | —              | 16                          | —                      | 16           |
| Net income (loss) attributable to Navistar International Corporation | \$(106) | \$(134)        | \$ 158                      | \$ (24)                | \$(106)      |

Condensed Consolidating Statement of Comprehensive Income (Loss) for the Six Months Ended April 30, 2015

| (in millions)  | NIC     | Navistar, Inc. | Non-Guaranteed Subsidiaries | Eliminations and Other | Consolidated |
|--|---------|----------------|-----------------------------|------------------------|--------------|
| Net income (loss)  | \$(106) | \$(134)        | \$ 174                      | \$ (24)                | \$(90)       |
| Other comprehensive income (loss):   |         |                |                             |                        |              |
| Foreign currency translation adjustment  | (86)    | —              | (86)                        | 86                     | (86)         |
| Defined benefit plans (net of tax)   | 65      | 62             | 3                           | (65)                   | 65           |
| Total other comprehensive income (loss)  | (21)    | 62             | (83)                        | 21                     | (21)         |
| Comprehensive income (loss)  | (127)   | (72)           | 91                          | (3)                    | (111)        |
| Less: Net income attributable to non-controlling interests                           | —       | —              | 16                          | —                      | 16           |
| Total comprehensive income (loss) attributable to Navistar International Corporation | \$(127) | \$(72)         | \$ 75                       | \$ (3)                 | \$(127)      |



Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

## Condensed Consolidating Balance Sheet as of October 31, 2015

| (in millions)   | NIC              | Navistar,<br>Inc. | Non-Guarantor<br>Subsidiaries | Eliminations<br>and Other | Consolidated    |
|---|------------------|-------------------|-------------------------------|---------------------------|-----------------|
| <b>Assets</b>   |                  |                   |                               |                           |                 |
| Cash and cash equivalents   | \$456            | \$ 81             | \$ 375                        | \$ —                      | \$ 912          |
| Marketable securities   | 112              | —                 | 47                            | —                         | 159             |
| Restricted cash   | 16               | 7                 | 98                            | —                         | 121             |
| Finance and other receivables, net  | 1                | 99                | 2,440                         | (103 )                    | 2,437           |
| Inventories   | —                | 809               | 342                           | (16 )                     | 1,135           |
| Investments in non-consolidated affiliates  | (7,679 )         | 6,204             | 64                            | 1,477                     | 66              |
| Property and equipment, net   | —                | 737               | 616                           | (8 )                      | 1,345           |
| Goodwill  | —                | —                 | 38                            | —                         | 38              |
| Deferred taxes, net   | 7                | 20                | 137                           | —                         | 164             |
| Other   | 33               | 128               | 155                           | (1 )                      | 315             |
| <b>Total assets</b>   | <b>\$(7,054)</b> | <b>\$ 8,085</b>   | <b>\$ 4,312</b>               | <b>\$ 1,349</b>           | <b>\$ 6,692</b> |
| <b>Liabilities and stockholders' equity (deficit)</b>                             |                  |                   |                               |                           |                 |
| <b>Debt</b>   |                  |                   |                               |                           |                 |
| Debt  | \$1,971          | \$ 1,180          | \$ 2,151                      | \$ (4 )                   | \$ 5,298        |
| Postretirement benefits liabilities   | —                | 2,909             | 179                           | —                         | 3,088           |
| Amounts due to (from) affiliates  | (7,574 )         | 10,280            | (2,879 )                      | 173                       | —               |
| Other liabilities   | 3,716            | 207               | (388 )                        | (69 )                     | 3,466           |
| <b>Total liabilities</b>  | <b>(1,887 )</b>  | <b>14,576</b>     | <b>(937 )</b>                 | <b>100</b>                | <b>11,852</b>   |
| Stockholders' equity attributable to non-controlling interest                     | —                | —                 | 7                             | —                         | 7               |
| Stockholders' equity (deficit) attributable to Navistar International Corporation | (5,167 )         | (6,491 )          | 5,242                         | 1,249                     | (5,167 )        |
| <b>Total liabilities and stockholders' equity (deficit)</b>                       | <b>\$(7,054)</b> | <b>\$ 8,085</b>   | <b>\$ 4,312</b>               | <b>\$ 1,349</b>           | <b>\$ 6,692</b> |

Navistar International Corporation and Subsidiaries  
Notes to Consolidated Financial Statements—(Continued)  
(Unaudited)

Condensed Consolidating Statement of Cash Flows for the Six Months Ended April 30, 2015

| (in millions)   | NIC     | Navistar, Inc. | Non-Guarantor Subsidiaries | Eliminations and Other | Consolidated |
|---|---------|----------------|----------------------------|------------------------|--------------|
| Net cash provided by (used in) operations                       | \$(168) | \$ 41          | \$ (188 )                  | \$ 78                  | \$ (237 )    |
| Cash flows from investment activities                           |         |                |                            |                        |              |
| Net change in restricted cash and cash equivalents              | 1       | (2 )           | 54                         | —                      | 53           |
| Net sales of marketable securities                              | 229     | —              | 103                        | —                      | 332          |
| Capital expenditures and purchase of equipment leased to others | —       | (30 )          | (35 )                      | —                      | (65 )        |
| Other investing activities                                      | —       | 7              | 5                          | —                      | 12           |
| Net cash provided by (used in) investing activities             | 230     | (25 )          | 127                        | —                      | 332          |
| Cash flows from financing activities                            |         |                |                            |                        |              |
| Net borrowings (repayments) of debt                             | —       | (52 )          | 66                         | 2                      | 16           |
| Other financing activities                                      | —       | 20             | 61                         | (80 )                  | 1            |
| Net cash provided by (used in) financing activities             | —       | (32 )          | 127                        | (78 )                  | 17           |
| Effect of exchange rate changes on cash and cash equivalents    | —       | —              | (26 )                      | —                      | (26 )        |
| Increase (decrease) in cash and cash equivalents                | 62      | (16 )          | 40                         | —                      | 86           |
| Cash and cash equivalents at beginning of the period            | 101     | 53             | 343                        | —                      | 497          |
| Cash and cash equivalents at end of the period                  | \$163   | \$ 37          | \$ 383                     | \$ —                   | \$ 583       |



## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is designed to provide information that is supplemental to, and should be read together with, our consolidated financial statements and the accompanying notes contained in our Annual Report on Form 10-K for the year ended October 31, 2015. Information in MD&A is intended to assist the reader in obtaining an understanding of (i) our consolidated financial statements, (ii) the changes in certain key items within those financial statements from year-to-year, (iii) the primary factors that contributed to those changes, (iv) any changes in known trends or uncertainties from items disclosed within the MD&A of our Annual Report on Form 10-K for the year ended October 31, 2015 that we are aware of and that may have a material effect on our future performance, and (v) how certain accounting principles affect our consolidated financial statements. In addition, MD&A provides information about our business segments and how the results of those segments impact our results of operations and financial condition as a whole. Operating results for interim reporting periods are not necessarily indicative of annual operating results.

### Executive Overview

Navistar is an international manufacturer of International® brand commercial and military trucks, proprietary brand diesel engines, and IC Bus™ ("IC") brand school and commercial buses, as well as a provider of service parts for trucks and diesel engines. Our core business is conducted in the North American truck and parts markets, where we principally participate in the U.S. and Canada school bus and Class 6 through 8 medium and heavy truck markets (our "Core" markets). We also provide retail, wholesale, and lease financing services for our trucks and parts.

### Second Quarter Summary

During the second quarter of 2016, we continued to focus on our strategy which includes: implementing our customer centric strategy, completing new product launches, improving financial performance and increasing profitable market share. We believe our strategy will enable us to improve our sales and market share, as well as to add value to our customers.

We continue to focus on our Core markets. On February 1, 2016 we launched the International® HX™ Series, the first in a series of new product launches. The HX™ is a Class 8 premium vocational truck designed to deliver the strength and durability required for the severe service industry.

We also continue to evaluate our portfolio of assets, with the purpose of closing or divesting non-core/non-strategic businesses, and identify opportunities to restructure our business and rationalize our Manufacturing operations to optimize our cost structure. In February 2016, we sold Pure Power Technologies ("PPT"), a components business focused on air and fuel systems.

### Financial Summary

**Continuing Operations Results** — In the second quarter of 2016, our consolidated net sales and revenues were \$2.2 billion, down 18% compared to the prior year quarter. The 18% decrease reflects lower sales from our Truck and Global Operations segments, partially offset by increased sales in our Parts segment. In the first half of 2016, our consolidated net sales and revenues were \$4.0 billion, down 23% compared to the first half of 2015. The 23% decrease reflects lower sales from our Truck, Parts, and Global Operations segments.

In the second quarter and first half of 2016, we recognized income from continuing operations before income taxes of \$29 million and zero, respectively, compared to a loss from continuing operations of \$39 million and \$65 million in the respective periods in the prior year. The improvement in the second quarter of 2016 was primarily driven by lower structural costs of \$56 million and improved product margin in our Core markets, partially offset by higher adjustments to pre-existing warranties. The improvement in the first half of 2016 was primarily driven by lower structural costs of \$113 million, improved product margin in our Core markets, and improved Other income of \$16 million primarily due to a one-time fee received from a third party and the accelerated recognition of deferred income for an intellectual property ("IP") license, partially offset by a gain recorded in the second quarter of 2015 related to the settlement of a customer dispute. These improvements were partially offset by higher adjustments to pre-existing warranties and an increase in our used truck reserves. Our gross used truck inventory increased to approximately \$448 million at April 30, 2016 from \$390 million at October 31, 2015 (offset by reserves of \$168 million and \$110 million, at the respective dates) due, in part, to an increase in used truck receipts coupled with a decrease in used truck sales. We continue to seek alternative channels to sell our used trucks, including certain export markets which have resulted in a lower price point as compared to our domestic channels.



In the second quarter of 2016, consolidated net income from continuing operations attributable to Navistar International Corporation, before manufacturing interest, taxes, depreciation and amortization expenses (“EBITDA”) was \$135 million, compared to EBITDA of \$85 million for the comparable period in 2015. After excluding net charges of \$52 million and \$17 million in the second quarters of 2016 and 2015, respectively, Adjusted EBITDA was \$187 million in the second quarter of 2016 compared to Adjusted EBITDA of \$102 million in the comparable period in 2015. In the first half of 2016 and 2015, EBITDA was \$217 million and \$186 million, respectively. After excluding a net charge of \$47 million and a net benefit of \$30 million in the first half of 2016 and 2015, respectively, Adjusted EBITDA was \$264 million in the first half of 2016 compared to Adjusted EBITDA of \$156 million for the comparable period in 2015. EBITDA and Adjusted EBITDA are not determined in accordance with U.S. GAAP, nor are they presented as alternatives to U.S. GAAP measures. For more information regarding this non-GAAP financial information, see Consolidated EBITDA and Adjusted EBITDA.

In the second quarter and first half of 2016, we recognized income tax expense from continuing operations of \$16 million and \$11 million, respectively, compared to income tax expense of \$18 million and \$25 million in the respective prior year periods. The difference in the income tax expense in the first half of 2016 compared to the first half of 2015 was primarily due to the \$13 million income tax benefit from the release of the valuation allowance on U.S. AMT credits in the first quarter of 2016.

In the second quarter of 2016, after income taxes, the income from continuing operations attributable to Navistar International Corporation was \$4 million, or \$0.05 per diluted share, and in the first half of 2016 the loss from continuing operations attributable to Navistar International Corporation, after income taxes, was \$29 million, or \$0.35 per diluted share. In the second quarter and first half of 2015, after income taxes, the loss from continuing operations attributable to Navistar International Corporation was \$64 million and \$106 million, or \$0.78 and \$1.30 per diluted share, respectively.

We ended the second quarter of 2016 with \$817 million of consolidated cash, cash equivalents and marketable securities, compared to \$1.1 billion as of October 31, 2015. The decrease in consolidated cash, cash equivalents and marketable securities was primarily attributable to an increase in inventories and other noncurrent assets as well as decreases in accounts payable and other current and noncurrent liabilities, repayment of short-term and long-term debt, and payments for capital expenditures, partially offset by collections of accounts and finance receivables, and proceeds received for the sale of property and equipment.

## Results of Continuing Operations

The following information summarizes our Consolidated Statements of Operations and illustrates the key financial indicators used to assess our consolidated financial results.

Results of Operations for the three and six months ended April 30, 2016 as compared to the three and six months ended April 30, 2015

| (in millions, except per share data and % change)            | Three Months Ended April 30, |          |         |          | Six Months Ended April 30, |          |           |          |
|--|------------------------------|----------|---------|----------|----------------------------|----------|-----------|----------|
|  | 2016                         | 2015     | Change  | % Change | 2016                       | 2015     | Change    | % Change |
| Sales and revenues, net                                      | \$2,197                      | \$2,693  | \$(496) | (18)%    | \$3,962                    | \$5,114  | \$(1,152) | (23)%    |
| Costs of products sold                                       | 1,845                        | 2,360    | (515)   | (22)%    | 3,311                      | 4,405    | (1,094)   | (25)%    |
| Restructuring charges  | 3                            | 6        | (3)     | (50)%    | 6                          | 9        | (3)       | (33)%    |
| Asset impairment charges                                     | 3                            | 1        | 2       | N.M.     | 5                          | 8        | (3)       | (38)%    |
| Selling, general and administrative expenses                 | 202                          | 243      | (41)    | (17)%    | 407                        | 484      | (77)      | (16)%    |
| Engineering and product development costs                    | 61                           | 76       | (15)    | (20)%    | 119                        | 155      | (36)      | (23)%    |
| Interest expense   | 81                           | 75       | 6       | 8%       | 162                        | 152      | 10        | 7%       |
| Other income, net  | (25)                         | (28)     | 3       | (11)%    | (47)                       | (31)     | (16)      | 52%      |
| Total costs and expenses                                     | 2,170                        | 2,733    | (563)   | (21)%    | 3,963                      | 5,182    | (1,219)   | (24)%    |
| Equity in income of non-consolidated affiliates              | 2                            | 1        | 1       | N.M.     | 1                          | 3        | (2)       | (67)%    |
| Income (loss) from continuing operations before income taxes | 29                           | (39)     | 68      | N.M.     | —                          | (65)     | 65        | N.M.     |
| Income tax expense   | (16)                         | (18)     | 2       | (11)%    | (11)                       | (25)     | 14        | (56)%    |
| Income (loss) from continuing operations                     | 13                           | (57)     | 70      | N.M.     | (11)                       | (90)     | 79        | (88)%    |
| Less: Net income attributable to non-controlling interests   | 9                            | 7        | 2       | 29%      | 18                         | 16       | 2         | 13%      |
| Income (loss) from continuing operations <sup>(A)</sup>      | 4                            | (64)     | 68      | N.M.     | (29)                       | (106)    | 77        | (73)%    |
| Income (loss) from discontinued operations, net of tax       | —                            | —        | —       | —%       | —                          | —        | —         | —%       |
| Net income (loss) <sup>(A)</sup>                             | \$4                          | \$(64)   | \$68    | N.M.     | \$(29)                     | \$(106)  | \$77      | (73)%    |
| Diluted income (loss) per share: <sup>(A)</sup>              |                              |          |         |          |                            |          |           |          |
| Continuing operations  | \$0.05                       | \$(0.78) | \$0.83  | N.M.     | \$(0.35)                   | \$(1.30) | \$0.95    | (73)%    |
| Discontinued operations                                      | —                            | —        | —       | —%       | —                          | —        | —         | —%       |
|  | \$0.05                       | \$(0.78) | \$0.83  | N.M.     | \$(0.35)                   | \$(1.30) | \$0.95    | (73)%    |
| Diluted weighted average shares outstanding                  | 82.0                         | 81.6     | 0.4     | —%       | 81.7                       | 81.5     | 0.2       | —%       |

N.M. Not meaningful.

(A) Amounts attributable to Navistar International Corporation.

Sales and revenues, net

Our sales and revenues, net, are principally generated via sales of products and services. Sales and revenues, net, by reporting segment were as follows:

| (in millions, except % change) | Three Months<br>Ended April 30, |         |         |             | Six Months<br>Ended April 30, |         |           |             |
|--------------------------------|---------------------------------|---------|---------|-------------|-------------------------------|---------|-----------|-------------|
|                                | 2016                            | 2015    | Change  | %<br>Change | 2016                          | 2015    | Change    | %<br>Change |
| Truck                          | \$1,480                         | \$1,966 | \$(486) | (25)%       | \$2,612                       | \$3,636 | \$(1,024) | (28)%       |
| Parts                          | 647                             | 613     | 34      | 6%          | 1,217                         | 1,239   | (22)      | (2)%        |
| Global Operations              | 77                              | 130     | (53)    | (41)%       | 169                           | 282     | (113)     | (40)%       |
| Financial Services             | 58                              | 60      | (2)     | (3)%        | 117                           | 120     | (3)       | (3)%        |
| Corporate and Eliminations     | (65)                            | (76)    | 11      | (14)%       | (153)                         | (163)   | 10        | (6)%        |
| Total                          | \$2,197                         | \$2,693 | \$(496) | (18)%       | \$3,962                       | \$5,114 | \$(1,152) | (23)%       |

In the second quarter of 2016, the Truck segment net sales decreased \$486 million, or 25%, primarily due to lower Core truck volumes, ceasing Ford sales through our BDT joint venture, and the impact of a shift in product mix in our Core markets. Chargeouts from our Core markets were down 15%. In the first half of 2016, the Truck segment net sales decreased \$1.0 billion, or 28%, primarily due to lower Core truck volumes, ceasing BDT sales, a decline in our export truck volumes, and the impact of a shift in product mix in our Core markets. Chargeouts from our Core markets were down 17%.

The Parts segment net sales improvement of \$34 million, or 6%, in the second quarter of 2016, was primarily due to enhanced retail programs in our U.S. market, partially offset by unfavorable movements in foreign currency exchange rates and market pressures, primarily in Canada and Mexico. In the first half of 2016, the Parts segment net sales decreased \$22 million, or 2%, as enhanced retail programs in our U.S. market were more than offset by unfavorable movements in foreign currency exchange rates and market pressures, primarily in Canada and Mexico, and a decline in BDP net sales due to a decrease of units in operation.

The Global Operations segment net sales decrease of \$53 million and \$113 million, or 41% and 40%, in the second quarter and first half of 2016, respectively, was primarily due to lower volumes in our South American engine operations due to the economic downturn in Brazil as well as unfavorable movements in foreign currency exchange rates.

In the second quarter and first half of 2016, the Financial Services segment net revenues decreased \$2 million and \$3 million, respectively, or 3%, primarily due to a decline in the average retail notes receivable balances and unfavorable movements in foreign currency exchange rates.

Costs of products sold

In the second quarter and first half of 2016, Costs of products sold decreased by \$515 million and \$1.1 billion, respectively, reflecting the impact of lower sales in our Core and global markets, ceasing BDT sales, improved purchasing and manufacturing costs in our Core markets, and the impact of a shift in product mix in our Core markets, partially offset by higher adjustments to pre-existing warranties and an increase in our used truck reserves. In the second quarter and first half of 2016, we recognized charges for adjustments to pre-existing warranties of \$46 million and \$51 million, compared to a charge for adjustments to pre-existing warranties of \$18 million and a benefit for adjustments to pre-existing warranties of \$39 million in the respective prior year periods. The pre-existing charges in 2016 primarily relate to increases in both claim frequency and cost of repair across both the Medium Duty and Big Bore engine families. These charges increase the reserve for Navistar's standard warranty obligations as well as the loss positions related to our Big Bore extended service contracts. For more information on our estimated warranty obligations, see Note 1, Summary of Significant Accounting Policies, to the accompanying consolidated financial statements.

Selling, general and administrative expenses

The Selling, general and administrative ("SG&A") expense decreases of \$41 million and \$77 million, in the second quarter and first half of 2016, respectively, are primarily due to the impact of our cost-reduction initiatives.

In the fourth quarter of 2015, we offered the majority of our U.S.-based non-represented salaried employees the opportunity to apply for a voluntary separation program ("VSP"). Along with the VSP, in the third quarter of 2015, we

used attrition and an involuntary reduction in force to eliminate additional positions in order to meet our targeted reductions goal. In addition to these actions in the U.S., our Brazilian operations continued to restructure its business through various actions including utilization of an involuntary reduction in force to eliminate positions. As a result of these actions, we have realized year-over-year savings. For more information on these initiatives, see Note 2, Restructurings and Impairments, to the accompanying consolidated financial statements.

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#### Engineering and product development costs

The Engineering and product development cost decreases of \$15 million and \$36 million, in the second quarter and first half of 2016, respectively, were primarily driven by our efforts to focus spending on our Core markets while putting less emphasis on engine development. Engineering spend is targeted at programs that will reduce cost, improve uptime for our customers, grow market share and allow us to meet new emissions standards in 2017. Over the next two years, we expect to introduce new vehicles across our entire product line.

#### Interest expense

In the second quarter and first half of 2016, interest expense increased \$6 million and \$10 million, respectively, compared to the comparable prior year periods, primarily driven by the refinancing of our Amended Term Loan Credit Facility with a new Senior Secured Term Loan Credit Facility in August 2015.

#### Other income, net

We recognized Other income of \$25 million and \$47 million in the second quarter and first half of 2016, respectively, compared to \$28 million and \$31 million in the comparable prior year periods. The increase in Other income in the first half of 2016 is primarily driven by the recognition of deferred income for an IP license of \$19 million in the second quarter of 2016 and a \$15 million one-time fee received from a third party in the first quarter of 2016, partially offset by a \$14 million gain recorded in the second quarter of 2015 related to the settlement of a customer dispute.

#### Income tax (expense) benefit

In the second quarter and first half of 2016, we recognized an income tax expense from continuing operations of \$16 million and \$11 million, respectively, compared to \$18 million and \$25 million in the comparable prior year periods. The decrease in income tax expense in the first half of 2016 is primarily due to the \$13 million income tax benefit from the 2016 release of the valuation allowance on U.S. AMT credits as well as geographical mix and certain discrete items. The release of the valuation allowance on U.S. AMT credits is the result of new tax legislation, which allows us to forego bonus depreciation in exchange for refunds of previously paid AMT. Income taxes attributable to U.S. operations in both periods was limited to current state income taxes, and the effect of discrete items, due to the valuation allowances on most of our U.S. deferred tax assets.

At October 31, 2015, we had \$2.6 billion of U.S. federal net operating loss carryforwards and \$252 million of federal tax credit carryforwards. We expect our cash payments of U.S. taxes will be minimal for as long as we are able to offset our U.S. taxable income by these U.S. net operating losses and tax credits, which have carryforward periods of up to 20 years. We also have U.S. state and foreign net operating losses that are available to reduce cash payments of U.S. state and foreign taxes in future periods. We maintain valuation allowances on most of our U.S. and certain foreign deferred tax assets because it is more likely than not that those deferred tax assets will not be realized. It is reasonably possible within the next twelve months that an additional valuation allowance may be required on certain foreign deferred tax assets. For more information, see Note 8, Income Taxes, to the accompanying consolidated financial statements.

#### Net income attributable to non-controlling interests

Net income attributable to non-controlling interests is the result of our consolidation of subsidiaries that we do not wholly own. Substantially all of our net income attributable to non-controlling interests in 2016 and 2015 relates to Ford's non-controlling interest in BDP.

## Segment Results of Continuing Operations

We define segment profit (loss) as net income (loss) from continuing operations attributable to NIC excluding income tax benefit (expense). The following sections analyze operating results as they relate to our four segments and do not include intersegment eliminations. For additional information concerning our segments, see Note 12, Segment Reporting, to the accompanying consolidated financial statements.

## Truck Segment

| (in millions, except % change) | Three Months<br>Ended April 30, |         |         |             | Six Months<br>Ended April 30, |         |           |             |
|--------------------------------|---------------------------------|---------|---------|-------------|-------------------------------|---------|-----------|-------------|
|                                | 2016                            | 2015    | Change  | %<br>Change | 2016                          | 2015    | Change    | %<br>Change |
| Truck segment sales, net       | \$1,480                         | \$1,966 | \$(486) | (25)%       | \$2,612                       | \$3,636 | \$(1,024) | (28)%       |
| Truck segment loss             | (23)                            | (51)    | 28      | (55)%       | (74)                          | (69)    | (5)       | 7%          |

## Segment sales

In the second quarter of 2016, the Truck segment net sales decreased \$486 million, or 25%, due to lower Core truck volumes, ceasing Ford sales through our BDT joint venture in 2015, and the impact of a shift in product mix in our Core markets. Truck chargeouts from our Core markets were down 15%, reflecting a 7% decrease in Class 6 and 7 medium trucks, a 33% decrease in Class 8 heavy trucks, and a 17% decrease in Class 8 severe service trucks, partially offset by a 22% increase in school buses.

In the first half of 2016, the Truck segment net sales decreased \$1.0 billion, or 28%, primarily due to lower Core truck volumes, ceasing BDT sales, a decline in our export truck volumes, and the impact of a shift in product mix in our Core markets. Truck chargeouts from our Core markets were down 17%, reflecting an 8% decrease in school buses, a 6% decrease in Class 6 and 7 medium trucks, a 30% decrease in Class 8 heavy trucks, and a 16% decrease in Class 8 severe service trucks.

## Segment loss

In the second quarter of 2016, the Truck segment results improved by \$28 million, or 55%. In the first half of 2016, the Truck segment loss increased by \$5 million, or 7%. The improvements were primarily driven by higher margins in our Core markets due to lower purchasing and manufacturing costs, improved SG&A and Engineering costs, lower accelerated depreciation charges, and higher Other income. Offsetting these improvements were higher adjustments to pre-existing warranties and an increase in our used truck reserves.

SG&A expenses and Engineering and product development costs continued to decline in 2016. The lower SG&A expenses reflect the impact of our cost-reduction initiatives. The lower Engineering and product development costs were primarily due to our efforts to focus spending on our Core markets while putting less emphasis on engine development. Engineering spend is targeted at programs that will reduce cost, improve uptime for our customers, grow market share and allow us to meet new emissions standards in 2017. Over the next two years, we expect to introduce new vehicles across our entire product line.

The Truck segment also realized certain other improvements. The segment incurred lower accelerated depreciation charges for certain assets related to foundry and engine facilities of \$12 million and \$23 million in the second quarter and first half of 2016, respectively, compared to the comparable prior year periods. For more information, see Note 2, Restructurings and Impairments, to the accompanying consolidated financial statements. Additionally, in the first quarter of 2016, the segment recorded a \$15 million one-time fee received from a third party and in the second quarter of 2016, we recognized deferred income for an IP license of \$19 million, in Other income, net.

Offsetting these factors are higher adjustments to pre-existing warranties. In the second quarter and first half of 2016, the Truck segment recorded charges for adjustments to pre-existing warranties of \$46 million and \$51 million, respectively, compared to charges for adjustments to pre-existing warranties of \$19 million and a benefit for adjustments to pre-existing warranties of \$36 million, respectively, in the comparable prior year periods. The pre-existing charges in 2016 primarily relate to increases in both claim frequency and cost of repair across both the Medium Duty and Big Bore engine families. These charges increase the reserve for Navistar's standard warranty obligations as well as the loss positions related to our Big Bore extended service contracts.





## Parts Segment

| (in millions, except % change) | Three Months Ended April 30, |       |        |          | Six Months Ended April 30, |         |          |          |
|--------------------------------|------------------------------|-------|--------|----------|----------------------------|---------|----------|----------|
|                                | 2016                         | 2015  | Change | % Change | 2016                       | 2015    | Change   | % Change |
| Parts segment sales, net       | \$647                        | \$613 | \$ 34  | 6 %      | \$1,217                    | \$1,239 | \$ (22 ) | (2 )%    |
| Parts segment profit           | 176                          | 133   | 43     | 32 %     | 326                        | 278     | 48       | 17 %     |

## Segment sales

In the second quarter of 2016, the Parts segment net sales improved \$34 million, or 6%, primarily due to enhanced retail programs in our U.S. market, partially offset by unfavorable movements in foreign currency exchange rates and market pressures, primarily in Canada and Mexico. In the first half of 2016, the Parts segment net sales decreased \$22 million, or 2%, as enhanced retail programs in our U.S. market were more than offset by unfavorable movements in foreign currency exchange rates and market pressures, primarily in Canada and Mexico, and a decline in BDP net sales due to a decrease of units in operation.

## Segment profit

In the second quarter and first half of 2016, the Parts segment increased its segment profit by \$43 million and \$48 million, or 32% and 17%, respectively, primarily due to margin improvements, cost-reduction initiatives, and lower intercompany access fees. Access fees are allocated to the Parts segment from the Truck segment, primarily for development of new products, and consist of certain engineering and product development costs, depreciation expense, and SG&A costs. The lower fees in 2016 are due to cost-reduction initiatives in the Truck segment.

## Global Operations Segment

| (in millions, except % change)          | Three Months Ended April 30, |       |          |          | Six Months Ended April 30, |       |           |          |
|---|------------------------------|-------|----------|----------|----------------------------|-------|-----------|----------|
|   | 2016                         | 2015  | Change   | % Change | 2016                       | 2015  | Change    | % Change |
| Global Operations segment sales, net    | \$77                         | \$130 | \$ (53 ) | (41 )%   | \$169                      | \$282 | \$ (113 ) | (40 )%   |
| Global Operations segment profit (loss) | (1 )                         | 1     | (2 )     | N.M.     | (14 )                      | (14 ) | —         | — %      |

## Segment sales

In the second quarter and first half of 2016, the Global Operations segment net sales decrease of \$53 million and \$113 million, or 41% and 40%, respectively, was primarily driven by a decrease in our South America engine operations, reflecting lower volumes, and unfavorable movements in foreign currency exchange rates, as the average conversion rate of the Brazilian Real to the U.S. dollar has weakened by 20% and 27%, respectively. The continued economic downturn in the Brazil economy has contributed to lower engine volumes of 46% and 29%, for the second quarter and first half of 2016, respectively, compared to the comparable prior year periods.

## Segment loss

In the second quarter and first half of 2016, the Global Operations segment results were comparable to the prior year. The comparative results were impacted by lower manufacturing and structural costs as a result of our prior year restructuring and cost-reduction efforts and favorable movements in foreign currency exchange rates, which was offset by a net gain of \$10 million recorded in the second quarter of 2015 related to the settlement of a customer dispute.

Financial Services Segment

| (in millions, except % change)        | Three Months Ended April 30, |      |         |          | Six Months Ended April 30, |       |         |          |
|---------------------------------------|------------------------------|------|---------|----------|----------------------------|-------|---------|----------|
|                                       | 2016                         | 2015 | Change  | % Change | 2016                       | 2015  | Change  | % Change |
| Financial Services segment sales, net | \$58                         | \$60 | \$ (2 ) | (3 )%    | \$117                      | \$120 | \$ (3 ) | (3 )%    |
| Financial Services segment profit     | 25                           | 22   | 3       | 14 %     | 51                         | 46    | 5       | 11 %     |

Segment revenues

In the second quarter and first half of 2016, net revenues in the Financial Services segment decreased by \$2 million and \$3 million, respectively, primarily driven by a decrease in the average retail notes receivable balances, partially offset by higher revenues from operating leases. The decline in the average retail notes receivable balance is primarily due to the continued liquidation of our U.S. retail portfolio and unfavorable movements in foreign currency in our Mexican retail portfolio.

Segment profit

In the second quarter and first half of 2016, the Financial Services segment profit increased by \$3 million and \$5 million, or 14% and 11%, respectively, primarily due to an increase in gains on lease terminations, a decrease in the provision for loan losses in Mexico, and cost reduction initiatives, partially offset by a decrease in revenue.

Supplemental Information

The following tables provide additional information on truck industry retail units, market share data, order units, backlog units, and chargeout units. These tables present key metrics and trends that provide quantitative measures on the performance of the Truck and Global Operations segments.

Truck Industry Retail Deliveries

The following table summarizes approximate industry retail deliveries for our Core markets, categorized by relevant class, according to Wards Communications and R.L. Polk & Co. ("Polk") and our Core retail deliveries:

| (in units)                      | Three Months Ended April 30, |        |         |          | Six Months Ended April 30, |         |          |          |  |
|---------------------------------|------------------------------|--------|---------|----------|----------------------------|---------|----------|----------|--|
|                                 | 2016                         | 2015   | Change  | % Change | 2016                       | 2015    | Change   | % Change |  |
| Core Markets (U.S. and Canada)  |                              |        |         |          |                            |         |          |          |  |
| School buses                    | 5,400                        | 4,400  | 1,000   | 23 %     | 11,700                     | 10,100  | 1,600    | 16 %     |  |
| Class 6 and 7 medium trucks     | 22,300                       | 20,000 | 2,300   | 12 %     | 43,000                     | 38,000  | 5,000    | 13 %     |  |
| Class 8 heavy trucks            | 41,900                       | 51,700 | (9,800) | (19 )%   | 89,600                     | 102,100 | (12,500) | (12 )%   |  |
| Class 8 severe service trucks   | 16,400                       | 14,700 | 1,700   | 12 %     | 30,700                     | 29,000  | 1,700    | 6 %      |  |
| Total Core Markets              | 86,000                       | 90,800 | (4,800) | (5 )%    | 175,000                    | 179,200 | (4,200 ) | (2 )%    |  |
| Combined class 8 trucks         | 58,300                       | 66,400 | (8,100) | (12 )%   | 120,300                    | 131,100 | (10,800) | (8 )%    |  |
| Navistar Core retail deliveries | 13,900                       | 15,500 | (1,600) | (10 )%   | 26,700                     | 28,500  | (1,800 ) | (6 )%    |  |

Truck Retail Delivery Market Share

The following table summarizes our approximate retail delivery market share percentages for the Class 6 through 8 U.S. and Canada truck markets, based on market-wide information from Wards Communications and Polk:

|                                | Three Months Ended |                  |                  |               |                |
|--------------------------------|--------------------|------------------|------------------|---------------|----------------|
|                                | April 30, 2016     | January 31, 2016 | October 31, 2015 | July 31, 2015 | April 30, 2015 |
| Core Markets (U.S. and Canada) |                    |                  |                  |               |                |
| Class 6 and 7 medium trucks    | 27%                | 20 %             | 19 %             | 24 %          | 27 %           |
| Class 8 heavy trucks           | 11%                | 10 %             | 11 %             | 12 %          | 12 %           |
| Class 8 severe service trucks  | 11%                | 16 %             | 15 %             | 15 %          | 15 %           |

Combined class 8 trucks            11% 11 % 12 % 13 % 13 %

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## Truck Orders, net

We define orders as written commitments received from customers and dealers during the year to purchase trucks. Net orders represent new orders received during the year less cancellations of orders made during the same year. Orders do not represent guarantees of purchases by customers or dealers and are subject to cancellation. Orders may be either sold orders, which will be built for specific customers, or stock orders, which will generally be built for dealer inventory for eventual sale to customers. These orders may be placed at our assembly plants in the U.S. and Mexico for destinations anywhere in the world and include trucks and buses. Historically, we have had an increase in net orders for stock inventory from our dealers at the end of the year due to a combination of demand and, from time to time, incentives to the dealers. Increases in stock orders typically translate to higher future chargeouts. The following table summarizes our approximate net orders for Core units:

| (in units)                     | Three Months<br>Ended April<br>30, |        |         |             | Six Months<br>Ended April<br>30, |        |         |             |
|--------------------------------|------------------------------------|--------|---------|-------------|----------------------------------|--------|---------|-------------|
|                                | 2016                               | 2015   | Change  | %<br>Change | 2016                             | 2015   | Change  | %<br>Change |
| Core Markets (U.S. and Canada) |                                    |        |         |             |                                  |        |         |             |
| School buses                   | 4,000                              | 3,500  | 500     | 14 %        | 6,000                            | 6,000  | —       | — %         |
| Class 6 and 7 medium trucks    | 3,500                              | 4,400  | (900 )  | (20 )%      | 8,800                            | 9,000  | (200 )  | (2 )%       |
| Class 8 heavy trucks           | 3,300                              | 5,600  | (2,300) | (41 )%      | 7,400                            | 13,700 | (6,300) | (46 )%      |
| Class 8 severe service trucks  | 1,800                              | 2,800  | (1,000) | (36 )%      | 4,200                            | 4,800  | (600 )  | (13 )%      |
| Total Core Markets             | 12,600                             | 16,300 | (3,700) | (23 )%      | 26,400                           | 33,500 | (7,100) | (21 )%      |
| Combined class 8 trucks        | 5,100                              | 8,400  | (3,300) | (39 )%      | 11,600                           | 18,500 | (6,900) | (37 )%      |

## Truck Backlogs

We define order backlogs ("backlogs") as orders yet to be built as of the end of the period. Our backlogs do not represent guarantees of purchases by customers or dealers and are subject to cancellation. Although backlogs are one of many indicators of market demand, other factors such as changes in production rates, internal and supplier available capacity, new product introductions, and competitive pricing actions may affect point-in-time comparisons. Backlogs exclude units in inventory awaiting additional modifications or delivery to the end customer. The following table summarizes our approximate backlog for Core units:

| (in units)                     | As of April<br>30, |        |         |             |
|--------------------------------|--------------------|--------|---------|-------------|
|                                | 2016               | 2015   | Change  | %<br>Change |
| Core Markets (U.S. and Canada) |                    |        |         |             |
| School buses                   | 2,700              | 3,000  | (300 )  | (10 )%      |
| Class 6 and 7 medium trucks    | 3,700              | 5,500  | (1,800) | (33 )%      |
| Class 8 heavy trucks           | 12,800             | 13,800 | (1,000) | (7 )%       |
| Class 8 severe service trucks  | 2,500              | 2,700  | (200 )  | (7 )%       |
| Total Core Markets             | 21,700             | 25,000 | (3,300) | (13 )%      |
| Combined class 8 trucks        | 15,300             | 16,500 | (1,200) | (7 )%       |

## Truck Chargeouts

We define chargeouts as trucks that have been invoiced to customers. The units held in dealer inventory represent the principal difference between retail deliveries and chargeouts. The following table summarizes our approximate worldwide chargeouts from our continuing operations:

| (in units)                     | Three Months<br>Ended April<br>30, |        |         |             | Six Months<br>Ended April<br>30, |        |          |             |
|--------------------------------|------------------------------------|--------|---------|-------------|----------------------------------|--------|----------|-------------|
|                                | 2016                               | 2015   | Change  | %<br>Change | 2016                             | 2015   | Change   | %<br>Change |
| Core Markets (U.S. and Canada) |                                    |        |         |             |                                  |        |          |             |
| School buses                   | 2,800                              | 2,300  | 500     | 22 %        | 4,600                            | 5,000  | (400 )   | (8 )%       |
| Class 6 and 7 medium trucks    | 6,200                              | 6,700  | (500 )  | (7 )%       | 10,100                           | 10,700 | (600 )   | (6 )%       |
| Class 8 heavy trucks           | 4,900                              | 7,300  | (2,400) | (33 )%      | 8,500                            | 12,100 | (3,600 ) | (30 )%      |
| Class 8 severe service trucks  | 1,900                              | 2,300  | (400 )  | (17 )%      | 3,600                            | 4,300  | (700 )   | (16 )%      |
| Total Core Markets             | 15,800                             | 18,600 | (2,800) | (15 )%      | 26,800                           | 32,100 | (5,300 ) | (17 )%      |
| Non "Core" military            | 200                                | —      | 200     | — %         | 200                              | —      | 200      | — %         |
| Other markets <sup>(A)</sup>   | 1,400                              | 5,400  | (4,000) | (74 )%      | 3,100                            | 12,400 | (9,300 ) | (75 )%      |
| Total worldwide units          | 17,400                             | 24,000 | (6,600) | (28 )%      | 30,100                           | 44,500 | (14,400) | (32 )%      |
| Combined class 8 trucks        | 6,800                              | 9,600  | (2,800) | (29 )%      | 12,100                           | 16,400 | (4,300 ) | (26 )%      |

Other markets primarily consist of Export Truck and Mexico and also include chargeouts related to BDT of 2,600 and 6,000 units during the three and six months ended April 30, 2015, respectively. There were no third party chargeouts related to BDT during the three and six months ended April 30, 2016 as Ford no longer purchases from BDT.

## Liquidity and Capital Resources

| (in millions)   | As of             |                     |                      |
|---|-------------------|---------------------|----------------------|
|   | April 30,<br>2016 | October 31,<br>2015 | April<br>30,<br>2015 |
| Consolidated cash and cash equivalents                        | \$589             | \$ 912              | \$583                |
| Consolidated marketable securities                            | 228               | 159                 | 273                  |
| Consolidated cash, cash equivalents and marketable securities | \$817             | \$ 1,071            | \$856                |

## Cash Requirements

Our primary sources of liquidity are cash provided by operating activities, including cash flow from the sale of trucks, buses, diesel engines, and parts, as well as from product financing provided to our dealers and retail customers by our Financial Services operations. It is our opinion that, in the absence of significant extraordinary cash demands, our: (i) level of cash, cash equivalents, and marketable securities, (ii) current and forecasted cash flow from our Manufacturing operations and Financial Services operations, (iii) availability under various funding facilities, (iv) current and forecasted availability from various funding alliances, and (v) access to capital in the capital markets will provide sufficient funds to meet operating requirements, capital expenditures, equity investments, and financial obligations both on a short-term and long-term basis. Future Manufacturing operations debt obligations are expected to be met through a combination of cash generation from operations and refinancing activities. We also believe the quality of our underlying portfolio of receivables will ensure the ongoing funding from various sources and alliance partners and will permit our Financial Services operations to meet the financing requirements of Navistar, our dealers, and retail customers.

Our Manufacturing operations have generally financed its operations with cash, funding from Financial Services, access to the capital markets, and, to a lesser extent, availability under our \$175 million Amended and Restated Asset-Based Credit Facility. Our borrowing capacity under our \$175 million Amended and Restated Asset-Based Credit Facility is subject to a \$35 million liquidity block, less outstanding standby letters of credit issued under this facility, and is impacted by inventory levels at certain aftermarket parts inventory locations. As of April 30, 2016, we had limited availability to borrow under the Amended and Restated Asset-Based Credit Facility. However, we maintain capacity under our various debt arrangements to incur incremental debt. In addition, the covenants in all of our debt agreements permit us to refinance existing debt instruments as they mature.

NFC makes intercompany loans to our Manufacturing operations, including the Intercompany Used Truck Loan. During the six months ended April 30, 2016 we increased our borrowings under the Intercompany Used Truck Loan by \$33 million to \$151 million. During 2015, we received \$125 million in dividends from NFC, of which \$80 million were funded by the partial repayment of an intercompany loan to NFC. In the second quarter of 2016, we received \$30 million in dividends from NFC. Also, in the second quarter of 2016, our Manufacturing operations in Mexico initiated a new program offered on vehicles ordered by the Mexico dealer network. In response to this program, our Financial Services operations in Mexico advance funded \$34 million of the pre-orders to the Manufacturing operations. The Financial Services segment has traditionally relied upon secured borrowings on finance receivables, short and long-term bank borrowings, medium and long-term debt, and commercial paper in Mexico to fund products sold or leased by Navistar, our dealers, and retail customers. We use a number of SPEs to securitize and sell receivables. Navistar Financial Securities Corporation ("NFSC") finances wholesale notes, Navistar Financial Retail Receivables Corporation ("NFRRC") finances retail notes and finance leases, International Truck Leasing Corporation ("ITLC") finances operating leases and some finance leases, and TRAC finances retail accounts. Our Mexican financial services operations include Navistar Financial, S.A. de C.V., Sociedad Financiera de Objeto Multiple, Entidad No Regulada ("NFM"), and Navistar Comercial S.A. de C.V., which provide vehicle financing and insurance brokerage to our dealers and retail customers in Mexico. As of April 30, 2016, the aggregate amount available to fund finance receivables under our financial services facilities was \$564 million.

In May 2016, NFC amended and extended its 2011 bank credit facility which was originally due in December 2016. The 2016 amendment extends the maturity date to June 2018 and initially reduces the revolving portion of the facility from \$500 million to \$400 million. The revolving portion will be further reduced to approximately \$275 million effective in December 2016. The amendment also provides for a reduction in the term loan facility, which was

previously \$229 million, to approximately \$82 million, effective in December 2016. The amendment allows NFC to increase revolving or term loan commitments, subject to obtaining commitments from existing or new lenders to provide additional or increased revolving commitments and/or additional term loans, to permit a maximum total facility size of \$700 million after giving effect to any such increase and without taking into account the non-extended loans and commitments. NFC plans to accommodate the December decrease of the bank facility with a partial pay down of the Intercompany Used Truck Loan, and other funding actions and strategies available to it, including a subsequent increase in NFC's bank facility, asset sales or securitizations, other secured borrowings or developing, expanding and executing additional alliances to finance an increasing share of Navistar, dealer or retail customer assets.

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In April, NFC extended its \$100 million TRAC facility until April 2017. In February, NFC also increased its VFN facility from \$375 million to \$500 million and in May the facility's maturity date was extended from October 2016 to May 2017.

Consolidated cash, cash equivalents and marketable securities was \$817 million at April 30, 2016, which includes \$2 million of cash and cash equivalents attributable to BDP, as well as an immaterial amount of cash and cash equivalents of certain VIEs that is generally not available to satisfy our obligations. For additional information on the consolidation of BDP, see Note 1, Summary of Significant Accounting Policies, to the accompanying consolidated financial statements.

Cash Flow Overview

| (in millions)  | Six Months Ended April 30, 2016          |                               |  |
|--|--|-------------------------------|--|
|  | Manufacturing Operations and Adjustments | Financial Services Operations | Condensed Consolidated Statement of Cash Flows |
| Net cash provided by (used in) operating activities          | \$(223)                                  | \$ 119                        | \$ (104 )                                      |
| Net cash used in investing activities                        | (86 )                                    | (80 )                         | (166 )   |
| Net cash used in financing activities                        | (54 )                                    | (17 )                         | (71 )  |
| Effect of exchange rate changes on cash and cash equivalents | 13                                       | 5                             | 18   |
| Increase (decrease) in cash and cash equivalents             | (350 )                                   | 27                            | (323 )   |
| Cash and cash equivalents at beginning of the period         | 877                                      | 35                            | 912  |
| Cash and cash equivalents at end of the period               | \$527                                    | \$ 62                         | \$ 589   |

| (in millions)  | Six Months Ended April 30, 2015          |                               |  |
|--|--|-------------------------------|--|
|  | Manufacturing Operations and Adjustments | Financial Services Operations | Condensed Consolidated Statement of Cash Flows |
| Net cash used in operating activities                        | \$(32 )                                  | \$( 205 )                     | \$ (237 )                                      |
| Net cash provided by investing activities                    | 295                                      | 37                            | 332  |
| Net cash provided by (used in) financing activities          | (132 )                                   | 149                           | 17   |
| Effect of exchange rate changes on cash and cash equivalents | (35 )                                    | 9                             | (26 )  |
| Increase (decrease) in cash and cash equivalents             | 96                                       | (10 )                         | 86   |
| Cash and cash equivalents at beginning of the period         | 440                                      | 57                            | 497  |
| Cash and cash equivalents at end of the period               | \$536                                    | \$ 47                         | \$ 583   |

Manufacturing operations cash flows and Financial Services operations cash flows are not presented in accordance with, and should not be viewed as an alternative to, GAAP. This non-GAAP financial information should be considered supplemental to, and not as a substitute for, or superior to, financial measures calculated in accordance with GAAP. However, we believe that non-GAAP reporting provides meaningful information and therefore we use it to supplement our GAAP reporting by identifying items that may not be related to the core manufacturing business. Management often uses this information to assess and measure the performance and liquidity of our operating segments. Our Manufacturing operations, for this purpose, include our Truck segment, Global Operations segment, Parts segment, and Corporate items which include certain eliminations. The reconciling differences between these non-GAAP financial measures and our GAAP consolidated financial statements in Item 1, Financial Statements and Supplementary Data, are our Financial Services operations and adjustments required to eliminate certain intercompany transactions between Manufacturing operations and Financial Services operations. Our Financial Services operations cash flows are presented consistent with their treatment in our Condensed Consolidated Statements of Cash Flows and may not be consistent with how they would be treated on a stand-alone basis. We have chosen to provide this supplemental information to allow additional analysis, to illustrate the respective cash flows

giving effect to the equity basis cash flow shown above, and to provide an additional measure of performance and liquidity.

Manufacturing Operations

Manufacturing Operations Cash Flow from Operating Activities

Cash used in operating activities was \$223 million and \$32 million in the six months ended April 30, 2016 and 2015, respectively. The net decrease in cash flow from operating activities in 2016 compared to 2015 was primarily attributable to increases in inventories and noncurrent assets, decreases in accounts payable due to higher payments, decreases in other current and noncurrent liabilities, and lower dividends received from our Financial Services operations, partially offset by a lower net loss, an increase in the collection of accounts receivable, an increase in fundings from our Financial Services operations under the Intercompany Used Truck Loan and a new program offered on vehicles ordered by the Mexico dealer network.

Cash paid for interest, net of amounts capitalized, was \$106 million and \$94 million in the six months ended April 30, 2016 and 2015, respectively.

#### Manufacturing Operations Cash Flow from Investing Activities

Cash used in investing activities was \$86 million in the six months ended April 30, 2016, compared to cash provided by investing activities of \$295 million in the six months ended April 30, 2015. The net decrease in cash flow from investing activities in 2016 compared to 2015 was primarily attributable to higher purchases and lower sales and maturities of marketable securities, partially offset by higher proceeds from sales of affiliates.

#### Manufacturing Operations Cash Flow from Financing Activities

Cash used in financing activities was \$54 million and \$132 million in the six months ended April 30, 2016 and 2015, respectively. The net change in cash flow from financing activities in 2016 was primarily attributable to lower principal repayments of debt and an intercompany loan due to our Financial Services operations.

#### Financial Services Operations

##### Financial Services Operations and Adjustments to Cash Flow from Operating Activities

Cash provided by operating activities was \$119 million in the six months ended April 30, 2016, compared to cash used in operating activities of \$205 million in the six months ended April 30, 2015. The increase in cash provided by operating activities in 2016 was primarily due to a decline in the level of finance receivables funded and a decline in the amount of dividends paid to the Manufacturing operations as compared to the prior year period. The increase was partially offset by an increase in fundings to the Manufacturing operations under the Intercompany Used Truck Loan and a new program offered on vehicles ordered by the Mexico dealer network.

Cash paid for interest, net of amounts capitalized, was \$31 million in both the six months ended April 30, 2016 and 2015.

##### Financial Services Operations and Adjustments to Cash Flow from Investing Activities

Cash used in investing activities was \$80 million in the six months ended April 30, 2016, compared to cash provided by investing activities of \$37 million in the six months ended April 30, 2015. Changes in restricted cash levels required under our secured borrowings were the primary sources and uses of cash from investing activities in 2016 and 2015, along with purchases of equipment leased to others. The increase in cash used in investing activities was primarily due to the increase in restricted cash relating to higher secured borrowings on retail accounts, and an increase in purchases of equipment leased to others. In the prior year period, restricted cash was liquidated in conjunction with the repayment of certain investor notes and a retail securitization.

##### Financial Services Operations and Adjustments to Cash Flow from Financing Activities

Cash used in financing activities was \$17 million in the six months ended April 30, 2016, compared to cash provided by financing activities of \$149 million in the six months ended April 30, 2015. The increase in cash used in financing activities in 2016 was primarily due to the repayment of debt associated with the decline in the level of finance receivables funded. The increase was partially offset by borrowings used to fund the increase in the Intercompany Used Truck Loan to the Manufacturing operations.

#### Consolidated EBITDA and Adjusted EBITDA

EBITDA and Adjusted EBITDA, which excludes certain identified items that we do not consider to be part of our ongoing business, are not in accordance with, and should not be viewed as an alternative to, U.S. GAAP. This non-GAAP financial information should be considered supplemental to, and not as a substitute for, or superior to, financial measures calculated in accordance with U.S. GAAP.

We believe EBITDA provides meaningful information about the performance of our business and therefore we use it to supplement our U.S. GAAP reporting. We believe that Adjusted EBITDA improves the comparability of year-to-year results, and is representative of our underlying performance. Management uses this information to assess and measure the performance of our operating segments. We have chosen to provide this supplemental information to investors, analysts and other interested parties to enable them to perform additional analyses of operating results, to illustrate the results of operations giving effect to the non-GAAP adjustments shown in the below reconciliations, and to provide an additional measure of performance.



EBITDA reconciliation:

| (in millions)  | Three Months Ended April 30, |        | Six Months Ended April 30, |         |
|--|------------------------------|--------|----------------------------|---------|
|  | 2016                         | 2015   | 2016                       | 2015    |
| Income (loss) from continuing operations attributable to NIC, net of tax | \$4                          | \$(64) | \$(29)                     | \$(106) |
| Plus:  |                              |        |                            |         |
| Depreciation and amortization expense                                    | 53                           | 74     | 111                        | 153     |
| Manufacturing interest expense <sup>(A)</sup>                            | 62                           | 57     | 124                        | 114     |
| Less:  |                              |        |                            |         |
| Income tax expense   | (16)                         | (18)   | (11)                       | (25)    |
| EBITDA   | \$135                        | \$85   | \$217                      | \$186   |

Manufacturing interest expense is the net interest expense primarily generated for borrowings that support the manufacturing and corporate operations, adjusted to eliminate intercompany interest expense with our Financial Services segment. The following table reconciles Manufacturing interest expense to the consolidated interest expense:

| (in millions)                             | Three Months Ended April 30, |      | Six Months Ended April 30, |       |
|---|------------------------------|------|----------------------------|-------|
|   | 2016                         | 2015 | 2016                       | 2015  |
| Interest expense                          | \$81                         | \$75 | \$162                      | \$152 |
| Less: Financial services interest expense | 19                           | 18   | 38                         | 38    |
| Manufacturing interest expense            | \$62                         | \$57 | \$124                      | \$114 |

Adjusted EBITDA Reconciliation:

| (in millions)   | Three Months Ended April 30, |       | Six Months Ended April 30, |       |
|---|------------------------------|-------|----------------------------|-------|
|   | 2016                         | 2015  | 2016                       | 2015  |
| EBITDA (reconciled above)                                     | \$135                        | \$85  | \$217                      | \$186 |
| Less significant items of:                                    |                              |       |                            |       |
| Adjustments to pre-existing warranties <sup>(A)</sup>         | 46                           | 18    | 51                         | (39)  |
| North America asset impairment charges <sup>(B)</sup>         | 3                            | 1     | 5                          | 8     |
| Cost reduction and other strategic initiatives <sup>(C)</sup> | 3                            | 2     | 6                          | 5     |
| Gain on settlement <sup>(D)</sup>                             | —                            | (10)  | —                          | (10)  |
| Brazil truck business actions <sup>(E)</sup>                  | —                            | 6     | —                          | 6     |
| One-time fee received <sup>(F)</sup>                          | —                            | —     | (15)                       | —     |
| Total adjustments   | 52                           | 17    | 47                         | (30)  |
| Adjusted EBITDA   | \$187                        | \$102 | \$264                      | \$156 |

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. Our warranty liability is generally affected by component failure rates, repair costs, and the timing of failures. Future events and circumstances related to these factors could materially change our estimates and require adjustments to our liability. In addition, new product launches require a greater use of judgment in developing estimates until historical experience becomes available.

(B)

In the first and second quarters of 2016, the Truck segment recorded \$2 million and \$3 million, respectively, of asset impairment charges relating to certain long lived assets. In the first quarter of 2015, the Truck segment recorded \$7 million of asset impairment charges relating to certain operating leases.

(C) Cost reduction and other strategic initiatives relates to costs associated with the divestiture of non-core facilities and efforts to optimize our cost structure.

(D) In the second quarter of 2015, the Global Operations segment recognized a \$10 million net gain related to the settlement of a customer dispute. The \$10 million net gain for the settlement included restructuring charges of \$4 million.

(E) In the second quarter of 2015 our Global Operations segment recorded \$6 million in inventory charges to right size the Brazil Truck business.

(F) In the first quarter of 2016, we received a \$15 million one-time fee from a third party which was recognized in Other income, net.

### Pension and Other Postretirement Benefits

Our pension plans are funded by contributions made from Company assets in accordance with applicable U.S. and Canadian government regulations. The regulatory funding requirements are computed using an actuarially determined funded status, which is determined using assumptions that often differ from assumptions used to measure the funded status for U.S. GAAP. U.S. funding targets are determined by rules promulgated under the Pension Protection Act of 2006 (the "PPA"). The PPA additionally requires underfunded plans to achieve 100% funding over a period of time. From time to time, we have discussions with and receive requests for certain information from the Pension Benefit Guaranty Corporation ("PBGC"). The PBGC was created by ERISA to encourage the continuation and maintenance of private-sector defined benefit pension plans, provide timely and uninterrupted payment of pension benefits, and keep pension insurance premiums at a minimum. In July 2012, the Moving Ahead for Progress in the 21<sup>st</sup> Century Act (the "MAP-21 Act") was signed into law, impacting the minimum funding requirements for pension plans, but not otherwise impacting our accounting for pension benefits. In August 2014, the Highway and Transportation Funding Act of 2014 ("HATFA"), which included an extension of pension funding interest rate relief, was signed into law. The Bi-Partisan Budget Act of 2015 was signed into law in November of 2015 and provided for further extension of interest rate relief. These legislative measures will reduce our funding requirements over the next five years. For the three and six months ended April 30, 2016, we contributed \$21 million and \$40 million, respectively, and for the three and six months ended April 30, 2015, we contributed \$32 million and \$62 million, respectively, to our U.S. and Canadian pension plans (the "Plans") to meet regulatory minimum funding requirements. We currently anticipate additional contributions of approximately \$57 million during the remainder of 2016. Future contributions are dependent upon a number of factors, principally the changes in values of plan assets, changes in interest rates, the impact of any future funding relief, and the impact of funding resulting from the closure of our Chatham, Ontario plant. We currently expect that from 2017 through 2019, we will be required to contribute \$100 million to \$200 million per year to the Plans, depending on asset performance and discount rates.

For more information, see Note 7, Postretirement Benefits, to the accompanying consolidated financial statements.

### Other Information

#### Impact of Environmental Regulation

Government regulation related to climate change is under consideration at the U.S. federal and state levels. Because our products use fossil fuels, they may be impacted indirectly due to regulation, such as a cap and trade program, affecting the cost of fuels. The EPA and the United States National Highway Traffic Safety Administration ("NHTSA") issued final rules for greenhouse gas ("GHG") emissions and fuel economy on September 15, 2011. These began to apply in calendar year 2014 and will be fully implemented in model year 2017. The agencies' stated goals for these rules were to increase the use of currently existing technologies. We are complying with these rules through use of existing technologies and implementation of emerging technologies as they become available. Several of our vehicles were certified early for the 2013 model year and the majority of our remaining vehicles and all engines were certified in 2014. The EPA and NHTSA issued a proposed rule on July 13, 2015 with the next phase of federal GHG emission and fuel economy regulations. This proposed rule contains more stringent emissions levels for engines and vehicles, adds regulation of trailers and is anticipated to take effect in model year 2021 and to be implemented in three stages culminating in model year 2027. The proposed rule is currently under discussion among the relevant agencies, manufacturers, including us, and other stakeholders. We filed comments on October 1, 2015. The EPA and NHTSA published a notice of data availability, requesting comment on additional information the agencies posted in the rulemaking docket. We filed comments on April 1, 2016. All of the comments are available in the rulemaking docket. The final rule is expected in calendar year 2016. Canada adopted its version of fuel economy and/or GHG emission regulations in February 2013. These regulations are substantially aligned with U.S. fuel economy and GHG emission regulations. Canada has announced it also is considering a heavy duty phase 2 greenhouse gas rulemaking aligned with EPA and NHTSA phase 2 rules. In December 2014, California adopted GHG emission rules for heavy duty vehicles equivalent to EPA rules and an optional lower emission standard for nitrogen oxide ("NOx") in California. California has stated its intention to lower NOx standards for California-certified engines and has requested that the EPA lower its standards. We expect that heavy duty vehicle and engine fuel economy and GHG emissions rules will be under consideration in other global jurisdictions in the future. These standards will impact development and production costs for vehicles and engines. There will also be administrative costs arising from the

implementation of the rules. EPA also issued a final rule in October 2015 that lowered the National Ambient Air Quality Standard for ozone to 70 parts per billion. This rule could lead to future lower emission standards for substances that contribute to ozone, including NOx from vehicles, at the federal and state levels. Our facilities may be subject to regulation related to climate change and climate change itself may also have some impact on our operations. However, these impacts are currently uncertain and we cannot predict the nature and scope of those impacts.

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### Critical Accounting Policies and Estimates

Our consolidated financial statements are prepared in accordance with U.S. GAAP. In connection with the preparation of our consolidated financial statements, we use estimates and make judgments and assumptions about future events that affect the reported amounts of assets, liabilities, revenue, expenses, and the related disclosures. Our assumptions, estimates, and judgments are based on historical experience, current trends, and other factors we believe are relevant at the time we prepare our consolidated financial statements.

Our significant accounting policies and critical accounting estimates are consistent with those discussed in Note 1, Summary of Significant Accounting Policies, to the consolidated financial statements and the MD&A section of our Annual Report on Form 10-K for the year ended October 31, 2015. During the six months ended April 30, 2016, there were no significant changes in our application of our critical accounting policies except for the addition of Inventories specifically related to the valuation on our used truck inventory as described below.

To aid in fully understanding and evaluating our reporting results, we have identified the following accounting policies as our most critical because they require us to make difficult, subjective, and complex judgments:

• Pension and Other Postretirement Benefits

• Allowance for Doubtful Accounts

• Income Taxes

• Impairment of Long-Lived Assets

• Contingency Accruals

• Inventories

**Inventories.** Inventories are valued at the lower of cost or market. Our gross used truck inventory increased to approximately \$448 million at April 30, 2016 from \$390 million at October 31, 2015, offset by reserves of \$168 million and \$110 million, respectively. The increase in used truck inventory is due, in part, to used truck receipts as a result of trades, repossessions and end of operating lease cycles exceeding used truck sales. As a result of these market dynamics, we expect it may take several years before our used truck inventory returns to the lower targeted levels. We continue to seek alternative channels to sell our used trucks, including certain export markets which have resulted in a lower price point as compared to our domestic channels.

In valuing our used truck inventory, we are required to make assumptions regarding the level of reserves required to value inventories at their net realizable value ("NRV"). Our judgments and estimates for used truck inventory are based on an analysis of current and forecasted sales prices, aging of and demand for used trucks, and the mix of sales through various market channels. The estimated NRV is subject to change based on numerous conditions taking into account age, specifications, mileage, timing of sales, market mix and current and forecasted pricing. While calculations are made involving these factors, significant management judgment regarding expectations for future events is involved. Future events that could significantly influence our judgment and related estimates include general economic conditions in markets where our products are sold, actions of our competitors, and the ability to sell used trucks in a timely manner.

#### Recently Issued and Adopted Accounting Standards

In the quarter ended April 30, 2016, we have not adopted any new accounting guidance that has had a material impact on our consolidated financial statements.

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers" (Topic 606), which supersedes the revenue recognition requirements in ASC 605, "Revenue Recognition." This ASU is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. In August 2015, the FASB issued ASU No. 2015-14, which postponed the effective date of ASU No. 2014-09 to fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017, with early adoption permitted on the original effective date of fiscal years beginning after December 15, 2016. Our effective date for this ASU is November 1, 2018. We are currently evaluating the method of adoption and the impact of this ASU on our consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases" (Topic 842). This ASU requires lessees to recognize, on the balance sheet, assets and liabilities for the rights and obligations created by leases of greater than twelve months. The accounting by lessors will remain largely unchanged. The ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, with early adoption permitted. Our effective date for this ASU is November 1, 2019. Adoption will require a modified retrospective transition. We are currently evaluating the method of adoption and the impact of this ASU on our consolidated financial statements.

#### Item 3. Quantitative and Qualitative Disclosures about Market Risk

See Item 7A, Quantitative and Qualitative Disclosures about Market Risk, of our Annual Report on Form 10-K for the year ended October 31, 2015. During the six months ended April 30, 2016, there have been no material changes in our exposure to market risk.

#### Item 4. Controls and Procedures

##### (a) Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC rules and forms, and that such information is accumulated and communicated to management, including our Chief Executive Officer and the Chief Financial Officer, to allow timely decisions regarding required disclosures.

As previously disclosed under "Item 9A-Controls and Procedures" in our Annual Report on Form 10-K for our fiscal year ended October 31, 2015, we concluded that our disclosure controls and procedures were not effective as of October 31, 2015 due to a material weakness in our internal control over financial reporting. Based on the material weakness, which we continue to remediate, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the quarter ended April 30, 2016, our disclosure controls and procedures were not effective. In light of the material weakness in internal control over financial reporting, prior to filing this Quarterly Report on Form 10-Q for the fiscal quarter ended April 30, 2016, we developed and completed substantive procedures that allowed us to conclude that the consolidated financial statements in this Quarterly Report on Form 10-Q fairly present, in all material respects, our financial position, results of operations, and cash flows for the periods presented in conformity with U.S. GAAP.

The material weakness in our internal control over financial reporting, which is described in our Annual Report on Form 10-K for the fiscal year ended October 31, 2015, and continued to exist as of April 30, 2016, is as follows:

- We did not have sufficient controls designed to validate the proper classification of warranty claims data, including type of warranty coverage and product/component, which is used to determine the warranty accrual and expense. This material weakness resulted in misstatements in our warranty accrual that were corrected prior to the issuance of our consolidated financial statements for the fiscal year ended October 31, 2015. The classification errors and resulting warranty accrual misstatements did not materially impact our consolidated financial statements, including our warranty cash outlays for claims. However, a reasonable

possibility exists that material misstatements in our consolidated financial statements will not be prevented or detected on a timely basis.

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#### Management's Remediation Initiatives

We continue to invest significant time and effort to address the material weakness related to validation and proper classification of warranty claims data used to determine the warranty accrual and expense. Specifically, the following actions were taken:

- Designed and implemented an automated process to validate proper classification of certain warranty claims data; and
- Increased our investment in training and job tools to improve the process and controls over the validation and proper classification of warranty claims data.

While progress has been made, there are additional controls that need to be designed and implemented and existing controls require enhancement to prevent or detect a material misstatement in our financial statements. Until full remediation is complete, we will continue to perform substantive procedures to ensure that, in all material respects, our financial statements are presented in conformity with U.S. GAAP.

#### (b) Changes in Internal Control over Financial Reporting

We are taking actions to remediate the material weakness related to our internal controls over financial reporting as described above. However, our remediation efforts were not complete as of April 30, 2016. Other than management's remediation initiatives disclosed above, there were no material changes in our internal control over financial reporting identified in connection with the evaluation required by Rules 13a-15 and 15d-15 under the Exchange Act that occurred during the quarter ended April 30, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II

### Item 1. Legal Proceedings

During the six months ended April 30, 2016, there have been no material developments from the legal proceedings disclosed in our Annual Report on Form 10-K for our fiscal year ended October 31, 2015, except as disclosed below:

#### EPA Clean Air Act Litigation

On May 13, 2016, the DOJ filed a motion for summary judgment on liability against Navistar International Corporation and Navistar, Inc. The Court set a ruling date of September 1, 2016 on the DOJ's motion.

#### Shareholder Litigation

On May 25, 2016, the Court entered an order preliminarily approving a settlement of the 10b-5 Cases, as well as the class notice to be sent in connection with the settlement. The Court scheduled the Final Approval Hearing for October 25, 2016.

#### IC Bus Civil RICO Litigation

On June 1, 2016, plaintiffs Polar Express School Bus and Lakeview Bus Lines filed a lawsuit against Navistar International Corporation, Navistar, Inc., and IC Bus, LLC in the U.S. District Court for the Northern District of Illinois. The lawsuit alleges that the forty (40) IC brand buses owned or operated by plaintiffs contain defective ABS braking systems and also engines with defective emissions control systems. Plaintiffs claim that NIC, its subsidiaries, and their authorized dealers deliberately concealed the alleged defects, and the lawsuit seeks to plead causes of action under the Racketeer Influenced and Corrupt Organizations Act (RICO) and common law fraud. Plaintiffs seek compensatory damages in the amount of \$6.7 million, treble damages, punitive damages in the amount of \$50 million, and attorneys' fees and costs. NIC, Navistar, Inc., and IC Bus dispute the allegations in the lawsuit.

### Item 1A. Risk Factors

During the six months ended April 30, 2016, there have been no material changes from the risk factors disclosed in our Annual Report on Form 10-K for our year ended October 31, 2015.

### Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

#### Recent Sales of Unregistered Securities

None.

#### Purchases of Equity Securities

None.

### Item 3. Defaults upon Senior Securities

None.

### Item 4. Mine Safety Disclosures

Not applicable.

### Item 5. Other Information

None.

## Item 6. Exhibits

| Exhibit:  | Description  | Page |
|-----------|--|------|
| (10)      | <u>Material Contracts</u>  | E-1  |
| (31.1)    | <u>CEO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u> | E-2  |
| (31.2)    | <u>CFO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u> | E-3  |
| (32.1)    | <u>CEO Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u> | E-4  |
| (32.2)    | <u>CFO Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u> | E-5  |
| (99.1)    | <u>Additional Financial Information (Unaudited)</u>                                | E-6  |
| (101.INS) | XBRL Instance Document   | N/A  |
| (101.SCH) | XBRL Taxonomy Extension Schema Document  | N/A  |
| (101.CAL) | XBRL Taxonomy Extension Calculation Linkbase Document                              | N/A  |
| (101.LAB) | XBRL Taxonomy Extension Label Linkbase Document                                    | N/A  |
| (101.PRE) | XBRL Taxonomy Extension Presentation Linkbase Document                             | N/A  |
| (101.DEF) | XBRL Taxonomy Extension Definition Linkbase Document                               | N/A  |

All exhibits other than those indicated above are omitted because of the absence of the conditions under which they are required or because the information called for is shown in the consolidated financial statements and notes thereto in the Quarterly Report on Form 10-Q for the period ended April 30, 2016.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NAVISTAR INTERNATIONAL CORPORATION

(Registrant)

/s/ SAMARA A. STRYCKER

Samara A. Strycker

Senior Vice President and Corporate Controller

(Principal Accounting Officer)

June 7, 2016