CATERPILLAR INC
Form 10-Q
August 01, 2014

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

FORM 10-Q
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2014
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: 1-768
CATERPILLAR INC.
(Exact name of registrant as specified in its charter)

Delaware	37-0602744
(State or other jurisdiction of incorporation)	(IRS Employer I.D. No.)
100 NE Adams Street, Peoria, Illinois	61629
(Address of principal executive offices)	(Zip Code)

Registrant’s telephone number, including area code:
(309) 675-1000

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, 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 x 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 definitions of “large accelerated filer”, “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x
At June 30, 2014, 627,846,602 shares of common stock of the registrant were outstanding.

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* Item omitted because no answer is called for or item is not applicable.

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Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

Caterpillar Inc.
Consolidated Statement of Results of Operations
(Unaudited)
(Dollars in millions except per share data)

	Three Months Ended June 30, 2014	2013
Sales and revenues:		
Sales of Machinery, Energy & Transportation	$13,391	$13,886
Revenues of Financial Products	759	735
Total sales and revenues	14,150	14,621
Operating costs:		
Cost of goods sold	10,197	10,773
Selling, general and administrative expenses	1,437	1,421
Research and development expenses	516	548
Interest expense of Financial Products	153	185
Other operating (income) expenses	372	137
Total operating costs	12,675	13,064
Operating profit	1,475	1,557
Interest expense excluding Financial Products	120	120
Other income (expense)	65	(84)
Consolidated profit before taxes	1,420	1,353
Provision (benefit) for income taxes	419	387
Profit of consolidated companies	1,001	966
Equity in profit (loss) of unconsolidated affiliated companies	1	(1)
Profit of consolidated and affiliated companies	1,002	965
Less: Profit (loss) attributable to noncontrolling interests	3	5
Profit [1]	$999	$960
Profit per common share	$1.60	$1.48
Profit per common share – diluted [2]	$1.57	$1.45
Weighted-average common shares outstanding (millions)		
– Basic	626.3	649.9

– Diluted[2]	638.3	662.7
Cash dividends declared per common share	$1.30	$1.12

[1] Profit attributable to common stockholders.
[2] Diluted by assumed exercise of stock-based compensation awards using the treasury stock method.

See accompanying notes to Consolidated Financial Statements.

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Caterpillar Inc.
Consolidated Statement of Comprehensive Income
(Unaudited)
(Dollars in millions)

	Three Months Ended June 30, 2014	2013
Profit of consolidated and affiliated companies	$1,002	$965
Other comprehensive income (loss), net of tax:		
Foreign currency translation, net of tax (provision)/benefit of: 2014 - $(8); 2013 - $29	28	(180)
Pension and other postretirement benefits:		
Current year actuarial gain (loss), net of tax (provision)/benefit of: 2014 - $(5); 2013 - $(6)	10	12
Amortization of actuarial (gain) loss, net of tax (provision)/benefit of: 2014 - $(44); 2013 - $(67)	86	130
Current year prior service credit (cost), net of tax (provision)/benefit of: 2014 - $0; 2013 - $0	1	—
Amortization of prior service (credit) cost, net of tax (provision)/benefit of: 2014 - $4; 2013 - $4	(6)	(9)
Derivative financial instruments:		
Gains (losses) deferred, net of tax (provision)/benefit of: 2014 - $6; 2013 - $(5)	(11)	7
(Gains) losses reclassified to earnings, net of tax (provision)/benefit of: 2014 - $3; 2013 - $(12)	(5)	22
Available-for-sale securities:		
Gains (losses) deferred, net of tax (provision)/benefit of: 2014 - $(8); 2013 - $6	15	(10)
(Gains) losses reclassified to earnings, net of tax (provision)/benefit of: 2014 - $0; 2013 - $0	—	1
Total other comprehensive income (loss), net of tax	118	(27)
Comprehensive income	1,120	938
Less: comprehensive income attributable to the noncontrolling interests	(3)	(7)
Comprehensive income attributable to stockholders	$1,117	$931

See accompanying notes to Consolidated Financial Statements.

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Caterpillar Inc.
Consolidated Statement of Results of Operations
(Unaudited)
(Dollars in millions except per share data)

	Six Months Ended June 30,	
	2014	2013
Sales and revenues:		
Sales of Machinery, Energy & Transportation	$25,884	$26,370
Revenues of Financial Products	1,507	1,461
Total sales and revenues	27,391	27,831
Operating costs:		
Cost of goods sold	19,634	20,412
Selling, general and administrative expenses	2,729	2,811
Research and development expenses	1,024	1,110
Interest expense of Financial Products	313	374
Other operating (income) expenses	818	349
Total operating costs	24,518	25,056
Operating profit	2,873	2,775
Interest expense excluding Financial Products	230	240
Other income (expense)	119	(55)
Consolidated profit before taxes	2,762	2,480
Provision (benefit) for income taxes	837	633
Profit of consolidated companies	1,925	1,847
Equity in profit (loss) of unconsolidated affiliated companies	2	—
Profit of consolidated and affiliated companies	1,927	1,847
Less: Profit (loss) attributable to noncontrolling interests	6	7
Profit [1]	$1,921	$1,840
Profit per common share	$3.06	$2.82
Profit per common share – diluted [2]	$3.00	$2.76
Weighted-average common shares outstanding (millions)		
– Basic	626.8	652.4
– Diluted [2]	639.3	666.6

Cash dividends declared per common share	$1.30	$1.12

[1] Profit attributable to common stockholders.
[2] Diluted by assumed exercise of stock-based compensation awards using the treasury stock method.

See accompanying notes to Consolidated Financial Statements.

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Caterpillar Inc.
Consolidated Statement of Comprehensive Income
(Unaudited)
(Dollars in millions)

	Six Months Ended June 30, 2014	2013
Profit of consolidated and affiliated companies	$1,927	$1,847
Other comprehensive income (loss), net of tax:		
Foreign currency translation, net of tax (provision)/benefit of: 2014 - $(8); 2013 - $8	67	(546)
Pension and other postretirement benefits:		
Current year actuarial gain (loss), net of tax (provision)/benefit of: 2014 - $(5); 2013 - $(16)	10	27
Amortization of actuarial (gain) loss, net of tax (provision)/benefit of: 2014 - $(88); 2013 - $(134)	172	259
Current year prior service credit (cost), net of tax (provision)/benefit of: 2014 - $0; 2013 - $0	1	—
Amortization of prior service (credit) cost, net of tax (provision)/benefit of: 2014 - $7; 2013 - $9	(12)	(18)
Amortization of transition (asset) obligation, net of tax (provision)/benefit of: 2014 - $0; 2013 - $0	—	1
Derivative financial instruments:		
Gains (losses) deferred, net of tax (provision)/benefit of: 2014 - $16; 2013 - $13	(27)	(24)
(Gains) losses reclassified to earnings, net of tax (provision)/benefit of: 2014 - $6; 2013 - $(19)	(10)	33
Available-for-sale securities:		
Gains (losses) deferred, net of tax (provision)/benefit of: 2014 - $(11); 2013 - $(2)	23	5
(Gains) losses reclassified to earnings, net of tax (provision)/benefit of: 2014 - $4; 2013 - $0	(10)	—
Total other comprehensive income (loss), net of tax	214	(263)
Comprehensive income	2,141	1,584
Less: comprehensive income attributable to the noncontrolling interests	(5)	(9)
Comprehensive income attributable to stockholders	$2,136	$1,575

See accompanying notes to Consolidated Financial Statements.

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Caterpillar Inc.
Consolidated Statement of Financial Position
(Unaudited)
(Dollars in millions)

	June 30, 2014	December 31, 2013
Assets		
Current assets:		
Cash and short-term investments	$7,927	$6,081
Receivables – trade and other	8,057	8,413
Receivables – finance	9,467	8,763
Deferred and refundable income taxes	1,463	1,553
Prepaid expenses and other current assets	1,307	900
Inventories	13,055	12,625
Total current assets	41,276	38,335
Property, plant and equipment – net	16,690	17,075
Long-term receivables – trade and other	1,548	1,397
Long-term receivables – finance	15,118	14,926
Investments in unconsolidated affiliated companies	259	272
Noncurrent deferred and refundable income taxes	737	594
Intangible assets	3,398	3,596
Goodwill	6,969	6,956
Other assets	1,832	1,745
Total assets	$87,827	$84,896
Liabilities		
Current liabilities:		
Short-term borrowings:		
Machinery, Energy & Transportation	$20	$16
Financial Products	5,534	3,663
Accounts payable	6,860	6,560
Accrued expenses	3,473	3,493
Accrued wages, salaries and employee benefits	1,910	1,622
Customer advances	2,344	2,360
Dividends payable	439	382
Other current liabilities	1,779	1,849
Long-term debt due within one year:		
Machinery, Energy & Transportation	509	760
Financial Products	6,873	6,592
Total current liabilities	29,741	27,297
Long-term debt due after one year:		
Machinery, Energy & Transportation	9,495	7,999
Financial Products	17,812	18,720
Liability for postemployment benefits	6,597	6,973
Other liabilities	3,259	3,029
Total liabilities	66,904	64,018
Commitments and contingencies (Notes 10 and 13)		

Stockholders’ equity		
Common stock of $1.00 par value:		
Authorized shares: 2,000,000,000 Issued shares: (6/30/14 and 12/31/13 – 814,894,624) at paid-in amount	4,890	4,709
Treasury stock (6/30/14 – 187,048,022 shares; 12/31/13 – 177,072,282 shares) at cost	(13,312)	(11,854)
Profit employed in the business	32,961	31,854
Accumulated other comprehensive income (loss)	(3,683)	(3,898)
Noncontrolling interests	67	67
Total stockholders’ equity	20,923	20,878
Total liabilities and stockholders’ equity	$87,827	$84,896

See accompanying notes to Consolidated Financial Statements.

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Caterpillar Inc.
Consolidated Statement of Changes in Stockholders' Equity
(Unaudited)
(Dollars in millions)

	Common stock	Treasury stock	Profit employed in the business	Accumulated other comprehensive income (loss)	Noncontrolling interests	Total
Six Months Ended June 30, 2013						
Balance at December 31, 2012	$4,481	$(10,074)	$29,558	$(6,433)	$50	$17,582
Profit of consolidated and affiliated companies	—	—	1,840	—	7	1,847
Foreign currency translation, net of tax	—	—	—	(548)	2	(546)
Pension and other postretirement benefits, net of tax	—	—	—	269	—	269
Derivative financial instruments, net of tax	—	—	—	9	—	9
Available-for-sale securities, net of tax	—	—	—	5	—	5
Change in ownership from noncontrolling interests	(6)	—	—	—	6	—
Dividends declared	—	—	(730)	—	—	(730)
Distribution to noncontrolling interests	—	—	—	—	(8)	(8)
Common shares issued from treasury stock for stock-based compensation: 4,108,681	(78)	134	—	—	—	56
Stock-based compensation expense	132	—	—	—	—	132
Net excess tax benefits from stock-based compensation	62	—	—	—	—	62
Common shares repurchased: 11,542,106 [1]	—	(1,000)	—	—	—	(1,000)
Balance at June 30, 2013	$4,591	$(10,940)	$30,668	$(6,698)	$57	$17,678
Six Months Ended June 30, 2014						
Balance at December 31, 2013	$4,709	$(11,854)	$31,854	$(3,898)	$67	$20,878
Profit of consolidated and affiliated companies	—	—	1,921	—	6	1,927
Foreign currency translation, net of tax	—	—	—	68	(1)	67
Pension and other postretirement benefits, net of tax	—	—	—	171	—	171
Derivative financial instruments, net of tax	—	—	—	(37)	—	(37)
Available-for-sale securities, net of tax	—	—	—	13	—	13
Change in ownership from noncontrolling interests	—	—	—	—	2	2
Dividends declared	—	—	(814)	—	—	(814)
Distribution to noncontrolling interests	—	—	—	—	(7)	(7)
Common shares issued from treasury stock for stock-based compensation: 8,134,995	(86)	280	—	—	—	194
Stock-based compensation expense	137	—	—	—	—	137
Net excess tax benefits from stock-based compensation	130	—	—	—	—	130
Common shares repurchased: 18,110,735 [1]	—	(1,738)	—	—	—	(1,738)

Balance at June 30, 2014	$4,890	$(13,312)	$32,961	$(3,683)	$ 67	$20,923

[1] See Note 11 regarding shares repurchased.

See accompanying notes to Consolidated Financial Statements.

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Caterpillar Inc.
Consolidated Statement of Cash Flow
(Unaudited)
(Millions of dollars)

	Six Months Ended June 30, 2014	2013
Cash flow from operating activities:		
Profit of consolidated and affiliated companies	$1,927	$1,847
Adjustments for non-cash items:		
Depreciation and amortization	1,570	1,484
Other	240	236
Changes in assets and liabilities, net of acquisitions and divestitures:		
Receivables – trade and other	138	231
Inventories	(439)	1,364
Accounts payable	551	305
Accrued expenses	7	(129)
Accrued wages, salaries and employee benefits	283	(580)
Customer advances	(14)	(95)
Other assets – net	(105)	(100)
Other liabilities – net	(24)	30
Net cash provided by (used for) operating activities	4,134	4,593
Cash flow from investing activities:		
Capital expenditures – excluding equipment leased to others	(710)	(1,387)
Expenditures for equipment leased to others	(825)	(810)
Proceeds from disposals of leased assets and property, plant and equipment	442	358
Additions to finance receivables	(5,760)	(5,544)
Collections of finance receivables	4,719	4,548
Proceeds from sale of finance receivables	104	89
Investments and acquisitions (net of cash acquired)	(15)	(26)
Proceeds from sale of businesses and investments (net of cash sold)	139	100
Proceeds from sale of securities	222	207
Investments in securities	(673)	(267)
Other – net	(25)	(68)
Net cash provided by (used for) investing activities	(2,382)	(2,800)
Cash flow from financing activities:		
Dividends paid	(757)	(342)
Distribution to noncontrolling interests	(7)	(8)
Contribution from noncontrolling interests	2	—
Common stock issued, including treasury shares reissued	194	56
Treasury shares purchased	(1,738)	(1,000)
Excess tax benefit from stock-based compensation	131	62
Proceeds from debt issued (original maturities greater than three months):		
Machinery, Energy & Transportation	1,990	119
Financial Products	4,961	5,067
Payments on debt (original maturities greater than three months):		

Machinery, Energy & Transportation	(770)	(1,003)
Financial Products	(5,574)	(5,300)
Short-term borrowings – net (original maturities three months or less)	1,749	1,217
Net cash provided by (used for) financing activities	181	(1,132)
Effect of exchange rate changes on cash	(87)	(41)
Increase (decrease) in cash and short-term investments	1,846	620
Cash and short-term investments at beginning of period	6,081	5,490
Cash and short-term investments at end of period	$7,927	$6,110

All short-term investments, which consist primarily of highly liquid investments with original maturities of three months or less, are considered to be cash equivalents.

See accompanying notes to Consolidated Financial Statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1.A. Basis of Presentation

In the opinion of management, the accompanying financial statements include all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of (a) the consolidated results of operations for the three and six month periods ended June 30, 2014 and 2013, (b) the consolidated comprehensive income for the three and six month periods ended June 30, 2014 and 2013, (c) the consolidated financial position at June 30, 2014 and December 31, 2013, (d) the consolidated changes in stockholders' equity for the six month periods ended June 30, 2014 and 2013, and (e) the consolidated cash flow for the six month periods ended June 30, 2014 and 2013. The financial statements have been prepared in conformity with generally accepted accounting principles in the United States of America (U.S. GAAP) and pursuant to the rules and regulations of the Securities and Exchange Commission. Certain amounts for prior periods have been reclassified to conform to the current period financial statement presentation.

We have revised previously reported amounts on the Consolidated Statement of Cash Flow for the six months ended June 30, 2013 to correct for customer advances invoiced but not yet paid and to correct for certain non-cash transactions impacting Receivables - trade and other and Accounts payable. Although these revisions did not impact Net cash provided by operating activities, cash provided by Receivables - trade and other decreased by $200 million, cash provided by Accounts payable increased by $83 million and cash used for Customer advances decreased by $117 million from the amounts previously reported for the six month period ended June 30, 2013. Management has concluded that the impact was not material to any period presented.

Interim results are not necessarily indicative of results for a full year. The information included in this Form 10-Q should be read in conjunction with the audited financial statements and notes thereto included in our Company's annual report on Form 10-K for the year ended December 31, 2013 (2013 Form 10-K).

The December 31, 2013 financial position data included herein is derived from the audited consolidated financial statements included in the 2013 Form 10-K but does not include all disclosures required by U.S. GAAP.

B. Nature of Operations

Information in our financial statements and related commentary are presented in the following categories:

Machinery, Energy & Transportation – Represents the aggregate total of Construction Industries, Resource Industries, Energy & Transportation, and All Other operating segments and related corporate items and eliminations.

Financial Products – Primarily includes the company's Financial Products Segment. This category includes Caterpillar Financial Services Corporation (Cat Financial), Caterpillar Financial Insurance Services (Insurance Services) and their respective subsidiaries.

2. New Accounting Guidance

Joint and several liability arrangements – In February 2013, the Financial Accounting Standards Board (FASB) issued accounting guidance on the recognition, measurement and disclosure of obligations resulting from joint and several liability arrangements. The guidance requires an entity to measure obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of this guidance is fixed at the reporting date, as the sum of the amount the reporting entity agreed to pay on the basis of its arrangement among its co-obligors and any additional amount the reporting entity expects to pay on behalf of its co-obligors. The entity is also required to disclose the nature and amount of the obligation as well as any other information about those obligations. This guidance was effective January 1, 2014, with retrospective application required. The guidance did not have a material impact on our financial statements.

Parent's accounting for the cumulative translation adjustment upon derecognition of certain subsidiaries or groups of assets within a foreign entity or of an investment in a foreign entity – In March 2013, the FASB issued accounting guidance on the parent's accounting for the cumulative translation adjustment (CTA) upon derecognition of certain subsidiaries or groups of assets within a foreign entity or of an investment in a foreign entity. The new standard clarifies existing guidance regarding when the CTA should be released into earnings upon various deconsolidation and consolidation

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transactions. This guidance was effective January 1, 2014. The guidance did not have a material impact on our financial statements.

Presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists – In July 2013, the FASB issued accounting guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. The guidance requires an unrecognized tax benefit, or a portion of an unrecognized tax benefit, to be presented as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward in the financial statements if available under the applicable tax jurisdiction. The guidance was effective January 1, 2014. The guidance did not have a material impact on our financial statements.

Reporting discontinued operations and disclosures of disposals of components of an entity – In April 2014, the FASB issued accounting guidance for determining which disposals can be presented as discontinued operations and modifies related disclosure requirements. The guidance defines a discontinued operation as a disposal of a component or group of components that is disposed of or is classified as held for sale and represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results. This guidance is effective January 1, 2015. We do not expect the adoption to have a material impact on our financial statements.

Revenue recognition – In May 2014, the FASB issued new revenue recognition guidance to provide a single, comprehensive revenue recognition model for all contracts with customers. Under the new guidance, an entity will recognize revenue to depict the transfer of promised goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. A five step model has been introduced for an entity to apply when recognizing revenue. The new guidance also includes enhanced disclosure requirements, and is effective January 1, 2017. Entities have the option to apply the new guidance under a retrospective approach to each prior reporting period presented, or a modified retrospective approach with the cumulative effect of initially applying the new guidance recognized at the date of initial application within the Consolidated Statement of Changes in Stockholders' Equity. We are in the process of evaluating the application and implementation of the new guidance.

3. Stock-Based Compensation

Accounting for stock-based compensation requires that the cost resulting from all stock-based payments be recognized in the financial statements based on the grant date fair value of the award. Stock-based compensation primarily consists of stock options, restricted stock units (RSUs) and stock-settled stock appreciation rights (SARs). We recognized pretax stock-based compensation cost in the amount of $84 million and $137 million for the three and six months ended June 30, 2014, respectively; and $83 million and $132 million for the three and six months ended and June 30, 2013, respectively.

The following table illustrates the type and fair value of the stock-based compensation awards granted during the six month periods ended June 30, 2014 and 2013, respectively:

	2014		2013	
	Shares Granted	Fair Value Per Award	Shares Granted	Fair Value Per Award
Stock options	4,448,218	$29.52	4,276,060	$28.34
RSUs	1,429,512	$89.18	1,614,870	$84.05

The stock price on the date of grant was $96.31 and $89.75 for 2014 and 2013, respectively.

The following table provides the assumptions used in determining the fair value of the stock-based awards for the six month periods ended June 30, 2014 and 2013, respectively:

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	Grant Year	
	2014	2013
Weighted-average dividend yield	2.15%	2.13%
Weighted-average volatility	28.2%	30.6%
Range of volatilities	18.4-36.2%	23.4-40.6%
Range of risk-free interest rates	0.12-2.60%	0.16-1.88%
Weighted-average expected lives	8 years	8 years

As of June 30, 2014, the total remaining unrecognized compensation cost related to nonvested stock-based compensation awards was $308 million, which will be amortized over the weighted-average remaining requisite service periods of approximately 2.1 years.

4. Derivative Financial Instruments and Risk Management

Our earnings and cash flow are subject to fluctuations due to changes in foreign currency exchange rates, interest rates and commodity prices. Our Risk Management Policy (policy) allows for the use of derivative financial instruments to prudently manage foreign currency exchange rate, interest rate and commodity price exposures. Our policy specifies that derivatives are not to be used for speculative purposes. Derivatives that we use are primarily foreign currency forward, option, and cross currency contracts, interest rate swaps, and commodity forward and option contracts. Our derivative activities are subject to the management, direction and control of our senior financial officers. Risk management practices, including the use of financial derivative instruments, are presented to the Audit Committee of the Board of Directors at least annually.

All derivatives are recognized on the Consolidated Statement of Financial Position at their fair value. On the date the derivative contract is entered into, we designate the derivative as (1) a hedge of the fair value of a recognized asset or liability (fair value hedge), (2) a hedge of a forecasted transaction or the variability of cash flow to be paid (cash flow hedge), or (3) an undesignated instrument. Changes in the fair value of a derivative that is qualified, designated and highly effective as a fair value hedge, along with the gain or loss on the hedged recognized asset or liability that is attributable to the hedged risk, are recorded in current earnings. Changes in the fair value of a derivative that is qualified, designated and highly effective as a cash flow hedge are recorded in Accumulated other comprehensive income (loss) (AOCI), to the extent effective, on the Consolidated Statement of Financial Position until they are reclassified to earnings in the same period or periods during which the hedged transaction affects earnings. Changes in the fair value of undesignated derivative instruments and the ineffective portion of designated derivative instruments are reported in current earnings. Cash flow from designated derivative financial instruments are classified within the same category as the item being hedged on the Consolidated Statement of Cash Flow. Cash flow from undesignated derivative financial instruments are included in the investing category on the Consolidated Statement of Cash Flow.

We formally document all relationships between hedging instruments and hedged items, as well as the risk-management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives that are designated as fair value hedges to specific assets and liabilities on the Consolidated Statement of Financial Position and linking cash flow hedges to specific forecasted transactions or variability of cash flow.

We also formally assess, both at the hedge’s inception and on an ongoing basis, whether the designated derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flow of hedged items. When a derivative is determined not to be highly effective as a hedge or the underlying hedged transaction is no longer probable, we discontinue hedge accounting prospectively, in accordance with the derecognition criteria for hedge accounting.

Foreign Currency Exchange Rate Risk

Foreign currency exchange rate movements create a degree of risk by affecting the U.S. dollar value of sales made and costs incurred in foreign currencies. Movements in foreign currency rates also affect our competitive position as these changes may affect business practices and/or pricing strategies of non-U.S.-based competitors. Additionally, we have balance sheet positions denominated in foreign currencies, thereby creating exposure to movements in exchange rates.

Our Machinery, Energy & Transportation operations purchase, manufacture and sell products in many locations around the world. As we have a diversified revenue and cost base, we manage our future foreign currency cash flow exposure on a net basis. We use foreign currency forward and option contracts to manage unmatched foreign currency cash inflow

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and outflow. Our objective is to minimize the risk of exchange rate movements that would reduce the U.S. dollar value of our foreign currency cash flow. Our policy allows for managing anticipated foreign currency cash flow for up to five years.

We generally designate as cash flow hedges at inception of the contract any Australian dollar, Brazilian real, British pound, Canadian dollar, Chinese yuan, euro, Indian rupee, Japanese yen, Mexican peso, Singapore dollar or Swiss franc forward or option contracts that meet the requirements for hedge accounting and the maturity extends beyond the current quarter-end. Designation is performed on a specific exposure basis to support hedge accounting. The remainder of Machinery, Energy & Transportation foreign currency contracts are undesignated, including any hedges designed to protect our competitive exposure.

As of June 30, 2014, $13 million of deferred net gains, net of tax, included in equity (AOCI in the Consolidated Statement of Financial Position), are expected to be reclassified to current earnings (Other income (expense) in the Consolidated Statement of Results of Operations) over the next twelve months when earnings are affected by the hedged transactions. The actual amount recorded in Other income (expense) will vary based on exchange rates at the time the hedged transactions impact earnings.

In managing foreign currency risk for our Financial Products operations, our objective is to minimize earnings volatility resulting from conversion and the remeasurement of net foreign currency balance sheet positions, and future transactions denominated in foreign currencies. Our policy allows the use of foreign currency forward, option and cross currency contracts to offset the risk of currency mismatch between our receivables and debt, and exchange rate risk associated with future transactions denominated in foreign currencies. Substantially all such foreign currency forward, option and cross currency contracts are undesignated.

Interest Rate Risk

Interest rate movements create a degree of risk by affecting the amount of our interest payments and the value of our fixed-rate debt. Our practice is to use interest rate derivatives to manage our exposure to interest rate changes and, in some cases, lower the cost of borrowed funds.

Our Machinery, Energy & Transportation operations generally use fixed-rate debt as a source of funding. Our objective is to minimize the cost of borrowed funds. Our policy allows us to enter into fixed-to-floating interest rate swaps and forward rate agreements to meet that objective. We designate fixed-to-floating interest rate swaps as fair value hedges at inception of the contract, and we designate certain forward rate agreements as cash flow hedges at inception of the contract.

As of June 30, 2014, $4 million of deferred net losses, net of tax, included in equity (AOCI in the Consolidated Statement of Financial Position), related to Machinery, Energy & Transportation forward rate agreements, are expected to be reclassified to current earnings (Interest expense excluding Financial Products in the Consolidated Statement of Results of Operations) over the next twelve months.

Financial Products operations has a match-funding policy that addresses interest rate risk by aligning the interest rate profile (fixed or floating rate) of Cat Financial's debt portfolio with the interest rate profile of their receivables portfolio within predetermined ranges on an ongoing basis. In connection with that policy, we use interest rate derivative instruments to modify the debt structure to match assets within the receivables portfolio. This matched funding reduces the volatility of margins between interest-bearing assets and interest-bearing liabilities, regardless of which direction interest rates move.

Our policy allows us to use fixed-to-floating, floating-to-fixed, and floating-to-floating interest rate swaps to meet the match-funding objective. We designate fixed-to-floating interest rate swaps as fair value hedges to protect debt against changes in fair value due to changes in the benchmark interest rate. We designate most floating-to-fixed interest rate swaps as cash flow hedges to protect against the variability of cash flows due to changes in the benchmark interest rate.

As of June 30, 2014, $4 million of deferred net losses, net of tax, included in equity (AOCI in the Consolidated Statement of Financial Position), related to Financial Products floating-to-fixed interest rate swaps, are expected to be reclassified to current earnings (Interest expense of Financial Products in the Consolidated Statement of Results of Operations) over the next twelve months. The actual amount recorded in Interest expense of Financial Products will vary based on interest rates at the time the hedged transactions impact earnings.

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We have, at certain times, liquidated fixed-to-floating and floating-to-fixed interest rate swaps at both Machinery, Energy & Transportation and Financial Products. The gains or losses associated with these swaps at the time of liquidation are amortized into earnings over the original term of the previously designated hedged item.

Commodity Price Risk

Commodity price movements create a degree of risk by affecting the price we must pay for certain raw material. Our policy is to use commodity forward and option contracts to manage the commodity risk and reduce the cost of purchased materials.

Our Machinery, Energy & Transportation operations purchase base and precious metals embedded in the components we purchase from suppliers. Our suppliers pass on to us price changes in the commodity portion of the component cost. In addition, we are subject to price changes on energy products such as natural gas and diesel fuel purchased for operational use.

Our objective is to minimize volatility in the price of these commodities. Our policy allows us to enter into commodity forward and option contracts to lock in the purchase price of a portion of these commodities within a five-year horizon. All such commodity forward and option contracts are undesignated.

The location and fair value of derivative instruments reported in the Consolidated Statement of Financial Position are as follows:

(Millions of dollars)

	Consolidated Statement of Financial Position Location	Asset (Liability) Fair Value June 30, 2014	December 31, 2013
Designated derivatives			
Foreign exchange contracts			
Machinery, Energy & Transportation	Receivables – trade and other	$34	$54
Machinery, Energy & Transportation	Accrued expenses	(14)	(39)
Interest rate contracts			
Financial Products	Receivables – trade and other	17	7
Financial Products	Long-term receivables – trade and other	84	115
Financial Products	Accrued expenses	(8)	(6)
		$113	$131
Undesignated derivatives			
Foreign exchange contracts			
Machinery, Energy & Transportation	Receivables – trade and other	$6	$19
Machinery, Energy & Transportation	Accrued expenses	(4)	(1)
Financial Products	Receivables – trade and other	4	7
Financial Products	Long-term receivables – trade and other	5	9
Financial Products	Accrued expenses	(5)	(4)
Commodity contracts			
Machinery, Energy & Transportation	Receivables – trade and other	3	—
		$9	$30

The total notional amounts of the derivative instruments are as follows:

(Millions of dollars)

	June 30, 2014	December 31, 2013
Machinery, Energy & Transportation	$2,767	$3,565
Financial Products	$5,974	$6,743

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The notional amounts of the derivative financial instruments do not represent amounts exchanged by the parties. The amounts exchanged by the parties are calculated by reference to the notional amounts and by other terms of the derivatives, such as foreign currency exchange rates, interest rates, or commodity prices.

The effect of derivatives designated as hedging instruments on the Consolidated Statement of Results of Operations is as follows:

Fair Value Hedges
(Millions of dollars)

		Three Months Ended June 30, 2014		Three Months Ended June 30, 2013	
	Classification	Gains (Losses) on Derivatives	Gains (Losses) on Borrowings	Gains (Losses) on Derivatives	Gains (Losses) on Borrowings
Interest rate contracts					
Financial Products	Other income (expense)	$(6)	$8	$(49)	$50
		$(6)	$8	$(49)	$50

		Six Months Ended June 30, 2014		Six Months Ended June 30, 2013	
	Classification	Gains (Losses) on Derivatives	Gains (Losses) on Borrowings	Gains (Losses) on Derivatives	Gains (Losses) on Borrowings
Interest rate contracts					
Financial Products	Other income (expense)	$(19)	$23	$(78)	$80
		$(19)	$23	$(78)	$80

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Cash Flow Hedges
(Millions of dollars)

	Three Months Ended June 30, 2014			
		Recognized in Earnings		
	Amount of Gains (Losses) Recognized in AOCI (Effective Portion)	Classification of Gains (Losses)	Amount of Gains (Losses) Reclassified from AOCI to Earnings	Recognized in Earnings (Ineffective Portion)
Foreign exchange contracts				
Machinery, Energy & Transportation	$12	Other income (expense)	$10	$—
Interest rate contracts				
Machinery, Energy & Transportation	(26)	Interest expense excluding Financial Products	(1)	—
Financial Products	(3)	Interest expense of Financial Products	(1)	—
	$(17)		$8	$—

	Three Months Ended June 30, 2013			
		Recognized in Earnings		
	Amount of Gains (Losses) Recognized in AOCI (Effective Portion)	Classification of Gains (Losses)	Amount of Gains (Losses) Reclassified from AOCI to Earnings	Recognized in Earnings (Ineffective Portion)
Foreign exchange contracts				
Machinery, Energy & Transportation	$9	Other income (expense)	$(31)	$—
Interest rate contracts				
Machinery, Energy & Transportation	—	Other income (expense)	(1)	—
Financial Products	3	Interest expense of Financial Products	(2)	—
	$12		$(34)	$—

	Six Months Ended June 30, 2014			
		Recognized in Earnings		
	Amount of Gains (Losses) Recognized in AOCI (Effective Portion)	Classification of Gains (Losses)	Amount of Gains (Losses) Reclassified from AOCI to Earnings	Recognized in Earnings (Ineffective Portion)
Foreign exchange contracts				
Machinery, Energy & Transportation	$25	Other income (expense)	$20	$—

Interest rate contracts				
Machinery, Energy & Transportation	(63)	Interest expense excluding Financial Products	(2)	—
Financial Products	(5)	Interest expense of Financial Products	(2)	—
	$(43)		$16	$—

	Six Months Ended June 30, 2013			
		Recognized in Earnings		
	Amount of Gains (Losses) Recognized in AOCI (Effective Portion)	Classification of Gains (Losses)	Amount of Gains (Losses) Reclassified from AOCI to Earnings	Recognized in Earnings (Ineffective Portion)
Foreign exchange contracts				
Machinery, Energy & Transportation	$(40)	Other income (expense)	$(48) [1]	$—
Interest rate contracts				
Machinery, Energy & Transportation	—	Other income (expense)	(1)	—
Financial Products	3	Interest expense of Financial Products	(3)	—
	$(37)		$(52)	$—

[1] Includes $3 million loss reclassified from AOCI to Other income (expense) in 2013 as certain derivatives were dedesignated as the related transactions are no longer probable to occur.

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The effect of derivatives not designated as hedging instruments on the Consolidated Statement of Results of Operations is as follows:

(Millions of dollars)

	Classification of Gains (Losses)	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013
Foreign exchange contracts			
Machinery, Energy & Transportation	Other income (expense)	$(2)	$12
Financial Products	Other income (expense)	(12)	16
Commodity contracts			
Machinery, Energy & Transportation	Other income (expense)	4	(3)
		$(10)	$25

	Classification of Gains (Losses)	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Foreign exchange contracts			
Machinery, Energy & Transportation	Other income (expense)	$9	$(8)
Financial Products	Other income (expense)	(17)	1
Commodity contracts			
Machinery, Energy & Transportation	Other income (expense)	3	(4)
		$(5)	$(11)

We enter into International Swaps and Derivatives Association (ISDA) master netting agreements within Machinery, Energy & Transportation and Financial Products that permit the net settlement of amounts owed under their respective derivative contracts. Under these master netting agreements, net settlement generally permits the company or the counterparty to determine the net amount payable for contracts due on the same date and in the same currency for similar types of derivative transactions. The master netting agreements generally also provide for net settlement of all outstanding contracts with a counterparty in the case of an event of default or a termination event.

Collateral is generally not required of the counterparties or of our company under the master netting agreements. As of June 30, 2014 and December 31, 2013, no cash collateral was received or pledged under the master netting agreements.

The effect of the net settlement provisions of the master netting agreements on our derivative balances upon an event of default or termination event is as follows:

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June 30, 2014				Gross Amounts Not Offset in the Statement of Financial Position		
(Millions of dollars)	Gross Amount of Recognized Assets	Gross Amounts Offset in the Statement of Financial Position	Net Amount of Assets Presented in the Statement of Financial Position	Financial Instruments	Cash Collateral Received	Net Amount of Assets
Derivatives						
Machinery, Energy & Transportation	$43	$—	$43	$(18)	$—	$25
Financial Products	110	—	110	(8)	—	102
Total	$153	$—	$153	$(26)	$—	$127

June 30, 2014				Gross Amounts Not Offset in the Statement of Financial Position		
(Millions of dollars)	Gross Amount of Recognized Liabilities	Gross Amounts Offset in the Statement of Financial Position	Net Amount of Liabilities Presented in the Statement of Financial Position	Financial Instruments	Cash Collateral Pledged	Net Amount of Liabilities
Derivatives						
Machinery, Energy & Transportation	$(18)	$—	$(18)	$18	$—	$—
Financial Products	(13)	—	(13)	8	—	(5)
Total	$(31)	$—	$(31)	$26	$—	$(5)

December 31, 2013				Gross Amounts Not Offset in the Statement of Financial Position		
(Millions of dollars)	Gross Amount of Recognized Assets	Gross Amounts Offset in the Statement of Financial Position	Net Amount of Assets Presented in the Statement of Financial Position	Financial Instruments	Cash Collateral Received	Net Amount of Assets
Derivatives						
Machinery, Energy & Transportation	$73	$—	$73	$(32)	$—	$41
Financial Products	138	—	138	(9)	—	129
Total	$211	$—	$211	$(41)	$—	$170

December 31, 2013				Gross Amounts Not Offset in the Statement of Financial Position		
(Millions of dollars)	Gross Amount of Recognized Liabilities	Gross Amounts Offset in the Statement of Financial	Net Amount of Liabilities Presented in the Statement of	Financial Instruments	Cash Collateral Pledged	Net Amount of Liabilities

		Position	Financial Position			
Derivatives						
Machinery, Energy & Transportation	$(40)	$—	$(40)	$32	$—	$(8)
Financial Products	(10)	—	(10)	9	—	(1)
Total	$(50)	$—	$(50)	$41	$—	$(9)

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5. Inventories

Inventories (principally using the last-in, first-out (LIFO) method) are comprised of the following:

(Millions of dollars)	June 30, 2014	December 31, 2013
Raw materials	$3,115	$2,966
Work-in-process	2,915	2,589
Finished goods	6,734	6,785
Supplies	291	285
Total inventories	$13,055	$12,625

6. Investments in Unconsolidated Affiliated Companies

Combined financial information of the unconsolidated affiliated companies accounted for by the equity method (generally on a lag of 3 months or less) was as follows:

Results of Operations of unconsolidated affiliated companies: (Millions of dollars)	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Sales	$410	$309	$800	$567
Cost of sales	316	233	617	438
Gross profit	$94	$76	$183	$129
Profit (loss)	$4	$(22)	$(10)	$(25)

Financial Position of unconsolidated affiliated companies: (Millions of dollars)	June 30, 2014	December 31, 2013
Assets:		
Current assets	$703	$683
Property, plant and equipment – net	665	710
Other assets	576	608
	1,944	2,001
Liabilities:		
Current liabilities	469	437
Long-term debt due after one year	897	900
Other liabilities	219	262
	1,585	1,599
Equity	$359	$402

Caterpillar's investments in unconsolidated affiliated companies: (Millions of dollars)	June 30, 2014	December 31, 2013
Investments in equity method companies	$249	$262
Plus: Investments in cost method companies	10	10
Total investments in unconsolidated affiliated companies	$259	$272

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7. Intangible Assets and Goodwill

A. Intangible assets

Intangible assets are comprised of the following:

		June 30, 2014			
(Millions of dollars)	Weighted Amortizable Life (Years)	Gross Carrying Amount	Accumulated Amortization		Net
Customer relationships	15	$2,615	$(613	)	$2,002
Intellectual property	11	1,769	(517	)	1,252
Other	11	242	(116	)	126
Total finite-lived intangible assets	14	4,626	(1,246	)	3,380
Indefinite-lived intangible assets - In-process research & development		18	—		18
Total intangible assets		$4,644	$(1,246	)	$3,398

		December 31, 2013			
	Weighted Amortizable Life (Years)	Gross Carrying Amount	Accumulated Amortization		Net
Customer relationships	15	$2,653	$(539	)	$2,114
Intellectual property	11	1,821	(495	)	1,326
Other	10	274	(136	)	138
Total finite-lived intangible assets	13	4,748	(1,170	)	3,578
Indefinite-lived intangible assets - In-process research & development		18	—		18
Total intangible assets		$4,766	$(1,170	)	$3,596

Gross customer relationship intangibles of $24 million and related accumulated amortization of $5 million were reclassified from Intangible assets to assets held for sale and/or divested during 2014, and are not included in the June 30, 2014 balances in the table above. These transactions were related to the divestiture of portions of the Bucyrus distribution business. See Note 19 for additional information on divestitures and assets held for sale.

Amortization expense for the three and six months ended June 30, 2014 was $93 million and $185 million, respectively. Amortization expense for the three and six months ended June 30, 2013 was $91 million and $185 million, respectively. Amortization expense related to intangible assets is expected to be:
(Millions of dollars)

2014	2015	2016	2017	2018	Thereafter
$364	$356	$334	$332	$328	$1,869

B. Goodwill

We test goodwill for impairment annually and whenever events or circumstances make it more likely than not that an impairment may have occurred. We perform our annual goodwill impairment test as of October 1 and monitor for interim triggering events on an ongoing basis. Goodwill is reviewed for impairment utilizing a qualitative assessment or a two-step process. We have an option to make a qualitative assessment of a reporting unit's goodwill for impairment. If we choose to perform a qualitative assessment and determine the fair value more likely than not exceeds the carrying value, no further evaluation is necessary. For reporting units where we perform the two-step process, the first step requires us to compare the fair value of each reporting unit, which we primarily determine using an income approach based on the present value of discounted cash flows, to the respective carrying value, which includes goodwill. If the fair value of the reporting unit exceeds its carrying value, the goodwill is not considered impaired. If the carrying value is higher than the fair value, there is an indication that an impairment may exist and the second step is required. In step two, the implied fair value of goodwill is calculated as the excess of the fair value of a reporting unit over the fair values assigned to its assets and liabilities. If the implied fair value of goodwill is less than the carrying value of the reporting unit's goodwill,

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the difference is recognized as an impairment loss. No goodwill for reporting units was impaired during the three and six months ended June 30, 2014 or 2013.

As discussed in Note 15, effective January 1, 2014, we revised our reportable segments in line with the changes to our organizational structure. Our reporting units did not significantly change as a result of the changes to our reportable segments. The segment information for 2013 has been retrospectively adjusted to conform to the 2014 presentation.

The changes in carrying amount of goodwill by reportable segment for the six months ended June 30, 2014 were as follows:

(Millions of dollars)

	December 31, 2013	Acquisitions	Held for Sale and Business Divestitures [1]	Other Adjustments [2]	June 30, 2014
Construction Industries					
Goodwill	$291	$—	$—	$15	$306
Resource Industries					
Goodwill	4,468	—	(10)	2	4,460
Impairments	(580)	—	—	—	(580)
Net goodwill	3,888	—	(10)	2	3,880
Energy & Transportation					
Goodwill	2,600	7	—	(1)	2,606
All Other [3]					
Goodwill	199	—	—	—	199
Impairments	(22)	—	—	—	(22)
Net goodwill	177	—	—	—	177
Consolidated total					
Goodwill	7,558	7	(10)	16	7,571
Impairments	(602)	—	—	—	(602)
Net goodwill	$6,956	$7	$(10)	$16	$6,969

[1] See Note 19 for additional details.
[2] Other adjustments are comprised primarily of foreign currency translation.
[3] Includes All Other operating segments (See Note 15).

8. Available-For-Sale Securities

We have investments in certain debt and equity securities, primarily at Insurance Services, that have been classified as available-for-sale and recorded at fair value based upon quoted market prices. These investments are primarily included in Other assets in the Consolidated Statement of Financial Position. Unrealized gains and losses arising from the revaluation of available-for-sale securities are included, net of applicable deferred income taxes, in equity (Accumulated other comprehensive income (loss) in the Consolidated Statement of Financial Position). Realized gains and losses on sales of investments are generally determined using the FIFO (first-in, first-out) method for debt instruments and the specific identification method for equity securities. Realized gains and losses are included in Other income (expense) in the Consolidated Statement of Results of Operations.

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(Millions of dollars)	June 30, 2014 Cost Basis	June 30, 2014 Unrealized Pretax Net Gains (Losses)	June 30, 2014 Fair Value	December 31, 2013 Cost Basis	December 31, 2013 Unrealized Pretax Net Gains (Losses)	December 31, 2013 Fair Value
Government debt						
U.S. treasury bonds	$10	$—	$10	$10	$—	$10
Other U.S. and non-U.S. government bonds	103	1	104	119	1	120
Corporate bonds						
Corporate bonds	691	24	715	612	21	633
Asset-backed securities	99	1	100	72	—	72
Mortgage-backed debt securities						
U.S. governmental agency	311	2	313	322	(1)	321
Residential	16	1	17	18	—	18
Commercial	68	6	74	87	6	93
Equity securities						
Large capitalization value	169	88	257	173	81	254
Smaller company growth	24	29	53	25	24	49
Total	$1,491	$152	$1,643	$1,438	$132	$1,570

During the three and six months ended June 30, 2014, there were no charges for other-than-temporary declines in the market values of securities. During the three and six months ended June 30, 2013, charges for other-than-temporary declines in the market values of securities were $1 million. These charges were accounted for as realized losses and were included in Other income (expense) in the Consolidated Statement of Results of Operations. The cost basis for the impacted securities was adjusted to reflect these charges.

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Investments in an unrealized loss position that are not other-than-temporarily impaired:

	June 30, 2014					
	Less than 12 months [1]		12 months or more [1]		Total	
(Millions of dollars)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Corporate bonds						
Asset-backed securities	$6	$—	$17	$1	$23	$1
Mortgage-backed debt securities						
U.S. governmental agency	30	—	147	3	177	3
Equity securities						
Large capitalization value	10	1	1	—	11	1
Total	$46	$1	$165	$4	$211	$5

	December 31, 2013					
	Less than 12 months [1]		12 months or more [1]		Total	
(Millions of dollars)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Corporate bonds						
Corporate bonds	$159	$2	$1	$—	$160	$2
Asset-backed securities	6	—	20	1	26	1
Mortgage-backed debt securities						
U.S. governmental agency	140	4	65	2	205	6
Total	$305	$6	$86	$3	$391	$9

[1] Indicates length of time that individual securities have been in a continuous unrealized loss position.

Corporate Bonds. The unrealized losses on our investments in asset-backed securities relate to changes in interest rates and credit-related yield spreads since time of purchase. We do not intend to sell the investments and it is not likely that we will be required to sell the investments before recovery of their amortized cost basis. We do not consider these investments to be other-than-temporarily impaired as of June 30, 2014.

Mortgage-Backed Debt Securities. The unrealized losses on our investments in mortgage-backed securities relate to changes in interest rates and credit-related yield spreads since time of purchase. We do not intend to sell the investments and it is not likely that we will be required to sell these investments before recovery of their amortized cost basis. We do not consider these investments to be other-than-temporarily impaired as of June 30, 2014.

Equity Securities. Insurance Services maintains a well-diversified equity portfolio consisting of two specific mandates: large capitalization value stocks and smaller company growth stocks. U.S. equity valuations were higher during the second quarter of 2014 on generally favorable economic data. The unrealized losses on our investments in equity securities relate to inherent risks of individual holdings and/or their respective sectors. We do not consider these investments to be other-than-temporarily impaired as of June 30, 2014.

The cost basis and fair value of the available-for-sale debt securities at June 30, 2014, by contractual maturity, is shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to prepay and creditors may have the right to call obligations.

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(Millions of dollars)	June 30, 2014 Cost Basis	Fair Value
Due in one year or less	$100	$100
Due after one year through five years	718	743
Due after five years through ten years	54	55
Due after ten years	31	31
U.S. governmental agency mortgage-backed securities	311	313
Residential mortgage-backed securities	16	17
Commercial mortgage-backed securities	68	74
Total debt securities – available-for-sale	$1,298	$1,333

Sales of Securities:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions of dollars)	2014	2013	2014	2013
Proceeds from the sale of available-for-sale securities	$107	$109	$222	$207
Gross gains from the sale of available-for-sale securities	$—	$1	$14	$2
Gross losses from the sale of available-for-sale securities	$—	$1	$—	$1

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9. Postretirement Benefits

A. Pension and postretirement benefit costs

(Millions of dollars)	U.S. Pension Benefits		Non-U.S. Pension Benefits		Other Postretirement Benefits	
	June 30,		June 30,		June 30,	
	2014	2013	2014	2013	2014	2013
For the three months ended:						
Components of net periodic benefit cost:						
Service cost	$40	$49	$27	$31	$23	$31
Interest cost	162	144	46	42	53	49
Expected return on plan assets [1]	(222)	(208)	(64)	(58)	(13)	(14)
Amortization of:						
Prior service cost (credit) [2]	4	5	—	1	(14)	(19)
Net actuarial loss (gain) [3]	98	137	21	33	11	27
Net periodic benefit cost	82	127	30	49	60	74
Curtailments, settlements and special termination benefits [4]	—	—	7	3	—	—
Total cost included in operating profit	$82	$127	$37	$52	$60	$74
For the six months ended:						
Components of net periodic benefit cost:						
Service cost	$79	$98	$55	$62	$43	$55
Interest cost	324	289	92	85	106	98
Expected return on plan assets [1]	(443)	(416)	(129)	(117)	(26)	(28)
Amortization of:						
Transition obligation (asset)	—	—	—	—	—	1
Prior service cost (credit) [2]	8	9	—	1	(27)	(37)
Net actuarial loss (gain) [3]	196	273	43	66	21	54
Net periodic benefit cost	164	253	61	97	117	143
Curtailments, settlements and special termination benefits [4]	—	—	7	3	—	—
Total cost included in operating profit	$164	$253	$68	$100	$117	$143
Weighted-average assumptions used to determine net cost:						
Discount rate	4.6%	3.7%	4.1%	3.7%	4.6%	3.7%
Expected rate of return on plan assets	7.8%	7.8%	6.9%	6.7%	7.8%	7.8%
Rate of compensation increase	4.0%	4.5%	4.2%	3.9%	4.0%	4.4%

1 Expected return on plan assets developed using calculated market-related value of plan assets which recognizes differences in expected and actual returns over a three-year period.

2 Prior service cost (credit) for both pension and other postretirement benefits are generally amortized using the straight-line method over the average remaining service period of active employees expected to receive benefits from the plan. For pension plans in which all or almost all of the plan's participants are inactive and other postretirement benefit plans in which all or almost all of the plan's participants are fully eligible for benefits under the plan, prior service cost (credit) are amortized using the straight-line method over the remaining life expectancy of those participants.

3

Net actuarial loss (gain) for pension and other postretirement benefit plans are generally amortized using the straight-line method over the average remaining service period of active employees expected to receive benefits from the plan. For plans in which all or almost all of the plan's participants are inactive, net actuarial loss (gain) are amortized using the straight-line method over the remaining life expectancy of the inactive participants.

4 Curtailments, settlements and termination benefits were recognized in Other operating (income) expenses in the Consolidated Statement of Results of Operations.

We made $108 million and $387 million of contributions to our pension plans during the three and six months ended June 30, 2014, respectively. We currently anticipate full-year 2014 contributions of approximately $510 million, all of which are required. We made $138 million and $280 million of contributions to our pension plans during the three and six months ended June 30, 2013, respectively.

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B. Defined contribution benefit costs

Total company costs related to our defined contribution plans were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Millions of dollars)	2014	2013	2014	2013
U.S. Plans	$89	$61	$170	$144
Non-U.S. Plans	21	17	41	31
	$110	$78	$211	$175

10. Guarantees and Product Warranty

We have provided an indemnity to a third-party insurance company for potential losses related to performance bonds issued on behalf of Caterpillar dealers. The bonds are issued to insure governmental agencies against nonperformance by certain dealers. We also provided guarantees to a third-party related to the performance of contractual obligations by certain Caterpillar dealers. The guarantees cover potential financial losses incurred by the third-party resulting from the dealers' nonperformance.

We provide loan guarantees to third-party lenders for financing associated with machinery purchased by customers. These guarantees have varying terms and are secured by the machinery. In addition, Cat Financial participates in standby letters of credit issued to third parties on behalf of their customers. These standby letters of credit have varying terms and beneficiaries and are secured by customer assets.

We have provided a guarantee to one of our customers in Brazil related to the performance of contractual obligations by a supplier consortium to which one of our Caterpillar subsidiaries is a member. The guarantees cover potential damages (some of them capped) incurred by the customer resulting from the supplier consortium's non-performance. The guarantee will expire when the supplier consortium performs all its contractual obligations, which is expected to be completed in 2025.

We have provided guarantees to third-party lessors for certain properties leased by Cat Logistics Services, LLC, in which we sold a 65 percent equity interest in the third quarter of 2012. The guarantees are for the possibility that the third party logistics business would default on real estate lease payments. The guarantees were granted at lease inception, which was prior to the divestiture, and generally will expire at the end of the lease terms.

No significant loss has been experienced or is anticipated under any of these guarantees. At June 30, 2014 and December 31, 2013, the related liability was $12 million and $13 million, respectively. The maximum potential amount of future payments (undiscounted and without reduction for any amounts that may possibly be recovered under recourse or collateralized provisions) we could be required to make under the guarantees are as follows:

(Millions of dollars)	June 30, 2014	December 31, 2013
Caterpillar dealer guarantees	$201	$193
Customer guarantees	58	62
Customer guarantees – supplier consortium	362	364
Third party logistics business guarantees	140	151
Other guarantees	34	35
Total guarantees	$795	$805

Cat Financial provides guarantees to repurchase certain loans of Caterpillar dealers from a special-purpose corporation (SPC) that qualifies as a variable interest entity. The purpose of the SPC is to provide short-term working capital loans to Caterpillar dealers. This SPC issues commercial paper and uses the proceeds to fund its loan program. Cat Financial has a loan purchase agreement with the SPC that obligates Cat Financial to purchase certain loans that are not paid at maturity. Cat Financial receives a fee for providing this guarantee, which provides a source of liquidity for the SPC. Cat Financial is the primary beneficiary of the SPC as its guarantees result in Cat Financial having both the power to direct

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the activities that most significantly impact the SPC's economic performance and the obligation to absorb losses, and therefore Cat Financial has consolidated the financial statements of the SPC. As of June 30, 2014 and December 31, 2013, the SPC's assets of $1,186 million and $1,005 million, respectively, are primarily comprised of loans to dealers and the SPC's liabilities of $1,185 million and $1,005 million, respectively, are primarily comprised of commercial paper. The assets of the SPC are not available to pay Cat Financial's creditors. Cat Financial may be obligated to perform under the guarantee if the SPC experiences losses. No loss has been experienced or is anticipated under this loan purchase agreement.

Our product warranty liability is determined by applying historical claim rate experience to the current field population and dealer inventory. Generally, historical claim rates are based on actual warranty experience for each product by machine model/engine size by customer or dealer location (inside or outside North America). Specific rates are developed for each product shipment month and are updated monthly based on actual warranty claim experience.

(Millions of dollars)	2014
Warranty liability, January 1	$1,367
Reduction in liability (payments)	(530)
Increase in liability (new warranties)	572
Warranty liability, June 30	$1,409

(Millions of dollars)	2013
Warranty liability, January 1	$1,477
Reduction in liability (payments)	(938)
Increase in liability (new warranties)	828
Warranty liability, December 31	$1,367

11. Profit Per Share

Computations of profit per share:	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in millions except per share data)	2014	2013	2014	2013
Profit for the period (A) [1]:	$999	$960	$1,921	$1,840
Determination of shares (in millions):				
Weighted-average number of common shares outstanding (B)	626.3	649.9	626.8	652.4
Shares issuable on exercise of stock awards, net of shares assumed to be purchased out of proceeds at average market price	12.0	12.8	12.5	14.2
Average common shares outstanding for fully diluted computation (C) [2]	638.3	662.7	639.3	666.6
Profit per share of common stock:				
Assuming no dilution (A/B)	$1.60	$1.48	$3.06	$2.82
Assuming full dilution (A/C) [2]	$1.57	$1.45	$3.00	$2.76
Shares outstanding as of June 30 (in millions)			627.8	647.6

[1] Profit attributable to common stockholders.
[2] Diluted by assumed exercise of stock-based compensation awards using the treasury stock method.

SARs and stock options to purchase 7,513,187 and 10,343,160 common shares were outstanding for the three and six months ended June 30, 2014, respectively, which were not included in the computation of diluted earnings per share because the effect would have been anti-dilutive. For the three and six months ended June 30, 2013, there were outstanding SARs and stock options to purchase 10,350,280 and 10,256,295 common shares which were anti-dilutive.

In February 2007, the Board of Directors authorized the repurchase of $7.5 billion of Caterpillar common stock (the 2007 Authorization), and in December 2011, the 2007 Authorization was extended through December 2015. In April 2013, we

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entered into a definitive agreement with Citibank, N.A. to purchase shares of our common stock under an accelerated stock repurchase transaction (April 2013 ASR Agreement), which was completed in June 2013. In accordance with the terms of the April 2013 ASR Agreement, a total of 11.5 million shares of our common stock were repurchased at an aggregate cost to Caterpillar of $1.0 billion.

In January 2014, we completed the 2007 Authorization and entered into a definitive agreement with Citibank, N.A. to purchase shares of our common stock under an accelerated stock repurchase transaction (January 2014 ASR Agreement), which was completed in March 2014. In accordance with the terms of the January 2014 ASR Agreement, a total of approximately 18.1 million shares of our common stock were repurchased at an aggregate cost to Caterpillar of approximately $1.7 billion.

In January 2014, the Board approved a new authorization to repurchase up to $10 billion of Caterpillar common stock, which will expire on December 31, 2018. In July 2014, we entered into definitive agreements with Société Générale to purchase shares of our common stock under accelerated stock repurchase transactions (July 2014 ASR Agreements). Pursuant to the terms of the July 2014 ASR Agreements, we have agreed to repurchase a total of $2.5 billion of our common stock from Société Générale, with an immediate delivery of approximately 22 million shares. The final number of shares to be repurchased and the aggregate cost per share to Caterpillar will be based on Caterpillar's volume-weighted average stock price during the term of the transactions, which are expected to be completed in September 2014.

12. Accumulated Other Comprehensive Income (Loss)

Comprehensive income and its components are presented in the Consolidated Statement of Comprehensive Income. Changes in Accumulated other comprehensive income (loss), net of tax, included in the Consolidated Statement of Changes in Stockholders' Equity, consisted of the following:

(Millions of dollars)	Foreign currency translation	Pension and other postretirement benefits	Derivative financial instruments	Available-for-sale securities	Total
Three Months Ended June 30, 2014					
Balance at March 31, 2014	$216	$(4,072)	$(26)	$ 81	$(3,801)
Other comprehensive income (loss) before reclassifications	28	11	(11)	15	43
Amounts reclassified from accumulated other comprehensive (income) loss	—	80	(5)	—	75
Other comprehensive income (loss)	28	91	(16)	15	118
Balance at June 30, 2014	$244	$(3,981)	$(42)	$ 96	$(3,683)
Three Months Ended June 30, 2013					
Balance at March 31, 2013	$90	$(6,778)	$(62)	$ 81	$(6,669)
Other comprehensive income (loss) before reclassifications	(182)	12	7	(10)	(173)
Amounts reclassified from accumulated other comprehensive (income) loss	—	121	22	1	144
Other comprehensive income (loss)	(182)	133	29	(9)	(29)

Balance at June 30, 2013	$(92)	$(6,645)	$(33)	$ 72	$(6,698)

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(Millions of dollars)	Foreign currency translation	Pension and other postretirement benefits	Derivative financial instruments	Available-for-sale securities	Total
Six Months Ended June 30, 2014					
Balance at December 31, 2013	$176	$(4,152)	$(5)	$ 83	$(3,898)
Other comprehensive income (loss) before reclassifications	68	11	(27)	23	75
Amounts reclassified from accumulated other comprehensive (income) loss	—	160	(10)	(10)	140
Other comprehensive income (loss)	68	171	(37)	13	215
Balance at June 30, 2014	$244	$(3,981)	$(42)	$ 96	$(3,683)
Six Months Ended June 30, 2013					
Balance at December 31, 2012	$456	$(6,914)	$(42)	$ 67	$(6,433)
Other comprehensive income (loss) before reclassifications	(548)	27	(24)	5	(540)
Amounts reclassified from accumulated other comprehensive (income) loss	—	242	33	—	275
Other comprehensive income (loss)	(548)	269	9	5	(265)
Balance at June 30, 2013	$(92)	$(6,645)	$(33)	$ 72	$(6,698)

The effect of the reclassifications out of Accumulated other comprehensive income (loss) on the Consolidated Statement of Results of Operations is as follows:

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