# APPENDIX

# CATERPILLAR INC.

## GENERAL AND FINANCIAL INFORMATION

## 2004

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# MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of Caterpillar Inc. (the Company) is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2004. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in *Internal Control — Integrated Framework*. Based on our assessment we concluded that, as of December 31, 2004, the Company's internal control over financial reporting was effective based on those criteria.

Our management's assessment of the effectiveness of the Company's internal control over financial reporting as of December 31, 2004 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which appears on page A-4.

Jim Owens

James W. Owens
Chairman of the Board

David B. Burritt
Chief Financial Officer

February 24, 2005

# REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

PRICEWATERHOUSECOOPERS

TO THE BOARD OF DIRECTORS AND STOCKHOLDERS OF CATERPILLAR INC.:

We have completed an integrated audit of Caterpillar Inc.'s 2004 consolidated financial statements and of its internal control over financial reporting as of December 31, 2004 and audits of its 2003 and 2002 consolidated financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Our opinions, based on our audits, are presented below.

## Consolidated financial statements

In our opinion, the accompanying statements of consolidated financial position and the related statements of consolidated results of operations, changes in stockholders' equity and consolidated cash flow, including pages A-5 through A-34, present fairly, in all material respects, the financial position of Caterpillar Inc. and its subsidiaries at December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2004 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

## Internal control over financial reporting

Also, in our opinion, management's assessment, included in Management's Report on Internal Control Over Financial Reporting appearing on page A-3, that the Company maintained effective internal control over financial reporting as of December 31, 2004 based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), is fairly stated, in all material respects, based on those criteria. Furthermore, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on criteria established in *Internal Control — Integrated Framework* issued by COSO. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express opinions on management's assessment and on the effectiveness of the Company's internal control over financial reporting based on our audit. We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PricewaterhouseCoopers LLP

Peoria, Illinois
February 24, 2005

## STATEMENT 1 — Caterpillar Inc.

## Consolidated Results of Operations for the Years Ended December 31

(Dollars in millions except per share data)

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| **Sales and revenues:** | | | |
| Sales of Machinery and Engines | **$28,336** | $21,048 | $18,648 |
| Revenues of Financial Products | **1,915** | 1,715 | 1,504 |
| Total sales and revenues | **30,251** | 22,763 | 20,152 |
| **Operating costs:** | | | |
| Cost of goods sold | **22,420** | 16,945 | 15,146 |
| Selling, general and administrative expenses | **3,072** | 2,470 | 2,094 |
| Research and development expenses | **928** | 669 | 656 |
| Interest expense of Financial Products | **520** | 470 | 521 |
| Other operating expenses | **578** | 521 | 411 |
| Total operating costs | **27,518** | 21,075 | 18,828 |
| **Operating profit** | **2,733** | 1,688 | 1,324 |
| Interest expense excluding Financial Products | **230** | 246 | 279 |
| Other income (expense) | **204** | 35 | 69 |
| **Consolidated profit before taxes** | **2,707** | 1,477 | 1,114 |
| Provision for income taxes | **731** | 398 | 312 |
| Profit of consolidated companies | **1,976** | 1,079 | 802 |
| Equity in profit (loss) of unconsolidated affiliated companies | **59** | 20 | (4) |
| **Profit** | **$ 2,035** | $ 1,099 | $ 798 |
| **Profit per common share** | **$ 5.95** | $ 3.18 | $ 2.32 |
| **Profit per common share — diluted**[1] | **$ 5.75** | $ 3.13 | $ 2.30 |
| **Weighted-average common shares outstanding (millions)** | | | |
| **— Basic** | **342.3** | 345.2 | 344.0 |
| **— Diluted**[1] | **353.7** | 351.4 | 346.9 |
| **Cash dividends declared per common share** | **$ 1.60** | $ 1.44 | $ 1.40 |

[1] Diluted by assumed exercise of stock options, using the treasury stock method.

See accompanying Notes to Consolidated Financial Statements.

## STATEMENT 2
## Changes in Consolidated Stockholders' Equity for the Years Ended December 31
(Dollars in millions)

| | **2004** | | 2003 | | 2002 | |
|---|---|---|---|---|---|---|
| **Common stock:** | | | | | | |
| Balance at beginning of year | **$ 1,059** | | $ 1,034 | | $ 1,043 | |
| Shares issued from treasury stock | **172** | | 25 | | (9) | |
| Balance at year-end | **1,231** | | 1,059 | | 1,034 | |
| **Treasury stock:** | | | | | | |
| Balance at beginning of year | **(2,914)** | | (2,669) | | (2,696) | |
| Shares issued: 2004 — 6,108,309; 2003 — 4,956,973; 2002 — 878,623 | **176** | | 160 | | 27 | |
| Shares repurchased: 2004 — 6,933,400; 2003 — 5,450,000 | **(539)** | | (405) | | — | |
| Balance at year-end | **(3,277)** | | (2,914) | | (2,669) | |
| **Profit employed in the business:** | | | | | | |
| Balance at beginning of year | **8,450** | | 7,849 | | 7,533 | |
| Profit | **2,035** | **$2,035** | 1,099 | $ 1,099 | 798 | $ 798 |
| Dividends declared | **(548)** | | (498) | | (482) | |
| Balance at year-end | **9,937** | | 8,450 | | 7,849 | |
| **Accumulated other comprehensive income:** | | | | | | |
| Foreign currency translation adjustment: | | | | | | |
| Balance at beginning of year | **348** | | 86 | | (17) | |
| Aggregate adjustment for year | **141** | **141** | 262 | 262 | 103 | 103 |
| Balance at year-end | **489** | | 348 | | 86 | |
| Minimum pension liability adjustment — consolidated companies: | | | | | | |
| Balance at beginning of year (net of tax of: 2004 — $460; 2003 — $383; 2002 — $82) | **(934)** | | (771) | | (161) | |
| Aggregate adjustment for year (net of tax of: 2004 — $25; 2003 — $77; 2002 — $301) | **(59)** | **(59)** | (163) | (163) | (610) | (610) |
| Balance at year-end (net of tax of: 2004 — $485; 2003 — $460; 2002 — $383) | **(993)** | | (934) | | (771) | |
| Minimum pension liability adjustment — unconsolidated companies: | | | | | | |
| Balance at beginning of year | **(48)** | | (37) | | (41) | |
| Aggregate adjustment for year | **—** | **—** | (11) | (11) | 4 | 4 |
| Balance at year-end | **(48)** | | (48) | | (37) | |
| Derivative financial instruments: | | | | | | |
| Balance at beginning of year (net of tax of: 2004 — $54; 2003 — $5; 2002 — $17) | **104** | | 11 | | (26) | |
| Gains deferred during year (net of tax of: 2004 — $48; 2003 — $29; 2002 — $10) | **90** | **90** | 53 | 53 | 15 | 15 |
| (Gains)/losses reclassified to earnings during year (net of tax of: 2004 — $44; 2003 — $20; 2002 — $11) | **(84)** | **(84)** | 40 | 40 | 22 | 22 |
| Balance at year-end (net of tax of: 2004 — $58; 2003 — $54; 2002 — $4) | **110** | | 104 | | 11 | |
| Available-for-sale securities: | | | | | | |
| Balance at beginning of year (net of tax of: 2004 — $7; 2003 — $17; 2002 — $13) | **13** | | (31) | | (24) | |
| Gains/(losses) deferred during year (net of tax of: 2004 — $3; 2003 — $12; 2002 — $16) | **6** | **6** | 23 | 23 | (29) | (29) |
| (Gains)/losses reclassified to earnings during year (net of tax of: 2004 — $1; 2003 — $11; 2002 — $12) | **(1)** | **(1)** | 21 | 21 | 22 | 22 |
| Balance at year-end (net of tax of: 2004 — $10; 2003 — $7; 2002 — $17) | **18** | | 13 | | (31) | |
| **Total accumulated other comprehensive income** | **(424)** | | (517) | | (742) | |
| Comprehensive income | | **$2,128** | | $ 1,324 | | $ 325 |
| **Stockholders' equity at year-end** | **$ 7,467** | | $ 6,078 | | $ 5,472 | |

See accompanying Notes to Consolidated Financial Statements.

## STATEMENT 3 Caterpillar Inc.
## Consolidated Financial Position at December 31
(Dollars in millions)

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| **Assets** | | | |
| Current assets: | | | |
| Cash and short-term investments | **$ 445** | $ 342 | $ 309 |
| Receivables — trade and other | **7,459** | 4,025 | 3,192 |
| Receivables — finance | **6,510** | 5,508 | 5,066 |
| Retained interests in securitized trade receivables | **—** | 1,550 | 1,145 |
| Deferred and refundable income taxes | **398** | 707 | 781 |
| Prepaid expenses | **1,369** | 1,424 | 1,224 |
| Inventories | **4,675** | 3,047 | 2,763 |
| Total current assets | **20,856** | 16,603 | 14,480 |
| Property, plant and equipment — net | **7,682** | 7,251 | 7,009 |
| Long-term receivables — trade and other | **764** | 510 | 433 |
| Long-term receivables — finance | **8,575** | 7,394 | 6,347 |
| Investments in unconsolidated affiliated companies | **517** | 800 | 747 |
| Deferred income taxes | **674** | 616 | 711 |
| Intangible assets | **315** | 239 | 281 |
| Goodwill | **1,450** | 1,398 | 1,402 |
| Other assets | **2,258** | 1,895 | 1,295 |
| **Total assets** | **$43,091** | $36,706 | $32,705 |
| **Liabilities** | | | |
| Current liabilities: | | | |
| Short-term borrowings: | | | |
| — Machinery and Engines | **$ 93** | $ 72 | $ 64 |
| — Financial Products | **4,064** | 2,685 | 2,111 |
| Accounts payable | **3,990** | 2,568 | 1,790 |
| Accrued expenses | **1,847** | 1,638 | 1,620 |
| Accrued wages, salaries and employee benefits | **1,730** | 1,802 | 1,779 |
| Customer advances | **555** | 305 | 259 |
| Dividends payable | **141** | 127 | 120 |
| Deferred and current income taxes payable | **259** | 216 | 70 |
| Long-term debt due within one year: | | | |
| — Machinery and Engines | **6** | 32 | 258 |
| — Financial Products | **3,525** | 2,949 | 3,654 |
| Total current liabilities | **16,210** | 12,394 | 11,725 |
| Long-term debt due after one year: | | | |
| — Machinery and Engines | **3,663** | 3,603 | 3,581 |
| — Financial Products | **12,174** | 10,943 | 8,193 |
| Liability for postemployment benefits | **2,986** | 3,172 | 3,333 |
| Deferred income taxes and other liabilities | **591** | 516 | 401 |
| **Total liabilities** | **35,624** | 30,628 | 27,233 |
| **Stockholders' equity** | | | |
| Common stock of $1.00 par value: | | | |
| Authorized shares: 900,000,000 | | | |
| Issued shares (2004, 2003 and 2002 — 407,447,312) at paid-in amount | **1,231** | 1,059 | 1,034 |
| Treasury stock (2004 — 64,510,363 shares; 2003 — 63,685,272 shares; and 2002 — 63,192,245 shares) at cost | **(3,277)** | (2,914) | (2,669) |
| Profit employed in the business | **9,937** | 8,450 | 7,849 |
| Accumulated other comprehensive income | **(424)** | (517) | (742) |
| **Total stockholders' equity** | **7,467** | 6,078 | 5,472 |
| **Total liabilities and stockholders' equity** | **$43,091** | $36,706 | $32,705 |

See accompanying Notes to Consolidated Financial Statements.

## STATEMENT 4
## Consolidated Statement of Cash Flow for the Years Ended December 31
(Millions of dollars)

| | **2004** | 2003 | 2002 |
|---|---|---|---|
| **Cash flow from operating activities:** | | | |
| Profit | **$ 2,035** | $ 1,099 | $ 798 |
| Adjustments for non-cash items: | | | |
| Depreciation and amortization | **1,397** | 1,347 | 1,220 |
| Other | **(113)** | (69) | 350 |
| Changes in assets and liabilities: | | | |
| Receivables — trade and other (see non-cash item below) | **(7,616)** | (8,115) | (6,323) |
| Inventories | **(1,391)** | (286) | 162 |
| Accounts payable and accrued expenses | **1,457** | 542 | 97 |
| Other — net | **240** | (129) | (266) |
| Net cash used for operating activities | **(3,991)** | (5,611) | (3,962) |
| **Cash flow from investing activities:** | | | |
| Capital expenditures — excluding equipment leased to others | **(926)** | (682) | (728) |
| Expenditures for equipment leased to others | **(1,188)** | (1,083) | (1,045) |
| Proceeds from disposals of property, plant and equipment | **673** | 761 | 561 |
| Additions to finance receivables | **(8,930)** | (6,868) | (5,933) |
| Collections of finance receivables | **6,216** | 5,251 | 4,569 |
| Proceeds from sale of finance receivables | **700** | 661 | 613 |
| Collections of retained interests in securitized trade receivables | **5,722** | 7,129 | 5,917 |
| Investments and acquisitions (net of cash acquired) | **(290)** | (268) | (294) |
| Proceeds from sale of partnership investment | **290** | — | — |
| Other — net | **(190)** | (17) | (40) |
| Net cash provided by investing activities | **2,077** | 4,884 | 3,620 |
| **Cash flow from financing activities:** | | | |
| Dividends paid | **(534)** | (491) | (481) |
| Common stock issued, including treasury shares reissued | **317** | 157 | 10 |
| Treasury shares purchased | **(539)** | (405) | — |
| Proceeds from long-term debt issued: | | | |
| — Machinery and Engines | **9** | 128 | 248 |
| — Financial Products | **5,079** | 5,506 | 3,889 |
| Payments on long-term debt: | | | |
| — Machinery and Engines | **(35)** | (463) | (225) |
| — Financial Products | **(2,973)** | (3,774) | (3,114) |
| Short-term borrowings — net | **550** | 87 | (102) |
| Net cash provided by financing activities | **1,874** | 745 | 225 |
| Effect of exchange rate changes on cash | **143** | 15 | 26 |
| **Increase (decrease) in cash and short-term investments** | **103** | 33 | (91) |
| Cash and short-term investments at beginning of period | **342** | 309 | 400 |
| Cash and short-term investments at end of period | **$ 445** | $ 342 | $ 309 |

*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.*

Non-cash operating and investing activities:

Trade receivables of $6,786 million, $7,534 million and $6,278 million were exchanged for retained interests in securitized trade receivables in 2004, 2003 and 2002, respectively. See Note 2 on page A-12 for further discussion.

See accompanying Notes to Consolidated Financial Statements.

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 1. Operations and summary of significant accounting policies

### A. Nature of operations

We operate in three principal lines of business:

(1) **Machinery** — A principal line of business which includes the design, manufacture, marketing and sales of construction, mining and forestry machinery — track and wheel tractors, track and wheel loaders, pipelayers, motor graders, wheel tractor-scrapers, track and wheel excavators, backhoe loaders, log skidders, log loaders, off-highway trucks, articulated trucks, paving products, telescopic handlers, skid steer loaders and related parts. Also includes logistics services for other companies.

(2) **Engines** — A principal line of business including the design, manufacture, marketing and sales of engines for Caterpillar machinery, electric power generation systems; on-highway vehicles and locomotives; marine, petroleum, construction, industrial, agricultural and other applications; and related parts. Reciprocating engines meet power needs ranging from 5 to over 22,000 horsepower (4 to over 16 200 kilowatts). Turbines range from 1,200 to 20,500 horsepower (900 to 15 000 kilowatts).

(3) **Financial Products** — A principal line of business consisting primarily of Caterpillar Financial Services Corporation (Cat Financial), Caterpillar Insurance Holdings, Inc. (Cat Insurance), Caterpillar Power Ventures Corporation (Cat Power Ventures) and their subsidiaries. Cat Financial provides a wide range of financing alternatives for Caterpillar machinery and engines, Solar gas turbines, as well as other equipment and marine vessels. Cat Financial also extends loans to customers and dealers. Cat Insurance provides various forms of insurance to customers and dealers to help support the purchase and lease of our equipment. Cat Power Ventures is an active investor in independent power projects using Caterpillar power generation equipment and services.

Our Machinery and Engines operations are highly integrated. Throughout the Notes, Machinery and Engines represents the aggregate total of these principal lines of business.

Our products are sold primarily under the brands "Caterpillar," "Cat," "Solar Turbines," "MaK," "Perkins," "FG Wilson" and "Olympian."

We conduct operations in our Machinery and Engines lines of business under highly competitive conditions, including intense price competition. We place great emphasis on the high quality and performance of our products and our dealers' service support. Although no one competitor is believed to produce all of the same types of machines and engines that we do, there are numerous companies, large and small, which compete with us in the sale of each of our products.

Machines are distributed principally through a worldwide organization of dealers (dealer network), 53 located in the United States and 145 located outside the United States. Worldwide, these dealers serve 178 countries and operate 3,324 places of business, including 1,437 dealer rental outlets. Reciprocating engines are sold principally through the dealer network and to other manufacturers for use in products manufactured by them. Some of the reciprocating engines manufactured by Perkins are also sold through a worldwide network of 170 distributors located in 150 countries. Most of the electric power generation systems manufactured by FG Wilson are sold through a worldwide network of 250 dealers located in 170 countries. Our dealers do not deal exclusively with our products; however, in most cases sales and servicing of our products are the dealers' principal business. Turbines and large marine reciprocating engines are sold through sales forces employed by Solar and MaK, respectively. Occasionally, these employees are assisted by independent sales representatives.

Manufacturing activities of the Machinery and Engines lines of business are conducted in 40 plants in the United States; nine in the United Kingdom; eight in Italy; five in Mexico; four in China; three each in France, India and Northern Ireland; two each in Australia, Germany, Brazil, and Japan; and one each in Belgium, Canada, Hungary, Indonesia, The Netherlands, Poland, Russia, South Africa and Switzerland. Thirteen parts distribution centers are located in the United States and twelve are located outside the United States.

The Financial Products line of business also conducts operations under highly competitive conditions. Financing for users of Caterpillar products is available through a variety of competitive sources, principally commercial banks and finance and leasing companies. We emphasize prompt and responsive service to meet customer requirements and offer various financing plans designed to increase the opportunity for sales of our products and generate financing income for our company. Financial Products activity is conducted primarily in the United States, with additional offices in Asia, Australia, Canada, Europe and Latin America.

See Note 2 on page A-12 for discussion of the reclassification of certain receivables and related cash flows.

### B. Basis of consolidation

The financial statements include the accounts of Caterpillar Inc. and its subsidiaries. Investments in companies that are owned 20% to 50% or are less than 20% owned and for which we have significant influence are accounted for by the equity method (see Note 11 on pages A-18 to A-19). We consolidate all variable interest entities where Caterpillar Inc. is the primary beneficiary.

Certain amounts for prior years have been reclassified to conform with the current-year financial statement presentation. These reclassifications had no impact on operating profit.

In the second quarter of 2003, we revised our policy regarding the classification of certain costs related to distributing replacement parts. Previously, these costs had been included in selling, general and administrative expenses and now are included in cost of goods sold. This classification is more consistent with industry practice. The parts distribution costs include shipping and handling (including warehousing) along with related support costs such as information technology, purchasing and inventory management. Prior period amounts have been revised to conform to the new classification. In 2003 and 2002, the amounts reclassified from selling, general and administrative expenses to cost of goods sold were $443 million and $437 million, respectively.

### C. Sales and revenue recognition

Sales of Machinery and Engines are recognized when title transfers and the risks and rewards of ownership have passed to customers or independently owned and operated dealers.

Our standard invoice terms are established by marketing region. When a sale is made to a dealer, the dealer is responsible for payment even if the product is not sold to an end customer and must make payment within the standard terms to avoid interest costs. Interest at or above prevailing market rates is charged on any past due balance. Our policy is to not forgive this interest. In 2004, 2003 and 2002, terms were extended to not more than one year for $15 million, $54 million and $193 million of receivables, respectively. For 2004 and 2003, these amounts represent less than 1% of consolidated sales. For 2002, this amount represents approximately 1% of consolidated sales.

Sales with payment terms of two months or more were as follows:

| (Dollars in millions) | 2004 | | 2003 | | 2002 | |
|---|---|---|---|---|---|---|
| Payment Terms (months) | Sales | Percent of Sales | Sales | Percent of Sales | Sales | Percent of Sales |
| 2 | **$ 96** | **0.3%** | $ 116 | 0.6% | $ 62 | 0.3% |
| 3 | **175** | **0.6%** | 27 | 0.1% | 118 | 0.6% |
| 4 | **117** | **0.4%** | 28 | 0.1% | 11 | 0.1% |
| 5 | **750** | **2.6%** | 594 | 2.8% | 447 | 2.4% |
| 6 | **6,172** | **21.9%** | 4,104 | 19.5% | 3,503 | 18.8% |
| 7-12 | **831** | **2.9%** | 671 | 3.2% | 465 | 2.5% |
| | **$8,141** | **28.7%** | $ 5,540 | 26.3% | $ 4,606 | 24.7% |

We establish a bad debt allowance for Machinery and Engines receivables when it becomes probable that the receivable will not be collected. Our allowance for bad debts is not significant. No significant write-offs of Machinery and Engines receivables were made during 2004, 2003 or 2002.

Revenues of Financial Products represent primarily finance and lease revenues of Cat Financial. Finance revenues are recognized over the term of the contract at a constant rate of return on the scheduled uncollected principal balance. Lease revenues are recognized in the period earned. Recognition of income is suspended when collection of future income is not probable. Accrual is resumed, and previously suspended income is recognized, when the receivable becomes contractually current and/or collection doubts are removed. Cat Financial provides wholesale inventory financing to dealers. Please refer to Note 7 on page A-16 for more information.

### D. Inventories

Inventories are stated at the lower of cost or market. Cost is principally determined using the last-in, first-out (LIFO) method. The value of inventories on the LIFO basis represented about 80% of total inventories at December 31, 2004, 2003 and 2002.

If the FIFO (first-in, first-out) method had been in use, inventories would have been $2,124 million, $1,863 million and $1,977 million higher than reported at December 31, 2004, 2003 and 2002, respectively.

### E. Securitized receivables

When retail finance receivables are securitized, we retain interest in the receivables in the form of interest-only strips, servicing rights, cash reserve accounts and subordinated certificates. Gains or losses on the securitization are dependent on the purchase price being allocated between the carrying value of the securitized receivables and the retained interests based on their relative fair value. We estimate fair value based on the present value of future expected cash flows using key assumptions for credit losses, prepayment speeds, forward yield curves and discount rates. Please refer to Note 8 on page A-17 for more information.

When trade receivables are securitized, we retain interests in the receivables in the form of certificates. The fair value of these certificated retained interests approximates carrying value due to their short-term nature. Please refer to Note 6 on page A-16 for more information.

### F. Depreciation and amortization

Depreciation of plant and equipment is computed principally using accelerated methods. Depreciation on equipment leased to others, primarily for Financial Products, is computed using the straight-line method over the term of the lease. The depreciable basis is the original cost of the equipment less the estimated residual value of the equipment at the end of the lease term. In 2004, 2003 and 2002, Financial Products depreciation on equipment leased to others was $575 million, $527 million and $415 million, respectively, and was included in "Other operating expenses" in Statement 1. Amortization of purchased intangibles is computed using the straight-line method, generally not to exceed a period of 20 years. Accumulated amortization was $91 million, $44 million and $47 million at December 31, 2004, 2003 and 2002, respectively.

### G. Foreign currency translation

The functional currency for most of our Machinery and Engines consolidated companies is the U.S. dollar. The functional currency for most of our Financial Products and equity basis companies is the respective local currency. Gains and losses resulting from the translation of foreign currency amounts to the functional currency are included in "Other income (expense)" in Statement 1. Gains and losses resulting from translating assets and liabilities from the functional currency to U.S. dollars are included in "Accumulated other comprehensive income" in Statement 3.

### H. Derivative financial instruments

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 exposure. Our policy specifies that derivatives are not to be used for speculative purposes. Derivatives that we use are primarily foreign currency forward and option contracts, interest rate swaps and commodity forward and option contracts. Our derivative activities are subject to the management, direction and control of our 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 Financial Position at their fair value. On the date the derivative contract is entered, we designate the derivative as (1) a hedge of the fair value of a recognized 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 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 other comprehensive income until earnings are affected by the forecasted transaction or the variability of cash flow and are then reported in current earnings. Changes in the fair value of undesignated derivative instruments and the ineffective portion of designated derivative instruments are reported in current earnings.

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 liabilities on the Consolidated 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 derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flow of hedged items. When it is determined that a derivative is not highly effective as a hedge or that it has ceased to be a highly effective hedge, we discontinue hedge accounting prospectively, in accordance with Statement of Financial Accounting Standards No. 133 "Accounting for Derivative Instruments and Hedging Activities" (SFAS 133). Please refer to Note 3 on pages A-13 to A-14 for more information on derivatives.

### I. Impairment of available-for-sale securities

Available-for-sale securities are reviewed monthly to identify market values below cost of 20% or more. If a decline for a debt security is in excess of 20% for six months, the investment is evaluated to determine if the decline is due to general declines in the marketplace or if the investment has been impaired and should be written down to market value pursuant to Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities" (SFAS 115). After the six-month period, debt securities with declines from cost in excess of 20% are evaluated monthly for impairment. For equity securities, if a decline from cost of 20% or more continues for a 12-month period, an other than temporary impairment is recognized without continued analysis.

### J. Income taxes

The provision for income taxes is determined using the asset and liability approach for accounting for income taxes in accordance with Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" (SFAS 109). Tax laws require items to be included in tax filings at different times than the items are reflected in the financial statements. A current liability is recognized for the estimated taxes payable for the current year. Deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. Deferred taxes are adjusted for enacted changes in tax rates and tax laws. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

### K. Estimates in financial statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect reported amounts. The more significant estimates include: residual values for leased assets, fair market values for goodwill impairment tests, and reserves for warranty, product liability and insurance losses, postemployment benefits, post-sale discounts, credit losses and income taxes.

### L. New accounting standards

In November 2004, the FASB issued Statement of Financial Accounting Standards No. 151 (SFAS 151), "Inventory Costs an amendment of ARB No. 43, Chapter 4." SFAS 151 discusses the general principles applicable to the pricing of inventory. Paragraph 5 of ARB 43, Chapter 4 provides guidance on allocating certain costs to inventory. This Statement amends ARB 43, Chapter 4, to clarify that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current-period charges. In addition, this Statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of production facilities. As required by SFAS 151, we will adopt this new accounting standard on January 1, 2006. The adoption of SFAS 151 is not expected to have a material impact on our financial statements.

In December 2004, the FASB issued Statement of Financial Accounting Standards No. 153 (SFAS 153), "Exchanges of Nonmonetary Assets — an amendment of APB Opinion No. 29." SFAS 153 addresses the measurement of exchanges of nonmonetary assets. It eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets in paragraph 21(b) of APB Opinion No. 29 "Accounting for Nonmonetary Transactions" and replaces it with an exception for exchanges that do not have commercial substance. A nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. As required by SFAS 153, we will adopt this new accounting standard effective July 1, 2005. The adoption of SFAS 153 is not expected to have a material impact on our financial statements.

In December 2004, the FASB issued Statement of Financial Accounting Standards No. 123R (SFAS 123R) "Share-Based Payment." SFAS 123R requires that the cost resulting from all share-based payment transactions be recognized in the financial statements. SFAS 123R also establishes fair value as the measurement method in accounting for share-based payments to employees. As required by SFAS 123R, we will adopt this new accounting standard effective July 1, 2005. We will transition to the new guidance using the modified prospective method. In anticipation of delaying vesting until three years after the grant date for future grants, the 2004 employee stock option grant (issued in June) fully vested on December 31, 2004. In order to better align our employee stock option program with the overall market, the number of options granted in 2005 (issued in February) was significantly reduced from the previous year. In response to this decrease, we elected to immediately vest the 2005 option grant. We expect the application of the expensing provisions of SFAS 123R will result in a pretax expense of approximately $20 million in the second half of 2005. As a result of the vesting decisions discussed above, a full complement of expense related to stock options will not be recognized in our results of operations until 2009. Based on the same assumptions used to calculate our 2004 stock option grant, we estimate our pretax expense associated with our stock option grants will range from $50 million in 2006 to $150 million in 2009.

### M. Stock based compensation

We currently use the intrinsic value method of accounting for stock-based employee compensation in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." Therefore, no compensation expense is recognized in association with our options.

The fair value of the options granted in 2004 was estimated using the binomial option-pricing model. We believe this model more accurately reflects the value of the options than using the

Black-Scholes option-pricing model. Previous years grants continue to be valued using the Black-Scholes model. Please refer to Note 18 on page A-25 for additional information on our stock based compensation plans.

**Pro forma net profit and profit per share using the binomial option-pricing model for the 2004 grant and the Black-Scholes option-pricing model for 2003 and previous grants were:**

| (Dollars in millions except per share data) | Years ended December 31, 2004 | 2003 | 2002 |
|---|---|---|---|
| Profit, as reported | **$2,035** | $ 1,099 | $ 798 |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects | **(161)** | (69) | (65) |
| Pro forma net income | **$1,874** | $ 1,030 | $ 733 |
| Profit per share of common stock: | | | |
| As reported: | | | |
| Basic | **$ 5.95** | $ 3.18 | $ 2.32 |
| Diluted | **$ 5.75** | $ 3.13 | $ 2.30 |
| Pro forma: | | | |
| Basic | **$ 5.48** | $ 2.98 | $ 2.13 |
| Diluted | **$ 5.30** | $ 2.93 | $ 2.13 |

**Pro forma net profit and profit per share in 2004 using the Black-Scholes option-pricing model would have been:**

| (Dollars in millions except per share data) | Years ended December 31, 2004 |
|---|---|
| Profit, as reported | **$2,035** |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects | **(202)** |
| Pro forma net income | **$1,833** |
| Profit per share of common stock: | |
| As reported: | |
| Basic | **$ 5.95** |
| Diluted | **$ 5.75** |
| Pro forma: | |
| Basic | **$ 5.35** |
| Diluted | **$ 5.18** |

## 2. Reclassification of certain receivables and related cash flows

### A. Consolidated financial position

Our Machinery and Engines operations generate trade receivables from the sale of inventory to dealers and customers. Certain of these receivables are sold to Cat Financial. Cat Financial holds the receivables and periodically securitizes a portion of the dealer receivables using a revolving securitization structure. Cat Financial's portion of the securitized trade receivables is represented by certificated retained interests. Cat Financial also generates wholesale inventory receivables from its direct financing of inventory purchases by dealers. Previously, the certificated retained interests as well as the wholesale inventory receivables were classified as Finance Receivables in our Consolidated Financial Position. In the fourth quarter of 2004, we reclassified the certificated retained interests from Finance Receivables to Retained Interests in Securitized Trade Receivables and the wholesale inventory receivables from Finance Receivables to Trade and Other Receivables in our Consolidated Financial Position. These changes were made to align the financial position with the cash flow changes discussed below.

### B. Consolidated statement of cash flow

During the fourth quarter of 2004, the staff of the Securities and Exchange Commission expressed concern regarding the classifications of certain cash flows by companies with captive finance subsidiaries. As a result of this concern, management decided to make reclassifications to the 2003 and 2002 Consolidated Statements of Cash Flow as described below.

#### Securitized trade receivables

Previously, we reported an increase in cash flow from operating activities in the Consolidated Statement of Cash Flow when Machinery and Engines sold receivables to Cat Financial that were subsequently securitized. Concurrently, Cat Financial's entire purchase of these receivables was included in Additions to Finance Receivables (investing activity) in the Consolidated Statement of Cash Flow. The receivables were immediately securitized and the portion sold to a third party was included in Proceeds from Sale of Finance Receivables (investing activity) in the Consolidated Statement of Cash Flow. Subsequently, collection of the certificated retained interests was included in Collection of Finance Receivables (investing activity) in the Consolidated Statement of Cash Flow. This cash flow treatment followed our principal lines of business reporting, however, when we reported an increase in cash flow from operating activities and a corresponding outflow from investing activities there was no increase in cash on a consolidated basis from the sale of inventory to our dealers and customers.

In the fourth quarter of 2004, we made a reclassification to eliminate the offsetting non-cash intercompany transactions in the Consolidated Statement of Cash Flow. In addition, we reclassified the proceeds from sale of trade receivables to operating activities. The reclassification properly classifies cash receipts from the sale of inventory as operating activities and reflects that these cash flows, although held and managed by Cat Financial, arise from our sale of Machinery and Engines inventory.

The securitization structure mentioned above involves a securitization trust. During 2002 and 2003, the trust was a qualifying special purpose entity (QSPE) and thus, in accordance with Statement of Financial Accounting Standards No. 140 (SFAS 140), "Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities," was not consolidated. (See Note 6 on page A-16 for discussion of the 2004 QSPE status of the trust.) When receivables were placed into the trust, we received cash for the portion sold to third party purchasers and the portion retained by Cat Financial was represented by certificated retained interests. Placing receivables into a securitization trust changes their nature and the receipt of certificated retained interests is considered a non-cash transaction. We have noted this non-cash transaction on the Consolidated Statement of Cash Flow and quantified the receivables decrease resulting from this transaction and thus excluded from operating activities. This reflects that certificated retained interests, not cash, were received for these sales. The certificated retained interests are considered held-to-maturity securities as defined by SFAS 115. SFAS 115 requires that collection of held-to-maturity securities be classified as an investing activity. We have therefore reclassified the collection of the certificated retained interests from Collection of Finance Receivables to Collections of Retained Interests in Securitized Trade Receivables within the investing activities section of the Consolidated Statement of Cash Flow. The impact of these changes is a significant reduction to cash flow from operating activities and a significant increase in cash flow from investing activities. This reflects that although inventory was sold, the nature of the receivable was changed to a security. The subsequent collection of that security is shown as an investing activity.

#### Wholesale inventory receivables

Previously, we reported an increase in cash flow from operating activities when a dealer remitted payment for a trade receivable that was subsequently financed with the issuance of a wholesale inventory receivable by Cat Financial. The issuance of a wholesale inventory receivable by Cat Financial was reported as an Addition to Finance Receivables in the Consolidated Statement of Cash Flow and the subsequent collection was reported as a Collection of Finance Receivables. Similar to securitized receivables, this cash flow treatment followed our principal lines of business reporting, however, when we reported an increase in cash flow from operating activities and a corresponding outflow from investing activities there was no increase in cash on a consolidated basis from the sale of inventory to our dealers and customers. We therefore eliminated the offsetting non-cash transaction in the Consolidated Statement of Cash Flow. In addition, we reclassified the collection of wholesale inventory receivables to operating activities. The reclassification properly classifies cash receipts from the sale of inventory as operating activities and reflects that these cash flows, although held and managed by Cat Financial, arise from our sale of Machinery and Engines inventory.

These reclassifications had no impact on the Increase in Cash and Short-term Investments on the Statement of Consolidated Cash Flow.

Prior amounts reported have been reclassified to conform to this presentation as follows:

| | 2003 | | | 2002 | | |
|---|---|---|---|---|---|---|
| (Millions of dollars) | Previous classification[1] | Change | As Reclassified | Previous classification[1] | Change | As Reclassified |
| **Consolidated Financial Position — Statement 3** | | | | | | |
| Receivables — trade and other | $ 3,666 | $ 359 | $ 4,025 | $ 2,838 | $ 354 | $ 3,192 |
| Receivables — finance | 7,417 | (1,909) | 5,508 | 6,565 | (1,499) | 5,066 |
| Retained interests in securitized trade receivables | — | 1,550 | 1,550 | — | 1,145 | 1,145 |
| Long-term receivables — trade and other | 82 | 428 | 510 | 66 | 367 | 433 |
| Long-term receivables — finance | 7,822 | (428) | 7,394 | 6,714 | (367) | 6,347 |
| **Consolidated Statement of Cash Flow — Statement 4** | | | | | | |
| Receivables — trade and other | $ (438) | $ (7,677) | $ (8,115) | $ 5 | $ (6,328) | $ (6,323) |
| **Net cash provided by (used for) operating activities** | **2,066** | **(7,677)** | **(5,611)** | **2,366** | **(6,328)** | **(3,962)** |
| Additions to finance receivables | (17,146) | 10,278 | (6,868) | (15,338) | 9,405 | (5,933) |
| Collections of finance receivables | 13,882 | (8,631) | 5,251 | 11,866 | (7,297) | 4,569 |
| Proceeds from sale of finance receivables | 1,760 | (1,099) | 661 | 2,310 | (1,697) | 613 |
| Collections of retained interests in securitized trade receivables | — | 7,129 | 7,129 | — | 5,917 | 5,917 |
| **Net cash provided by (used for) investing activities** | **(2,793)** | **7,677** | **4,884** | **(2,708)** | **6,328** | **3,620** |

[1] Certain amounts do not agree to prior period reported amounts due to unrelated reclassifications.

## 3. Derivative financial instruments and risk management

### A. 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 currency, thereby creating exposure to movements in exchange rates.

Our Machinery and Engines 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 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 four years.

We generally designate as cash flow hedges at inception of the contract any Australian dollar, Brazilian real, British pound, Canadian dollar, euro, Japanese yen, Mexican peso or Singapore dollar forward or option contracts that exceed 90 days in duration. Designation is performed on a specific exposure basis to support hedge accounting. The remainder of Machinery and Engines foreign currency contracts are undesignated.

As of December 31, 2004, $102 million of deferred net gains included in equity (“Accumulated other comprehensive income” in Statement 3), related to Machinery and Engines foreign currency contracts designated as cash flow hedges, is expected to be reclassified to current earnings [“Other income (expense)”] over the next twelve months. There were no circumstances where hedge treatment was discontinued during 2004, 2003 or 2002.

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. Our policy allows the use of foreign currency forward contracts to offset the risk of currency mismatch between our receivables and debt. All such foreign currency forward contracts are undesignated.

**(Losses) included in current earnings [Other income (expense)] on undesignated contracts:**

| (Millions of dollars) | **2004** | 2003 | 2002 |
|---|---|---|---|
| Machinery and Engines: | | | |
| On undesignated contracts | **$ (9)** | $ (1) | $ — |
| Due to changes in time and volatility value on options | **—** | — | $ (1) |
| Financial Products: | | | |
| On undesignated contracts | **$ (46)** | $ (121) | $ (96) |
| | **$ (55)** | $ (122) | $ (97) |

Gains and losses on the Financial Products contracts above are substantially offset by balance sheet remeasurement and conversion gains and losses.

### B. 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 policy is to use interest rate swap agreements and forward rate agreements to manage our exposure to interest rate changes and lower the cost of borrowed funds.

Machinery and Engines 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 fixed-to-floating interest rate swaps and forward rate agreements to meet that objective with the intent to designate as fair value hedges at inception of the contract all fixed-to-floating interest rate swaps. Designation as a hedge of the fair value of our fixed rate debt is performed to support hedge accounting. During 2001, our Machinery and Engines operations liquidated all fixed-to-floating interest rate swaps. Deferred gains on liquidated fixed-to-floating interest rate swaps, which were previously designated as fair value hedges, are being amortized to earnings ratably over the remaining life of the hedged debt. We designate as cash flow hedges at inception of the contract all forward rate agreements. Designation as a hedge of the anticipated issuance of debt is performed to support hedge accounting. Machinery and Engines forward rate agreements are 100% effective.

Financial Products operations have a "match funding" objective whereby, within specified boundaries, the interest rate profile (fixed rate or floating rate) of their debt portfolio matches the interest rate profile of their receivables. In connection with that objective, we use interest rate derivative instruments to modify the debt structure to match the receivable portfolio. This "match funding" reduces the volatility of margins between interest-bearing assets and interest-bearing liabilities, regardless of which direction interest rates move. We also use these instruments to gain an economic and/or competitive advantage through a lower cost of borrowed funds. This is accomplished by changing the characteristics of existing debt instruments or entering into new agreements in combination with the issuance of new debt.

Our policy allows us to issue floating-to-fixed, fixed-to-floating and floating-to-floating interest rate swaps to meet the "match funding" objective. To support hedge accounting, we designate fixed-to-floating interest rate swaps as fair value hedges of the fair value of our fixed rate debt at inception of the swap contract. Financial Products policy is to designate most floating-to-fixed interest rate swaps as cash flow hedges of the variability of future cash flows at inception of the swap contract. Designation as a hedge of the variability of cash flow is performed to support hedge accounting. During 2004, Financial Products operations liquidated three fixed-to-floating interest rate swaps and during 2002, Financial Products liquidated four such swaps. As a result, the fair value adjustment of the original debt is being amortized to earnings ratably over the remaining life of the hedged debt.

**Gains (losses) included in current earnings [Other income (expense)]:**

| (Millions of dollars) | **2004** | 2003 | 2002 |
|---|---|---|---|
| Fixed-to-floating interest rate swaps | | | |
| Machinery and Engines: | | | |
| Gain on liquidated swaps | **$ 5** | $ 6 | $ 8 |
| Financial Products: | | | |
| Gain/(loss) on designated interest rate derivatives | **(28)** | (20) | 17 |
| Gain/(loss) on hedged debt | **28** | 20 | (17) |
| Gain on liquidated swaps — included in interest expense | **2** | 2 | 1 |
| | **$ 7** | $ 8 | $ 9 |

As of December 31, 2004, $3 million of deferred net losses included in equity ("Accumulated other comprehensive income" in Statement 3), related to Financial Products floating-to-fixed interest rate swaps, is expected to be reclassified to current earnings ("Interest expense of Financial Products") over the next twelve months. There were no circumstances where hedge treatment was discontinued during 2004, 2003 or 2002 in either Machinery and Engines or Financial Products.

### C. 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 and Engines operations purchase aluminum, copper and nickel embedded in the components we purchase from suppliers. Our suppliers pass on to us price changes in the commodity portion of the component cost.

Our objective is to minimize volatility in the price of these commodities. Our policy allows us to enter commodity forward and option contracts to lock in the purchase price of the commodities within a four-year horizon. All such commodity forward and option contracts are undesignated. Gains on the undesignated contracts of $15 million, $27 million and $1 million were recorded in current earnings ["Other income (expense)"] for 2004, 2003 and 2002, respectively.

## 4. Other income (expense)

| | Years ended December 31, | | |
|---|---|---|---|
| (Millions of dollars) | **2004** | 2003 | 2002 |
| Investment and interest income | **$ 96** | $ 49 | $ 31 |
| Foreign exchange gains | **116** | 35 | 13 |
| Charge for early retirement of debt | **—** | (55) | — |
| Miscellaneous income (loss) | **(8)** | 6 | 25 |
| | **$ 204** | $ 35 | $ 69 |

## 5. Income taxes

**The components of profit before taxes were:**

| (Millions of dollars) | Years ended December 31, 2004 | 2003 | 2002 |
|---|---|---|---|
| U.S. | **$1,106** | $ 489 | $ 343 |
| Non-U.S. | **1,601** | 988 | 771 |
| | **$2,707** | $ 1,477 | $1,114 |

Profit before taxes, as shown above, is based on the location of the entity to which such earnings are attributable. However, since such earnings are subject to taxation in more than one country, the income tax provision shown below as U.S. or non-U.S. may not correspond to the earnings shown above.

**The components of the provision for income taxes were:**

| (Millions of dollars) | Years ended December 31, 2004 | 2003 | 2002 |
|---|---|---|---|
| Current tax provision (credit): | | | |
| U.S. Federal | **$ 136** | $ 24 | $ (62) |
| Non-U.S. | **308** | 196 | 210 |
| State (U.S.) | **13** | 10 | 1 |
| | **457** | 230 | 149 |
| Deferred tax provision (credit): | | | |
| U.S. Federal | **301** | 182 | 172 |
| Non-U.S. | **(24)** | (21) | (20) |
| State (U.S.) | **(3)** | 7 | 11 |
| | **274** | 168 | 163 |
| Total provision for income taxes | **$ 731** | $ 398 | $ 312 |

**Reconciliation of the U.S. federal statutory rate to effective rate:**

| | Years ended December 31, 2004 | 2003 | 2002 |
|---|---|---|---|
| U.S. statutory rate | **35.0 %** | 35.0 % | 35.0 % |
| (Decreases) increases in taxes resulting from: | | | |
| Benefit of foreign sales corporation/ extraterritorial income exclusion | **(4.9)%** | (4.9)% | (4.4)% |
| Non-U.S. subsidiaries taxed at other than 35% | **(3.7)%** | (4.0)% | (3.4)% |
| Other — net | **0.6 %** | 0.9 % | 0.8 % |
| Provision for income taxes | **27.0 %** | 27.0 % | 28.0 % |

We paid income taxes of $326 million, $55 million and $124 million in 2004, 2003 and 2002, respectively.

We have recorded income tax expense at U.S. tax rates on all profits, except for undistributed profits of non-U.S. companies which are considered indefinitely reinvested. Determination of the amount of unrecognized deferred tax liability related to indefinitely reinvested profits is not feasible.

Certain subsidiaries operating in China qualify for holidays from income tax, which consist of a two-year full exemption from tax followed by a three-year 50% reduction in the applicable tax rate. The tax holiday begins the first year the subsidiary generates taxable income after utilization of any carryforward losses. The dollar effect in 2004 was $2 million or less than $.01 per share and $10 million or $.03 per share in 2003.

**Deferred income tax assets and liabilities:**

| (Millions of dollars) | December 31, 2004 | 2003 | 2002 |
|---|---|---|---|
| Deferred income tax assets: | | | |
| Postemployment benefits other than pensions | **$1,092** | $ 1,147 | $1,130 |
| Warranty reserves | **212** | 163 | 204 |
| Unrealized profit excluded from inventories | **153** | 136 | 109 |
| Tax carryforwards | **480** | 370 | 230 |
| Inventory valuation method | **35** | 37 | 60 |
| Pension | **—** | — | 39 |
| Deferred compensation | **57** | 48 | 38 |
| Allowance for credit losses | **73** | 66 | 55 |
| Unremitted earnings of non-U.S. subs | **—** | 25 | 60 |
| Other | **200** | 158 | 144 |
| | **2,302** | 2,150 | 2,069 |
| Deferred income tax liabilities: | | | |
| Capital assets | **(903)** | (731) | (597) |
| Pension | **(216)** | (102) | — |
| Unremitted earnings of non-U.S. subs | **(131)** | — | — |
| | **(1,250)** | (833) | (597) |
| Valuation allowance for deferred tax assets | **(24)** | (37) | (34) |
| Deferred income taxes — net | **$1,028** | $ 1,280 | $1,438 |

SFAS 109 requires that individual tax-paying entities of the company offset all current deferred tax liabilities and assets within each particular tax jurisdiction and present them as a single amount in the Consolidated Financial Position. A similar procedure is followed for all noncurrent deferred tax liabilities and assets. Amounts in different tax jurisdictions cannot be offset against each other. The amount of deferred income taxes at December 31, included on the following lines in Statement 3, are as follows:

| (Millions of dollars) | 2004 | 2003 | 2002 |
|---|---|---|---|
| Assets: | | | |
| Deferred and refundable income taxes | **$ 397** | $ 702 | $ 777 |
| Deferred income taxes | **674** | 616 | 711 |
| | **$1,071** | $ 1,318 | $1,488 |
| Liabilities: | | | |
| Deferred and current income taxes payable | **$ 20** | $ 18 | $ 8 |
| Deferred income taxes and other liabilities | **23** | 20 | 42 |
| Deferred income taxes — net | **$1,028** | $ 1,280 | $1,438 |

A valuation allowance has been recorded at certain non-U.S. subsidiaries that have not yet demonstrated consistent and/or sustainable profitability to support the recognition of net deferred tax assets.

As of December 31, 2004, amounts and expiration dates of net operating loss carryforwards in various non-U.S. taxing jurisdictions were:

(Millions of dollars)

| 2005 | 2006 | 2007 | 2008 | 2009-2014 | Unlimited | Total |
|---|---|---|---|---|---|---|
| $9 | $10 | $6 | $6 | $95 | $557 | $683 |

As of December 31, 2004, approximately $592 million of state tax net operating loss carryforwards were available. Of these, 86% expire after 2014.

As of December 31, 2004, approximately $222 million of regular foreign tax credits and $19 million of credit for research activities were available to carry forward in the United States. Of the foreign tax credits, $115 million will expire in 2013, $75 million will expire in 2014, and $32 million will expire in 2015. The research credits will begin to expire in 2023.

In December 2004, the FASB issued FASB Staff Position No. 109-1 "Application of FASB Statement No. 109, *Accounting for Income Taxes,* to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004" (FSP 109-1). FSP 109-1 provides accounting guidance for companies that will be eligible for a tax deduction resulting from "qualified production activities income" as defined in the American Jobs Creation Act of 2004 (the Act). FSP 109-1 requires this deduction be treated as a special deduction in accordance with SFAS 109, which does not require a revaluation of our U.S. deferred tax assets. We will apply the guidance in FSP 109-1 upon recognition of this tax deduction beginning January 1, 2005. The application of FSP 109-1 will not have a material impact on our financial statements.

In December 2004, the FASB issued FASB Staff Position No. 109-2 "Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004" (FSP 109-2). FSP 109-2 provides accounting guidance for the one-time tax deduction of 85% of certain non-U.S. earnings that are repatriated in excess of a base amount as defined in the Act. SFAS 109 requires a company to reflect in the period of enactment the effect of a new tax law. Due to the lack of clarification of certain provisions within the Act, FSP 109-2 allows companies time beyond the financial reporting period of enactment to evaluate the effect of the Act.

We have started an evaluation of the effects of the repatriation provision. However, we do not expect to be able to complete this evaluation until after Congress and the Treasury Department provide additional clarification on key elements of the provision. We expect to complete our evaluation of the effects of the repatriation provision within a reasonable period of time following the publication of all relevant guidance. The range of possible amounts, including the base, which we are considering for repatriation under this provision, is between zero and $1 billion. The related potential range of incremental provision for income taxes is between zero and $75 million.

## 6. Retained interests in securitized trade receivables

Our Machinery and Engines operations generate trade receivables from the sale of inventory to dealers and customers. Certain of these receivables are sold to Cat Financial. Cat Financial holds the receivables and periodically securitizes a portion of the dealer receivables using a revolving securitization structure. The trust issues a collateralized trust obligation (CTO) certificate to third party purchasers for their portion of these receivables. The trust also issues a transferor certificate (certificated retained interests) to Cat Financial for the portion not represented by the CTO.

For 2002 and 2003 and through August of 2004, the trust was a qualifying special purpose entity (QSPE) and thus, in accordance SFAS 140 was not consolidated. The outstanding principal balance of the CTO was not included in our Consolidated Financial Position during these periods. The certificated retained interests were included in "Retained Interests in Securitized Trade Receivables" in Statement 3.

From September through December of 2004, because of a significant increase in Machinery and Engines' sales and subsequent sale of the receivables to Cat Financial, our certificated retained interests in the trust exceeded 90% of the fair value of trust assets. Thus, during this period, the trust did not qualify as a QSPE as defined by SFAS 140. We therefore consolidated the trust in accordance with FIN 46R, "Consolidation of Variable Interest Entities" (revised) as it represents a variable interest entity for which Cat Financial is the primary beneficiary. As of December 31, 2004, assets of the trust of $2,587 million were included in "Receivables — trade and other" in Statement 3 and the CTO of $240 million was included in "Short-term Borrowings." Please refer to Note 15 on page A-24.

Cat Financial services the dealer receivables and receives an annual servicing fee of approximately 1% of the average outstanding principal balance of the CTO. Consolidated expenses of $7 million, $6 million and $10 million related to the CTO were recognized during 2004, 2003 and 2002, respectively, and are included in "Other income (expense)" on Statement 1. Expected credit losses are assumed to be 0% because dealer receivables have historically had no losses and none are expected in the future. The fair value of the certificated retained interests in dealer receivables approximates carrying value due to their short-term nature. Other than the certificated retained interests (assets of the trust when consolidated), the investors and the securitization facilities have no recourse to Cat Financial's assets for failure of debtors to pay when due.

| | **2004** | 2003 | 2002 |
|---|---|---|---|
| **Cash flow from securitizations:** | | | |
| Proceeds from sales of receivables[1] | **$ 663** | $ 1,099 | $ 1,696 |
| Servicing fees received | **2** | 2 | 3 |
| **Characteristics of securitized receivables:** | | | |
| Principal balance at December 31: | | | |
| Certificated retained interests | **$ —** | $ 1,550 | $ 1,145 |
| Collateralized trust obligation | **—** | 240 | 240 |
| Average balance for the year ended December 31[1]: | | | |
| Certificated retained interests | **1,936** | 1,350 | 1,012 |
| Collateralized trust obligation | **240** | 240 | 324 |

[1] For 2004, proceeds and average balances include only the periods the trust was a QSPE.

## 7. Wholesale inventory receivables

Wholesale inventory receivables are receivables of Cat Financial that arise when Cat Financial provides financing for a dealer's purchase of inventory. These receivables are included in "Receivables — trade and other" and "Long-term receivables — trade and other" in Statement 3 and were $991 million, $764 million and $691 million at December 31, 2004, 2003 and 2002, respectively. Please refer to Note 20 on pages A-25 and A-26 and Table III on page A-27 for fair value information.

**Contractual maturities of outstanding wholesale inventory receivables:**

| | December 31, 2004 | | | |
|---|---|---|---|---|
| Amounts Due In | Wholesale Installment Contracts | Wholesale Finance Leases | Wholesale Notes | Total |
| 2005 | $ 40 | $ 23 | $ 424 | $ 487 |
| 2006 | 12 | 17 | 177 | 206 |
| 2007 | 7 | 16 | 125 | 148 |
| 2008 | 1 | 11 | 111 | 123 |
| 2009 | — | 5 | 8 | 13 |
| Thereafter | — | — | 2 | 2 |
| | 60 | 72 | 847 | 979 |
| Guaranteed residual value | — | 53 | — | 53 |
| Less: Unearned income | 1 | 14 | 26 | 41 |
| Total | $ 59 | $ 111 | $ 821 | $ 991 |

## 8. Finance receivables

Finance receivables are receivables of Cat Financial, which generally can be repaid or refinanced without penalty prior to contractual maturity. Total finance receivables reported in Statement 3 are net of an allowance for credit losses.

During 2004, 2003 and 2002, Cat Financial securitized retail installment sale contracts and finance leases into public asset-backed securitization facilities. The securitization facilities are qualifying special purpose entities and thus, in accordance with SFAS 140, are not consolidated. These finance receivables, which are being held in securitization trusts, are secured by new and used equipment. Cat Financial retained servicing responsibilities and subordinated interests related to these securitizations. For 2004, subordinated interests included subordinated certificates with an initial fair value of $8 million, an interest in certain future cash flow (excess) with an initial fair value of $2 million and a reserve account with an initial fair value of $10 million. For 2003, subordinated interests included subordinated certificates with an initial fair value of $9 million, an interest in certain future cash flow (excess) with an initial fair value of $14 million and a reserve account with an initial fair value of $10 million. For 2002, subordinated interests included subordinated certificates with an initial fair value of $8 million, an interest in certain future cash flow (excess) with an initial fair value of $11 million and a reserve account with an initial fair value of $10 million. The company's retained interests generally are subordinate to the investors' interests. Net gains of $13 million, $22 million and $18 million were recognized on these transactions in 2004, 2003 and 2002, respectively.

Significant assumptions used to estimate the fair value of the retained interests and subordinated certificates at the time of the transaction were:

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Discount rate | **10.7%** | 11.0% | 10.9% |
| Weighted-average prepayment rate | **14.0%** | 14.0% | 14.0% |
| Expected credit losses | **1.0%** | 1.0% | 1.0% |

The company receives annual servicing fees of approximately 1% of the unpaid note value.

As of December 31, 2004, 2003 and 2002, the subordinated retained interests in the public securitizations totaled $73 million, $73 million and $47 million, respectively. Key assumptions used to determine the fair value of the retained interests were:

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| Cash flow discount rates on retained interests and subordinated tranches | **10.7%** | 9.1-10.8% | 9.0-10.7% |
| Weighted-average maturity | **28 months** | 27 months | 29 months |
| Average prepayment rate | **14.0%** | 14.0% | 14.0% |
| Expected credit losses | **1.0%** | 1.0% | 1.0% |

The investors and the securitization trusts have no recourse to Cat Financial's other assets for failure of debtors to pay when due.

We estimated the impact of individual 10% and 20% changes to the key economic assumptions used to determine the fair value of residual cash flow in retained interests on our income. An independent, adverse change to each key assumption had an immaterial impact on the fair value of residual cash flow.

We consider an account past due if any portion of an installment is due and unpaid for more than 30 days. Recognition of income is suspended when management determines that collection of future income is not probable (generally after 120 days past due). Accrual is resumed, and previously suspended income is recognized, when the receivable becomes contractually current and/or collection doubts are removed. Investment in loans/finance leases on non-accrual status were $176 million, $233 million and $370 million and past due over 90 days and still accruing were $11 million, $25 million and $72 million as of December 31, 2004, 2003, and 2002, respectively.

Cat Financial provides financing only when acceptable criteria are met. Credit decisions are based on, among other things, the customer's credit history, financial strength and intended use of equipment. Cat Financial typically maintains a security interest in retail financed equipment and requires physical damage insurance coverage on financed equipment.

Please refer to Table I on page A-18 for additional finance receivables information and Note 20 on pages A-25 to A-26 and Table III on page A-27 for fair value information.

## 9. Inventories

| (Millions of dollars) | December 31, 2004 | 2003 | 2002 |
|---|---|---|---|
| Raw materials | **$1,592** | $ 1,105 | $ 900 |
| Work-in-process | **664** | 377 | 311 |
| Finished goods | **2,209** | 1,381 | 1,365 |
| Supplies | **210** | 184 | 187 |
| Total inventories | **$4,675** | $ 3,047 | $2,763 |

We had long-term material purchase obligations of approximately $815 million at December 31, 2004.

## 10. Property, plant and equipment

| (Dollars in millions) | Useful Lives (Years) | December 31, 2004 | 2003 | 2002 |
|---|---|---|---|---|
| Land | — | **$ 152** | $ 149 | $ 149 |
| Buildings and land improvements | 20-45 | **3,089** | 3,006 | 3,039 |
| Machinery, equipment and other | 3-10 | **7,361** | 7,039 | 7,015 |
| Equipment leased to others | — | **3,975** | 3,609 | 2,996 |
| Construction-in-process | — | **587** | 487 | 305 |
| Total property, plant and equipment, at cost | | **15,164** | 14,290 | 13,504 |
| Less: Accumulated depreciation | | **7,482** | 7,039 | 6,495 |
| Property, plant and equipment — net | | **$7,682** | $ 7,251 | $7,009 |

We had commitments for the purchase or construction of capital assets of approximately $169 million at December 31, 2004.

**Assets recorded under capital leases[1]:**

| (Millions of dollars) | December 31, 2004 | 2003 | 2002 |
|---|---|---|---|
| Gross capital leases[2] | **$ 326** | $ 321 | $ 259 |
| Less: Accumulated depreciation | **220** | 213 | 170 |
| Net capital leases | **$ 106** | $ 108 | $ 89 |

[1] Included in Property, plant and equipment table above.
[2] Consists primarily of machinery and equipment.

**TABLE I — Finance Receivables Information (Millions of dollars)**

**Contractual maturities of outstanding finance receivables:**

| Amounts Due In | Retail Installment Contracts | Retail Finance Leases | Retail Notes | Wholesale Notes | Total |
|---|---|---|---|---|---|
| | December 31, 2004 | | | | |
| 2005 | $ 2,361 | $ 1,804 | $ 1,698 | $ 168 | $ 6,031 |
| 2006 | 1,712 | 1,355 | 767 | 12 | 3,846 |
| 2007 | 1,089 | 820 | 536 | 8 | 2,453 |
| 2008 | 576 | 445 | 395 | 5 | 1,421 |
| 2009 | 189 | 210 | 366 | 4 | 769 |
| Thereafter | 47 | 242 | 775 | 3 | 1,067 |
| | 5,974 | 4,876 | 4,537 | 200 | 15,587 |
| Residual value | — | 919 | — | — | 919 |
| Less: Unearned income | 534 | 550 | 56 | 3 | 1,143 |
| Total | $ 5,440 | $ 5,245 | $ 4,481 | $ 197 | $ 15,363 |

**Impaired loans and leases:**

| | **2004** | 2003 | 2002 |
|---|---|---|---|
| Average recorded investment | **$ 265** | $ 321 | $ 292 |
| At December 31: | | | |
| Recorded investment | **$ 181** | $ 275 | $ 366 |
| Less: Impaired loans/finance leases for which there is no related allowance for credit losses (due to the fair value of underlying collateral) | **130** | 177 | 233 |
| Impaired loans/finance leases for which there is a related allowance for credit losses | **$ 51** | $ 98 | $ 133 |

**Allowance for credit loss activity:**

| | **2004** | 2003 | 2002 |
|---|---|---|---|
| Balance at beginning of year | **$ 241** | $ 207 | $ 177 |
| Provision for credit losses | **105** | 101 | 109 |
| Receivables written off | **(88)** | (104) | (103) |
| Recoveries on receivables previously written off | **16** | 22 | 18 |
| Other — net | **4** | 15 | 6 |
| Balance at end of year | **$ 278** | $ 241 | $ 207 |

In estimating the allowance for credit losses, we review accounts that are past due, non-performing or in bankruptcy.

**Cat Financial's net retail finance leases:**

| | December 31, | | |
|---|---|---|---|
| | **2004** | 2003 | 2002 |
| Total minimum lease payments receivable | **$4,876** | $ 4,096 | $ 3,752 |
| Estimated residual value of leased assets: | | | |
| Guaranteed | **379** | 323 | 268 |
| Unguaranteed | **540** | 558 | 597 |
| | **5,795** | 4,977 | 4,617 |
| Less: Unearned income | **550** | 498 | 473 |
| Net retail finance leases | **$5,245** | $ 4,479 | $ 4,144 |

| | **2004** | 2003 | 2002 |
|---|---|---|---|
| **Cash flow from securitizations:** | | | |
| Proceeds from initial sales of receivables | **$ 639** | $ 661 | $ 614 |
| Servicing fees received | **9** | 8 | 7 |
| Cash flows received on retained interests | **34** | 15 | 33 |
| **Characteristics of securitized receivables:** | | | |
| At December 31: | | | |
| Total securitized principal balance | **$ 815** | $ 813 | $ 726 |
| Loans more than 30 days past due | **26** | 34 | 32 |
| Weighted average maturity (in months) | **28** | 27 | 29 |
| For the year ended December 31: | | | |
| Average securitized principal balance | **873** | 884 | 619 |
| Net credit losses | **4** | 6 | 5 |

**Equipment leased to others (primarily by Financial Products):**

| (Millions of dollars) | December 31, **2004** | 2003 | 2002 |
|---|---|---|---|
| Equipment leased to others — at original cost | **$3,975** | $ 3,609 | $ 2,996 |
| Less: Accumulated depreciation | **1,196** | 1,074 | 809 |
| Equipment leased to others — net | **$2,779** | $ 2,535 | $ 2,187 |

At December 31, 2004, scheduled minimum rental payments to be received for equipment leased to others were:

(Millions of dollars)

| 2005 | 2006 | 2007 | 2008 | 2009 | After 2009 |
|---|---|---|---|---|---|
| $603 | $438 | $278 | $150 | $70 | $31 |

## 11. Investment in unconsolidated affiliated companies

Our investment in affiliated companies accounted for by the equity method consists primarily of a 50% interest in Shin Caterpillar Mitsubishi Ltd. (SCM) located in Japan. Combined financial information of the unconsolidated affiliated companies accounted for by the equity method (generally on a three-month lag, e.g., SCM results reflect the periods ending September 30) was as follows:

| (Millions of dollars) | Years ended December 31, **2004** | 2003 | 2002 |
|---|---|---|---|
| Results of Operations: | | | |
| Sales | **$3,628** | $ 2,946 | $ 2,734 |
| Cost of goods sold | **2,788** | 2,283 | 2,168 |
| Gross profit | **840** | 663 | 566 |
| Profit (loss) | **$ 129** | $ 48 | $ (1) |
| Caterpillar's profit (loss) | **$ 59** | $ 20 | $ (4) |

| (Millions of dollars) | December 31, 2004 | 2003 | 2002 |
|---|---|---|---|
| Financial Position: | | | |
| Assets: | | | |
| Current assets | **$1,540** | $ 1,494 | $1,389 |
| Property, plant and equipment — net | **1,097** | 961 | 1,209 |
| Other assets | **145** | 202 | 493 |
| | **2,782** | 2,657 | 3,091 |
| Liabilities: | | | |
| Current liabilities | **$1,345** | $ 1,247 | $1,117 |
| Long-term debt due after one year | **276** | 343 | 808 |
| Other liabilities | **214** | 257 | 249 |
| | **1,835** | 1,847 | 2,174 |
| Ownership | **$ 947** | $ 810 | $ 917 |

**Caterpillar's investment in unconsolidated affiliated companies:**

| (Millions of dollars) | | | |
|---|---|---|---|
| Investment in equity method companies | **$ 487** | $ 432 | $ 437 |
| Plus: Investment in cost method companies | **30** | 368 | 310 |
| Investment in unconsolidated affiliated companies | **$ 517** | $ 800 | $ 747 |

At December 31, 2004, consolidated "Profit employed in the business" in Statement 2 included $153 million representing undistributed profit of the unconsolidated affiliated companies. In 2004, 2003 and 2002, we received $20 million, $25 million and $4 million, respectively, in dividends from unconsolidated affiliated companies.

Certain investments in unconsolidated affiliated companies are accounted for using the cost method. During first quarter 2001, Cat Financial invested for a limited partnership interest in a venture financing structure associated with Caterpillar's rental strategy in the United Kingdom. In the fourth quarter 2004, we sold our investment in this limited partnership. This sale had no impact on earnings.

## 12. Intangible assets and goodwill

### A. Intangible assets

Intangible assets are comprised of the following:

| (Millions of dollars) | 2004 | 2003 | 2002 |
|---|---|---|---|
| Intellectual property | **$ 213** | $ 126 | $ 137 |
| Pension-related | **120** | 157 | 191 |
| Other | **73** | — | — |
| Total intangible assets — gross | **406** | 283 | 328 |
| Less: Accumulated amortization of finite lived intangible assets | **(91)** | (44) | (47) |
| Intangible assets — net | **$ 315** | $ 239 | $ 281 |

During 2004 we acquired finite lived intangible assets of $130 million. (See Note 26 on page A-34 for details on the acquisition of these assets.) Amortization expense was $18 million, $15 million and $13 million for 2004, 2003 and 2002, respectively.

Amortization expense related to intangible assets is expected to be:

(Millions of dollars)

| 2005 | 2006 | 2007 | 2008 | 2009 | Thereafter |
|---|---|---|---|---|---|
| $22 | $21 | $18 | $16 | $15 | $104 |

### B. Goodwill

During 2004 we acquired assets with related goodwill of $55 million. (See Note 26 on page A-34 for details on the acquisition of these assets.) No goodwill was acquired during the years ended December 31, 2003 and 2002. During 2003 we disposed of assets with related goodwill of $3 million. No goodwill was disposed of during the years ended December 31, 2004 and 2002. On an annual basis, we test goodwill for impairment in accordance with Statement of Financial Accounting Standards No. 142 "Goodwill and Other Intangible Assets." No goodwill was impaired during the years ended December 31, 2004, 2003 and 2002.

## 13. Available-for-sale securities

Cat Insurance and Caterpillar Investment Management Ltd. had investments in certain debt and equity securities at December 31, 2004, 2003 and 2002, that have been classified as available-for-sale in accordance with SFAS 115 and recorded at fair value based upon quoted market prices. These fair values are included in "Other assets" in Statement 3. 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" in Statement 3). Realized gains and losses on sales of investments are generally determined using the specific identification method for debt instruments and the FIFO method for equity securities. Realized gains and losses are included in "Other income (expense)" in Statement 1.

| (Millions of dollars) | December 31, 2004 Cost Basis | Unrealized Pre-Tax Net Gains (Losses) | Fair Value |
|---|---|---|---|
| Government debt | $ 239 | $ (1) | $ 238 |
| Corporate bonds | 342 | — | 342 |
| Equity securities | 203 | 21 | 224 |
| | $ 784 | $ 20 | $ 804 |

| (Millions of dollars) | December 31, 2003 Cost Basis | Unrealized Pre-Tax Net Gains | Fair Value |
|---|---|---|---|
| Government debt | $ 102 | $ — | $ 102 |
| Corporate bonds | 288 | 3 | 291 |
| Equity securities | 191 | 21 | 212 |
| | $ 581 | $ 24 | $ 605 |

| (Millions of dollars) | December 31, 2002 Cost Basis | Unrealized Pre-Tax Net Gains (Losses) | Fair Value |
|---|---|---|---|
| Government debt | $ 89 | $ — | $ 89 |
| Corporate bonds | 208 | 1 | 209 |
| Equity securities | 220 | (51) | 169 |
| | $ 517 | $ (50) | $ 467 |

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

| | December 31, 2004 Less than 12 months[1] | | More than 12 months[1] | | Total | |
|---|---|---|---|---|---|---|
| (Millions of dollars) | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| Government debt | 166 | 1 | 9 | — | 175 | 1 |
| Corporate bonds | 156 | 2 | 35 | 1 | 191 | 3 |
| Equity securities | 46 | 1 | 2 | — | 48 | 1 |
| Total | $ 368 | $ 4 | $ 46 | $ 1 | $ 414 | $ 5 |

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

The fair value of available-for-sale debt securities at December 31, 2004, 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.

| (Millions of dollars) | Fair Value |
|---|---|
| Due in one year or less | $ 30 |
| Due after one year through five years | $273 |
| Due after five years through ten years | $ 50 |
| Due after ten years | $227 |

Proceeds from sales of investments in debt and equity securities during 2004, 2003 and 2002 were $408 million, $329 million and $288 million, respectively. Gross gains of $8 million, $3 million and $9 million and gross losses of $6 million, $2 million and $2 million have been included in current earnings as a result of these sales for 2004, 2003 and 2002, respectively.

During 2003 and 2002, we recognized pretax charges in accordance with the application of SFAS 115 for "other than temporary" declines in the market value of securities in the Cat Insurance and Caterpillar Investment Management Ltd. investment portfolios of $33 million and $41 million, respectively. During 2004, there were no pretax charges for "other than temporary" declines in the market value of securities.

## 14. Postemployment benefit plans

We have both U.S. and non-U.S. pension plans covering substantially all of our U.S. employees and a portion of our non-U.S. employees, primarily in our European facilities. Our defined benefit plans provide a benefit based on years of service and/or the employee's average earnings near retirement. Our defined contribution plans allow employees to contribute a portion of their salary to help save for retirement and, in certain cases, we provide a matching contribution.

We also have defined benefit retirement health care and life insurance plans covering substantially all of our U.S. employees. Plan amendments made in 2002 included an increase in retiree cost sharing of health care benefits, elimination of company payments for Medicare Part B premiums and significant reductions in retiree life insurance.

We use a November 30th measurement date for our U.S. pension and other postretirement benefit plans and a September 30th measurement date for all of our non-U.S. pension plans. Year-end asset and obligation amounts are disclosed as of the plan measurement dates.

### A. Benefit obligations

| | U.S. Pension Benefits | | | Non-U.S. Pension Benefits | | | Other Postretirement Benefits | | |
|---|---|---|---|---|---|---|---|---|---|
| (Millions of dollars) | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 |
| **Change in benefit obligation:** | | | | | | | | | |
| Benefit obligation, beginning of year | **$ 8,993** | $ 7,844 | $ 7,382 | **$ 1,836** | $ 1,517 | $ 1,229 | **$ 5,004** | $ 4,465 | $ 4,514 |
| Service cost | **143** | 122 | 115 | **53** | 43 | 38 | **66** | 70 | 80 |
| Interest cost | **548** | 554 | 529 | **97** | 83 | 70 | **265** | 298 | 292 |
| Plan amendments | **—** | (27) | — | **—** | — | — | **—** | (6) | (474) |
| Actuarial losses (gains) | **584** | 1,148 | 395 | **54** | 118 | 135 | **(64)** | 474 | 340 |
| Foreign currency exchange rates | **—** | — | — | **135** | 137 | 100 | **2** | 4 | 2 |
| Participant contributions | **—** | — | — | **11** | 10 | 10 | **58** | 25 | 5 |
| Benefits paid | **(675)** | (648) | (611) | **(89)** | (72) | (65) | **(405)** | (326) | (294) |
| Special termination benefits[1] | **—** | — | 34 | **—** | — | — | **—** | — | — |
| Benefit obligation, end of year | **$ 9,593** | $ 8,993 | $ 7,844 | **$ 2,097** | $ 1,836 | $ 1,517 | **$ 4,926** | $ 5,004 | $ 4,465 |
| Accumulated benefit obligation, end of year | **$ 9,040** | $ 8,379 | $ 7,482 | **$ 1,844** | $ 1,660 | $ 1,355 | | | |
| **Weighted-average assumptions used to determine benefit obligations, end of year:** | | | | | | | | | |
| Discount rate[2] | **5.9%** | 6.2% | 7.0% | **5.2%** | 5.1% | 5.4% | **5.9%** | 6.1% | 7.0% |
| Rate of compensation increase[2] | **4.0%** | 4.0% | 4.0% | **3.5%** | 3.2% | 3.3% | **4.0%** | 4.0% | 4.0% |

[1] Amount recognized as expense in 2001 in conjunction with a planned U.S. salaried and management employee reduction that took place in 2002.
[2] End of year rates are used to determine net periodic cost for the subsequent year. See Note 14E on page A-23.

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

| (Millions of dollars) | One-percentage-point increase | One-percentage-point decrease |
|---|---|---|
| Effect on 2004 service and interest cost components of other postretirement benefit cost | $ 23 | $ (21) |
| Effect on accumulated postretirement benefit obligation | $306 | $(271) |

## B. Plan assets

| (Millions of dollars) | U.S. Pension Benefits 2004 | 2003 | 2002 | Non-U.S. Pension Benefits 2004 | 2003 | 2002 | Other Postretirement Benefits 2004 | 2003 | 2002 |
|---|---|---|---|---|---|---|---|---|---|
| **Change in plan assets:** | | | | | | | | | |
| Fair value of plan assets, beginning of year | **$ 7,728** | $ 6,443 | $ 7,431 | **$ 1,262** | $ 1,024 | $ 1,050 | **$ 867** | $ 849 | $ 1,109 |
| Actual return on plan assets | **1,106** | 1,290 | (512) | **124** | 120 | (87) | **118** | 140 | (113) |
| Foreign currency exchange rates | **—** | — | — | **91** | 96 | 72 | **—** | — | — |
| Company contributions | **566** | 643 | 135 | **104** | 84 | 44 | **356** | 179 | 142 |
| Participant contributions | **—** | — | — | **11** | 10 | 10 | **58** | 25 | 5 |
| Benefits paid | **(675)** | (648) | (611) | **(89)** | (72) | (65) | **(405)** | (326) | (294) |
| Fair value of plan assets, end of year | **$ 8,725** | $ 7,728 | $ 6,443 | **$ 1,503** | $ 1,262 | $ 1,024 | **$ 994** | $ 867 | $ 849 |

The asset allocation for our pension and other postretirement benefit plans at the end of 2004, 2003 and 2002, and the target allocation for 2005, by asset category, are as follows:

| | Target Allocation 2005 | Percentage of Plan Assets at Year End 2004 | 2003 | 2002 |
|---|---|---|---|---|
| **U.S. pension:** | | | | |
| Equity securities | 70% | **74%** | 75% | 70% |
| Debt securities | 30% | **26%** | 25% | 29% |
| Real estate | — | **—** | — | 1% |
| Total | 100% | **100%** | 100% | 100% |
| **Non-U.S. pension:** | | | | |
| Equity securities | 55% | **54%** | 56% | 54% |
| Debt securities | 38% | **38%** | 39% | 41% |
| Real estate | 7% | **6%** | 4% | 3% |
| Other | — | **2%** | 1% | 2% |
| Total | 100% | **100%** | 100% | 100% |
| **Other postretirement benefits:** | | | | |
| Equity securities | 80% | **84%** | 84% | 79% |
| Debt securities | 20% | **16%** | 16% | 21% |
| Total | 100% | **100%** | 100% | 100% |

Our target asset allocations reflect our investment strategy of maximizing the long-term rate of return on plan assets and the resulting funded status, within an appropriate level of risk. The U.S. plans are rebalanced to plus or minus five percentage points of the target asset allocation ranges on a monthly basis. The frequency of rebalancing for the non-U.S. plans varies depending on the plan.

Equity securities within plan assets include Caterpillar Inc. common stock in the amounts of:

| (Millions of dollars) | U.S. Pension Benefits[1] 2004 | 2003 | 2002 | Other Postretirement Benefits 2004 | 2003 | 2002 |
|---|---|---|---|---|---|---|
| Caterpillar Inc. common stock | **$ 299** | $ 245 | $ 154 | **$ 1** | $ 2 | $ 1 |

[1] Amounts represent 3% of total plan assets for 2004 and 2003, and 2% for 2002.

## C. Funded status

The funded status of the plans, reconciled to the amount reported on the Consolidated Financial Position, is as follows:

| (Millions of dollars) End of Year | U.S. Pension Benefits 2004 | 2003 | 2002 | Non-U.S. Pension Benefits 2004 | 2003 | 2002 | Other Postretirement Benefits 2004 | 2003 | 2002 |
|---|---|---|---|---|---|---|---|---|---|
| Fair value of plan assets | **$ 8,725** | $ 7,728 | $ 6,443 | **$ 1,503** | $ 1,262 | $ 1,024 | **$ 994** | $ 867 | $ 849 |
| Benefit obligations | **9,593** | 8,993 | 7,844 | **2,097** | 1,836 | 1,517 | **4,926** | 5,004 | 4,465 |
| Over (under) funded status | **(868)** | (1,265) | (1,401) | **(594)** | (574) | (493) | **(3,932)** | (4,137) | (3,616) |
| Amounts not yet recognized: | | | | | | | | | |
| Unrecognized prior service cost (benefit) | **158** | 202 | 278 | **27** | 31 | 33 | **(232)** | (280) | (283) |
| Unrecognized net actuarial loss | **2,552** | 2,518 | 2,009 | **726** | 677 | 547 | **1,232** | 1,364 | 976 |
| Unrecognized net obligation existing at adoption of SFAS 87/106 | **—** | — | — | **3** | 6 | 9 | **16** | 17 | — |
| Contributions made after measurement date | **—** | 1 | — | **22** | 14 | 22 | **27** | 57 | 20 |
| Net amount recognized in financial position | **$ 1,842** | $ 1,456 | $ 886 | **$ 184** | $ 154 | $ 118 | **$(2,889)** | $ (2,979) | $ (2,903) |

| (Millions of dollars) | U.S. Pension Benefits | | | Non-U.S. Pension Benefits | | | Other Postretirement Benefits | | |
|---|---|---|---|---|---|---|---|---|---|
| **End of Year** | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 |
| **Components of net amount recognized in financial position:** | | | | | | | | | |
| Prepaid benefit costs | **$ 1,099** | $ 1,136 | $ 1,071 | **$ 28** | $ 61 | $ 52 | **$ —** | $ — | $ — |
| Accrued benefit liabilities | **(97)** | (548) | (735) | **(173)** | (127) | (89) | **(402)** | (341) | (289) |
| Intangible assets | **95** | 127 | 156 | **25** | 30 | 35 | **—** | — | — |
| Liability for postemployment benefits | **(248)** | (136) | (361) | **(181)** | (327) | (279) | **(2,487)** | (2,638) | (2,614) |
| Accumulated other comprehensive income (pretax) | **993** | 877 | 755 | **485** | 517 | 399 | **—** | — | — |
| Net asset (liability) recognized | **$ 1,842** | $ 1,456 | $ 886 | **$ 184** | $ 154 | $ 118 | **$(2,889)** | $ (2,979) | $ (2,903) |

The following amounts relate to our pension plans with projected benefit obligations in excess of plan assets:

| | U.S. Pension Benefits at Year-end | | | Non-U.S. Pension Benefits at Year-end | | |
|---|---|---|---|---|---|---|
| (Millions of dollars) | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 |
| Projected benefit obligation | **$ (9,593)** | $ (8,993) | $ (7,844) | **$ (2,059)** | $ (1,800) | $ (1,497) |
| Accumulated benefit obligation | **$ (9,040)** | $ (8,379) | $ (7,482) | **$ (1,813)** | $ (1,633) | $ (1,338) |
| Fair value of plan assets | **$ 8,725** | $ 7,728 | $ 6,443 | **$ 1,455** | $ 1,216 | $ 995 |

The following amounts relate to our pension plans with accumulated benefit obligations in excess of plan assets:

| | U.S. Pension Benefits at Year-end | | | Non-U.S. Pension Benefits at Year-end | | |
|---|---|---|---|---|---|---|
| (Millions of dollars) | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 |
| Projected benefit obligation | **$ (3,975)** | $ (3,785) | $ (3,439) | **$ (2,003)** | $ (1,761) | $ (1,490) |
| Accumulated benefit obligation | **$ (3,959)** | $ (3,751) | $ (3,416) | **$ (1,767)** | $ (1,601) | $ (1,334) |
| Fair value of plan assets | **$ 3,614** | $ 3,083 | $ 2,345 | **$ 1,406** | $ 1,181 | $ 990 |

The accumulated postretirement benefit obligation exceeds plan assets for all of our other postretirement benefit plans.

### D. Expected cash flow

Information about the expected cash flow for the pension and other postretirement benefit plans follows:

| (Millions of dollars) | U.S. Pension Benefits | Non-U.S. Pension Benefits | Other Postretirement Benefits |
|---|---|---|---|
| **Employer contributions:** | | | |
| 2005 (expected) | $ 30 | $ 140 | $ 360 |
| **Expected benefit payments:** | | | |
| 2005 | 670 | 60 | 360 |
| 2006 | 680 | 60 | 380 |
| 2007 | 680 | 70 | 390 |
| 2008 | 690 | 80 | 400 |
| 2009 | 690 | 80 | 420 |
| 2010-2014 | 3,470 | 460 | 2,160 |
| Total | $ 6,880 | $ 810 | $ 4,110 |

The above table reflects the total benefits expected to be paid from the plan or from company assets and does not include the participants' share of the cost. The expected benefit payments for our other postretirement benefits include payments for prescription drug benefits. Expected Medicare Part D subsidy receipts are as follows:

| (Millions of dollars) | 2005 | 2006 | 2007 | 2008 | 2009 | 2010-2014 | Total |
|---|---|---|---|---|---|---|---|
| Other postretirement benefits | $ — | $ 20 | $ 20 | $ 20 | $ 30 | $ 160 | $ 250 |

### E. Net periodic cost

| (Millions of dollars) | U.S. Pension Benefits 2004 | 2003 | 2002 | Non-U.S. Pension Benefits 2004 | 2003 | 2002 | Other Postretirement Benefits 2004 | 2003 | 2002 |
|---|---|---|---|---|---|---|---|---|---|
| **Components of net periodic benefit cost:** | | | | | | | | | |
| Service cost | **$ 143** | $ 122 | $ 115 | **$ 53** | $ 43 | $ 38 | **$ 66** | $ 70 | $ 80 |
| Interest cost | **548** | 554 | 529 | **97** | 83 | 70 | **265** | 298 | 292 |
| Expected return on plan assets | **(697)** | (680) | (783) | **(103)** | (94) | (94) | **(74)** | (88) | (115) |
| Amortization of: | | | | | | | | | |
| Net asset existing at adoption of SFAS 87/106 | **—** | — | — | **3** | 3 | (2) | **2** | — | — |
| Prior service cost[1] | **44** | 49 | 50 | **6** | 5 | 5 | **(48)** | (47) | (22) |
| Net actuarial loss (gain) | **142** | 27 | (1) | **38** | 14 | — | **45** | 36 | 5 |
| Total cost (benefit) included in operating profit | **$ 180** | $ 72 | $ (90) | **$ 94** | $ 54 | $ 17 | **$ 256** | $ 269 | $ 240 |
| **Weighted-average assumptions used to determine net cost:** | | | | | | | | | |
| Discount rate | **6.2%** | 7.0% | 7.3% | **5.1%** | 5.4% | 5.7% | **6.1%** | 7.0% | 7.2% |
| Expected return on plan assets[2] | **9.0%** | 9.0% | 9.8% | **7.4%** | 7.1% | 7.6% | **9.0%** | 9.0% | 9.8% |
| Rate of compensation increase | **4.0%** | 4.0% | 4.0% | **3.2%** | 3.3% | 3.3% | **4.0%** | 4.0% | 4.0% |

[1] Prior service costs are amortized using the straight-line method over the average remaining service period to the full retirement eligibility date of employees expected to receive benefits from the plan amendment.
[2] The weighted-average rates for 2005 are 9.0% and 7.4% for U.S. and non-U.S. plans, respectively.

Our U.S. expected long-term rate of return on plan assets is based on our estimate of long-term passive returns for equities and fixed income securities weighted by the allocation of our pension assets. Based on historical performance, we increase the passive returns due to our active management of the plan assets. To arrive at our expected long-term return, the amount added for active management was 1% for 2004, 2003 and 2002. A similar process is used to determine this rate for our non-U.S. plans.

The assumed health care trend rate represents the rate at which health care costs are assumed to increase. To calculate the 2004 benefit expense, we assumed an increase of 8.5% for 2004. This rate was assumed to decrease gradually to the ultimate health care trend rate of 4.5% in 2009. This rate represents 2.5% general inflation plus 2.0% additional health care inflation. Based on our recent expenses and our forecast of changes, we expect an increase of 8.4% during 2005 with a gradual decrease to the ultimate health care trend rate of 5.0% in 2012. The revised ultimate rate represents 3.0% general inflation plus 2.0% additional health care inflation.

Our U.S. postretirement health care plans provide for prescription drug benefits. On December 8, 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act) was signed into law. The Act introduces a prescription drug benefit under Medicare (Medicare Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. In January 2004, the FASB issued FASB Staff Position No. 106-1 (FSP 106-1), "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003." As permitted by FSP 106-1, we made a one-time election to defer accounting for the effects of the Act pending further guidance from the FASB.

In May 2004, the FASB issued FASB Staff Position No. 106-2 (FSP 106-2), which superseded FSP 106-1. FSP 106-2 provides accounting guidance to employers that have determined that prescription drug benefits available under their retiree health care benefit plans are at least actuarially equivalent to Medicare Part D. The FSP requires that the benefit attributable to past service be accounted for as an actuarial gain and the benefit related to current service be reported as a reduction in service cost.

We have determined that most of our U.S. retiree health care plans are at least actuarially equivalent to Medicare Part D and will qualify for the federal subsidy. In the third quarter of 2004, we adopted FSP 106-2 retroactive to December 31, 2003 (the period end that includes the date of the Act's enactment) as permitted by the FSP. The impact was a reduction in our accumulated postretirement benefit obligation of $284 million related to benefits attributed to past service. The reduction in the components of 2004 net periodic postretirement benefits expense was as follows:

| (Millions of dollars) | 2004 |
|---|---|
| Service cost | **$ 4** |
| Interest cost | **18** |
| Amortization of actuarial gain | **29** |
| Total reduction in net periodic postretirement benefit cost | **$ 51** |

### F. Other postemployment benefit plans

We offer long-term disability benefits, continued health care for disabled employees, survivor income benefits insurance and supplemental unemployment benefits to substantially all eligible U.S. employees.

### G. Summary of long-term liability:

| (Millions of dollars) | December 31, 2004 | 2003 | 2002 |
|---|---|---|---|
| Pensions: | | | |
| U.S. pensions | **$ 248** | $ 136 | $ 361 |
| Non-U.S. pensions | **181** | 327 | 279 |
| Total pensions | **429** | 463 | 640 |
| Postretirement benefits other than pensions | **2,487** | 2,638 | 2,614 |
| Other postemployment benefits | **70** | 71 | 79 |
| | **$2,986** | $ 3,172 | $3,333 |

### H. Defined contribution plans

We have both U.S. and non-U.S. employee defined contribution plans to help employees save for retirement. In January 2003, we introduced a company match to our U.S. 401(k) plan. This plan allows eligible employees to contribute a portion of their salary to the plan on a tax-deferred basis, and we provide a matching contribution equal to 100% of employee contributions to the plan up to 6% of their compensation.

Various other U.S. and non-U.S. defined contribution plans allow eligible employees to contribute a portion of their salary to the plans and, in some cases, we provide a matching contribution to the funds.

Total company costs related to U.S. and non-U.S. defined contribution plans were:

| (Millions of dollars) | **2004** | 2003 | 2002 |
|---|---|---|---|
| U.S. plans | **$ 110** | $ 106 | $ 28 |
| Non-U.S. plans | **11** | 11 | 7 |
| | **$ 121** | $ 117 | $ 35 |

## 15. Short-term borrowings

| (Millions of dollars) | December 31, **2004** | 2003 | 2002 |
|---|---|---|---|
| Machinery and Engines: | | | |
| Notes payable to banks | **$ 93** | $ 72 | $ 64 |
| Financial Products: | | | |
| Notes payable to banks | **370** | 183 | 174 |
| Commercial paper | **2,972** | 2,087 | 1,682 |
| Collateralized trust obligation | **240** | — | — |
| Demand notes | **482** | 415 | 255 |
| | **4,064** | 2,685 | 2,111 |
| Total short-term borrowings | **$4,157** | $ 2,757 | $ 2,175 |

See Note 6 on page A-16 for further discussion of the collateralized trust obligation.

The weighted average interest rates on external short-term borrowings outstanding were:

| | December 31, **2004** | 2003 | 2002 |
|---|---|---|---|
| Notes payable to banks | **5.9%** | 6.5% | 5.7% |
| Commercial paper | **2.5%** | 2.1% | 2.5% |
| Collateralized trust obligation | **2.3%** | — | — |
| Demand notes | **2.3%** | 2.3% | 2.8% |

Please refer to Note 20 on pages A-25 to A-26 and Table III on page A-27 for fair value information on short-term borrowings.

## 16. Long-term debt

| (Millions of dollars) | December 31, **2004** | 2003 | 2002 |
|---|---|---|---|
| Machinery and Engines: | | | |
| Notes — 6.550% due 2011 | **$ 250** | $ 250 | $ 249 |
| Debentures — 9.000% due 2006 | **206** | 208 | 209 |
| Debentures — 6.000% due 2007 | **—** | — | 189 |
| Debentures — 7.250% due 2009 | **313** | 315 | 318 |
| Debentures — 9.375% due 2011 | **123** | 123 | 123 |
| Debentures — 9.375% due 2021 | **236** | 236 | 236 |
| Debentures — 8.000% due 2023 | **199** | 199 | 199 |
| Debentures — 6.625% due 2028 | **299** | 299 | 299 |
| Debentures — 7.300% due 2031 | **348** | 348 | 348 |
| Debentures — 6.950% due 2042 | **249** | 249 | 249 |
| Debentures — 7.375% due 2097 | **297** | 297 | 297 |
| Medium-term notes | **—** | — | 25 |
| Capital lease obligations | **665** | 611 | 538 |
| Commercial paper | **40** | 45 | — |
| Deposit obligations | **245** | 236 | 178 |
| Other | **193** | 187 | 124 |
| Total Machinery and Engines | **3,663** | 3,603 | 3,581 |
| Financial Products: | | | |
| Commercial paper | **$ 1,400** | $ 1,825 | $ 1,825 |
| Medium-term notes | **10,468** | 8,775 | 6,298 |
| Deposit obligations | **232** | 232 | — |
| Other | **74** | 111 | 70 |
| Total Financial Products | **12,174** | 10,943 | 8,193 |
| Total long-term debt due after one year | **$15,837** | $ 14,546 | $ 11,774 |

All outstanding notes and debentures are unsecured. The capital lease obligations are collateralized by leased manufacturing equipment and/or security deposits. The deposit obligations have corresponding security deposits, which are included in "Other assets" in Statement 3. These deposit obligations and corresponding security deposits relate to two finance arrangements which provide us a return. These finance arrangements require that we commit to certain long-term obligations and provide security deposits which will fulfill these obligations when they become due.

The 6% debentures due in 2007 were sold at significant original issue discounts ($144 million). This issue was carried net of the unamortized portion of its discount, which was amortized as interest expense over the life of the issue. These debentures had a principal at maturity of $250 million and an effective annual rate of 13.3%. The debentures were redeemed in August 2003.

We may redeem the 6.55% notes and the 7.25%, 6.625%, 7.3%, 6.95% and 7.375% debentures in whole or in part at our option at any time at a redemption price equal to the greater of 100% of the principal amount of the debentures to be redeemed or the sum of the present value of the remaining scheduled payments.

The terms of other notes and debentures do not specify a redemption option prior to maturity.

Based on long-term credit agreements, $1,440 million, $1,870 million and $1,825 million of commercial paper outstanding at December 31, 2004, 2003 and 2002, respectively, was classified as long-term debt due after one year.

Medium-term notes are offered by prospectus and are issued through agents at fixed and floating rates. Financial Products medium-term notes have a weighted average interest rate of 3.3% with remaining maturities up to 20 years at December 31, 2004.

The aggregate amounts of maturities of long-term debt during each of the years 2005 through 2009, including amounts due within one year and classified as current, are:

| (Millions of dollars) | December 31, 2005 | 2006 | 2007 | 2008 | 2009 |
|---|---|---|---|---|---|
| Machinery and Engines | $ 6 | $ 290 | $ 297 | $ 26 | $ 363 |
| Financial Products | 3,525 | 4,137 | 2,567 | 1,134 | 3,103 |
| | $ 3,531 | $ 4,427 | $ 2,864 | $ 1,160 | $ 3,466 |

Interest paid on short-term and long-term borrowings for 2004, 2003 and 2002 was $766 million, $718 million and $815 million, respectively.

Financial Products was in compliance with all debt covenants at December 31, 2004 except Cat Financial's debt-to-equity ratio, as defined under the global credit facilities, which was 8.23 to 1 at December 31, 2004. By covenant, this is not to exceed 8.00 to 1 at year-end (8.5 to 1 moving six-month average at other than year-end). At December 31, 2004, there were no borrowings under these facilities. The higher year-end ratio was primarily the result of unexpected record levels of financing activity in the fourth quarter. Cat Financial received a waiver from its banks for said failure.

Please refer to Note 20 on pages A-25 to A-26 and Table III on page A-27 for fair value information on long-term debt.

## 17. Credit commitments

| (Millions of dollars) | Consolidated | Machinery and Engines | Financial Products |
|---|---|---|---|
| | December 31, 2004 | | |
| Credit lines available: | | | |
| Global credit facilities | $5,000 [1] | $ 600 [1] | $4,400 [1] |
| Other external | 1,849 | 758 | 1,091 |
| Total credit lines available | 6,849 | 1,358 | 5,491 |
| Less: Global credit facilities supporting commercial paper | 4,412 | 40 | 4,372 |
| Less: Utilized credit | 463 | 93 | 370 |
| Available credit | $1,974 | $1,225 | $ 749 |

[1] We have two global credit facilities with a syndicate of banks totaling $5,000 million available in the aggregate to both Machinery and Engines and Financial Products to support commercial paper programs. Based on management's allocation decision, which can be revised at any time during the year, the portion of the facility available to Cat Financial at December 31, 2004 was $4,400 million. The five-year facility of $2,500 million expires in September 2009. The 364-day facility of $2,500 million expires in September 2005. The facility expiring in September 2005 has a provision that allows Caterpillar or Cat Financial to obtain a one-year loan in September 2005 that would mature in September 2006.

## 18. Capital stock

### A. Stock options

In 1996, stockholders approved the Stock Option and Long-Term Incentive Plan (the Plan) providing for the granting of options to purchase common stock to officers and other key employees, as well as non-employee directors. The Plan reserves 72 million shares of common stock for issuance (64 million under the Plan and 8 million under prior stock option plans). Options granted prior to 2004 vest at the rate of one-third per year over the three year period following the date of grant. In anticipation of delaying vesting until three years after the grant date for future grants, the 2004 grant vested on December 31, 2004. All grants continue to have a maximum term of 10 years. Common shares issued under stock options, including treasury shares reissued, totaled 6,103,710 for 2004, 4,925,496 for 2003 and 882,580 for 2002. We recognized income tax benefits related to employees' exercise of stock options of $80 million, $45 million, and $13 million in 2004, 2003 and 2002, respectively.

The Plan grants options which have exercise prices equal to the average market price on the date of grant. A summary of the pro forma net income and profit per share amounts is shown in Item M of Note 1 on pages A-11 to A-12. The fair value of options granted in 2004 was estimated at the date of grant using the binomial option-pricing model. We believe this model more accurately reflects the value of the options than using the Black-Scholes option-pricing model. Previous years' grants continue to be valued using the Black-Scholes model.

Please refer to Table II on page A-26 for additional financial information on our stock options.

### B. Restricted stock

The Plan permits the award of restricted stock to officers and other key employees. During 2004, 2003 and 2002, officers and other key employees were awarded 44,350 shares, 42,210 shares and 52,475 shares, respectively, of restricted stock. Restricted shares (in phantom form) awarded to officers and other key employees totaled 7,400, 4,425 and 8,450 in 2004, 2003 and 2002, respectively.

### C. Stockholders' rights plan

We are authorized to issue 5,000,000 shares of preferred stock, of which 2,000,000 shares have been designated as Series A Junior Participating Preferred Stock of $1 par value. None of the preferred shares have been issued.

Stockholders would receive certain preferred stock purchase rights if someone acquired or announced a tender offer to acquire 15% or more of outstanding Caterpillar stock. In essence, those rights would permit each holder (other than the acquiring person) to purchase one share of Caterpillar stock at a 50% discount for every share owned. The rights, designed to protect the interests of Caterpillar stockholders during a takeover attempt, expire December 11, 2006.

## 19. Profit per share

**Computations of profit per share:**

| (Dollars in millions except per share data) | **2004** | 2003 | 2002 |
|---|---|---|---|
| Profit for the period (A) | **$2,035** | $ 1,099 | $ 798 |
| Determination of shares (millions): | | | |
| Weighted average number of common shares outstanding (B) | **342.3** | 345.2 | 344.0 |
| Shares issuable on exercise of stock options, net of shares assumed to be purchased out of proceeds at average market price | **11.4** | 6.2 | 2.9 |
| Average common shares outstanding for fully diluted computation (C) | **353.7** | 351.4 | 346.9 |
| Profit per share of common stock: | | | |
| Assuming no dilution (A/B) | **$ 5.95** | $ 3.18 | $ 2.32 |
| Assuming full dilution (A/C) | **$ 5.75** | $ 3.13 | $ 2.30 |
| Shares outstanding as of December 31 (in millions) | **342.9** | 343.8 | 344.3 |

Stock options to purchase 52,000, 4,267,544 and 27,881,279 shares of common stock at a weighted-average price of $81.27, $62.34 and $54.34 were outstanding during 2004, 2003 and 2002, respectively, but were not included in the computation of diluted profit per share because the options' exercise price was greater than the average market price of the common shares.

## 20. Fair values of financial instruments

We used the following methods and assumptions to estimate the fair value of our financial instruments:

**Cash and short-term investments** — carrying amount approximated fair value.

**Long-term investments (other than investments in unconsolidated affiliated companies)** — fair value for available for sale securities was estimated based on quoted market prices. Fair value for security deposits approximated carrying value.

**Foreign currency forward and option contracts** — fair value of forward contracts was determined by discounting the future cash flow resulting from the differential between the contract price and the forward rate. Fair value of option contracts was determined by using the Black-Scholes model.

**Finance receivables** — fair value was estimated by discounting the future cash flow using current rates, representative of receivables with similar remaining maturities. Historical bad-debt experience also was considered.

**Wholesale inventory receivables** — fair value was estimated by discounting the future cash flow using current rates, representative of receivables with similar remaining maturities.

**TABLE II — Financial Information Related to Capital Stock**

**Changes in the status of common shares subject to issuance under options:**

| | **2004** Shares | **2004** Weighted-Average Exercise Price | 2003 Shares | 2003 Weighted-Average Exercise Price | 2002 Shares | 2002 Weighted-Average Exercise Price |
|---|---|---|---|---|---|---|
| Fixed Options: | | | | | | |
| Outstanding at beginning of year | **39,499,672** | **$ 51.38** | 38,721,364 | $ 48.91 | 32,295,230 | $ 47.34 |
| Granted to officers and key employees | **8,890,733** | **$ 77.26** | 8,418,100 | $ 54.29 | 8,050,864 | $ 50.72 |
| Granted to outside directors | **52,000** | **$ 81.27** | 56,000 | $ 52.06 | 52,000 | $ 58.87 |
| Exercised | **(6,825,920)** | **$ 47.72** | (7,629,020) | $ 42.04 | (1,580,754) | $ 26.41 |
| Lapsed | **(392,311)** | **$ 51.19** | (66,772) | $ 50.18 | (95,976) | $ 50.28 |
| Outstanding at end of year | **41,224,174** | **$ 57.61** | 39,499,672 | $ 51.38 | 38,721,364 | $ 48.91 |
| Options exercisable at year-end | **33,620,616** | **$ 58.57** | 23,650,987 | $ 50.28 | 23,909,130 | $ 48.23 |
| Weighted-average fair value of options granted during the year | **$ 18.06** | | $ 12.82 | | $ 14.85 | |

**Stock options outstanding and exercisable:**

| Exercise Prices | Options Outstanding: # Outstanding at 12/31/04 | Options Outstanding: Weighted-Average Remaining Contractual Life (Years) | Options Outstanding: Weighted-Average Exercise Price | Options Exercisable: # Outstanding at 12/31/04 | Options Exercisable: Weighted-Average Exercise Price |
|---|---|---|---|---|---|
| $27.91-$39.19 | 3,948,490 | 4.4 | $36.88 | 3,948,490 | $36.88 |
| $43.75-$62.34 | 28,332,951 | 6.5 | $54.29 | 20,781,393 | $54.69 |
| $77.26-$81.27 | 8,942,733 | 9.4 | $77.28 | 8,890,733 | $77.26 |
| | 41,224,174 | | $57.61 | 33,620,616 | $58.57 |

**Weighted-average assumptions used in determining fair value of option grants:**

| | Grant Year **2004**[1] | 2003[2] | 2002[2] |
|---|---|---|---|
| Dividend yield | **1.88-1.91%** | 2.75% | 2.55% |
| Expected volatility | **25.8-28.1%** | 29.6% | 35.0% |
| Risk-free interest rates | **1.90-5.76%** | 2.52% | 4.13% |
| Expected lives | **6 years** | 6 years | 5 years |

[1] Assumptions used in the binomial option-pricing model valuation.
[2] Assumptions used in Black-Scholes valuation.

**Short-term borrowings** — carrying amount approximated fair value.

**Long-term debt** — for Machinery and Engines notes and debentures, fair value was estimated based on quoted market prices. For Financial Products, fair value was estimated by discounting the future cash flow using our current borrowing rates for similar types and maturities of debt, except for floating rate notes and commercial paper supported by long-term credit agreements for which the carrying amounts were considered a reasonable estimate of fair value. For deposit obligations carrying value approximated fair value.

**Interest rate swaps** — fair value was estimated based on the amount that we would receive or pay to terminate our agreements as of year-end.

**Guarantees** — fair value is estimated based on the premium we would require to issue the same guarantee in a stand alone arm's-length transaction with an unrelated party.

Please refer to Table III on page A-27 for the fair values of our financial instruments.

## 21. Concentration of credit risk

Financial instruments with potential credit risk consist primarily of trade and finance receivables and short-term and long-term investments. Additionally, to a lesser extent, we have a potential credit risk associated with counterparties to derivative contracts.

Trade receivables are primarily short-term receivables from independently owned and operated dealers which arise in the normal course of business. We perform regular credit evaluations of our dealers. Collateral generally is not required, and the majority of our trade receivables are unsecured. We do, however, when deemed necessary, make use of various devices such as security agreements and letters of credit to protect our interests. No single dealer or customer represents a significant concentration of credit risk.

Finance receivables and wholesale inventory receivables primarily represent receivables under installment sales contracts, receivables arising from leasing transactions and notes receivable. We generally maintain a secured interest in the equipment financed. No single customer or region represents a significant concentration of credit risk.

Short-term and long-term investments are held with high quality institutions and, by policy, the amount of credit exposure to any one institution is limited. Long-term investments, included in "Other assets" in Statement 3, are comprised primarily of investments which collateralize capital lease obligations and deposit obligations (see Note 16 on page A-24) and investments of Cat Insurance supporting insurance reserve requirements.

For derivatives contracts, collateral is not required of the counterparties or of our company. We do not anticipate nonperformance by any of the counterparties. Our exposure to credit loss in the event of nonperformance by the counterparties is limited to only those gains that we have recorded, but have not yet received cash payment. At December 31, 2004, 2003 and 2002, the exposure to credit loss was $312 million, $336 million and $176 million, respectively.

Please refer to Note 20 on pages A-25 to A-26 and Table III below for fair value information.

## 22. Operating leases

We lease certain computer and communications equipment, transportation equipment and other property through operating leases. Total rental expense for operating leases was $271 million, $242 million and $240 million for 2004, 2003 and 2002, respectively.

Minimum payments for operating leases having initial or remaining non-cancelable terms in excess of one year are:

Years ended December 31, (Millions of dollars)

| 2005 | 2006 | 2007 | 2008 | 2009 | After 2009 | Total |
|---|---|---|---|---|---|---|
| $163 | $132 | $90 | $69 | $59 | $384 | $897 |

## 23. Guarantees and product warranty

We have guaranteed to repurchase loans of certain Caterpillar dealers from third party lenders in the event of default. These guarantees arose in conjunction with Cat Financial's relationship with third party dealers who sell Caterpillar equipment. These guarantees have terms ranging from one to four years and are secured primarily by dealer assets.

In 2004, Cat Financial provided a limited indemnity to a third party bank for $45 million resulting from the assignment of certain leases to that bank. The indemnity is for the remote chance that the insurers of these leases would become insolvent. The indemnity/guarantee is for eight years and is unsecured.

No loss has been experienced or is anticipated under any of these guarantees. At December 31, 2004, 2003 and 2002, the related book value was $10 million, $5 million and $0, 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 at December 31 are as follows:

| (Millions of dollars) | **2004** | 2003 | 2002 |
|---|---|---|---|
| Guarantees with Caterpillar dealers | **$ 364** | $ 380 | $ 290 |
| Guarantees — other | **62** | 37 | 34 |
| Total guarantees | **$ 426** | $ 417 | $ 324 |

Our product warranty liability is determined by applying historical claim rate experience to the current field population and dealer inventory. Historical claim rates are developed using a rolling average of actual warranty payments. Effective in the third quarter of 2004, we refined our process to utilize more detailed claim rates by product. This provides more comprehensive product

**TABLE III — Fair Values of Financial Instruments**

| (Millions of dollars) | **2004** Carrying Amount | **2004** Fair Value | 2003 Carrying Amount | 2003 Fair Value | 2002 Carrying Amount | 2002 Fair Value | Reference |
|---|---|---|---|---|---|---|---|
| Asset (Liability) at December 31 | | | | | | | |
| Cash and short-term investments | **$ 445** | **$ 445** | $ 342 | $ 342 | $ 309 | $ 309 | Statement 3 |
| Long-term investments | **1,852** | **1,852** | 1,574 | 1,574 | 1,089 | 1,089 | Notes 13 and 21 |
| Foreign currency contracts | **176** | **176** | 167 | 167 | 47 | 47 | Note 3 |
| Finance receivables — net (excluding finance type leases[1]) | **13,457** | **13,445** | 11,439 | 11,489 | 10,098 | 10,168 | Note 8 |
| Wholesale inventory receivables — net (excluding finance type leases[1]) | **882** | **857** | 681 | 666 | 637 | 641 | Note 7 |
| Short-term borrowings | **(4,157)** | **(4,157)** | (2,757) | (2,757) | (2,175) | (2,175) | Note 15 |
| Long-term debt (including amounts due within one year) | | | | | | | |
| Machinery and Engines | **(3,669)** | **(4,186)** | (3,635) | (4,109) | (3,839) | (4,363) | Note 16 |
| Financial Products | **(15,699)** | **(15,843)** | (13,892) | (14,078) | (11,847) | (12,118) | Note 16 |
| Interest rate swaps | | | | | | | |
| Financial Products — | | | | | | | |
| in a net receivable position | **75** | **75** | 87 | 87 | 84 | 84 | Note 3 |
| in a net payable position | **(69)** | **(69)** | (59) | (59) | (85) | (85) | Note 3 |
| Guarantees[2] | **(10)** | **(10)** | (5) | (9) | — | (6) | Note 23 |

[1] Total excluded items have a net carrying value at December 31, 2004, 2003 and 2002 of $1,737 million, $1,546 million and $1,369 million, respectively.

[2] The carrying amount provisions of FASB Interpretation No. 45 related to guarantees are effective for guarantees issued or modified subsequent to December 31, 2002 only, whereas the fair value amount is for all guarantees.

warranty information for management. This change did not have a material impact on our financial statements.

| (Millions of dollars) | **2004** | 2003 | 2002 |
|---|---|---|---|
| Warranty liability, January 1 | **$ 622** | $ 693 | $ 652 |
| Payments | **(535)** | (484) | (494) |
| Provision for warranty | **695** | 413 | 535 |
| Warranty liability, December 31 | **$ 782** | $ 622 | $ 693 |

## 24. Environmental and legal matters

The company is regulated by federal, state and international environmental laws governing our use of substances and control of emissions in all our operations. Compliance with these existing laws has not had a material impact on our capital expenditures or earnings.

We are cleaning up hazardous waste at a number of locations, often with other companies, pursuant to federal and state laws. When it is likely we will pay clean-up costs at a site and those costs can be estimated, the costs are charged against our earnings. In formulating that estimate, we do not consider amounts expected to be recovered from insurance companies and others.

The amount recorded for environmental clean-up is not material and is included in "Accrued expenses" in Statement 3. If a range of liability estimates is available on a particular site, we accrue at the lower end of that range.

We cannot estimate costs on sites in the very early stages of clean-up. Currently, we have several sites in the very early stages of clean-up, and there is no more than a remote chance that a material amount for clean-up will be required.

Pursuant to a consent decree Caterpillar entered with the EPA, the company was required to meet certain emission standards by October 2002. The decree provides that if engine manufacturers were unable to meet the standards at that time, they would be required to pay a Non-Conformance Penalty (NCP) on each engine sold that did not meet the standard. The amount of the NCP would be based on how close to meeting the standard the engine came — the more out of compliance the higher the penalty. The company began introduction of fully compliant ACERT engines in 2003 and by the end of 2003 Caterpillar was only producing fully compliant engine models. As a result, NCPs were not payable for any engines built in 2004. NCPs of $153 million were paid in 2003.

In addition, the consent decree required Caterpillar to pay a fine of $25 million, which was expensed in 1998, and to make investments totaling $35 million in environmental-related products by July 7, 2007. Total qualifying investments to date for these projects are $34.9 million, of which $5.9 million was made during 2004. Caterpillar expects to reach the $35 million requirement during the first quarter of 2005. A future benefit is expected to be realized from these environmental projects related to Caterpillar's ability to capitalize on the technologies it developed in complying with its environmental project obligations. In short, Caterpillar expects to receive a positive net return on the environmental projects by being able to market the technology it developed.

We are a party to litigation matters and claims that are normal in the course of our operations, and, while the results of such litigation and claims cannot be predicted with certainty, management believes, based on the advice of counsel, the final outcome of such matters will not have a materially adverse effect on our financial statements.

On January 16, 2002, Caterpillar commenced an action in the Circuit Court of the Tenth Judicial Circuit of Illinois in Peoria, Illinois, against Navistar International Transportation Corporation and International Truck and Engine Corporation (collectively Navistar). The lawsuit arises out of a long-term purchase contract between Caterpillar and Navistar effective May 31, 1988, as amended from time to time (the Purchase Agreement). The pending complaint alleges that Navistar breached its contractual obligations by: (i) paying Caterpillar $8.08 less per fuel injector than the agreed upon price for new unit injectors delivered by Caterpillar; (ii) refusing to pay contractually agreed upon surcharges owed as a result of Navistar ordering less than planned volumes of replacement unit injectors; and (iii) refusing to pay contractually agreed upon interest stemming from Navistar's late payments. As of December 31, 2004, the net past due receivable from Navistar regarding the foregoing and included in "Long-term receivables — trade and other" in Statement 3 totaled $139 million. The pending complaint also has claims alleging that Franklin Power Products, Inc., Newstream Enterprises, and Navistar, collectively and individually, failed to pay the applicable price for shipments of unit injectors to Franklin and Newstream. As of December 31, 2004, the net past due receivables for the foregoing, included in "Long-term receivables — trade and other" in Statement 3 totaled $13 million. The pending complaint further alleges that Sturman Industries, Inc., and Sturman Engine Systems, Inc., colluded with Navistar to utilize technology that Sturman Industries, Inc., misappropriated from Caterpillar to help Navistar develop its G2 fuel system, and tortiously interfered with the Purchase Agreement and Caterpillar's prospective economic relationship with Navistar. The pending complaint further alleges that the two parties' collusion led Navistar to select Sturman Engine Systems, Inc. and another company, instead of Caterpillar, to develop and manufacture the G2 fuel system.

On May 7, 2002, International Truck and Engine Corporation (International) commenced an action against Caterpillar in the Circuit Court of DuPage County, Illinois that alleges Caterpillar breached various aspects of a long-term agreement term sheet. In its fifth amended complaint, International seeks a declaration from the court that the term sheet constitutes a legally binding contract for the sale of heavy-duty engines at specified prices through the end of 2006, alleges that Caterpillar breached the term sheet by raising certain prices effective October 1, 2002, and also alleges that Caterpillar breached an obligation to negotiate a comprehensive long-term agreement referenced in the term sheet. International has also asserted a claim for "unjust enrichment" related to certain revenues received by Caterpillar from another customer. International seeks damages "in an amount to be determined at trial" and injunctive relief. Caterpillar denies International's claims and has filed a counterclaim seeking a declaration that the term sheet has been effectively terminated. Caterpillar also asserts that International has released Caterpillar from certain of its claims. On September 24, 2003, the Appellate Court of Illinois, ruling on an interlocutory appeal, issued an order consistent with Caterpillar's position that, even if the court subsequently determines that the term sheet is a binding contract, it is indefinite in duration and was therefore terminable at will by

Caterpillar after a reasonable period. Caterpillar anticipates that a trial currently scheduled to begin in June 2005 will address all remaining issues in this matter. This matter is not related to the breach of contract action brought by Caterpillar against Navistar currently pending in the Circuit Court of Peoria County, Illinois.

In 2004, the European Union (EU) imposed retaliatory tariffs on certain U.S. origin goods as a result of a WTO decision that found the extraterritorial income exclusion (ETI) provisions of the FSC Repeal and Extraterritorial Income Exclusion Act of 2000 constituted a prohibited export subsidy. These tariffs, which began in March of 2004 at 5 percent, increased 1 percentage point per month. Given the makeup of the final retaliation list, some Caterpillar parts and components were subject to these tariffs. However, these tariffs have not materially impacted our financial results. In addition to the United States, the company has production facilities in the EU, Russia, Asia, and South America. Products sold into the EU from these plants were not affected by this retaliatory tariff. The American Jobs Creation Act of 2004 (Act), enacted on October 22, 2004, phases-out the ETI provisions. As a result, the EU has lifted the sanctions effective January 1, 2005 pending the outcome of a WTO review to determine whether certain provisions of the Act are compliant with the ruling against the FSC/ETI regime.

In a letter dated November 15, 2004, the United States Environmental Protection Agency (EPA), proposed a civil penalty of $641,392 to Caterpillar for the alleged failure to comply with certain requirements of the federal Clean Air Act. The EPA alleges that Caterpillar constructed a facility in Emporia, Kansas and failed to comply with Section 112(g)(2)(B) of the Clean Air Act. Caterpillar sold the Emporia facility in December 2002. We are seeking a settlement of this matter with all concerned parties and the company believes the outcome will not have a material impact on our financial statements.

## 25. Segment information

### A. Basis for segment information

The company is organized based on a decentralized structure that has established accountabilities to continually improve business focus and increase our ability to react quickly to changes in both the global business cycle and competitors' actions. Our current structure uses a product, geographic matrix organization comprised of multiple profit and service center divisions.

Caterpillar is a highly integrated company. The majority of our profit centers are product focused. They are primarily responsible for the design, manufacture and ongoing support of their products. However, some of these product-focused profit centers also have marketing responsibilities. We also have geographically-based profit centers that are focused primarily on marketing. However, most of these profit centers also have some manufacturing responsibilities. One of our profit centers provides various financial services to our customers and dealers. The service center divisions perform corporate functions and provide centralized services.

We have developed an internal measurement system to evaluate performance and to drive continuous improvement. This measurement system, which is not based on generally accepted accounting principles (GAAP), is intended to motivate desired behavior of employees and drive performance. It is not intended to measure a division's contribution to enterprise results. The sales and cost information used for internal purposes varies significantly from our consolidated, externally reported information resulting in substantial reconciling items. Each division has specific performance targets and is evaluated and compensated based on achieving those targets. Performance targets differ from division to division; therefore, meaningful comparisons cannot be made among the profit or service center divisions. It is the comparison of actual results to budgeted results that makes our internal reporting valuable to management. Consequently, we feel that the financial information required by Statement of Financial Accounting Standards No. 131 (SFAS 131), "Disclosures about Segments of an Enterprise and Related Information" has limited value for our external readers.

Due to Caterpillar's high level of integration and our concern that segment disclosures based on SFAS 131 requirements have limited value to external readers, we are continuing to disclose financial results for our three principal lines of business (Machinery, Engines and Financial Products) in our Management's Discussion and Analysis beginning on page A-36.

### B. Description of segments

The profit center divisions meet the SFAS 131 definition of "operating segments;" however, the service center divisions do not. Several of the profit centers have similar characteristics and have been aggregated. The following is a brief description of our seven reportable segments and the business activities included in the *All Other* category.

**Asia/Pacific Marketing:** Primarily responsible for marketing products through dealers in Australia, Asia (excluding Japan) and the Pacific Rim. Also includes the regional manufacturing of some products which are also produced by *Construction & Mining Products*.

**Construction & Mining Products:** Primarily responsible for the design, manufacture and ongoing support of small, medium and large machinery used in a variety of construction and mining applications. Also includes the design, manufacture, procurement and marketing of components and control systems that are consumed primarily in the manufacturing of our machinery.

**EAME Marketing:** Primarily responsible for marketing products (excluding *Power Products*) through dealers in Europe, Africa, the Middle East and the Commonwealth of Independent States. Also includes the regional manufacturing of some products which are also produced by *Construction & Mining Products* and *Power Products*.

**Financing & Insurance Services:** Provides financing to customers and dealers for the purchase and lease of Caterpillar and other equipment, as well as some financing for Caterpillar sales to dealers. Financing plans include operating and finance leases, installment sale contracts, working capital loans and wholesale financing plans.The division also provides various forms of insurance to customers and dealers to help support the purchase and lease of our equipment.

**Latin America Marketing:** Primarily responsible for marketing products through dealers in Latin America. Also includes the regional manufacturing of some products that are also produced by *Construction & Mining Products*.

**Power Products:** Primarily responsible for the design, manufacture, marketing and ongoing support of reciprocating and turbine engines along with related systems. These engines and related systems are used in products manufactured in other segments, on-highway trucks and locomotives; and in a variety of construction, electric power generation, marine, petroleum and industrial applications.

**North America Marketing:** Primarily responsible for marketing products (excluding *Power Products*) through dealers in the United States and Canada.

**All Other:** Primarily includes activities such as: service support and parts distribution to Caterpillar dealers worldwide; logistics services for other companies; service tools for Caterpillar dealers; and the remanufacture of Caterpillar engines and components and remanufacturing services for other companies.

### C. Segment measurement and reconciliations

Please refer to Table IV on pages A-31 to A-33 for financial information regarding our segments. There are several accounting differences between our segment reporting and our external reporting. Our segments are measured on an accountable basis; therefore, only those items for which divisional management is directly responsible are included in the determination of segment profit/(loss) and assets. We made several changes to our segment reporting methodologies in the first quarter of 2004. Most notable are a change in the current cost methodology used to value inventory and cost of sales for segment reporting purposes, as well as a change in the manner that interest expense is charged to segments. Amounts for 2003 and 2002 presented in Table IV of this Note 25 have been restated to conform to the new methodology.

The following is a list of the more significant accounting differences:

- Generally, liabilities are managed at the corporate level and are not included in segment operations. Segment accountable assets generally include inventories, receivables, property, plant and equipment.
- We account for intersegment transfers using a system of market-based prices. With minor exceptions, each of the profit centers either sells or purchases virtually all of its products to or from other profit centers within the company. Our high level of integration results in our internally reported sales being approximately double that of our consolidated, externally reported sales.
- Segment inventories and cost of sales are valued using a current cost methodology.
- Postretirement benefit expenses are split; segments are generally responsible for service and prior services costs, with the remaining elements of net periodic benefit cost included as a methodology difference.
- Interest expense is imputed (i.e., charged) to profit centers based on their level of accountable assets.
- Accountable profit is determined on a pretax basis.

Reconciling items are created based on accounting differences between segment reporting and our consolidated, external reporting. Please refer to Table IV on pages A-31 to A-33 for financial information regarding significant reconciling items. Most of our reconciling items are self-explanatory given the above explanations of accounting differences. However, for the reconciliation of profit, we have grouped the reconciling items as follows:

- **Corporate costs:** Certain corporate costs are not charged to our segments. These costs are related to corporate requirements and strategies that are considered to be for the benefit of the entire organization.
- **Timing:** Timing differences in the recognition of costs between segment reporting and consolidated external reporting.
- **Methodology differences:** See previous discussion of significant accounting differences between segment reporting and consolidated external reporting.

**TABLE IV — Segment Information (Millions of dollars)**

## Business Segments:

| | Machinery and Engines | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Asia/ Pacific Marketing | Construction & Mining Products | EAME Marketing | Latin America Marketing | Power Products | North America Marketing | All Other | Total | Financing & Insurance Services | Total |
| **2004** | | | | | | | | | | |
| External sales and revenues | **$ 2,137** | **575** | **3,938** | **1,785** | **8,909** | **9,229** | **1,554** | **28,127** | **2,373** | **$ 30,500** |
| Intersegment sales and revenues | **$ 617** | **12,311** | **3,567** | **881** | **8,669** | **363** | **2,617** | **29,025** | **1** | **$ 29,026** |
| Total sales and revenues | **$ 2,754** | **12,886** | **7,505** | **2,666** | **17,578** | **9,592** | **4,171** | **57,152** | **2,374** | **$ 59,526** |
| Depreciation and amortization | **$ 15** | **179** | **62** | **45** | **288** | **1** | **91** | **681** | **604** | **$ 1,285** |
| Imputed interest expense | **$ 18** | **75** | **34** | **21** | **114** | **2** | **88** | **352** | **539** | **$ 891** |
| Accountable profit (loss) | **$ 133** | **1,150** | **380** | **180** | **408** | **434** | **655** | **3,340** | **460** | **$ 3,800** |
| Accountable assets at Dec. 31 | **$ 574** | **2,789** | **1,267** | **802** | **3,881** | **28** | **3,514** | **12,855** | **24,446** | **$ 37,301** |
| Capital expenditures | **$ 14** | **221** | **99** | **41** | **234** | **6** | **117** | **732** | **1,327** | **$ 2,059** |
| 2003 | | | | | | | | | | |
| External sales and revenues | $ 1,573 | 248 | 3,183 | 1,187 | 6,793 | 6,763 | 1,121 | 20,868 | 2,018 | $ 22,886 |
| Intersegment sales and revenues | $ 384 | 9,129 | 2,391 | 533 | 6,541 | 242 | 2,553 | 21,773 | 2 | $ 21,775 |
| Total sales and revenues | $ 1,957 | 9,377 | 5,574 | 1,720 | 13,334 | 7,005 | 3,674 | 42,641 | 2,020 | $ 44,661 |
| Depreciation and amortization | $ 13 | 188 | 72 | 42 | 292 | 1 | 81 | 689 | 551 | $ 1,240 |
| Imputed interest expense | $ 14 | 65 | 33 | 23 | 109 | 9 | 76 | 329 | 473 | $ 802 |
| Accountable profit (loss) | $ 110 | 560 | 214 | 99 | 25 | 316 | 347 | 1,671 | 337 | $ 2,008 |
| Accountable assets at Dec. 31 | $ 627 | 2,190 | 1,018 | 692 | 3,710 | 293 | 2,537 | 11,067 | 20,467 | $ 31,534 |
| Capital expenditures | $ 22 | 137 | 80 | 35 | 212 | 8 | 103 | 597 | 1,220 | $ 1,817 |
| 2002 | | | | | | | | | | |
| External sales and revenues | $ 1,310 | 214 | 2,825 | 1,231 | 6,142 | 5,908 | 920 | 18,550 | 1,779 | $ 20,329 |
| Intersegment sales and revenues | $ 41 | 8,499 | 2,242 | 423 | 6,357 | 204 | 1,620 | 19,386 | — | $ 19,386 |
| Total sales and revenues | $ 1,351 | 8,713 | 5,067 | 1,654 | 12,499 | 6,112 | 2,540 | 37,936 | 1,779 | $ 39,715 |
| Depreciation and amortization | $ 12 | 191 | 53 | 43 | 293 | — | 68 | 660 | 436 | $ 1,096 |
| Imputed interest expense | $ 13 | 60 | 30 | 25 | 111 | 52 | 60 | 351 | 539 | $ 890 |
| Accountable profit (loss) | $ 86 | 311 | 125 | 64 | (81) | 88 | 201 | 794 | 270 | $ 1,064 |
| Accountable assets at Dec. 31 | $ 414 | 2,178 | 778 | 965 | 3,568 | (213) | 2,862 | 10,552 | 17,417 | $ 27,969 |
| Capital expenditures | $ 13 | 159 | 65 | 33 | 236 | 2 | 80 | 588 | 1,177 | $ 1,765 |

## Reconciliations:

| | Machinery and Engines | Financing & Insurance Services | Consolidating Adjustments | Consolidated Total |
|---|---|---|---|---|
| **Sales & Revenues** | | | | |
| **2004** | | | | |
| Total external sales and revenues from business segments | **$ 28,127** | **$ 2,373** | **$ —** | **$ 30,500** |
| Other | **209** | **(264)** | **(194)** [1] | **(249)** |
| Total sales and revenues | **$ 28,336** | **$ 2,109** | **$ (194)** | **$ 30,251** |
| 2003 | | | | |
| Total external sales and revenues from business segments | $ 20,868 | $ 2,018 | $ — | $ 22,886 |
| Other | 180 | (123) | (180) [1] | (123) |
| Total sales and revenues | $ 21,048 | $ 1,895 | $ (180) | $ 22,763 |
| 2002 | | | | |
| Total external sales and revenues from business segments | $ 18,550 | $ 1,779 | $ — | $ 20,329 |
| Other | 98 | (101) | (174) [1] | (177) |
| Total sales and revenues | $ 18,648 | $ 1,678 | $ (174) | $ 20,152 |

[1] Elimination of Financial Product revenues from Machinery and Engines.

Continued on Page A-32

**TABLE IV Continued — Segment Information (Millions of dollars)**

## Reconciliations:

| Profit before taxes | Machinery and Engines | Financing & Insurance Services | Consolidated Total |
|---|---|---|---|
| **2004** | | | |
| Total accountable profit from business segments | **$ 3,340** | **$ 460** | **$ 3,800** |
| Corporate costs | **(601)** | **—** | **(601)** |
| Timing | **(94)** | **—** | **(94)** |
| Methodology differences: | | | |
| Inventory/cost of sales | **(62)** | **—** | **(62)** |
| Postretirement benefit expense | **(270)** | **—** | **(270)** |
| Financing costs | **52** | **—** | **52** |
| Equity in profit of unconsolidated affiliated companies | **(56)** | **(3)** | **(59)** |
| Currency | **(37)** | **—** | **(37)** |
| Other methodology differences | **(87)** | **48** | **(39)** |
| Other | **17** | **—** | **17** |
| Total profit before taxes | **$ 2,202** | **$ 505** | **$ 2,707** |
| 2003 | | | |
| Total accountable profit from business segments | $ 1,671 | $ 337 | $ 2,008 |
| Corporate costs | (512) | — | (512) |
| Timing | 54 | — | 54 |
| Methodology differences: | | | |
| Inventory/cost of sales | (30) | — | (30) |
| Postretirement benefit expense | (162) | — | (162) |
| Financing costs | 84 | — | 84 |
| Equity in profit of unconsolidated affiliated companies | (16) | (4) | (20) |
| Currency | 3 | — | 3 |
| Other methodology differences | (32) | 38 | 6 |
| Other | 46 | — | 46 |
| Total profit before taxes | $ 1,106 | $ 371 | $ 1,477 |
| 2002 | | | |
| Total accountable profit from business segments | $ 794 | $ 270 | $ 1,064 |
| Corporate costs | (236) | — | (236) |
| Timing | (21) | — | (21) |
| Methodology differences: | | | |
| Inventory/cost of sales | 33 | — | 33 |
| Postretirement benefit expense | 147 | — | 147 |
| Financing costs | (24) | — | (24) |
| Equity in profit of unconsolidated affiliated companies | 12 | (8) | 4 |
| Currency | 14 | — | 14 |
| Other methodology differences | 61 | 25 | 86 |
| Other | 47 | — | 47 |
| Total profit before taxes | $ 827 | $ 287 | $ 1,114 |

| Assets | Machinery and Engines | Financing & Insurance Services | Consolidating Adjustments | Consolidated Total |
|---|---|---|---|---|
| **2004** | | | | |
| Total accountable assets from business segments | **$ 12,855** | **$ 24,446** | **$ —** | **$ 37,301** |
| Items not included in segment assets: | | | | |
| Cash and short-term investments | **270** | **175** | **—** | **445** |
| Intercompany trade receivables | **443** | **18** | **(461)** | **—** |
| Investments in unconsolidated affiliated companies | **348** | **—** | **(1)** | **347** |
| Investment in Financial Products | **3,012** | **—** | **(3,012)** | **—** |
| Deferred income taxes and prepaids | **2,477** | **92** | **(317)** | **2,252** |
| Intangible assets and other assets | **2,177** | **—** | **—** | **2,177** |
| Service center assets | **945** | **—** | **—** | **945** |
| Liabilities included in segment assets | **1,346** | **—** | **—** | **1,346** |
| Inventory methodology differences | **(2,235)** | **—** | **—** | **(2,235)** |
| Other | **627** | **(119)** | **5** | **513** |
| Total assets | **$ 22,265** | **$ 24,612** | **$ (3,786)** | **$ 43,091** |

Continued on Page A-33

**TABLE IV Continued — Segment Information (Millions of dollars)**

## Reconciliations:

| | Machinery and Engines | Financing & Insurance Services | Consolidating Adjustments | Consolidated Total |
|---|---|---|---|---|
| **Assets** | | | | |
| 2003 | | | | |
| Total accountable assets from business segments | $ 11,067 | $ 20,467 | $ — | $ 31,534 |
| Items not included in segment assets: | | | | |
| Cash and short-term investments | 220 | 122 | — | 342 |
| Intercompany trade receivables | 572 | 397 | (969) | — |
| Investments in unconsolidated affiliated companies | 325 | — | — | 325 |
| Investment in Financial Products | 2,547 | — | (2,547) | — |
| Deferred income taxes and prepaids | 2,736 | 77 | (228) | 2,585 |
| Intangible assets and other assets | 2,110 | — | — | 2,110 |
| Service center assets | 895 | — | — | 895 |
| Liabilities included in segment assets | 925 | — | — | 925 |
| Inventory methodology differences | (2,035) | — | — | (2,035) |
| Other | 84 | (91) | 32 | 25 |
| Total assets | $ 19,446 | $ 20,972 | $ (3,712) | $ 36,706 |
| 2002 | | | | |
| Total accountable assets from business segments | $ 10,552 | $ 17,417 | $ — | $ 27,969 |
| Items not included in segment assets: | | | | |
| Cash and short-term investments | 146 | 163 | — | 309 |
| Intercompany trade receivables | 917 | 343 | (1,260) | — |
| Investments in unconsolidated affiliated companies | 283 | — | — | 283 |
| Investment in Financial Products | 1,961 | — | (1,961) | — |
| Deferred income taxes and prepaids | 2,698 | 75 | (133) | 2,640 |
| Intangible assets and other assets | 1,719 | — | — | 1,719 |
| Service center assets | 810 | — | — | 810 |
| Liabilities included in segment assets | 848 | — | — | 848 |
| Inventory methodology differences | (1,845) | — | — | (1,845) |
| Other | 78 | (110) | 4 | (28) |
| Total assets | $ 18,167 | $ 17,888 | $ (3,350) | $ 32,705 |

## Enterprise-wide Disclosures:

### External sales and revenues from products and services:

| | **2004** | 2003 | 2002 |
|---|---|---|---|
| Machinery | **$18,844** | $13,678 | $11,975 |
| Engines | **9,492** | 7,370 | 6,673 |
| Financial Products | **1,915** | 1,715 | 1,504 |
| Total consolidated | **$30,251** | $22,763 | $20,152 |

## Information about Geographic Areas:

| | External Sales & Revenues[1] | | | Net property, plant and equipment December 31, | | |
|---|---|---|---|---|---|---|
| | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 |
| Inside United States | **$ 14,161** | $ 10,058 | $ 9,291 | **$ 4,424** | $ 4,276 | $ 4,487 |
| Outside United States | **16,090** | 12,705 | 10,861 | **3,258[2]** | 2,975[2] | 2,522[2] |
| Total | **$ 30,251** | $ 22,763 | $ 20,152 | **$ 7,682** | $ 7,251 | $ 7,009 |

[1] Sales of machinery and engines are based on dealer location. Revenues from services provided are based on where service is rendered.

[2] Amount includes $681 million, $675 million and $680 million of net property, plant and equipment located in the United Kingdom as of December 31, 2004, 2003 and 2002, respectively.

## 26. Acquisitions

### Turbomach S.A.

In June 2004, we acquired Turbomach S.A. from Borsig Energy Gmbh for $41 million, subject to certain post-closing adjustments. Turbomach S.A. is a Swiss corporation that has packaged, distributed and provided aftermarket services for Solar brand gas turbine engines since 1985 for the industrial power generation market. Turbomach also provides integrated systems for power projects, including balance of plant design, procurement and site construction. The acquisition expands our participation within the global power generation market, particularly in the expanding markets of Europe, Africa and Asia.

The transaction, which was financed with available cash and commercial paper borrowings, was accounted for by the purchase method of accounting and, accordingly, the results of the acquired business for the period from the acquisition date are included in the accompanying consolidated financial statements and reported in the "Power Products" segment. Net tangible assets acquired and liabilities assumed of $41 million were recorded at their fair values. No significant intangible assets were acquired. Assuming this transaction had been made at January 1, 2004, the consolidated pro forma results for the year would not be materially different from reported results.

### Parts and Accessories Distribution Business of MG Rover Ltd.

In August 2004, we acquired the global parts and accessories business of U.K. auto manufacturer MG Rover, a wholly owned subsidiary of Phoenix Venture Holdings Limited, for $178 million, including $169 million at closing (subject to certain post-closing adjustments) and a $9 million promissory note to be paid in 2006. The business acquired includes the sourcing, marketing, distribution and sale of automotive service parts and accessories to MG Rover dealers, distributors, importers and other related customers worldwide.

The transaction, which was financed with available cash and commercial paper borrowings, was accounted for by the purchase method of accounting and, accordingly, the results of the acquired business for the period from the acquisition date are included in the accompanying consolidated financial statements and reported in the "All Other" segment. Net tangible assets acquired and liabilities assumed of $73 million were recorded at their fair values. Finite-lived intangible assets acquired of $87 million relate primarily to technology and trademark rights, which are being amortized on a straight-line basis over 15 and 20 years, respectively. Goodwill of $18 million represents the excess of cost over the fair value of net tangible and finite-lived intangible assets acquired. Assuming this transaction had been made at January 1, 2004, the consolidated pro forma results for the year would not be materially different from reported results.

### Williams Technologies, Inc.

In September 2004, we acquired Williams Technologies, Inc., a wholly owned subsidiary of Remy International, Inc., for $105 million, subject to certain post-closing adjustments. Williams Technologies, Inc. is a leading remanufacturer of automatic transmissions, torque converters and engines for automotive and medium and heavy-duty truck applications. This acquisition represents an expansion of our remanufacturing operations into the automotive powertrain remanufacturing business.

The transaction, which was financed with available cash and commercial paper borrowings, was accounted for by the purchase method of accounting and, accordingly, the results of the acquired business for the period from the acquisition date are included in the accompanying consolidated financial statements and reported in the "All Other" segment. Net tangible assets acquired and liabilities assumed of $25 million were recorded at their fair values. Finite-lived intangible assets acquired of $43 million relate primarily to customer relationships, and are being amortized on a straight-line basis over 20 years. Goodwill of $37 million represents the excess of cost over the fair value of net tangible and finite-lived intangible assets acquired. Assuming this transaction had been made at January 1, 2004, the consolidated pro forma results for the year would not be materially different from reported results.

## 27. Selected quarterly financial results (unaudited)

| | 2004 Quarter | | | |
|---|---|---|---|---|
| (Dollars in millions except per share data) | 1st | 2nd | 3rd | 4th |
| Sales and revenues | **$6,467** | **$7,564** | **$7,649** | **$8,571** |
| Less: Revenues | **465** | **464** | **474** | **512** |
| Sales | **6,002** | **7,100** | **7,175** | **8,059** |
| Cost of goods sold | **4,683** | **5,541** | **5,728** | **6,468** |
| Gross margin | **1,319** | **1,559** | **1,447** | **1,591** |
| Profit | **420** | **566** | **498** | **551** |
| Profit per common share | **$ 1.23** | **$ 1.65** | **$ 1.45** | **$ 1.61** |
| Profit per common share — diluted | **$ 1.19** | **$ 1.59** | **$ 1.41** | **$ 1.55** |

| | 2003 Quarter | | | |
|---|---|---|---|---|
| (Dollars in millions except per share data) | 1st | 2nd | 3rd | 4th |
| Sales and revenues | $ 4,821 | $ 5,932 | $ 5,545 | $ 6,465 |
| Less: Revenues | 397 | 431 | 433 | 454 |
| Sales | 4,424 | 5,501 | 5,112 | 6,011 |
| Cost of goods sold | 3,630 | 4,329 | 4,143 | 4,843 |
| Gross margin | 794 | 1,172 | 969 | 1,168 |
| Profit | 129 | 399 | 222 | 349 |
| Profit per common share | $ .37 | $ 1.16 | $ .64 | $ 1.01 |
| Profit per common share — diluted | $ .37 | $ 1.15 | $ .62 | $ .97 |

As discussed in Note 14E on page A-23, we recognized the impact of Medicare Part D in the third quarter of 2004, retroactive to December 31, 2003. Previously issued amounts for the first and second quarters of 2004 were as follows:

| | 2004 Quarter | |
|---|---|---|
| (Dollars in millions except per share data) | 1st | 2nd |
| Profit | **$ 412** | **$ 552** |
| Profit per common share | **$ 1.20** | **$ 1.61** |
| Profit per common share — diluted | **$ 1.16** | **$ 1.55** |

## Five-year Financial Summary

Caterpillar Inc.

(Dollars in millions except per share data)

| Years ended December 31, | 2004 | 2003 | 2002 | 2001 | 2000 |
|---|---|---|---|---|---|
| Sales and revenues | **$30,251** | 22,763 | 20,152 | 20,450 | 20,175 |
| Sales | **$28,336** | 21,048 | 18,648 | 19,027 | 18,913 |
| Percent inside the United States | **46%** | 44% | 45% | 49% | 50% |
| Percent outside the United States | **54%** | 56% | 55% | 51% | 50% |
| Revenues | **$ 1,915** | 1,715 | 1,504 | 1,423 | 1,262 |
| Profit[1] | **$ 2,035** | 1,099 | 798 | 805 | 1,053 |
| Profit per common share[1][2] | **$ 5.95** | 3.18 | 2.32 | 2.35 | 3.04 |
| Profit per common share — diluted[1][3] | **$ 5.75** | 3.13 | 2.30 | 2.32 | 3.02 |
| Dividends declared per share of common stock | **$ 1.600** | 1.440 | 1.400 | 1.390 | 1.345 |
| Return on average common stockholders' equity[4] | **30.0%** | 19.0% | 14.4% | 14.4% | 19.0% |
| Capital expenditures: | | | | | |
| Property, plant and equipment | **$ 926** | 682 | 728 | 1,100 | 928 |
| Equipment leased to others | **$ 1,188** | 1,083 | 1,045 | 868 | 665 |
| Depreciation and amortization | **$ 1,397** | 1,347 | 1,220 | 1,169 | 1,063 |
| Research and development expenses | **$ 928** | 669 | 656 | 696 | 649 |
| As a percent of sales and revenues | **3.1%** | 2.9% | 3.3% | 3.4% | 3.2% |
| Wages, salaries and employee benefits | **$ 6,001** | 4,980 | 4,360 | 4,272 | 4,029 |
| Average number of employees | **73,033** | 67,828 | 70,973 | 70,678 | 67,200 |
| **December 31,** | | | | | |
| Total assets | **$43,091** | 36,706 | 32,705 | 30,489 | 28,246 |
| Long-term debt due after one year: | | | | | |
| Consolidated | **$15,837** | 14,546 | 11,774 | 11,452 | 11,334 |
| Machinery and Engines | **$ 3,663** | 3,603 | 3,581 | 3,653 | 2,854 |
| Financial Products | **$12,174** | 10,943 | 8,193 | 7,799 | 8,480 |
| Total debt: | | | | | |
| Consolidated | **$23,525** | 20,284 | 17,861 | 16,763 | 15,067 |
| Machinery and Engines | **$ 3,762** | 3,707 | 3,903 | 3,945 | 3,427 |
| Financial Products | **$19,763** | 16,577 | 13,958 | 12,818 | 11,640 |

[1] In 2002, we adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" and therefore no longer amortize goodwill.

[2] Computed on weighted-average number of shares outstanding.

[3] Computed on weighted-average number of shares outstanding diluted by assumed exercise of stock options, using the treasury stock method.

[4] Represents profit divided by average stockholders' equity (beginning of year stockholders' equity plus end of year stockholders' equity divided by two).

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## OVERVIEW

Without question, 2004 was one of the most remarkable years in our proud history. In 1997, with sales and revenues less than $19 billion, we set the goal of becoming a $30 billion company by the middle of this decade. While many thought it was overly ambitious, at the close of 2004 we're able to celebrate that tremendous accomplishment ahead of schedule. Throughout the year, Team Caterpillar — our employees, dealers and suppliers — effectively responded to an unprecedented recovery in nearly every market we serve and enhanced our long-term strategic position by meeting record customer demand and building substantial field population. We're clearly pleased to have reached this important $30 billion milestone, but we have not yet delivered bottom line performance in line with our own expectations. While we remain committed to satisfying our customers, we're disappointed with our cost structure, particularly steel related costs and supply chain inefficiencies due to lack of material availability. That, coupled with a record order backlog which delayed ***price realization***,* caused incremental margins to lag in 2004.

Also in 2004, we delivered solid improvement in cash flow and the company ended the year with an even stronger financial position. After providing continued funding for growth opportunities and new product development, the company was able to make significant contributions to pension plans, increase dividends to shareholders and repurchase Caterpillar shares. Pension plans remain well funded due to solid investment returns and over $600 million in contributions for the second year in a row. The company has increased its dividend in ten of the last eleven years and repurchased almost seven million shares during 2004. This financial strength positions Caterpillar very well for the future.

In January 2005 the company and about 9,000 employees represented by the United Auto Workers reached a new six-year labor agreement that will expire on March 1, 2011. Through thoughtful and professional negotiations, we've reached an agreement that positions the company and all our employees for long-term competitiveness.

This year's opportunities certainly presented us with significant challenges. However, we are pleased we were still able to deliver record profits and increased return on sales. We will continue to meet customer requirements and strengthen our long-term market position. While significant cost pressures are common during periods of explosive growth, we're focusing the expertise of hundreds of ***6 Sigma*** teams to aggressively address these issues and improve our cost structure in 2005. We'll continue to build on the value of 6 Sigma and the opportunities unleashed by an engaged global team to set new records this year, create long-term value for our customers and deliver exceptional returns to our shareholders.

It is our objective to provide the most meaningful disclosures in our Management's Discussion and Analysis in order to explain significant changes in our company's results of operations and liquidity and capital resources. As discussed in Note 25 on pages A-29 to A-30, our segment financial information is not based on generally accepted accounting principles and it is not intended to measure contributions to enterprise results. Therefore, it is impractical for us to try to discuss our company's results of operations and liquidity and capital resources solely based on segment information. Where practical, we have linked our discussions to segment information provided in Note 25 and Table IV on pages A-29 to A-33 (see "Reconciliation of Machinery and Engines Sales by Geographic Region to External Sales by Marketing Segment" on page A-37). Our discussions will focus on consolidated results and our three principal lines of business as described below:

**Consolidated** — represents the consolidated data of Caterpillar Inc. and all its consolidated subsidiaries.

**Machinery** — A principal line of business which includes the design, manufacture, marketing and sales of construction, mining and forestry machinery — track and wheel tractors, track and wheel loaders, pipelayers, motor graders, wheel tractor-scrapers, track and wheel excavators, backhoe loaders, log skidders, log loaders, off-highway trucks, articulated trucks, paving products, telescopic handlers, skid steer loaders and related parts. Also includes logistics services for other companies.

**Engines** — A principal line of business including the design, manufacture, marketing and sales of engines for Caterpillar machinery, electric power generation systems; on-highway vehicles and locomotives; marine, petroleum, construction, industrial, agricultural and other applications; and related parts. Reciprocating engines meet power needs ranging from 5 to over 22,000 horsepower (4 to over 16 200 kilowatts). Turbines range from 1,200 to 20,500 horsepower (900 to 15 000 kilowatts).

**Financial Products** — A principal line of business consisting primarily of Caterpillar Financial Services Corporation (Cat Financial), Caterpillar Insurance Holdings, Inc. (Cat Insurance), Caterpillar Power Ventures Corporation (Cat Power Ventures) and their subsidiaries. Cat Financial provides a wide range of financing alternatives for Caterpillar machinery and engines, Solar gas turbines, as well as other equipment and marine vessels. Cat Financial also extends loans to customers and dealers. Cat Insurance provides various forms of insurance to customers and dealers to help support the purchase and lease of our equipment. Cat Power Ventures is an active investor in independent power projects using Caterpillar power generation equipment and services.

*Glossary of terms included on pages A-47 to A-48; first occurrence of terms shown in bold italics.

## 2004 COMPARED WITH 2003

### Sales and Revenues by Geographic Region

| (Millions of dollars) | Total | North America | EAME | Latin America | Asia/Pacific |
|---|---|---|---|---|---|
| **2004** | | | | | |
| Machinery | **$18,844** | **$10,337** | **$ 4,511** | **$ 1,510** | **$ 2,486** |
| Engines[1] | **9,492** | **4,184** | **2,994** | **862** | **1,452** |
| Financial Products[2] | **1,915** | **1,347** | **327** | **116** | **125** |
| | **$30,251** | **$15,868** | **$ 7,832** | **$ 2,488** | **$ 4,063** |
| **2003** | | | | | |
| Machinery | $13,678 | $ 7,310 | $ 3,596 | $ 928 | $ 1,844 |
| Engines[1] | 7,370 | 3,222 | 2,356 | 793 | 999 |
| Financial Products[2] | 1,715 | 1,231 | 303 | 94 | 87 |
| | $22,763 | $11,763 | $ 6,255 | $ 1,815 | $ 2,930 |

[1] Does not include internal engine transfers of $1.745 billion and $1.358 billion in 2004 and 2003, respectively. Internal engine transfers are valued at prices comparable to those for unrelated parties.

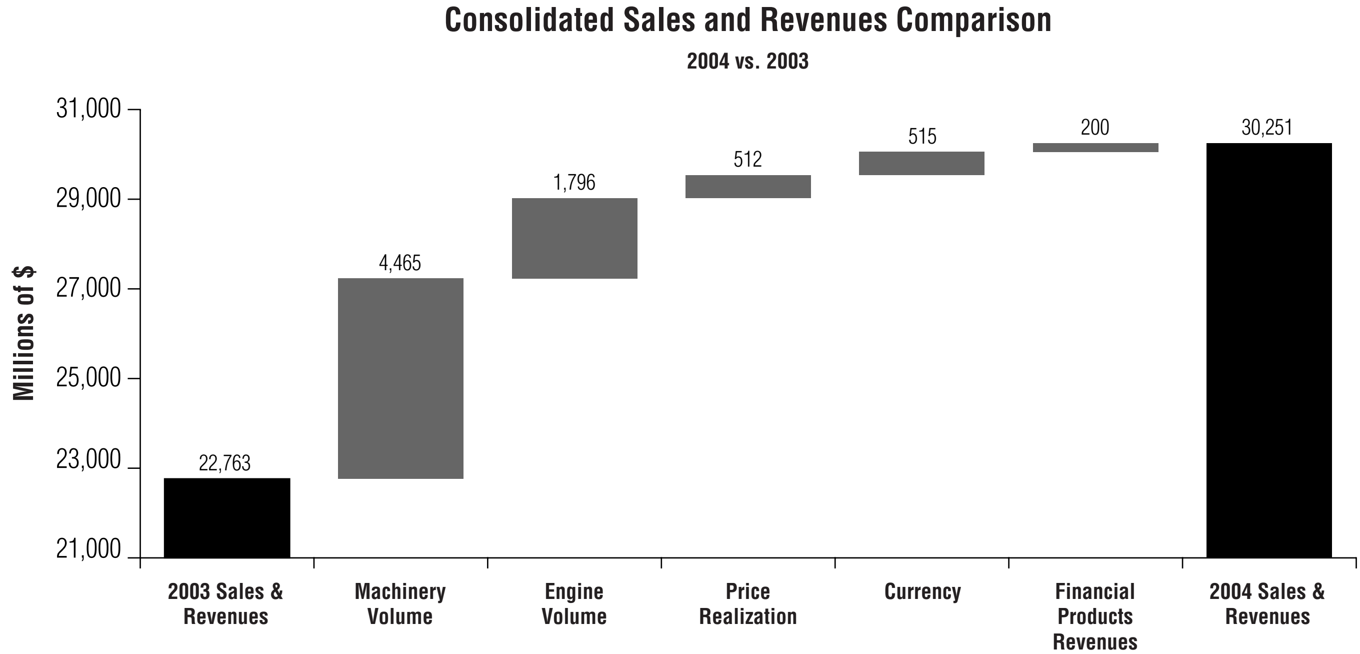
[2] Does not include revenues earned from Machinery and Engines of $194 million and $180 million in 2004 and 2003, respectively.

### Reconciliation of Machinery and Engine Sales by Geographic Region to External Sales by Marketing Segment

| (Millions of dollars) | **2004** | 2003 | 2002 |
|---|---|---|---|
| North America Geographic Region | **$ 14,521** | $ 10,532 | $ 9,480 |
| Engine sales included in the Power Products segment | **(4,184)** | (3,221) | (2,968) |
| Company owned dealer sales included in the All Other segment | **(558)** | (388) | (350) |
| Other* | **(550)** | (160) | (254) |
| North America Marketing external sales | **$ 9,229** | $ 6,763 | $ 5,908 |
| EAME Geographic Region | **$ 7,505** | $ 5,952 | $ 5,178 |
| Power Products sales not included in the EAME Marketing segment | **(2,873)** | (1,897) | (1,613) |
| Other* | **(694)** | (872) | (740) |
| EAME Marketing external sales | **$ 3,938** | $ 3,183 | $ 2,825 |
| Latin America Geographic Region | **$ 2,372** | $ 1,721 | $ 1,598 |
| Power Products sales not included in the Latin America Marketing segment | **(833)** | (667) | (689) |
| Other* | **246** | 133 | 322 |
| Latin America Marketing external sales | **$ 1,785** | $ 1,187 | $ 1,231 |
| Asia/Pacific Geographic Region | **$ 3,938** | $ 2,843 | $ 2,392 |
| Power Products sales not included in the Asia/Pacific Marketing segment | **(1,019)** | (1,008) | (872) |
| Other* | **(782)** | (262) | (210) |
| Asia/Pacific Marketing external sales | **$ 2,137** | $ 1,573 | $ 1,310 |

*Mostly represents external sales of Construction & Mining Products and All Other segments.

## SALES AND REVENUES




The chart above graphically illustrates reasons for the change in Consolidated Sales and Revenues between 2003 (at left) and 2004 (at right). Items favorably impacting sales and revenues appear as upward stair steps with the corresponding dollar amounts above each bar. Caterpillar management utilizes these charts internally to visually communicate with its Board and employees.

Sales and revenues for 2004 were $30.25 billion, $7.49 billion or 33 percent higher than 2003. The increase was due to higher ***Machinery and Engines*** volume of $6.26 billion, the favorable impact of ***currency*** on sales of $515 million due primarily to the strengthening euro and British pound, improved price realization of $512 million and higher Financial Products revenues of $200 million.

**Machinery sales** were $18.84 billion in 2004, a $5.17 billion or 38 percent increase over 2003. Record ***sales volume***, up 33 percent from 2003, accounted for most of the gain. Improved price realization added about 3 percent and the favorable impact of currency accounted for the remaining 2 percent. The volume increase was the result of a 28 percent increase in dealer deliveries to end users and an increase in dealer inventories to meet future demand. Dealers carried about the same months of sales in inventory at the end of 2004 as they did at the end of 2003.

In North America, 2004 sales were 41 percent higher than in 2003. Volume increased 37 percent, reaching a record high. The rest of the gain resulted from improved price realization. Volume benefited from a 33 percent increase in dealer deliveries, with sizable gains occurring in most applications. Low interest rates, higher commodity prices and accelerated depreciation provisions all encouraged users to replace existing machines and increase fleet sizes. ***EAME*** sales rose 25 percent, with about 16 percent coming from more volume, about 7 percent due to the favorable impact of a stronger euro and the remainder due to improved price realization. Half the volume growth occurred in Europe, where low interest rates contributed to some recovery in construction. Volume increased in both Africa/Middle East (AME) and the CIS, largely due to higher metals and energy prices. Sales in ***Latin America*** increased 63 percent, the fastest growth of any region. Volume surged about 55 percent, improved price realization contributed about 7 percent with the remainder due to currency. Dealers delivered 56 percent more machines to end users and built inventories even faster to accommodate the steep recovery in activity. The Asia/Pacific region had a 35 percent increase in sales in 2004, primarily due to volume. Volume declined in China, but this was more than offset by large gains in Australia, Indonesia and India. Dealer deliveries into coal mining, benefiting from higher coal prices, increased sharply in all three countries.

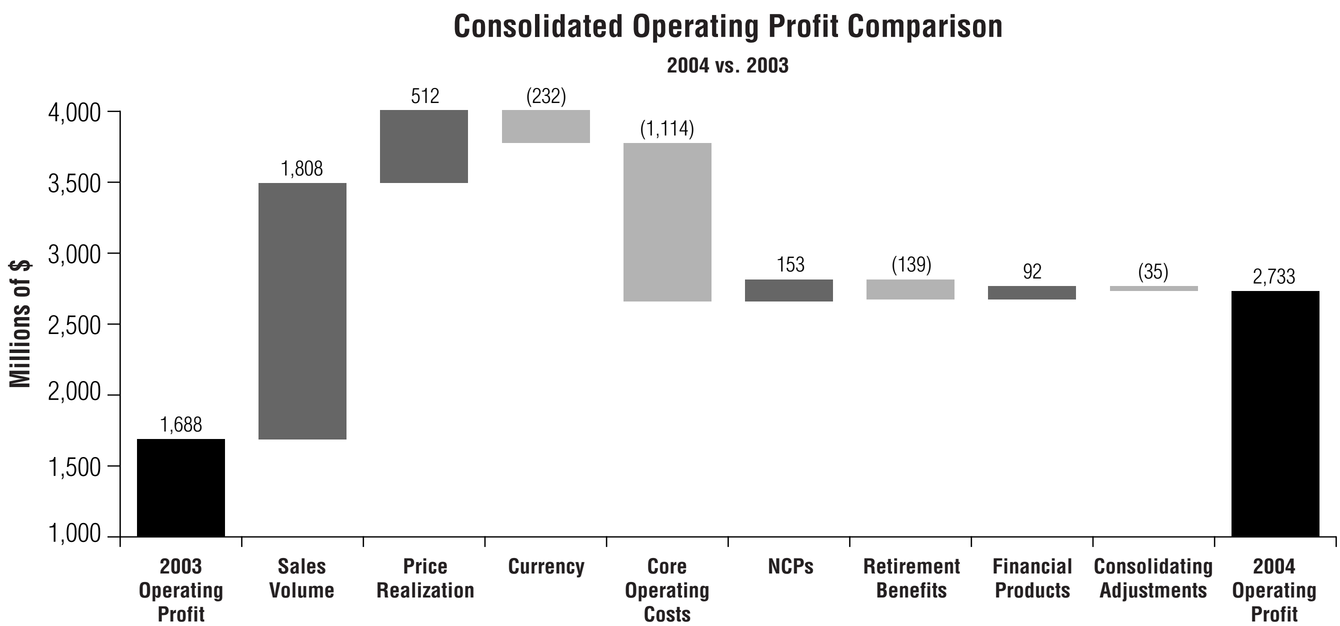
**Engines sales** were $9.49 billion, an increase of $2.12 billion or 29 percent from 2003. Sales volume was up about 24 percent, the favorable impact of currency accounted for about 3 percent and the remainder was due to improved price realization.

Engine sales increased substantially in all regions. The North America engine sales gain of 30 percent was driven primarily by a 37 percent increase in sales of on-highway truck engines, as strong freight demand and improved industry financial health drove expansion and replacement. Sales of engines to the electric power sector increased 25 percent compared to last year, benefiting from increased demand for quality power, and growth in non-residential construction and business investment. Sales of engines to the industrial sector rose 62 percent, with strong widespread demand from industrial Original Equipment Manufacturer (OEM) products and growing preference for Caterpillar engines. Sales of marine engines increased 20 percent primarily from healthy demand for pleasure craft engines. Sales of petroleum engines remained about flat compared to 2003, as strong demand for reciprocating engines to maximize existing production was slightly more than offset by reduced investment in turbines and turbine related services for pipeline and major infrastructure expansion. Engine sales rose 27 percent in EAME with strong increases in all sectors.

Sales of engines into the electric power sector increased 54 percent due to stronger demand for prime and cogeneration systems, Middle Eastern demand for large engines and power modules, and favorable currency versus euro-based competition. Sales of engines to the petroleum sector increased 29 percent, with the vast majority of the increase coming from sales of turbines and turbine-related services to support increases in petroleum investment. Sales of engines to the marine sector increased 27 percent due to increased investment in oceangoing and workboat vessels, driven by higher demand for inland waterway transportation and strengthening oceangoing vessel lease rates. Sales of engines into the industrial sector increased 10 percent. Engine sales in Latin America increased 9 percent with gains in most sectors from an improved business investment climate. Sales of petroleum engines in Latin America increased 16 percent with increased demand for turbines and turbine related services for pipeline applications. Sales of electric power engines in Latin America decreased 27 percent, primarily due to the absence of a large turbine electric power project that occurred during 2003. Widespread economic growth in Asia/Pacific contributed to the 45 percent increase in engine sales. Sales of engines into the electric power sector nearly doubled as strong growth drove increased demand for commercial standby and self-generation, as well as for generator sets to support ongoing demand from transmission shortages in China. Sales of petroleum engines increased 30 percent as growth in exploration and production drove strong demand for turbines and turbine related services. Sales of engines to the marine sector increased 48 percent due to increased demand for dredge equipment in support of construction growth, as well as broad increases in demand for offshore supply boats, pleasure craft and oceangoing vessels.

**Financial Products revenues** were $1.92 billion, an increase of $200 million or 12 percent from 2003. The increase was due primarily to a $228 million favorable impact at Cat Financial from continued growth of ***earning assets***, partially offset by a $60 million impact of lower interest rates on new and existing finance receivables. Also, there was a $19 million increase in earned premiums at Cat Insurance and a $14 million increase in electric plant revenue at Cat Power Ventures.

## OPERATING PROFIT




The chart above graphically illustrates reasons for the change in Consolidated Operating Profit between 2003 (at left) and 2004 (at right). Items favorably impacting operating profit appear as upward stair steps with the corresponding dollar amounts above each bar, while items negatively impacting operating profit appear as downward stair steps with dollar amounts reflected in parentheses above each bar. Caterpillar management utilizes these charts internally to visually communicate with its Board and employees.

Higher sales volume in all regions resulted in a favorable operating profit impact of $1.81 billion. Operating profit was also favorably impacted by improved price realization of $512 million, the absence of $153 million of ***Non-Conformance Penalties (NCPs)*** that were recorded in 2003 and improved profitability of Financial Products of $92 million.

Partially offsetting the favorable items were $1.11 billion in higher ***core operating costs***, a $232 million unfavorable impact of currency on operating profit due primarily to the weakening of the dollar compared with the British pound and the Japanese yen and $139 million of higher ***retirement benefits***.

Our main focus throughout 2004 has been to satisfy unprecedented customer demand despite incurring additional core operating costs to respond to the steep market upturn. The additional core operating costs reflect increases in manufacturing costs and higher general support costs to meet demand. These additional manufacturing costs included higher material costs resulting primarily from steel related and commodity price increases and higher freight and expediting costs to ensure timely delivery of material. The remainder of the core operating cost increase is largely attributable to higher SG&A expense to support growth and development programs, planned spending on product development, higher incentive compensation costs as well as increased warranty expense. These unfavorable items were partially offset by ongoing cost reductions resulting from hundreds of 6 Sigma projects.

**Operating Profit Table**

| (Millions of dollars) | 2004 | 2003 |
|---|---|---|
| Machinery[1] | **$1,825** | $1,246 |
| Engines[1] | **597** | 188 |
| Financial Products | **437** | 345 |
| *Consolidating Adjustments*[2] | **(126)** | (91) |
| | **$2,733** | $1,688 |

[1] Caterpillar operations are highly integrated; therefore, the company uses a number of allocations to determine lines of business operating profit for Machinery and Engines.

[2] Consolidating adjustments consist of eliminations of transactions between Machinery and Engines and Financial Products.

**Machinery operating profit** of $1.83 billion was up $579 million, or 46 percent, from 2003. The favorable impact of higher sales volume and improved price realization was partially offset by higher core operating costs (as outlined above), the unfavorable impact of currency and higher retirement benefits.

**Engines operating profit** of $597 million was up $409 million, or 218 percent, from 2003. The favorable impact of higher sales volume, the absence of NCPs and improved price realization were partially offset by higher core operating costs (as outlined above), higher retirement benefits and the unfavorable impact of currency.

**Financial Products operating profit** of $437 million was up $92 million, or 27 percent, from 2003. The increase was primarily due to a $105 million impact from the growth of earning assets and a $16 million improvement in gain/loss on sale of used equipment at Cat Financial, and a $45 million increase in underwriting income ($26 million due to favorable reserve adjustments resulting from better than anticipated claim experience; remainder due to growth) at Cat Insurance. These favorable items were partially offset by a $39 million increase in operating expenses at Cat Financial primarily related to increased labor costs to support growth in earning assets and a $34 million impact of lower interest spreads.

## OTHER PROFIT/LOSS ITEMS

**Interest expense excluding Financial Products** was $16 million lower compared to 2003 primarily due to lower average borrowing rates.

**Other income/expense** was income of $204 million compared with income of $35 million in 2003 for a favorable impact of $169 million. The change was primarily due to the favorable impact of Machinery and Engines currency gains of $75 million, the absence of a $55 million non-recurring bond retirement charge recorded in the third quarter 2003 and the absence of investment impairments at Cat Insurance of $27 million.

Caterpillar's profit and cash flows are subject to fluctuation due to changes in foreign exchange rates. The company uses currency forward and option contracts to reduce the impact of exchange rate changes. As mentioned above, the result of this activity in 2004 on Machinery and Engines other income/expense was favorable $75 million. This reduces the net unfavorable impact of currency on profit before tax to $157 million.

**The provision for income taxes** for both 2003 and 2004 reflects an effective annual tax rate of 27 percent. A change in our geographic mix of profits was offset by the change in retirement benefits discussed on pages A-54 to A-55.

On October 22, 2004, the American Jobs Creation Act (the Act) was signed into law. Among other things, the Act provides for the phase-out of Extraterritorial Income Exclusion (ETI) benefits over the next two years and creates a new deduction in 2005 of 85 percent of certain non-U.S. earnings that are repatriated in excess of a base amount, as defined in the Act. We have started an evaluation of the effects of the repatriation provision. However, we do not expect to be able to complete this evaluation until after Congress and the Treasury Department provide additional clarification on key elements of the provision. We expect to complete our evaluation of the effects of the repatriation provision within a reasonable period of time following the publication of all relevant guidance. The range of possible amounts, including the base, which we are considering for repatriation under this provision, is between zero and $1 billion. The related potential range of incremental provision for income taxes is between zero and $75 million.

**The equity in profit/loss of unconsolidated affiliated companies** favorably impacted profit by $39 million over 2003, primarily driven by increased profitability at Shin Caterpillar Mitsubishi Ltd. (SCM). The increase in profitability at SCM was driven largely by increased exports.

**Supplemental Information**

| (Millions of dollars) | 2004 | 2003 | 2002 |
|---|---|---|---|
| **Identifiable Assets:** | | | |
| Machinery | **$ 13,713** | $ 11,801 | $ 10,867 |
| Engines | **8,552** | 7,645 | 7,300 |
| Financial Products | **24,612** | 20,972 | 17,888 |
| Consolidating Adjustments | **(3,786)** | (3,712) | (3,350) |
| Total | **$ 43,091** | $ 36,706 | $ 32,705 |
| **Capital Expenditures:** | | | |
| Machinery | **$ 546** | $ 386 | $ 393 |
| Engines | **297** | 278 | 305 |
| Financial Products | **1,271** | 1,101 | 1,075 |
| Total | **$ 2,114** | $ 1,765 | $ 1,773 |
| **Depreciation and Amortization:** | | | |
| Machinery | **$ 442** | $ 453 | $ 437 |
| Engines | **353** | 345 | 348 |
| Financial Products | **602** | 549 | 435 |
| Total | **$ 1,397** | $ 1,347 | $ 1,220 |

Caterpillar operations are highly integrated; therefore, the company uses a number of allocations to determine lines of business financial data.

## UAW LABOR AGREEMENT

In January 2005 the company and about 9,000 employees represented by the United Auto Workers reached a new six-year labor agreement that will expire on March 1, 2011. This agreement positions the company and all our employees for long-term competitiveness. While the initial impact will be about a $100 million increase in retirement benefits in 2005, with the establishment of a very competitive market-based new hire wage package, the introduction of employee and retiree health care cost-sharing and other operational effectiveness improvements, we believe we have a long-term cost structure that enables us to compete from our traditional manufacturing and logistics locations.

**Sales and Revenues**

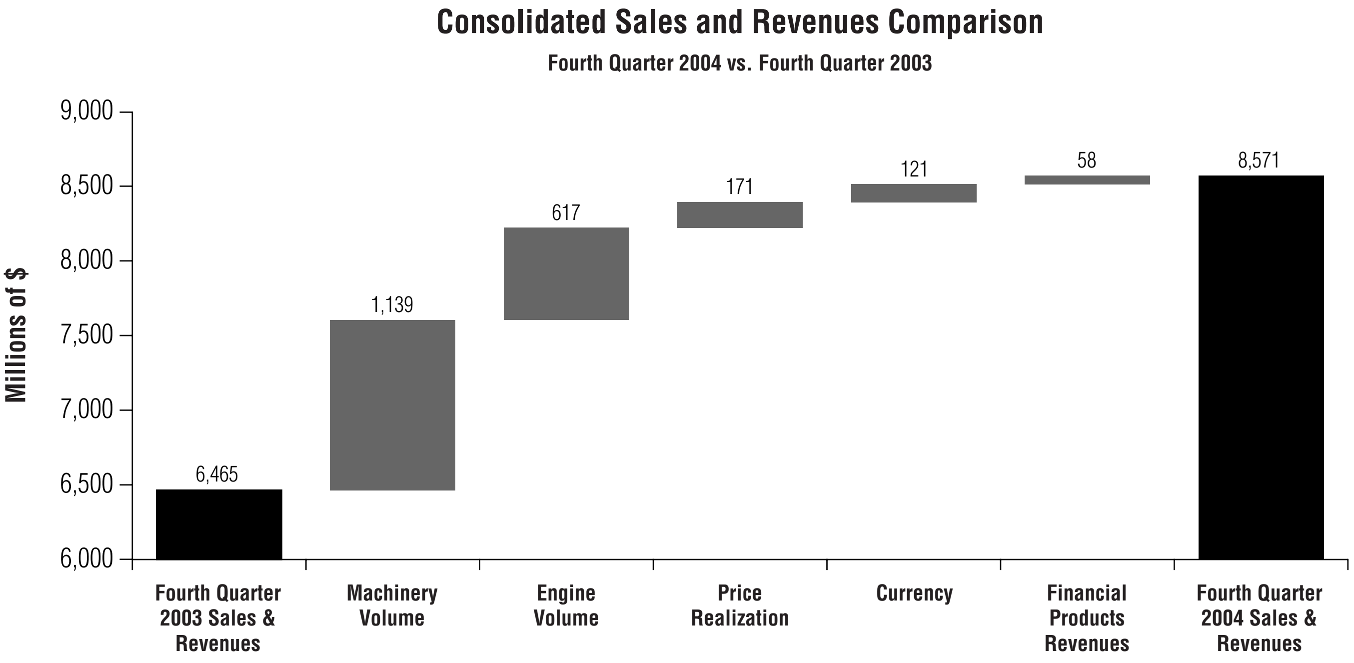
| (Millions of dollars) | Total | North America | EAME | Latin America | Asia/Pacific |
|---|---|---|---|---|---|
| **Fourth Quarter 2004** | | | | | |
| Machinery | **$ 5,157** | **$ 2,783** | **$ 1,279** | **$ 447** | **$ 648** |
| Engines[1] | **2,902** | **1,213** | **955** | **276** | **458** |
| Financial Products[2] | **512** | **361** | **84** | **31** | **36** |
| | **$ 8,571** | **$ 4,357** | **$ 2,318** | **$ 754** | **$ 1,142** |
| **Fourth Quarter 2003** | | | | | |
| Machinery | $ 3,827 | $ 2,088 | $ 939 | $ 291 | $ 509 |
| Engines[1] | 2,184 | 876 | 703 | 300 | 305 |
| Financial Products[2] | 454 | 325 | 79 | 23 | 27 |
| | $ 6,465 | $ 3,289 | $ 1,721 | $ 614 | $ 841 |

[1] Does not include internal engine transfers of $484 million and $362 million in fourth quarter 2004 and fourth quarter 2003, respectively. Internal engine transfers are valued at prices comparable to those for unrelated parties.

[2] Does not include revenues earned from Machinery and Engines of $56 million and $47 million in fourth quarter 2004 and fourth quarter 2003, respectively.

## FOURTH QUARTER 2004 COMPARED WITH FOURTH QUARTER 2003

### SALES AND REVENUES




The chart above graphically illustrates reasons for the change in Consolidated Sales and Revenues between fourth quarter 2003 (at left) and fourth quarter 2004 (at right). Items favorably impacting sales and revenues appear as upward stair steps with the corresponding dollar amounts above each bar. Caterpillar management utilizes these charts internally to visually communicate with its Board and employees.

**Machinery sales** were a record $5.16 billion in fourth quarter 2004, a $1.33 billion or 35 percent increase from fourth quarter 2003. Sales volume, which accounted for most of the gain, was up 30 percent from fourth quarter 2003. Improved price realization added 3 percent and the remainder was due to the favorable impact of currency.

In North America, machinery sales increased 33 percent from fourth quarter 2003. Volume increased about 31 percent and the rest was improved price realization. Nearly all the volume growth was the result of increased dealer deliveries to end users, primarily into mining and construction. Machinery sales in EAME were up 36 percent, with about 26 percent due to volume, about 6 percent due to the favorable currency impact of a stronger euro and the remainder due to improved price realization. Volume was a record for a fourth quarter, with good gains in Europe, AME and the CIS. Latin American machinery sales increased 54 percent, with volume contributing about 43 percent of the change and the remainder due to improved price realization.

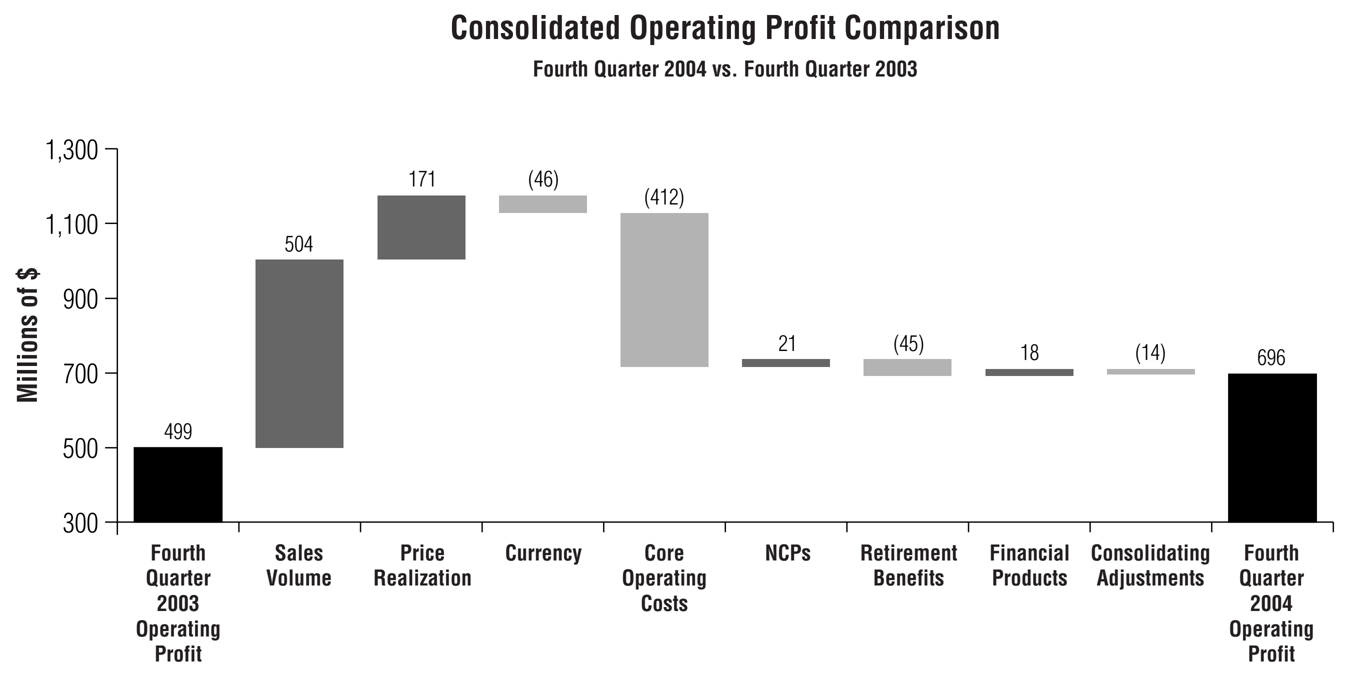
December machine shipments to dealers set a record, which caused a big increase in reported inventories since dealers did not have enough time to convert all shipments into deliveries. In the Asia/Pacific region, machinery sales in fourth quarter 2004 were 27 percent higher than a year earlier, with volume contributing about 23 percent, improved price realization accounting for about 3 percent and the remainder due to currency. A sharp drop in volume in China was more than offset by gains in Indonesia, Australia and India. Deliveries into mining were up sharply in all three countries.

**Engines sales** were $2.90 billion, an increase of $718 million, or 33 percent, compared to fourth quarter 2003. Sales volume was up about 29 percent, the favorable impact of currency accounted for about 2 percent and improved price realization added about 2 percent.

Most regions experienced strong increases in engine sales compared to fourth quarter 2003. The North American engine sales gain of 38 percent was driven primarily by a 43 percent increase in sales of on-highway truck engines. Sales of engines to the petroleum sector increased 24 percent benefiting from strong demand for reciprocating engines to expand and maximize production of existing gas and oil fields. Sales of engines to the industrial sector increased 81 percent with widespread increases in demand for nearly all types of industrial OEM equipment, as well as demand for hurricane cleanup efforts in Florida and surrounding regions. Sales of engines to the electric power sector increased 13 percent with continued demand from commercial construction and business investment. Engine sales rose 36 percent in EAME with increases in most sectors. Sales of engines into the electric power sector increased 81 percent due to strong economics for combined heat and power applications for turbines and reciprocating generator sets, as well as increased sales opportunity via the acquisition of Turbomach. Middle Eastern demand for large engines and power modules and favorable currency versus euro-based competition also contributed to the gain. Sales of engines to the marine sector increased 36 percent with increased workboat demand, while sales to the industrial sector increased 10 percent. Engine sales in Latin America decreased 8 percent compared to fourth quarter 2003. Increases in sales of engines occurred in all sectors, with the exception of a 54 percent reduction in sales of engines to electric power. Electric power was impacted by a major turbine project that occurred in fourth quarter 2003, as well as decreased demand for large prime and standby generator sets. Widespread economic growth in Asia/Pacific contributed to the 50 percent increase in engine sales, with strong increases in nearly all sectors. Sales of engines to the petroleum sector increased 67 percent driven primarily by increased demand for turbines and turbine related services to support expansion in exploration and production. Sales of engines into the electric power sector increased 53 percent with increased demand for prime and standby generator sets. Sales of engines into the marine sector nearly doubled with increased demand for workboat and oceangoing vessel engines.

**Financial Products revenues** were $512 million, an increase of $58 million or 13 percent from fourth quarter 2003. The increase was due primarily to the favorable impact from continued growth of earning assets at Cat Financial.

## OPERATING PROFIT




The chart above graphically illustrates reasons for the change in Consolidated Operating Profit between fourth quarter 2003 (at left) and fourth quarter 2004 (at right). Items favorably impacting operating profit appear as upward stair steps with the corresponding dollar amounts above each bar, while items negatively impacting operating profit appear as downward stair steps with dollar amounts reflected in parentheses above each bar. Caterpillar management utilizes these charts internally to visually communicate with its Board and employees.

Higher sales volume in all regions and most industries favorably impacted operating profit by $504 million. Operating profit was also favorably impacted by improved price realization of $171 million, the absence of $21 million of NCPs that were recorded in the fourth quarter 2003 and improved profitability of Financial Products of $18 million.

Partially offsetting the favorable items were $412 million in higher core operating costs, a $46 million unfavorable impact of currency on operating profit due primarily to the weakening of the dollar compared with the British pound and $45 million of higher retirement benefits.

We continued to meet unprecedented customer demand and satisfy our customers in the fourth quarter, despite incurring additional core operating costs to respond to record volumes. The additional core operating costs reflect increases in manufacturing costs to satisfy customer requirements, higher SG&A expense to support growth and development programs and planned spending on product development programs. The additional manufacturing costs were due to higher material costs resulting primarily from steel related price increases.

**Operating Profit Table**

| (Millions of dollars) | Fourth Quarter **2004** | 2003 |
|---|---|---|
| Machinery[1] | **$ 384** | $ 367 |
| Engines[1] | **246** | 70 |
| Financial Products | **105** | 87 |
| Consolidating Adjustments[2] | **(39)** | (25) |
| | **$ 696** | $ 499 |

[1] Caterpillar operations are highly integrated; therefore, the company uses a number of allocations to determine lines of business operating profit for Machinery and Engines.

[2] Consolidating adjustments consist of eliminations of transactions between Machinery and Engines and Financial Products.

**Machinery operating profit** of $384 million was up $17 million, or 5 percent, from fourth quarter 2003. The favorable impact of higher sales volume and improved price realization was mostly offset by higher core operating costs (as outlined above), the unfavorable impact of currency and higher retirement benefits.

**Engines operating profit** of $246 million was up $176 million, or 251 percent, from fourth quarter 2003. The favorable impact of higher sales volume, improved price realization and the absence of NCPs were partially offset by higher core operating costs (as outlined above).

**Financial Products operating profit** of $105 million was up $18 million, or 21 percent, from fourth quarter 2003. The increase was primarily due to a favorable impact from the growth of earning assets, partially offset by the impact of lower interest spreads at Cat Financial.

## OTHER PROFIT/LOSS ITEMS

**Other income/expense** was income of $69 million compared with income of $20 million in fourth quarter 2003, a favorable impact of $49 million. The change was due mainly to the favorable impact of Machinery and Engines currency gains of $27 million and a $9 million favorable change in currency exchange gain/loss at Cat Power Ventures.

Also, Caterpillar's profit and cash flows are subject to fluctuation due to changes in foreign exchange rates. The company uses currency forward and option contracts to reduce the impact of exchange rate changes. As mentioned above, the result of this activity in the fourth quarter on Machinery and Engines other income/expense was favorable $27 million. This reduced the net unfavorable impact of currency on profit before tax to $19 million.

**The provision for income taxes** for both 2003 and 2004 reflects an effective annual tax rate of 27 percent. In addition, the fourth quarter 2004 provision includes a favorable adjustment of $10 million to recognize the impact of an effective tax rate change from 27.5 percent used for the first nine months primarily due to a change in our geographic mix of profits.

**The equity in profit/loss of unconsolidated affiliated companies** favorably impacted profit by $13 million over fourth quarter a year ago, primarily driven by increased profitability at Shin Caterpillar Mitsubishi Ltd. (SCM). The increase in profitability at SCM was driven largely by increased exports.

## SUPPLEMENTAL INFORMATION

We are providing supplemental information including deliveries to users and dealer inventory levels. We sell the majority of our machines and engines to independently owned and operated dealers and OEMs to meet the demands of their customers, the end users. Due to time lags between our sales and the deliveries to end users we believe this information will help readers better understand our business and the industries we serve. All information provided in the supplemental section is calculated in ***constant dollars***.

### Dealer New Machine Deliveries

Worldwide dealer deliveries of new machines to end users increased 28 percent in 2004, reaching record levels. Strength was widespread, with growth occurring in all regions and in all major applications. The worldwide recovery in manufacturing boosted demand for most commodities. The resulting higher prices and increased production caused increased deliveries into mining, energy development and forestry. Low interest rates and better economic growth raised construction spending, benefiting deliveries into residential and commercial construction.

North American dealers had a record year, delivering 33 percent more new machines than in 2003. Deliveries increased into all major applications as the result of increased activity, better output prices and accelerated depreciation provisions. Dealers increased deliveries to rental fleets by 40 percent to accommodate an increased demand for rental machines and a higher rate of deliveries from existing rental fleets.

Deliveries into both North American coal mining and metals mining more than doubled. Better coal prices and a weaker U.S. dollar caused a 4 percent increase in mine production, the best year for production growth since 1994. Metals price increases ranged from 10 to 70 percent and mine production increased slightly, the first increase in output since 1997. Deliveries into general construction were up 38 percent from 2003. Housing starts increased to a 1.95 million-unit rate, the highest since 1978. Positives for housing construction were continued low mortgage interest rates, higher home prices and a significant shift away from mobile homes. Nonresidential construction recovered from a three year downturn, the result of better profits, increased business sales and better financing conditions. Dealers delivered 31 percent more new machines into heavy construction in 2004. Deliveries into highway construction increased due to past increases in Federal highway funding, and energy development and exploration benefited from higher oil and natural gas prices. Deliveries into both sewer and water and site development increased due to more residential and commercial construction. Increased construction raised the demand for quarry products and aggregates and deliveries into that application increased 26 percent. The increase in housing starts drove lumber prices higher and deliveries into forestry increased 23 percent.

EAME dealers, benefiting from a strong fourth quarter, increased deliveries of new machines 11 percent in 2004. In Europe, where the economic recovery was sluggish, deliveries increased 4 percent. Positive factors included some recovery in housing in the Euro-zone economies, the result of low interest rates, and increased deliveries to rental fleets. Deliveries in AME rose 35 percent. Higher commodity prices led to increased investment in mining and significantly boosted regional income, allowing governments to increase infrastructure investment. In the CIS, deliveries increased 2 percent. Better energy and metals prices, along with much higher production, caused increased investment.

Latin American dealers, enjoying their best year since 1998, delivered 56 percent more new machines than in 2003. Mining deliveries rose 84 percent, due to higher coal and metals prices plus significant increases in production. In addition, general economic recoveries led to increased construction. Most of the increase in deliveries occurred in Chile, Colombia, Argentina and Mexico.

Dealer new machine deliveries in Asia/Pacific increased 26 percent. China, where deliveries more than doubled between 2001 and 2003, had a 25 percent decline because the government implemented measures to moderate development. Demand in the rest of the region, however, was extremely strong, particularly in mining. Deliveries into Australia increased 41 percent and those into Indonesia more than doubled.

### Dealer Inventories of New Machines

Worldwide dealer inventories at the end of 2004 were 38 percent higher than at the end of 2003. A good part of that increase was the normal outcome of rapidly increasing dealer deliveries to end users – more machines were in transit to dealers or in preparation for customer delivery. In addition, plants shipped a record volume of machines in the fourth quarter and dealers did not always have time to convert late-quarter shipments into customer deliveries. Worldwide dealer inventories relative to deliveries were the same as a year earlier. Dealer inventories in both North America and EAME were slightly lower relative to deliveries than at the end of 2003.

### Engine Deliveries to End Users and OEMs

In North America, engine deliveries to end users and OEMs were up 22 percent compared to 2003. Engine deliveries increased in nearly all sectors, led by a 35 percent increase in engines delivered to North American truck and bus manufacturers as higher freight tonnage and improved carrier financial health drove expansion and replacement purchases. Engine deliveries to end users and OEMs in the industrial sector increased 50 percent due to stronger industry demand driven by near record levels of business investment and increased preference for Caterpillar engines. Deliveries of engines into the marine sector rose 10 percent from higher demand for pleasure craft engines. Deliveries of engines into the electric power and petroleum sectors remained about flat.

In EAME, overall engine deliveries to end users and OEMs rose 22 percent with increases in deliveries to all sectors. Electric Power deliveries rose 47 percent benefiting from increased demand for combined heat and power self generation, as well as demand for Middle East infrastructure support. Petroleum deliveries rose 26 percent, as higher energy prices drove increased investment to expand production. Deliveries into the marine sector increased 2 percent, while industrial deliveries declined 5 percent.

Deliveries to end users and OEMs in Latin America increased 2 percent compared to 2003. An improved investment climate drove increases in most sectors, led by a 14 percent increase in petroleum deliveries resulting from investment in pipeline activity. Electric power deliveries declined 33 percent driven by the absence of a large turbine project that occurred during 2003.

Deliveries to end users and OEMs in Asia/Pacific were up 47 percent compared to 2003. Engine deliveries into the electric power sector increased 80 percent due to widespread increases in demand for prime power and standby products, primarily driven by transmission constraints and increased business investment from strong economic growth. Asia/Pacific deliveries of engines into the petroleum sector rose 28 percent driven primarily by increased demand for turbines and turbine related services to support growth in exploration and production. Deliveries into the marine sector increased 39 percent as competitive shipyard rates drove demand for oceangoing vessels, and deliveries increased for pleasure craft and offshore supply boats.

### Dealer Inventories of Engines

Worldwide dealer engine inventories at the end of 2004 were approximately 32 percent above year-end 2003 levels, and were above selling rate increases primarily due to higher in-transit inventories awaiting delivery. Inventory increased in most regions relative to selling rates, while North America held flat with strong deliveries in most sectors. Asia/Pacific dealer inventories continued to increase slightly faster than selling rates, due to in-process deliveries to support higher electric power and marine demand, as well as some continued delay in deliveries to electric power opportunity in China. EAME dealer inventories increased above selling rates, driven by higher in-transit inventory and higher delivery lead times associated with complex projects, as well as some addition of inventory by dealers to serve growing demand for small standby and large prime generator sets.

## 2003 COMPARED WITH 2002

Caterpillar had an excellent year in 2003. We took full advantage of the recovering capital goods market to make real progress on our growth objectives while continuing to lower core operating costs. With a 13 percent sales and revenue increase this year, we are well on our way to achieving our growth target of $30 billion of sales and revenues in this decade. Our performance this year demonstrated to investors our commitment to deliver long-term profitable growth. In addition, we made significant progress on other key strategic initiatives. After an aggressive development program, we introduced ACERT® technology, earning Caterpillar the distinction of being the only engine manufacturer with a full line of 2004 EPA certified and compliant clean diesel engines.

Also in 2003, we supported our dealers' continued expansion of Cat Rental stores as they enhanced their position as the world's leading providers of rental equipment. We strengthened our long-term relationships in the Asia-Pacific region, expanding operations in China and India to serve the increasing demand in these important emerging markets. Amid this growth and change, we continued to embrace the discipline of 6 Sigma, which allowed Caterpillar people to develop process improvements and discover new ways to better serve our customers. As the company grows, we will continue to rely on the proven processes of 6 Sigma to create value and develop growth opportunities. As we move into 2004, we will continue our focus on 6 Sigma and profitable growth, reinforcing the positive changes in our culture that are making Caterpillar a better company.

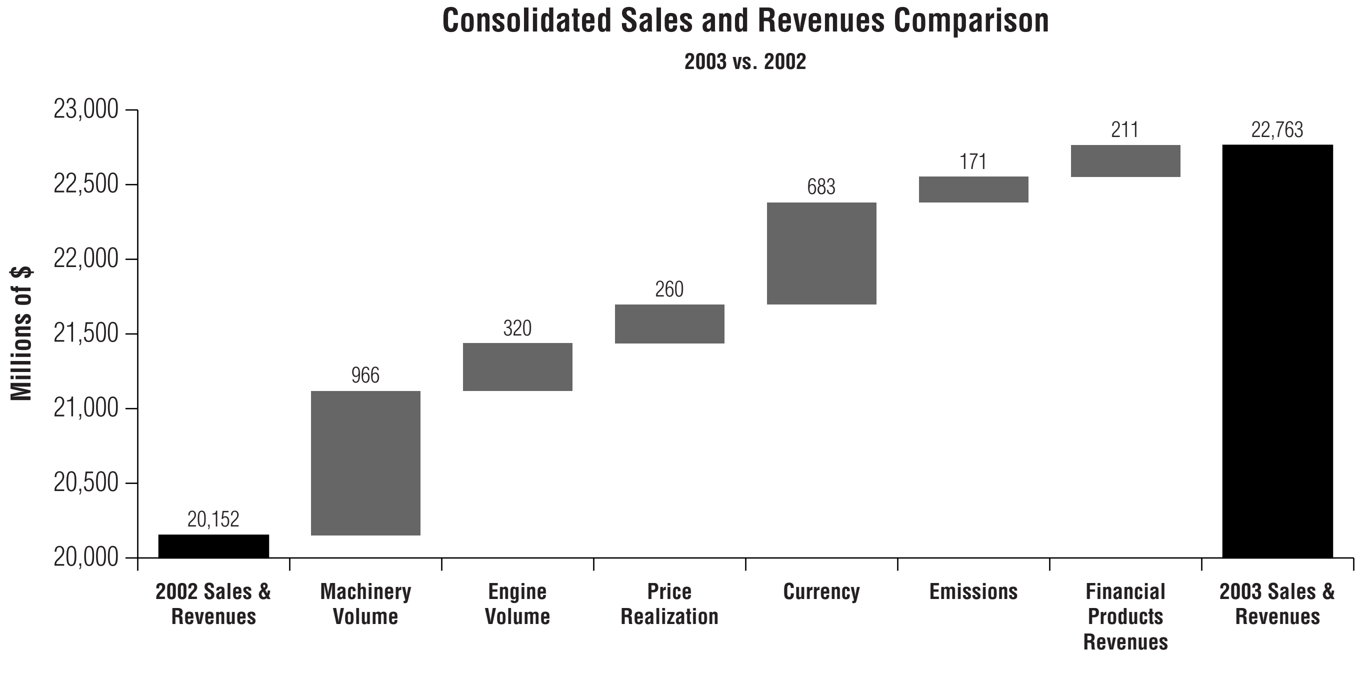
**Sales and Revenues by Geographic Region**

| (Millions of dollars) | Total | North America | EAME | Latin America | Asia/Pacific |
|---|---|---|---|---|---|
| **2003** | | | | | |
| Machinery | **$13,678** | **$ 7,310** | **$ 3,596** | **$ 928** | **$ 1,844** |
| Engines[1] | **7,370** | **3,222** | **2,356** | **793** | **999** |
| Financial Products[2] | **1,715** | **1,231** | **303** | **94** | **87** |
| | **$22,763** | **$11,763** | **$ 6,255** | **$ 1,815** | **$ 2,930** |
| **2002** | | | | | |
| Machinery | $11,975 | $ 6,517 | $ 3,156 | $ 818 | $ 1,484 |
| Engines[1] | 6,673 | 2,963 | 2,022 | 780 | 908 |
| Financial Products[2] | 1,504 | 1,116 | 257 | 55 | 76 |
| | $20,152 | $10,596 | $ 5,435 | $ 1,653 | $ 2,468 |

[1] Does not include internal engine transfers of $1.358 billion and $1.286 billion in 2003 and 2002, respectively. Internal engine transfers are valued at prices comparable to those for unrelated parties.

[2] Does not include revenues earned from Machinery and Engines of $180 million and $174 million in 2003 and 2002, respectively.

## SALES AND REVENUES



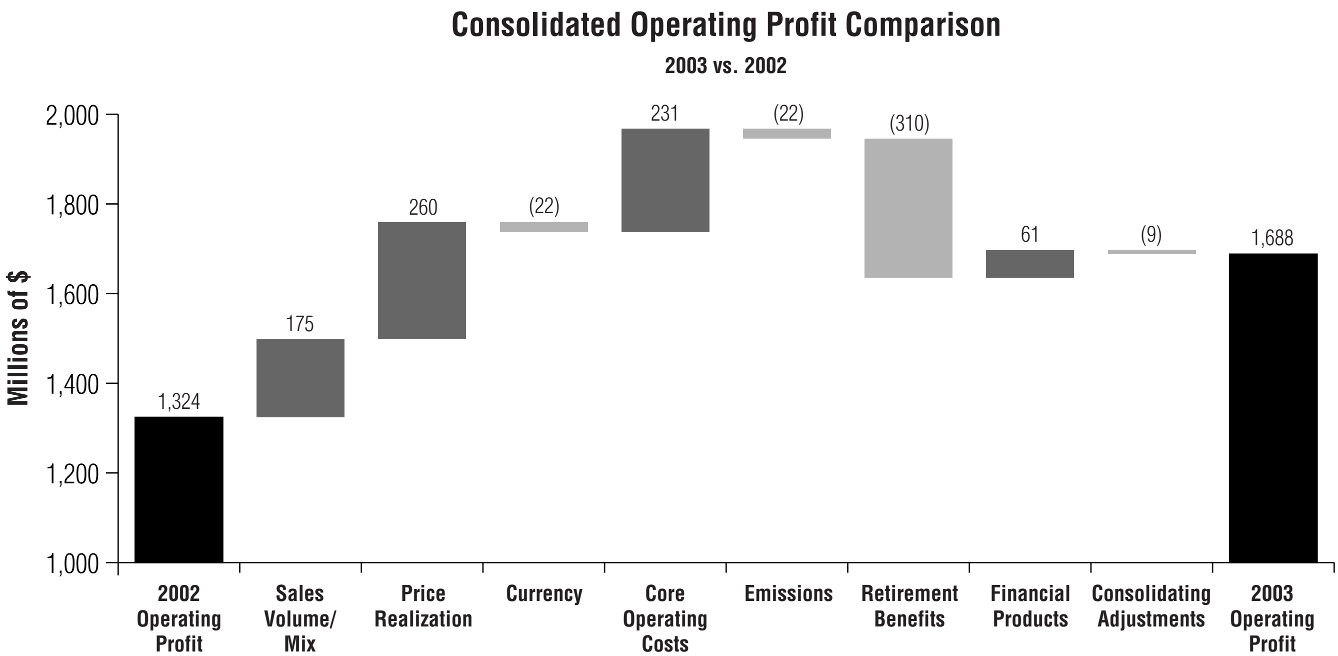

The chart above graphically illustrates reasons for the change in Consolidated Sales and Revenues between 2002 (at left) and 2003 (at right). Items favorably impacting sales and revenues appear as upward stair steps with the corresponding dollar amounts above each bar. Caterpillar management utilizes these charts internally to visually communicate with its Board and employees.

**Machinery sales** were $13.68 billion, an increase of $1.70 billion or 14 percent from 2002. Sales volume was up about 8 percent, the favorable impact of currency accounted for about 4 percent and improved price realization added about 2 percent. In North America, machinery sales increased 12 percent due mostly to higher volume and favorable price realization. Sales volume rose because of an 11 percent increase in dealer deliveries, the result of users (especially rental fleets) upgrading their fleets and a last half improvement in construction activity. Dealers also increased inventories to support higher delivery rates. EAME sales were up 14 percent due to the favorable impact of a stronger euro and improved price realization partially offset by lower sales volume due to weak economic conditions in Europe. In Latin America, sales were up 13 percent, benefiting from increased dealer deliveries into mining and some building of dealer inventories in anticipation of higher end-user demand. Company sales in Asia/Pacific surged 24 percent as dealer deliveries increased significantly due to strong economies in the region.

**Engines sales** were $7.37 billion, an increase of $697 million or 10 percent from 2002. Sales volume was up about 5 percent, the favorable impact of currency accounted for about 3 percent and emissions-related price increases added about 2 percent. North American sales rose 9 percent due to improved emissions-related price increases for truck engines and higher volume in most key engine sectors. Engine sales in EAME rose 17 percent due to the favorable effects of currency and higher sales into the Middle East. Sales in Latin America rose 2 percent with all of the gain coming from higher sales of truck and bus engines. Sales in Asia/Pacific rose 10 percent due to higher volume in almost all sectors as economic growth strengthened. Worldwide Caterpillar truck engine sales rose 19 percent with a significant improvement in emissions-related price realization and higher volume of 4 percent. Worldwide sales of electric power and industrial engines rose 10 and 8 percent, respectively, benefiting from the favorable effects of currency and slight industry growth. Worldwide sales into petroleum rose 4 percent due to higher demand for engines used in gas compression and higher North American land drilling activity. Sales to the marine sector rose 2 percent, helped by slightly higher industry demand and favorable effects of currency.

**Financial Products revenues** were $1.72 billion, an increase of $211 million or 14 percent from 2002. The increase was due primarily to the favorable impact of $223 million from continued growth of earning assets at Cat Financial and a $63 million increase in earned premiums on extended service contracts at Cat Insurance. These favorable items were partially offset by the $120 million impact of lower interest rates on new and existing finance receivables (including retained interests in securitized trade receivables) at Cat Financial.

## OPERATING PROFIT




The chart above graphically illustrates reasons for the change in Consolidated Operating Profit between 2002 (at left) and 2003 (at right). Items favorably impacting operating profit appear as upward stair steps with the corresponding dollar amounts above each bar, while items negatively impacting operating profit appear as downward stair steps with dollar amounts reflected in parenthesis above each bar. Caterpillar management utilizes these charts internally to visually communicate with its Board and employees.

The favorable profit impact of additional machinery and engine sales volume was partially offset by unfavorable sales mix resulting in a net positive impact of $175 million. The unfavorable sales mix was primarily due to lower sales of higher margin fuel system components to Navistar International Transportation Corporation ("Navistar") attributable to the imminent expiration of a long-term purchase contract in 2003 between Caterpillar and Navistar as well as higher sales of lower margin small diesel engines and compact construction equipment. Improved price realization reflected the favorable impact of modest price increases taken in January 2003 on most machines and parts. Material cost reductions and quality improvements reflected in lower warranty costs were partially offset by higher incentive compensation of about $140 million for a net improvement in core operating costs of $231 million. The higher incentive compensation benefits employees at all levels as corporate financial performance improves. This reflects the structure of our compensation plans where employees have a component of their pay tied to the performance of the company.

Partially offsetting the favorable items was $310 million of higher retirement benefits. This increase was primarily due to the impact of previous poor performance of equity markets on pension plan assets and increased expense resulting from the introduction of a company match to our 401(k) plan in 2003.

**Operating Profit Table**

| (Millions of dollars) | **2003** | 2002 |
|---|---|---|
| Machinery[1] | **$1,246** | $ 947 |
| Engines[1] | **188** | 175 |
| Financial Products | **345** | 284 |
| Consolidating Adjustments[2] | **(91)** | (82) |
| | **$1,688** | $1,324 |

[1] Caterpillar operations are highly integrated; therefore, the company uses a number of allocations to determine lines of business operating profit for Machinery and Engines.

[2] Consolidating adjustments consist of eliminations of transactions between Machinery and Engines and Financial Products.

**Machinery operating profit** increased 32 percent, or $299 million, from 2002. The favorable impact of improved price realization, higher sales volume (net of unfavorable sales mix) and lower core operating costs more than offset higher retirement benefits.

**Engines operating profit** increased 7 percent, or $13 million, from 2002 as lower core operating costs were almost entirely offset by higher retirement benefits and the unfavorable impact of ***Changes in Emissions Standards***. The favorable impact of volume was offset by negative sales mix resulting from lower sales of higher margin fuel system components as well as higher sales of lower margin small diesel engines.

**Financial Products** operating profit increased 21 percent, or $61 million, from 2002. The increase was primarily due to the impact of growth of earning assets of $59 million, higher fee income of $12 million and higher securitization income of $8 million at Cat Financial. These favorable items were partially offset by increased operating costs to support growth at Cat Financial.

## OTHER PROFIT/LOSS ITEMS

**Interest expense excluding Financial Products** was $33 million lower compared to 2002 primarily due to lower average short-term and long-term borrowings.

**Other income/expense** was income of $35 million down from $69 million in 2002. The change was primarily due to a $55 million charge for early retirement of the $250 million 6 percent debentures due in 2007.

**The provision for income taxes** reflects an estimated annual tax rate of 27 percent for 2003 compared to 28 percent a year ago due to the geographic mix of profits and changes in the estimated tax benefits from export sales.

**The equity in profit/loss of unconsolidated affiliated companies** favorably impacted profit $24 million from 2002, due mostly to improved profitability of Shin Caterpillar Mitsubishi Ltd. resulting from improved export business into China and North America.

## OPERATING COST RECLASSIFICATION

In the second quarter of 2003, we revised our policy regarding the classification of certain costs related to distributing replacement parts. Previously, these costs were included in SG&A and now are included in cost of goods sold. This classification is more consistent with industry practice. The parts distribution costs include shipping and handling (including warehousing) along with related support costs such as information technology, purchasing and inventory management.

The amounts reclassified from SG&A expense to cost of goods sold were $437 million and $443 million for 2002 and 2003, respectively. The reclassification had no impact on operating profit.

## GLOSSARY OF TERMS

1. **Changes in Emissions Standards (Emissions)** — Generally, emissions describes the financial impacts of industry emission standard changes for on-highway truck and bus engines in North America. With respect to sales and revenues, emissions represents the impact of price increases. With respect to operating profit, emissions represents the net impact of price increases, production cost increases which include incremental ramp-up production costs and non-conformance penalties (NCPs).
2. **Consolidating Adjustments** — Eliminations of transactions between Machinery and Engines and Financial Products.
3. **Constant Dollars** — The dollar value of machine and engine deliveries adjusted for changes in price and currency.
4. **Core Operating Costs** — Machinery and Engines operating cost change adjusted for volume. It excludes the impact of currency, retirement benefits and Non-Conformance Penalties.
5. **Currency** — With respect to sales and revenues, currency represents the translation impact on sales resulting from changes in foreign currency exchange rates versus the U.S. dollar. With respect to operating profit, currency represents the net translation impact on sales and operating costs resulting from changes in foreign currency exchange rates versus the U.S. dollar. With respect to profit before tax, currency represents the net translation impact on sales, operating costs and other income/expense resulting from changes in foreign currency exchange rates versus the U.S. dollar. Also included in the currency impact on profit before tax is the effect of currency forward and option contracts entered into by the company to reduce the risk of fluctuations in exchange rates. Currency includes the impacts on sales and operating profit for the Machinery and Engines lines of business only; currency impacts on the Financial Products line of business are included in the Financial Products portions of the respective analyses.

6. **EAME** — Geographic region including Europe, Africa, the Middle East and the Commonwealth of Independent States (CIS).
7. **Earning Assets** — These assets consist primarily of total net finance receivables plus retained interests in securitized trade receivables, plus equipment on operating leases, less accumulated depreciation at Cat Financial. Net finance receivables represent the gross receivables amount less unearned income and the allowance for credit losses.
8. **Latin America** — Geographic region including the Central and South American countries and Mexico.
9. **Machinery and Engines** — Due to the highly integrated nature of operations, represents the aggregate total of the Machinery and Engines lines of business and includes primarily our manufacturing, marketing and parts distribution operations.
10. **Non-Conformance Penalties (NCPs)** — Pursuant to a consent decree Caterpillar and other engine manufacturers entered into with the United States Environmental Protection Agency (EPA), the company was required to meet certain emission standards by October 2002 for engines manufactured for on-highway use. Under the consent decree, an engine manufacturer was required to pay a non-conformance penalty (NCP) to the EPA for each engine manufactured after October 1, 2002 that did not meet the standards. The amount of the NCP was based on how close to meeting the standards the engine came — the more the engine was out of compliance, the higher the penalty per engine.
11. **Price Realization** — The impact of net price changes excluding currency.
12. **Retirement Benefits** — Cost of defined benefit pension plans, defined contribution plans and retirement health care and life insurance.
13. **Sales Volume** — With respect to sales and revenues, sales volume represents the impact of changes in the quantities sold for machines, engines and parts. With respect to operating profit, sales volume represents the impact of changes in the quantities sold for machines, engines and parts combined with the net operating profit impact of changes in the relative weighting of machines, engines and parts sales with respect to total sales.
14. **Sales Volume/Mix** — The net operating profit impact of changes in the quantities sold for machines, engines and parts combined with the net operating profit impact of changes in the relative weighting of machines, engines and parts sales with respect to total sales.
15. **6 Sigma** — On a technical level, 6 Sigma represents a measure of variation that achieves 3.4 defects per million opportunities. At Caterpillar, 6 Sigma represents a much broader cultural philosophy to drive continuous improvement throughout the value chain. It is a fact-based, data-driven methodology that we are using to improve processes, enhance quality, cut costs, grow our business and deliver greater value to our customers through Black Belt-led project teams. At Caterpillar, 6 Sigma goes beyond mere process improvement; it has become the way we work as teams to process business information, solve problems and manage our business successfully.

## LIQUIDITY & CAPITAL RESOURCES

### Reclassification of certain receivables and related cash flows

#### A. Consolidated financial position

Our Machinery and Engines operations generate trade receivables from the sale of inventory to dealers and customers. Certain of these receivables are sold to Cat Financial. Cat Financial holds the receivables and periodically securitizes a portion of the dealer receivables using a revolving securitization structure. Cat Financial's portion of the securitized trade receivables is represented by certificated retained interests. Cat Financial also generates wholesale inventory receivables from its direct financing of inventory purchases by dealers. Previously, the certificated retained interests as well as the wholesale inventory receivables were classified as Finance Receivables in our Consolidated Financial Position. In the fourth quarter of 2004, we reclassified the certificated retained interests from Finance Receivables to Retained Interests in Securitized Trade Receivables and the wholesale inventory receivables from Finance Receivables to Trade and Other Receivables in our Consolidated Financial Position. These changes were made to align the financial position with the cash flow changes discussed below.

#### B. Consolidated statement of cash flow

During the fourth quarter of 2004, the staff of the Securities and Exchange Commission expressed concern regarding the classifications of certain cash flows by companies with captive finance subsidiaries. As a result of this concern, management decided to make reclassifications to the 2002 and 2003 Consolidated Statements of Cash Flow as described below.

#### Securitized trade receivables

Previously, we reported an increase in cash flow from operating activities in the Consolidated Statement of Cash Flow when Machinery and Engines sold receivables to Cat Financial that were subsequently securitized. Concurrently, Cat Financial's entire purchase of these receivables was included in Additions to Finance Receivables (investing activity) in the Consolidated Statement of Cash Flow. The receivables were immediately securitized and the portion sold to a third party was included in Proceeds from Sale of Finance Receivables (investing activity) in the Consolidated Statement of Cash Flow. Subsequently, collection of the certificated retained interests was included in Collection of Finance Receivables (investing activity) in the Consolidated Statement of Cash Flow. This cash flow treatment followed our principal lines of business reporting, however, when we reported an increase in cash flow from operating activities and a corresponding outflow from investing activities there was no increase in cash on a consolidated basis from the sale of inventory to our dealers and customers.

In the fourth quarter of 2004, we made a reclassification to eliminate the offsetting non-cash intercompany transactions in the Consolidated Statement of Cash Flow. In addition, we reclassified the proceeds from sale of trade receivables to operating activities. The reclassification properly classifies cash receipts from the sale of inventory as operating activities and reflects that these cash flows, although held and managed by Cat Financial, arise from our sale of Machinery and Engines inventory.

The securitization structure mentioned above involves a securitization trust. During 2003 and 2002, the trust was a qualifying special purpose entity (QSPE) and thus, in accordance with Statement of Financial Accounting Standards No. 140 (SFAS 140), "Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities," was not consolidated. When receivables were placed into the trust, we received cash for the portion sold to third party purchasers and the portion retained by Cat Financial was represented by certificated retained interests. Placing receivables into a securitization trust changes their nature and the receipt of certificated retained interests is considered a non-cash transaction. We have noted this non-cash transaction on the Consolidated Statement of Cash Flow and quantified the receivables decrease resulting from this transaction and thus excluded from operating activities. This reflects that certificated retained interests, not cash, were received for these sales. The certificated retained interests are considered held-to-maturity securities as defined by Statement of Financial Accounting Standards No. 115 (SFAS 115), "Accounting for Certain Investments in Debt and Equity Securities." SFAS 115 requires that collection of held-to-maturity securities be classified as an investing activity. We have therefore reclassified the collection of the certificated retained interests from Collection of Finance Receivables to Collections of Retained Interests in Securitized Trade Receivables within the investing activities section of the Consolidated Statement of Cash Flow. The impact of these changes is a significant reduction to cash flow from operating activities and a significant increase in cash flow from investing activities. This reflects that although inventory was sold, the nature of the receivable was changed to a security. The subsequent collection of that security is shown as an investing activity.

### Wholesale inventory receivables

Previously, we reported an increase in cash flow from operating activities when a dealer remitted payment for a trade receivable that was subsequently financed with the issuance of a wholesale inventory receivable by Cat Financial. The issuance of a wholesale inventory receivable by Cat Financial was reported as an Addition to Finance Receivables in the Consolidated Statement of Cash Flow and the subsequent collection was reported as a Collection of Finance Receivables. Similar to securitized receivables, this cash flow treatment followed our principal lines of business reporting, however, when we reported an increase in cash flow from operating activities and a corresponding outflow from investing activities there was no increase in cash on a consolidated basis from the sale of inventory to our dealers and customers. We therefore eliminated the offsetting non-cash transaction in the Consolidated Statement of Cash Flow. In addition, we reclassified the collection of wholesale inventory receivables to operating activities. The reclassification properly classifies cash receipts from the sale of inventory as operating activities and reflects that these cash flows, although held and managed by Cat Financial, arise from our sale of Machinery and Engines inventory.

These reclassifications had no impact on the Increase in Cash and Short-term Investments on the Statement of Consolidated Cash Flow.

Prior amounts reported have been reclassified to conform to this presentation as follows:

| | 2003 | | | 2002 | | |
|---|---|---|---|---|---|---|
| (Millions of dollars) | Previous classification[1] | Change | As Reclassified | Previous classification[1] | Change | As Reclassified |
| **Consolidated Financial Position — Statement 3** | | | | | | |
| Receivables — trade and other | $ 3,666 | $ 359 | $ 4,025 | $ 2,838 | $ 354 | $ 3,192 |
| Receivables — finance | 7,417 | (1,909) | 5,508 | 6,565 | (1,499) | 5,066 |
| Retained interests in securitized trade receivables | — | 1,550 | 1,550 | — | 1,145 | 1,145 |
| Long-term receivables — trade and other | 82 | 428 | 510 | 66 | 367 | 433 |
| Long-term receivables — finance | 7,822 | (428) | 7,394 | 6,714 | (367) | 6,347 |
| **Consolidated Statement of Cash Flow — Statement 4** | | | | | | |
| Receivables — trade and other | $ (438) | $ (7,677) | $ (8,115) | $ 5 | $ (6,328) | $ (6,323) |
| **Net cash provided by (used for) operating activities** | **2,066** | **(7,677)** | **(5,611)** | **2,366** | **(6,328)** | **(3,962)** |
| Additions to finance receivables | (17,146) | 10,278 | (6,868) | (15,338) | 9,405 | (5,933) |
| Collections of finance receivables | 13,882 | (8,631) | 5,251 | 11,866 | (7,297) | 4,569 |
| Proceeds from sale of finance receivables | 1,760 | (1,099) | 661 | 2,310 | (1,697) | 613 |
| Collections of retained interests in securitized trade receivables | — | 7,129 | 7,129 | — | 5,917 | 5,917 |
| **Net cash provided by (used for) investing activities** | **(2,793)** | **7,677** | **4,884** | **(2,708)** | **6,328** | **3,620** |

[1] Certain amounts do not agree to prior period reported amounts due to unrelated reclassifications.

### Sources of funds

We generate our capital resources primarily through operations and collections of certificated retained interests in trade receivables (discussed above). Collections of certificated retained interests take place when the securitization trust collects cash and distributes it to Cat Financial. In 2004, operating cash flow was negative $3.99 billion and collections of certificated retained interests in trade receivables were $5.72 billion totaling positive $1.73 billion. In 2003, operating cash flow was negative $5.61 billion and collections of certificated retained interests in trade receivables were $7.13 billion totaling positive $1.52 billion. The increase in the total of these sources of funds from $1.52 billion in 2003 to $1.73 billion in 2004 is primarily the result of higher profitability in 2004 as compared to 2003, largely offset by an increase in working capital requirements. The decrease in collections of certificated retained interests from 2003 to 2004 of $1.41 billion reflects that the securitization trust was a QSPE (and thus not consolidated) for all of 2003 compared with eight months of

2004, partially offset by a higher volume of collections in 2004. From September to December of 2004, because of a significant increase in Machinery and Engines' sales and subsequent sale of the receivables to Cat Financial, our certificated retained interests in the trust exceeded 90% of the fair value of trust assets. Thus, during this period, the trust did not qualify as a QSPE as defined by SFAS 140. We therefore consolidated the trust in accordance with FIN 46R, "Consolidation of Variable Interest Entities" (revised) as it represents a variable interest entity for which Cat Financial is the primary beneficiary. We anticipate that the majority of future capital resource requirements will be funded by operating cash flow, which is largely sourced from our profits. See our Outlook on page A-60.

Total debt as of December 31, 2004 was $23.5 billion, an increase of $3.24 billion from year-end 2003. Debt related to Machinery and Engines increased only $55 million, as cash for capital expenditures, the stock repurchase program, payment of dividends, and acquisitions were largely provided by operations. Debt related to Financial Products increased $3.19 billion due to financing a higher amount of assets at Cat Financial.

We have two global credit facilities with a syndicate of banks totaling $5.0 billion available in the aggregate to both Machinery and Engines and Financial Products to support commercial paper programs. Based on Management's allocation decision, which can be revised at any time during the year, the portion of the facility available to Cat Financial at December 31, 2004 was $4.4 billion. The five-year facility of $2.5 billion expires in September 2009. The 364-day facility of $2.5 billion expires in September 2005. The facility expiring in September 2005 has a provision that allows Caterpillar or Cat Financial to obtain a one-year loan in September 2005 that would mature in September 2006. Our total credit commitments as of December 31, 2004 were:

| (Millions of dollars) | Consolidated | Machinery and Engines | Financial Products |
|---|---|---|---|
| Credit lines available: | | | |
| Global credit facilities | $5,000 | $ 600 | $4,400 |
| Other external | 1,849 | 758 | 1,091 |
| Total credit lines available | 6,849 | 1,358 | 5,491 |
| Less: Global credit facilities supporting commercial paper | 4,412 | 40 | 4,372 |
| Less: Utilized credit | 463 | 93 | 370 |
| Available credit | $1,974 | $1,225 | $ 749 |

We also generate funding through the securitization and syndication of receivables where the investors and/or the securitization trusts have limited or no recourse to Caterpillar or Cat Financial. In 2004, we generated $663 million of capital resources from the securitization of trade receivables. These receivables arose from our sale of inventory to dealers. During 2004, Cat Financial sold retail (customer) leases and installment sale contracts through syndications; proceeds of $61 million were received from the sale of such contracts.

To maintain an alternative funding source, Cat Financial periodically (generally once a year) securitizes retail (customer) installment sale contracts and finance leases. In this process, these finance receivables are sold into a public asset-backed securitization trust. The trusts, bankruptcy remote qualified special purpose entities (QSPEs) that are not consolidated in our financial statements, held total assets of $815 million related to these securitizations at year-end 2004. We use QSPEs in a manner consistent with conventional practices in the securitization industry to isolate these finance receivables, which are secured by new and used equipment, for the benefit of securitization investors. Our sensitivity analysis indicated that the impact of a 20 percent adverse change to all individual assumptions used to calculate the fair value of all our retained interests at December 31, 2004 would be less than $2 million.

The use of the QSPEs enables us to access the U.S. securitization market for the sale of these types of financial assets. The amounts of funding from securitizations reflect such factors as capital market accessibility, relative costs of funding sources, and assets available for securitization. We had total proceeds from initial sales of these receivables of $659 million and $693 million, and recognized a pre-tax gain of $13 million and $22 million, for 2004 and 2003, respectively. Subordinated retained interests in the public securitizations from 2004 and earlier years totaled $73 million.

We do not generate material funding through structured finance transactions.

### Machinery and Engines

Machinery and Engines operating cash flow was $1.92 billion for 2004, compared with $1.43 billion for 2003. This increase is primarily the result of higher profit. The increase in sales volume has resulted in higher inventory. The surge in volume has also resulted in key component shortages, which have resulted in delayed production driving additional inventory increases. This increase in inventory was about offset by an increase in accounts payable resulting from the additional volume as well as a change in invoice payment terms that impacted most of our U.S. locations. The terms change was effective November 1, 2004 and offered suppliers a choice of a cash discount with an accelerated payment or extension of existing payment terms by an average of one month. Most suppliers chose the terms extension.

Pursuant to the share repurchase program authorized by the Board of Directors in October 2003, $539 million was spent to repurchase 6.9 million shares during 2004. There were 342.9 million shares outstanding at the end of 2004. The goal of the share repurchase program, which expires in October 2008, is to reduce the company's outstanding shares to 320 million.

Capital expenditures, excluding equipment leased to others, during 2004 were $841 million, an increase of $187 million from 2003 to support growth and new product initiatives. Acquisitions resulted in a decrease to cash of $295 million primarily from the acquisitions of the MG Rover Ltd. parts distribution business and Williams Technologies, Inc.

### Financial Products

Operating cash flow was $962 million for 2004, compared with $463 million for 2003. The increase is primarily the result of an increase in profit and lower working capital requirements. Cash used to purchase equipment leased to others was $1.19 billion for 2004 compared to $1.07 billion for 2003. In addition, net cash used for finance receivables and retained interests in securitized trade receivables was $3.15 billion for 2004, compared with $1.33 billion for 2003 due to growth at Cat Financial.

**Contractual obligations**

The company has committed cash outflow related to long-term debt, operating lease agreements, purchase obligations and other contractual obligations. Minimum payments for these long-term obligations are:

| (Millions of dollars) | 2005 | 2006 | 2007 | 2008 | 2009 | After 2009 | Total |
|---|---|---|---|---|---|---|---|
| Long-term debt: | | | | | | | |
| Machinery and Engines | $ 6 | $ 290 | $ 297 | $ 26 | $ 363 | $ 2,022 | $ 3,004 |
| Financial Products | 3,525 | 4,137 | 2,567 | 1,134 | 3,103 | 1,233 | 15,699 |
| Total long-term debt | 3,531 | 4,427 | 2,864 | 1,160 | 3,466 | 3,255 | 18,703 |
| Capital leases | 32 | 31 | 30 | 30 | 31 | 918 | 1,072 |
| Operating leases | 163 | 132 | 90 | 69 | 59 | 384 | 897 |
| Postretirement obligations[1] | 530 | 510 | 770 | 530 | 540 | 2,550 | 5,430 |
| Purchase obligations: | | | | | | | |
| Accounts payable[2] | 3,990 | — | — | — | — | — | 3,990 |
| Purchase orders[3] | 3,954 | — | — | — | — | — | 3,954 |
| Other contractual obligations[4] | 121 | 121 | 101 | 3 | 1 | 468 | 815 |
| Total purchase obligations | 8,065 | 121 | 101 | 3 | 1 | 468 | 8,759 |
| Other long-term liabilities[5] | 156 | 134 | 87 | 62 | 37 | 73 | 549 |
| Interest on long-term debt[6] | 599 | 471 | 366 | 303 | 245 | 4,140 | 6,124 |
| Total contractual obligations | $13,076 | $ 5,826 | $ 4,308 | $2,157 | $ 4,379 | $11,788 | $41,534 |

[1] Amounts represent expected contributions to our pension and other postretirement benefit plans through 2014, offset by expected Medicare Part D subsidy receipts.
[2] Amount represents invoices received and recorded as liabilities in 2004, but scheduled for payment in 2005. These represent short-term obligations made in the ordinary course of business.
[3] Amount represents contractual obligations for material and services on order at December 31, 2004 but not yet delivered. These represent short-term obligations made in the ordinary course of business.
[4] Amounts represent long-term commitments entered into with key suppliers for minimum purchases quantities.
[5] Amounts represent contractual obligations related to software license contracts, IT consulting contracts and outsourcing contracts for benefit plan administration and software system support.
[6] Amounts represent estimated contractual interest payments on long-term debt.

Financial Products total borrowings were $19.76 billion at December 31, 2004, an increase of $3.19 billion from December 31, 2003 due to financing a higher amount of assets. Debt repayment in Financial Products depends primarily on timely repayment and collectibility of the receivables portfolio. At December 31, 2004, finance receivables past due over 30 days were 1.6%, compared with 2.5% at December 31, 2003. The allowance for credit losses was 1.38% of finance receivables, net of unearned income, at December 31, 2004, compared to 1.49% at December 31, 2003. Receivables written off due to uncollectibility, net of recoveries on receivables previously written off, were $72 million and $82 million for 2004 and 2003, respectively.

Financial Products was in compliance with all debt covenants at December 31, 2004 except Cat Financial's debt-to-equity ratio, as defined under the global credit facilities, which was 8.23 to 1 at December 31, 2004. By covenant, this is not to exceed 8.00 to 1 at year-end (8.5 to 1 moving six-month average at other than year-end). At December 31, 2004, there were no borrowings under these facilities. The higher year-end ratio was primarily the result of unexpected record levels of financing activity in the fourth quarter. Cat Financial received a waiver from its banks for said failure and expects to be in compliance with all credit facility agreement covenants throughout 2005.

**Dividends paid per common share**

| Quarter | **2004** | 2003 | 2002 |
|---|---|---|---|
| First | **$ .370** | $ .350 | $ .350 |
| Second | **.370** | .350 | .350 |
| Third | **.410** | .350 | .350 |
| Fourth | **.410** | .370 | .350 |
| | **$1.560** | $1.420 | $1.400 |

## CRITICAL ACCOUNTING POLICIES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect reported amounts. The more significant estimates include: residual values for leased assets, fair market values for goodwill impairment tests, and reserves for warranty, product liability and insurance losses, postretirement benefits, post-sale discounts, credit losses and income taxes. We have incorporated many years of data into the determination of each of these estimates and we have not historically experienced significant adjustments. These assumptions are reviewed at least annually with the Audit Committee of the Board of Directors. Following are the methods and assumptions used in determining our estimates and an indication of the risks inherent in each.

**Residual values for leased assets** — Determined based on the product, specifications, application and hours of usage. Each product has its own model for evaluation that includes market value cycles and forecasts. Consideration is also given to the amount of assets that will be returned from lease during a given time frame. Residual values could decline due to economic factors, obsolescence or other adverse circumstances.

**Fair market values for goodwill impairment tests** — Determined for each reporting unit by discounting projected cash flow for five years and adding a year-five residual value based upon a market Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) multiple. The estimated fair value could be impacted by changes in interest rates, growth rates, costs, capital expenditures and market conditions.

**Warranty reserve** — Determined by applying historical claim rate experience to the current field population and dealer inventory.

Historical claim rates are developed using a rolling average of actual warranty payments. Effective in the third quarter of 2004, we refined our process to utilize more detailed claim rates by product. This provides more comprehensive product warranty information for management. This change did not have a material impact on our financial statements. Warranty payments may differ from those estimated if actual claim rates are higher or lower than our historical rates.

**Product liability and insurance loss reserve** — Determined based upon reported claims in process of settlement and actuarial estimates for losses incurred but not reported. Loss reserves, including incurred but not reported reserves, are based on estimates and ultimate settlements may vary significantly from such estimates due to increased claims frequency or severity over historical levels.

**Postretirement benefits** — Primary actuarial assumptions were determined as follows: (See Tables on pages A-55 to A-56 for Sensitivity information for these assumptions.)

- The U.S. expected long-term rate of return on plan assets is based on our estimate of long-term passive returns for equities and fixed income securities weighted by the allocation of our plan assets. Based on historical performance, we increase the passive returns due to our active management of the plan assets. A similar process is used to determine the rate for our non-U.S. pension plans. This rate is impacted by changes in general market conditions, but because it represents a long-term rate, it is not significantly impacted by short-term market swings. Changes in our allocation of plan assets would also impact this rate. For example, a shift to more fixed income securities would lower the rate. A decrease in the rate would increase our expense.
- The assumed discount rate is used to discount future benefit obligations back to today's dollars. The U.S. discount rate is based on the Moody's Aa bond yield as of our measurement date, November 30, and represents the rate at which our benefit obligations could effectively be settled. A similar process is used to determine the assumed discount rate for our non-U.S. plans. This rate is sensitive to changes in interest rates. A decrease in the discount rate would increase our obligation and expense.
- The expected rate of compensation increase is used to develop benefit obligations using projected pay at retirement. It represents average long-term salary increases. This rate is influenced by our long-term compensation policies. An increase in the rate would increase our obligation and expense.
- The assumed health care trend rate represents the rate at which health care costs are assumed to increase and is based on historical and expected experience. Changes in our projections of future health care costs due to general economic conditions and those specific to health care (e.g. technology driven cost changes) will impact this trend rate. An increase in the trend rate would increase our obligation and expense.

**Post-sale discount reserve** — The company extends numerous merchandising programs that provide discounts to dealers as products are sold to end users. The reserve is determined based on historical data adjusted for known changes in merchandising programs. Discounts paid may differ from those estimated if actual program usage is higher or lower than our historical or expected rates.

**Credit loss reserve** — The allowance for credit losses is evaluated on a regular basis and adjusted based upon management's best estimate of probable losses inherent in our finance receivables. In estimating probable losses, we review accounts that are past due, non-performing, or in bankruptcy. We also review accounts that may be at risk using information available about the customer, such as financial statements, news reports, and published credit ratings. We also use general information regarding industry trends and the general economic environment. Using an estimate of current fair market value of collateral and factoring in credit enhancements, such as additional collateral and third party guarantees, we arrive at an estimated loss for specific accounts and estimate an additional amount for the remainder of the finance receivables based upon historical trends. Adverse economic conditions or other factors that might cause deterioration of the financial health of our customers could change the timing and level of payments received and thus necessitate a change in our estimated losses.

**Income tax reserve** — Despite our belief that our tax return positions are consistent with applicable tax laws, we believe that certain positions are likely to be challenged by taxing authorities. Settlement of any challenge can result in no change, a complete disallowance, or some partial adjustment reached through negotiations or litigation. Significant judgment is required in evaluating our tax reserves. Our reserves are adjusted in light of changing facts and circumstances, such as the progress of our tax audits. Our income tax expense includes the impact of reserve provisions and changes to reserves that we consider appropriate, as well as related interest and penalties. Unfavorable settlement of any particular issue would require use of our cash. Favorable resolution would be recognized as a reduction to income tax expense at the time of resolution.

## EMPLOYMENT

At December 31, 2004, Caterpillar's worldwide employment was 76,920 compared with 69,169 one year ago. The increase is primarily due to hourly labor additions to support increased volume and the addition of approximately 2,500 employees from acquisitions and growing Caterpillar Logistics operations.

**Full-Time Employees at Year End**

| | **2004** | 2003 | 2002 |
|---|---|---|---|
| Inside U.S. | **38,128** | 35,260 | 36,463 |
| Outside U.S. | **38,792** | 33,909 | 32,527 |
| Total | **76,920** | 69,169 | 68,990 |
| By Region: | | | |
| North America | **38,396** | 35,486 | 36,667 |
| EAME | **22,169** | 20,547 | 21,302 |
| Latin America | **10,733** | 8,533 | 7,143 |
| Asia/Pacific | **5,622** | 4,603 | 3,878 |
| Total | **76,920** | 69,169 | 68,990 |

## OTHER MATTERS

### ENVIRONMENTAL AND LEGAL MATTERS

The company is regulated by federal, state, and international environmental laws governing our use of substances and control of emissions in all our operations. Compliance with these existing laws has not had a material impact on our capital expenditures or earnings. We believe that our Advanced Combustion Emission Reduction Technology (ACERT) developed to comply with EPA emissions regulations provides Caterpillar a competitive advantage now and in the future to meet emission requirements.

We are cleaning up hazardous waste at a number of locations, often with other companies, pursuant to federal and state laws. When it is likely we will pay clean-up costs at a site and those costs can be estimated, the costs are charged against our earnings. In doing that estimate, we do not consider amounts expected to be recovered from insurance companies and others.

The amount recorded for environmental clean-up is not material and is included in “Accrued expenses” in Statement 3. If a range of liability estimates is available on a particular site, we accrue at the lower end of that range.

We cannot estimate costs on sites in the very early stages of clean-up. Currently, we have several sites in the very early stages of clean-up, and there is no more than a remote chance that a material amount for clean-up will be required.

Pursuant to a consent decree Caterpillar entered with the EPA, the company was required to meet certain emission standards by October 2002. The decree provides that if engine manufacturers were unable to meet the standards at that time, they would be required to pay a Non-Conformance Penalty (NCP) on each engine sold that did not meet the standard. The amount of the NCP would be based on how close to meeting the standard the engine came — the more out of compliance the higher the penalty. The company began introduction of fully compliant ACERT engines in 2003 and by the end of 2003 Caterpillar was only producing fully compliant engine models. As a result, NCPs were not payable for any engines built in 2004. NCPs of $153 million were paid in 2003.

In addition, the consent decree required Caterpillar to pay a fine of $25 million, which was expensed in 1998, and to make investments totaling $35 million in environmental-related products by July 7, 2007. Total qualifying investments to date for these projects are $34.9 million, of which $5.9 million was made during 2004. Caterpillar expects to reach the $35 million requirement during the first quarter of 2005. A future benefit is expected to be realized from these environmental projects related to Caterpillar’s ability to capitalize on the technologies it developed in complying with its environmental project obligations. In short, Caterpillar expects to receive a positive net return on the environmental projects by being able to market the technology it developed.

We are a party to litigation matters and claims that are normal in the course of our operations, and, while the results of such litigation and claims cannot be predicted with certainty, management believes, based on the advice of counsel, the final outcome of such matters will not have a materially adverse effect on our financial statements.

On January 16, 2002, Caterpillar commenced an action in the Circuit Court of the Tenth Judicial Circuit of Illinois in Peoria, Illinois, against Navistar International Transportation Corporation and International Truck and Engine Corporation (collectively Navistar). The lawsuit arises out of a long-term purchase contract between Caterpillar and Navistar effective May 31, 1988, as amended from time to time (the Purchase Agreement). The pending complaint alleges that Navistar breached its contractual obligations by: (i) paying Caterpillar $8.08 less per fuel injector than the agreed upon price for new unit injectors delivered by Caterpillar; (ii) refusing to pay contractually agreed upon surcharges owed as a result of Navistar ordering less than planned volumes of replacement unit injectors; and (iii) refusing to pay contractually agreed upon interest stemming from Navistar’s late payments. As of December 31, 2004, the net past due receivable from Navistar regarding the foregoing and included in “Long-term receivables — trade and other” in Statement 3 totaled $139 million. The pending complaint also has claims alleging that Franklin Power Products, Inc., Newstream Enterprises, and Navistar, collectively and individually, failed to pay the applicable price for shipments of unit injectors to Franklin and Newstream. As of December 31, 2004, the net past due receivables for the foregoing, included in “Long-term receivables — trade and other” in Statement 3 totaled $13 million. The pending complaint further alleges that Sturman Industries, Inc., and Sturman Engine Systems, Inc., colluded with Navistar to utilize technology that Sturman Industries, Inc., misappropriated from Caterpillar to help Navistar develop its G2 fuel system, and tortiously interfered with the Purchase Agreement and Caterpillar’s prospective economic relationship with Navistar. The pending complaint further alleges that the two parties’ collusion led Navistar to select Sturman Engine Systems, Inc. and another company, instead of Caterpillar, to develop and manufacture the G2 fuel system.

On May 7, 2002, International Truck and Engine Corporation (International) commenced an action against Caterpillar in the Circuit Court of DuPage County, Illinois that alleges Caterpillar breached various aspects of a long-term agreement term sheet. In its fifth amended complaint, International seeks a declaration from the court that the term sheet constitutes a legally binding contract for the sale of heavy-duty engines at specified prices through the end of 2006, alleges that Caterpillar breached the term sheet by raising certain prices effective October 1, 2002, and also alleges that Caterpillar breached an obligation to negotiate a comprehensive long-term agreement referenced in the term sheet. International has also asserted a claim for “unjust enrichment” related to certain revenues received by Caterpillar from another customer. International seeks damages “in an amount to be determined at trial” and injunctive relief. Caterpillar denies International’s claims and has filed a counterclaim seeking a declaration that the term sheet has been effectively terminated. Caterpillar also asserts that International has released Caterpillar from certain of its claims. On September 24, 2003, the Appellate Court of Illinois, ruling on an interlocutory appeal, issued an order consistent with Caterpillar’s position that, even if the court subsequently determines that the term sheet is a binding contract, it is indefinite in duration and was therefore terminable at will by Caterpillar after a reasonable period. Caterpillar anticipates that a trial currently scheduled to begin in June 2005 will address all remaining issues in this matter. This matter is not related to the breach of contract action brought by Caterpillar against Navistar currently pending in the Circuit Court of Peoria County, Illinois.

In 2004, the European Union (EU) imposed retaliatory tariffs on certain U.S. origin goods as a result of a WTO decision that found the extraterritorial income exclusion (ETI) provisions of the FSC Repeal and Extraterritorial Income Exclusion Act of 2000 constituted a prohibited export subsidy. These tariffs, which began in March of 2004 at 5 percent, increased 1 percentage point per month. Given the makeup of the final retaliation list, some Caterpillar parts and components were subject to these tariffs. However, these tariffs have not materially impacted our financial results. In addition to the United States, the company has production facilities in the EU, Russia, Asia, and South America. Products sold into the EU from these plants were not affected by this retaliatory tariff. The American Jobs Creation Act of 2004 (Act), enacted on October 22, 2004, phases-out the ETI provisions. As a result, the EU has lifted the sanctions effective January 1, 2005 pending the outcome of a WTO review to determine whether certain provisions of the Act are compliant with the ruling against the FSC/ETI regime.

In a letter dated November 15, 2004, the United States Environmental Protection Agency (EPA), proposed a civil penalty of $641,392 to Caterpillar Inc. (Caterpillar) for the alleged failure to comply with certain requirements of the federal Clean Air Act. The EPA alleges that Caterpillar constructed a facility in Emporia, Kansas and failed to comply with Section 112(g)(2)(B) of the Clean Air Act. Caterpillar sold the Emporia facility in December 2002. We are seeking a settlement of this matter with all concerned parties and the company believes the outcome will not have a material impact on our financial statements.

## RETIREMENT BENEFITS

We recognized pension expense of $274 million in 2004 as compared to $126 million in 2003. The increase in expense was primarily a result of the amortization of actuarial losses resulting from a declining discount rate and poor performance of the equity markets in 2002 and 2001. Statement of Financial Accounting Standards No. 87 (SFAS 87), "Employers' Accounting for Pensions" requires companies to discount future benefit obligations back to today's dollars using a discount rate that is based on high-quality fixed-income investments. A decrease in the discount rate increases the pension benefit obligation. This increase is amortized into earnings as an actuarial loss. SFAS 87 also requires companies to use an expected long-term rate of return on plan assets for computing current year pension expense. Differences between the actual and expected asset returns are also amortized into earnings as actuarial gains and losses. At the end of 2004, total unrecognized actuarial losses were $3.28 billion, as compared to $3.20 billion for 2003. The majority of the unrecognized losses are due to declining discount rates in recent years. The $80 million increase in unrecognized losses during 2004 was the result of a lower discount rate, largely offset by better than expected asset returns.

In 2004, we recognized other postretirement benefit expense of $256 million compared to $269 million in 2003. The decrease is the result of the recognition of anticipated benefits from the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (see further discussion below), largely offset by an increase in expense due to the amortization of actuarial losses resulting from a declining discount rate, higher than expected benefit costs and an increase in expected health care inflation. Unrecognized actuarial losses for other postretirement benefit plans were $1.23 billion at the end of 2004. These losses reflect a declining discount rate, an increase in expected health care inflation and higher than expected benefit costs. The unrecognized losses were $132 million lower than at the end of 2003 as the benefit from anticipated Medicare Part D subsidies, lower than expected health care costs and higher than planned asset returns more than offset the unfavorable impact of an increase in expected health care inflation and a lower discount rate.

The unrecognized actuarial losses for both pensions and other postretirement benefits will be impacted in future periods by actual asset returns, actual health care inflation, discount rate changes and other factors that impact these expenses. These losses will be amortized on a straight-line basis over the average remaining service period of active employees expected to receive benefits under the benefit plans. At the end of 2004, the average remaining service period of active employees was 13 years for our U.S. pension plans, 12 years for our non-U.S. pension plans and eight years for other postretirement benefit plans. We expect our amortization of net actuarial losses to increase approximately $100 million in 2005 as compared to 2004, primarily because of a decrease in the discount rate.

For our U.S. pension plans, our current asset allocation is 74 percent equity securities and 26 percent debt securities, and our target allocation for 2005 is 70 percent equity securities and 30 percent debt securities. The current asset allocation for our non-U.S. pension plans is 54 percent equity securities, 38 percent debt securities, 6 percent real estate and 2 percent other. The target allocation for 2005 for our non-U.S. pension plans is 55 percent equity securities, 38 percent debt securities and 7 percent real estate. Our target asset allocations reflect our investment strategy of maximizing the rate of return on plan assets and the resulting funded status, within an appropriate level of risk. The U.S. plans are rebalanced to plus or minus five percentage points of the target asset allocation ranges on a monthly basis. The frequency of rebalancing for the non-U.S. plans varies depending on the plan.

Our U.S. postretirement health care plans provide for prescription drug benefits. On December 8, 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act) was signed into law. The Act introduces a prescription drug benefit under Medicare (Medicare Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. In January 2004, the FASB issued FASB Staff Position No. 106-1 (FSP 106-1), "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003." As permitted by FSP 106-1, we made a one-time election to defer accounting for the effects of the Act pending further guidance from the FASB.

In May 2004, the FASB issued FASB Staff Position No. 106-2 (FSP 106-2), which superseded FSP 106-1. FSP 106-2 provides accounting guidance to employers that have determined that prescription drug benefits available under their retiree health care benefit plans are at least actuarially equivalent to Medicare Part D. The FSP requires that the benefit attributable to past service be accounted for as an actuarial gain and the benefit related to current service be reported as a reduction in service cost.

We have determined that most of our U.S. retiree health care plans are at least actuarially equivalent to Medicare Part D and will qualify for the federal subsidy. In the third quarter of 2004, we adopted FSP 106-2 retroactive to December 31, 2003 (the period end that includes the date of the Act's enactment), as permitted by the FSP. The impacts were a reduction in our accumulated postretirement benefit obligation of $284 million related to benefits attributed to past service and a benefit of $51 million to net periodic postretirement benefit expense. The benefits for the first, second, third and fourth quarters were $8 million, $14 million, $15 million and $14 million, respectively. Because the federal subsidy is tax exempt, no tax was provided for the benefit in the provision for income taxes. This lowered our estimated annual tax rate approximately one-half of one percentage point.

SFAS 87 requires the recognition of an Additional Minimum Liability if the market value of plan assets is less than the accumulated benefit obligation at the end of the measurement date. Based on these values, the company increased the Additional Minimum Liability by $47 million in the fourth quarter of 2004, bringing the total additional minimum pension liability to $1.60 billion. This resulted in a decrease in Accumulated Other Comprehensive Income (a component of Shareholder's Equity on the Consolidated Financial Position) of $59 million after tax. This adjustment was significantly less than our estimate based on third-quarter 2004 asset values primarily because of higher than expected asset returns in the fourth quarter for a primary U.S. pension plan. This resulted in plan assets being greater than the accumulated benefit obligation and thus no additional minimum pension liability was required. Future changes to the Additional Minimum Liability will be dependent on several factors including our assumed discount rate, actual returns on our pension plan assets, company contributions and benefit plan changes. During 2004, we made cash contributions of $565 million to our U.S. defined benefit pension plans and $112 million to our non-U.S. pension plans.

Although we have no ERISA funding requirements in 2005, we expect to make approximately $30 million of voluntary cash contributions to fund our U.S. pension plans. We also expect to make approximately $140 million of contributions to our non-U.S. pension plans during the year. We have adequate liquidity resources to fund both U.S. and non-U.S. plans.

Actuarial assumptions have a significant impact on both pension and other postretirement benefit expenses. The effects of a one-percentage point change in our primary actuarial assumptions on 2004 benefit costs and year-end obligations are included in the table below.

## SENSITIVITY

### Foreign Exchange Rate Sensitivity

Based on the anticipated and firmly committed cash inflow and outflow for our Machinery and Engines operations for the next 12 months and the foreign currency derivative instruments in place at year end, a hypothetical 10 percent weakening of the U.S. dollar relative to all other currencies would adversely affect our expected 2005 cash flow for our Machinery and Engines operations by approximately $200 million. Last year, similar assumptions and calculations yielded a potential $9 million adverse impact on 2004 cash flow. The change from 2004 to 2005 sensitivity analysis is due mainly to a decrease in our outstanding foreign currency derivative instruments, an increase in alternative sourcing from foreign subsidiaries, and foreign acquisitions. We determine our net exposures by calculating the difference in cash inflow and outflow by currency and adding or subtracting outstanding foreign currency derivative instruments. We multiply these net amounts by 10 percent to determine the sensitivity.

Since our policy for Financial Products operations is to hedge the foreign exchange risk when the currency of our debt portfolio does not match the currency of our receivable portfolio, a 10 percent change in the value of the U.S. dollar relative to all other currencies would not have a material effect on our Consolidated Financial Position, results of operations or cash flow. Neither

### Postretirement Benefit Plan Actuarial Assumptions Sensitivity

Following are the effects of a one percentage-point change in our primary pension and other postretirement benefit actuarial assumptions (included in the following table) on 2004 pension and other postretirement benefits costs and obligations:

| | 2004 Benefit Cost | | Year-end Benefit Obligation | |
|---|---|---|---|---|
| (Millions of dollars) | One percentage-point increase | One percentage-point decrease | One percentage-point increase | One percentage-point decrease |
| Pension benefits: | | | | |
| Assumed discount rate | $ (92) | $ 100 | $(1,281) | $1,445 |
| Expected rate of compensation increase | 39 | (37) | 201 | (192) |
| Expected long-term rate of return on plan assets | (90) | 91 | — | — |
| Other postretirement benefits: | | | | |
| Assumed discount rate | (22) | 41 | (430) | 472 |
| Expected rate of compensation increase | 1 | (1) | 4 | (3) |
| Expected long-term rate of return on plan assets | (8) | 8 | — | — |
| Assumed health care cost trend rate | 53 | (46) | 294 | (262) |

**Primary Actuarial Assumptions**

| | U.S. Pension Benefits | | | Non-U.S. Pension Benefits | | | Other Postretirement Benefits | | |
|---|---|---|---|---|---|---|---|---|---|
| | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 |
| **Weighted-average assumptions used to determine benefit obligations, end of year:** | | | | | | | | | |
| Discount rate | **5.9%** | 6.2% | 7.0% | **5.2%** | 5.1% | 5.4% | **5.9%** | 6.1% | 7.0% |
| Rate of compensation increase | **4.0%** | 4.0% | 4.0% | **3.5%** | 3.2% | 3.3% | **4.0%** | 4.0% | 4.0% |
| **Weighted-average assumptions used to determine net cost:** | | | | | | | | | |
| Discount rate | **6.2%** | 7.0% | 7.3% | **5.1%** | 5.4% | 5.7% | **6.1%** | 7.0% | 7.2% |
| Expected return on plan assets | **9.0%** | 9.0% | 9.8% | **7.4%** | 7.1% | 7.6% | **9.0%** | 9.0% | 9.8% |
| Rate of compensation increase | **4.0%** | 4.0% | 4.0% | **3.2%** | 3.3% | 3.3% | **4.0%** | 4.0% | 4.0% |
| **Health care cost trend rates at year end:** | | | | | | | | | |
| Health care trend rate assumed for next year | | | | | | | **8.4%** | 8.5% | 9.0% |
| Rate that the cost trend rate gradually declines to | | | | | | | **5.0%** | 4.5% | 4.5% |
| Year that the cost trend rate reaches ultimate rate | | | | | | | **2012** | 2009 | 2009 |

our policy nor the effect of a 10 percent change in the value of the U.S. dollar has changed from that reported at the end of last year.

The effect of the hypothetical change in exchange rates ignores the effect this movement may have on other variables, including competitive risk. If it were possible to quantify this competitive impact, the results would probably be different from the sensitivity effects shown above. In addition, it is unlikely that all currencies would uniformly strengthen or weaken relative to the U.S. dollar. In reality, some currencies may weaken while others may strengthen. Our primary exposure (excluding competitive risk) is to exchange rate movements in the British pound and Japanese Yen.

### Interest Rate Sensitivity

For our Machinery and Engines operations, we have the option to use interest rate swaps to lower the cost of borrowed funds by attaching fixed-to-floating interest rate swaps to fixed-rate debt. A hypothetical 100 basis point adverse move (increase) in interest rates along the entire interest rate yield curve would adversely affect 2005 pretax earnings of Machinery and Engines by $5 million. Last year, similar assumptions and calculations yielded a potential $4 million adverse impact on 2004 pretax earnings. This effect is caused by the interest rate fluctuations on our short-term debt.

For our Financial Products operations, we use interest rate derivative instruments primarily to meet our match funding objectives and strategies. A hypothetical 100 basis point adverse move (increase) in interest rates along the entire interest rate yield curve would adversely affect the 2005 pretax earnings of Financial Products by $13 million. Last year, similar assumptions and calculations yielded a potential $18 million adverse impact on 2004 pretax earnings. To estimate the impact of interest rate sensitivity on our income, we compute the difference in baseline and sensitized interest expense over the next 12 months. We determine the baseline interest expense by applying a market interest rate to the unmatched portion of our debt portfolio. The unmatched portion of our debt is an estimate of fixed-rate assets funded by floating-rate liabilities. We incorporate the effects of interest rate swap agreements in the estimate of our unmatched debt. We determine the sensitized interest expense by adding 100 basis points to the market interest rate applied to baseline interest expense and apply this rate to the unmatched debt. Our analysis assumes no new fixed-rate assets were extended and no further action was taken to alter our current interest rate sensitivity.

The effect of the hypothetical change in interest rates ignores the effect this movement may have on other variables including changes in actual sales volumes that could be indirectly attributed to changes in interest rates. The actions that management would take in response to such a change are also ignored. If it were possible to quantify this impact, the results could be different than the sensitivity effects shown above.

## SUPPLEMENTAL CONSOLIDATING DATA

We are providing supplemental consolidating data for the purpose of additional analysis. The data has been grouped as follows:

**Consolidated** — Caterpillar Inc. and its subsidiaries.

**Machinery and Engines** — The Machinery and Engines data contained in the schedules on pages A-57 to A-59 are "non-GAAP financial measures" as defined by the Securities and Exchange Commission in Regulation G. These non-GAAP financial measures have no standardized meaning prescribed by U.S. GAAP, and therefore, are unlikely to be comparable with the calculation of similar measures for other companies. Management does not intend these items to be considered in isolation or as a substitute for the related GAAP measures. Caterpillar defines Machinery and Engines as it is presented in the supplemental data as Caterpillar Inc. and its subsidiaries with Financial Products accounted for on the equity basis. Machinery and Engines information relates to our design, manufacturing, marketing and parts distribution operations. Financial Products information relates to the financing to customers and dealers for the purchase and lease of Caterpillar and other equipment. The nature of these businesses is different especially with regard to the financial position and cash flow items. Caterpillar management utilizes this presentation internally to highlight these differences. We also believe this presentation will assist readers in understanding our business.

**Financial Products** — our finance and insurance subsidiaries, primarily Cat Financial and Cat Insurance.

**Consolidating Adjustments** — eliminations of transactions between Machinery and Engines and Financial Products.

Pages A-57 to A-59 reconcile Machinery and Engines with Financial Products on the Equity Basis to Caterpillar Inc. Consolidated financial information.

### Supplemental Data for Results of Operations For The Years Ended December 31

(Millions of dollars)

| | Consolidated | | | Supplemental consolidating data: Machinery and Engines[1] | | | Financial Products | | | Consolidating Adjustments | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 | **2004** | 2003 | 2002 |
| **Sales and revenues:** | | | | | | | | | | | | |
| Sales of Machinery and Engines | **$ 28,336** | $ 21,048 | $ 18,648 | **$ 28,336** | $ 21,048 | $ 18,648 | **$ —** | $ — | $ — | **$ —** | $ — | $ — |
| Revenues of Financial Products | **1,915** | 1,715 | 1,504 | **—** | — | — | **2,109** | 1,895 | 1,678 | **(194)[2]** | (180)[2] | (174)[2] |
| Total sales and revenues | **30,251** | 22,763 | 20,152 | **28,336** | 21,048 | 18,648 | **2,109** | 1,895 | 1,678 | **(194)** | (180) | (174) |
| **Operating costs:** | | | | | | | | | | | | |
| Cost of goods sold | **22,420** | 16,945 | 15,146 | **22,420** | 16,945 | 15,146 | **—** | — | — | **—** | — | — |
| Selling, general and administrative expenses | **3,072** | 2,470 | 2,094 | **2,548** | 2,009 | 1,739 | **580** | 538 | 430 | **(56)[3]** | (77)[3] | (75)[3] |
| Research and development expenses | **928** | 669 | 656 | **928** | 669 | 656 | **—** | — | — | **—** | — | — |
| Interest expense of Financial Products | **520** | 470 | 521 | **—** | — | — | **532** | 482 | 538 | **(12)[4]** | (12)[4] | (17)[4] |
| Other operating expenses | **578** | 521 | 411 | **18** | (9) | (15) | **560** | 530 | 426 | **—** | — | — |
| Total operating costs | **27,518** | 21,075 | 18,828 | **25,914** | 19,614 | 17,526 | **1,672** | 1,550 | 1,394 | **(68)** | (89) | (92) |
| **Operating profit** | **2,733** | 1,688 | 1,324 | **2,422** | 1,434 | 1,122 | **437** | 345 | 284 | **(126)** | (91) | (82) |
| Interest expense excluding Financial Products | **230** | 246 | 279 | **235** | 259 | 279 | **—** | — | — | **(5)[4]** | (13)[4] | — |
| Other income (expense) | **204** | 35 | 69 | **15** | (69) | (16) | **68** | 26 | 3 | **121[5]** | 78[5] | 82[5] |
| **Consolidated profit before taxes** | **2,707** | 1,477 | 1,114 | **2,202** | 1,106 | 827 | **505** | 371 | 287 | **—** | — | — |
| Provision for income taxes | **731** | 398 | 312 | **566** | 286 | 204 | **165** | 112 | 108 | **—** | — | — |
| Profit of consolidated companies | **1,976** | 1,079 | 802 | **1,636** | 820 | 623 | **340** | 259 | 179 | **—** | — | — |
| Equity in profit (loss) of unconsolidated affiliated companies | **59** | 20 | (4) | **56** | 16 | (12) | **3** | 4 | 8 | **—** | — | — |
| Equity in profit of Financial Products' subsidiaries | **—** | — | — | **343** | 263 | 187 | **—** | — | — | **(343)[6]** | (263)[6] | (187)[6] |
| **Profit** | **$ 2,035** | $ 1,099 | $ 798 | **$ 2,035** | $ 1,099 | $ 798 | **$ 343** | $ 263 | $ 187 | **$ (343)** | $ (263) | $ (187) |

[1] Represents Caterpillar Inc. and its subsidiaries with Financial Products accounted for on the equity basis.

[2] Elimination of Financial Products revenues earned from Machinery and Engines.

[3] Elimination of expenses recorded by Machinery and Engines paid to Financial Products.

[4] Elimination of interest expense recorded between Financial Products and Machinery and Engines.

[5] Elimination of discount recorded by Machinery and Engines on receivables sold to Financial Products and of interest earned between Machinery and Engines and Financial Products.

[6] Elimination of Financial Products profit due to equity method of accounting.

### Supplemental Data for Financial Position
### At December 31
(Millions of dollars)

| | Consolidated | | Supplemental consolidating data: Machinery and Engines[1] | | Financial Products | | Consolidating Adjustments | |
|---|---|---|---|---|---|---|---|---|
| | **2004** | 2003 | **2004** | 2003 | **2004** | 2003 | **2004** | 2003 |
| **Assets** | | | | | | | | |
| Current assets: | | | | | | | | |
| Cash and short-term investments | **$ 445** | $ 342 | **$ 270** | $ 220 | **$ 175** | $ 122 | **$ —** | $ — |
| Receivables — trade and other | **7,459** | 4,025 | **3,272** | 2,993 | **465** | 875 | **3,722 [2][3]** | 157 [2][3] |
| Receivables — finance | **6,510** | 5,508 | **—** | — | **10,653** | 6,602 | **(4,143)[3]** | (1,094)[3] |
| Retained interests in securitized trade receivables | **—** | 1,550 | **—** | — | **—** | 1,550 | **—** | — |
| Deferred and refundable income taxes | **398** | 707 | **333** | 645 | **65** | 62 | **—** | — |
| Prepaid expenses | **1,369** | 1,424 | **1,367** | 1,403 | **16** | 27 | **(14)[4]** | (6)[4] |
| Inventories | **4,675** | 3,047 | **4,675** | 3,047 | **—** | — | **—** | — |
| Total current assets | **20,856** | 16,603 | **9,917** | 8,308 | **11,374** | 9,238 | **(435)** | (943) |
| Property, plant and equipment — net | **7,682** | 7,251 | **4,820** | 4,682 | **2,862** | 2,569 | **—** | — |
| Long-term receivables — trade and other | **764** | 510 | **255** | 81 | **37** | 1 | **472 [3]** | 428 [3] |
| Long-term receivables — finance | **8,575** | 7,394 | **—** | — | **9,082** | 7,822 | **(507)[3]** | (428)[3] |
| Investments in unconsolidated affiliated companies | **517** | 800 | **479** | 426 | **39** | 374 | **(1)[5]** | — |
| Investments in Financial Products subsidiaries | **—** | — | **3,012** | 2,547 | **—** | — | **(3,012)[6]** | (2,547)[6] |
| Deferred income taxes | **674** | 616 | **950** | 819 | **27** | 19 | **(303)[7]** | (222)[7] |
| Intangible assets | **315** | 239 | **307** | 230 | **8** | 9 | **—** | — |
| Goodwill | **1,450** | 1,398 | **1,450** | 1,398 | **—** | — | **—** | — |
| Other assets | **2,258** | 1,895 | **1,075** | 955 | **1,183** | 940 | **—** | — |
| **Total assets** | **$ 43,091** | $ 36,706 | **$ 22,265** | $ 19,446 | **$ 24,612** | $ 20,972 | **$ (3,786)** | $ (3,712) |
| **Liabilities** | | | | | | | | |
| Current liabilities: | | | | | | | | |
| Short-term borrowings | **$ 4,157** | $ 2,757 | **$ 93** | $ 72 | **$ 4,396** | $ 3,160 | **$ (332)[8]** | $ (475)[8] |
| Accounts payable | **3,990** | 2,568 | **3,869** | 2,773 | **205** | 243 | **(84)[9]** | (448)[9] |
| Accrued expenses | **1,847** | 1,638 | **1,012** | 857 | **855** | 802 | **(20)[10]** | (21)[10] |
| Accrued wages, salaries and employee benefits | **1,730** | 1,802 | **1,716** | 1,788 | **14** | 14 | **—** | — |
| Customer advances | **555** | 305 | **555** | 305 | **—** | — | **—** | — |
| Dividends payable | **141** | 127 | **141** | 127 | **—** | — | **—** | — |
| Deferred and current income taxes payable | **259** | 216 | **212** | 166 | **47** | 50 | **—** | — |
| Long-term debt due within one year | **3,531** | 2,981 | **6** | 32 | **3,525** | 2,949 | **—** | — |
| Total current liabilities | **16,210** | 12,394 | **7,604** | 6,120 | **9,042** | 7,218 | **(436)** | (944) |
| Long-term debt due after one year | **15,837** | 14,546 | **3,697** | 3,603 | **12,175** | 10,943 | **(35)[8]** | — |
| Liability for postemployment benefits | **2,986** | 3,172 | **2,986** | 3,172 | **—** | — | **—** | — |
| Deferred income taxes and other liabilities | **591** | 516 | **511** | 473 | **383** | 264 | **(303)[7]** | (221)[7] |
| **Total liabilities** | **35,624** | 30,628 | **14,798** | 13,368 | **21,600** | 18,425 | **(774)** | (1,165) |
| **Stockholders' equity** | | | | | | | | |
| Common stock | **1,231** | 1,059 | **1,231** | 1,059 | **888** | 890 | **(888)[6]** | (890)[6] |
| Treasury stock | **(3,277)** | (2,914) | **(3,277)** | (2,914) | **—** | — | **—** | — |
| Profit employed in the business | **9,937** | 8,450 | **9,937** | 8,450 | **1,824** | 1,495 | **(1,824)[6]** | (1,495)[6] |
| Accumulated other comprehensive income | **(424)** | (517) | **(424)** | (517) | **300** | 162 | **(300)[6]** | (162)[6] |
| **Total stockholders' equity** | **7,467** | 6,078 | **7,467** | 6,078 | **3,012** | 2,547 | **(3,012)** | (2,547) |
| **Total liabilities and stockholders' equity** | **$ 43,091** | $ 36,706 | **$ 22,265** | $ 19,446 | **$ 24,612** | $ 20,972 | **$ (3,786)** | $ (3,712) |

[1] Represents Caterpillar Inc. and its subsidiaries with Financial Products accounted for on the equity basis.
[2] Elimination of receivables between Machinery and Engines and Financial Products.
[3] Reclassification of Machinery and Engines trade receivables purchased by Cat Financial and Cat Financial's wholesale inventory receivables.
[4] Elimination of Machinery and Engines insurance premiums which are prepaid to Financial Products.
[5] Elimination of Machinery and Engines investment in Financial Products subsidiary.
[6] Elimination of Financial Products equity which is accounted for on Machinery and Engines on the equity basis.
[7] Reclassification of Financial Products deferred tax liability to a deferred tax asset on a consolidated basis.
[8] Elimination of debt between Machinery and Engines and Financial Products.
[9] Elimination of payables between Machinery and Engines and Financial Products.
[10] Elimination of prepaid insurance in Financial Products' accrued expenses.

## Supplemental Data for Statement of Cash Flow
## For The Years Ended December 31
(Millions of dollars)

| | Consolidated | | Supplemental consolidating data | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | Machinery and Engines[1] | | Financial Products | | Consolidating Adjustments | |
| | **2004** | 2003 | **2004** | 2003 | **2004** | 2003 | **2004** | 2003 |
| **Cash flow from operating activities:** | | | | | | | | |
| Profit | **$ 2,035** | $ 1,099 | **$ 2,035** | $ 1,099 | **$ 343** | $ 263 | **$ (343)[2]** | $ (263)[2] |
| Adjustments for non-cash items: | | | | | | | | |
| Depreciation and amortization | **1,397** | 1,347 | **795** | 798 | **602** | 549 | **—** | — |
| Undistributed profit of Financial Products | **—** | — | **(328)** | (263) | **—** | — | **328 [3]** | 263 [3] |
| Other | **(113)** | (69) | **(111)** | (12) | **(145)** | (146) | **143 [4]** | 89 [4] |
| Changes in assets and liabilities: | | | | | | | | |
| Receivables — trade and other | **(7,616)** | (8,115) | **(531)** | (376) | **43** | (238) | **(7,128)[4](5)** | (7,501)[4](5) |
| Inventories | **(1,391)** | (286) | **(1,391)** | (286) | **—** | — | **—** | — |
| Accounts payable and accrued expenses | **1,457** | 542 | **1,325** | 628 | **11** | (26) | **121 [4]** | (60)[4] |
| Other — net | **240** | (129) | **124** | (161) | **108** | 61 | **8 [4]** | (29)[4] |
| Net cash provided by (used for) operating activities | **(3,991)** | (5,611) | **1,918** | 1,427 | **962** | 463 | **(6,871)** | (7,501) |
| **Cash flow from investing activities:** | | | | | | | | |
| Capital expenditures — excluding equipment leased to others | **(926)** | (682) | **(841)** | (654) | **(85)** | (28) | **—** | — |
| Expenditures for equipment leased to others | **(1,188)** | (1,083) | **(2)** | (10) | **(1,186)** | (1,073) | **—** | — |
| Proceeds from disposals of property, plant and equipment | **673** | 761 | **27** | 133 | **646** | 628 | **—** | — |
| Additions to finance receivables | **(8,930)** | (6,868) | **—** | — | **(20,515)** | (12,572) | **11,585 [5]** | 5,704 [5] |
| Collections of finance receivables | **6,216** | 5,251 | **—** | — | **16,963** | 9,802 | **(10,747)[5]** | (4,551)[5] |
| Proceeds from sale of finance receivables | **700** | 661 | **—** | — | **1,363** | 1,760 | **(663)[5]** | (1,099)[5] |
| Additions to retained interests in securitized trade receivables | **—** | — | **—** | — | **(6,686)** | (7,447) | **6,686 [6]** | 7,447 [6] |
| Collections of retained interests in securitized trade receivables | **5,722** | 7,129 | **—** | — | **5,722** | 7,129 | **—** | — |
| Net intercompany borrowings | **—** | — | **159** | 376 | **209** | 53 | **(368)[7]** | (429)[7] |
| Investments and acquisitions (net of cash acquired) | **(290)** | (268) | **(295)** | (18) | **—** | (250) | **5** | — |
| Proceeds from sale of partnership investment | **290** | — | **—** | — | **290** | — | **—** | — |
| Other — net | **(190)** | (17) | **(82)** | (23) | **(102)** | (47) | **(6)[8]** | 53 [8] |
| Net cash provided by (used for) investing activities | **2,077** | 4,884 | **(1,034)** | (196) | **(3,381)** | (2,045) | **6,492** | 7,125 |
| **Cash flow from financing activities:** | | | | | | | | |
| Dividends paid | **(534)** | (491) | **(534)** | (491) | **(15)** | — | **15 [9]** | — |
| Common stock issued, including treasury shares reissued | **317** | 157 | **317** | 157 | **(2)** | 53 | **2 [8]** | (53)[8] |
| Treasury shares purchased | **(539)** | (405) | **(539)** | (405) | **—** | — | **—** | — |
| Net intercompany borrowings | **—** | — | **(209)** | (53) | **(159)** | (376) | **368 [7]** | 429 [7] |
| Proceeds from long-term debt issued | **5,088** | 5,634 | **9** | 128 | **5,079** | 5,506 | **—** | — |
| Payments on long-term debt | **(3,008)** | (4,237) | **(35)** | (463) | **(2,973)** | (3,774) | **—** | — |
| Short-term borrowings — net | **550** | 87 | **21** | (37) | **529** | 124 | **—** | — |
| Net cash provided by (used for) financing activities | **1,874** | 745 | **(970)** | (1,164) | **2,459** | 1,533 | **385** | 376 |
| Effect of exchange rate changes on cash | **143** | 15 | **136** | 7 | **13** | 8 | **(6)[10]** | — |
| **Increase (decrease) in cash and short-term investments** | **103** | 33 | **50** | 74 | **53** | (41) | **—** | — |
| Cash and short-term investments at beginning of period | **342** | 309 | **220** | 146 | **122** | 163 | **—** | — |
| Cash and short-term investments at end of period | **$ 445** | $ 342 | **$ 270** | $ 220 | **$ 175** | $ 122 | **$ —** | $ — |

[1] Represents Caterpillar Inc. and its subsidiaries with Financial Products accounted for on the equity basis.

[2] Elimination of Financial Products profit after tax due to equity method of accounting.

[3] Non-cash adjustment for the undistributed earnings from Financial Products.

[4] Elimination of non-cash adjustments and changes in assets and liabilities related to consolidated reporting. Receivables amounts include adjustment for consolidated non-cash receipt of retained interests in securitized trade receivables. Please refer to Liquidity and Capital Resources on pages A-48 to A-51 for further discussion.

[5] Reclassification of Cat Financial's cash flow activity from investing to operating for receivables that arise from the sale of inventory.

[6] Elimination of Cat Financial's additions to retained interests in securitized trade receivables that arose from an intercompany purchase of receivables.

[7] Net proceeds and payments to/from Machinery and Engines and Financial Products.

[8] Change in investment and common stock related to Financial Products.

[9] Elimination of dividend from Financial Products to Machinery and Engines.

[10] Elimination of the effect of exchange on intercompany balances.

## OUTLOOK

### SALES AND REVENUES OUTLOOK

We project another record year in 2005. Company sales and revenues should increase 12 to 15 percent, with machinery and engines volume increasing about 8 percent. Improved price realization should add about 3 percent and the rest will come from the favorable impact of currency on sales and Financial Products revenues.

Many central banks raised short-term interest rates in 2004 and are expected to raise rates further in 2005. However, we expect short-term rates at the end of the year will still be favorable to continued economic growth and investment. In most countries, inflation rates are near targets, economic growth is close to trend and labor markets have excess capacity. Continued low interest rates should prolong construction recoveries, particularly in the developed economies.

Sizable increases in energy and metals prices boosted some inflation measures in 2004 but increases in 2005 likely will be much lower. In most commodities, prices are already well above the minimums needed to make new investments attractive. Increased production, along with somewhat slower growth in demand, should moderate commodity price pressures.

Past commodity price increases reduced consumer incomes in the developed countries but did not halt recoveries or investment. As an offset, higher prices boosted incomes in the developing countries, which led to much-needed increases in investment. Overall, the world economy gained since commodity production increased.

We expect similar trends to continue in 2005 and both mining and energy development should further benefit sales. Developing countries should allocate more of the income gains from higher commodity prices and production to construction.

#### North America (United States and Canada)

The U. S. economy is growing at more than a 3 percent rate, employment is increasing only slightly faster than the labor force and core inflation measures are rising at near 2 percent rates. These conditions do not yet reflect much of the impact of the Fed's rate increases in last half of 2004. Consequently, we believe the Fed will be able to prevent any long-term inflation problems with fairly modest rate hikes, raising the Fed funds target to around 3.5 percent by the end of 2005.

Long-term rates, which barely moved in response to short-term rate hikes last year, likely will increase this year, although somewhat less than short-term rates. Overall, interest rates should continue to support growth, particularly in business investment, and the economy should grow more than 3.5 percent in 2005.

Both mining and nonresidential construction started recoveries from multi-year declines last year and output is below previous peaks. We expect activity in these sectors to increase rapidly this year, which along with favorable output prices, will support further sales growth. Housing construction, which has increased for the past four years, likely will decline slightly this year. We expect the large backlog of unused housing permits and higher home prices will offset much of the negative impact of higher mortgage interest rates.

The Canadian economy, benefiting from low interest rates and high commodity prices, should grow about 3 percent in 2005. We estimate that favorable investment climates in the North American economies will result in about a 17 percent increase in Machinery and Engines sales.

#### EAME

The Euro-zone economy appeared to improve at the end of 2004 and the European Central Bank is expected to hold interest rates steady through the middle of the year. We believe any subsequent rate increases will be cautious in order to allow a recovery in domestic spending to offset the impact of a stronger euro. The U. K. economy likely will slow but robust recoveries should continue in Central Europe. Overall European growth is expected to exceed 2 percent in 2005, somewhat better than in 2004. Construction spending should continue to recover.

We anticipate that both AME and the CIS will benefit further from favorable commodity prices and increased production of metals and energy. Higher revenues will be used to fund capacity expansions as well as infrastructure development. The AME economy should grow about 4.5 percent and the CIS economy more than 6 percent, both marginally slower than in 2004. We forecast that Machinery and Engines sales in EAME will increase about 10 percent this year.

#### Latin America

Latin American economies should grow more than 3.5 percent in 2005, the result of favorable metals and energy prices, increased capital inflows and a more favorable foreign debt profile. Both mining output and construction spending should increase again. We project that sales of Machinery and Engines will increase about 13 percent in 2005.

#### Asia/Pacific

We expect regional growth will average about 6 percent this year, with most countries slowing some from last year's pace. Low interest rates should prolong recoveries in consumer spending and business investment while competitive exchange rates likely will continue to boost exports.

Early indications are that contract prices for coal, particularly coking coal, will increase substantially this year. Coal mining should again be a major contributor to sales. Fast growth in the region, which has taxed infrastructure capacity, should prompt governments to increase infrastructure spending. Also, reconstruction in areas hit by the tsunami likely will require additional machines and engines. In China, government administrative measures are expected to continue, causing sales into that country to decline. Overall, we expect sales of Machinery and Engines to increase about 10 percent in 2005.

#### Financial Products

We expect continued growth in Financial Products for 2005, with revenues expected to increase approximately 16 percent versus 2004 primarily due to higher average earning assets in 2005.

### PROFIT OUTLOOK

We expect profit per share to be up about 25 percent from 2004. The year will benefit from improved price realization, increased volume, manufacturing efficiencies and an intensified focus on our cost structure. We expect material cost pressures to continue for the first half of 2005, with some relief in the last six months.

As a result, we expect the last half of 2005 to be stronger than the first half. Our plan is to more than offset material cost increases with price realization in 2005, as evidenced by the price increase already announced on January 1, 2005. We are continually monitoring material costs and their impact on our results, and we are also reviewing possible further price actions, which we will take if necessary to meet our goals.

We expect our effective tax rate for 2005 to increase approximately two percentage points due to the phase-out of the Extraterritorial Income Exclusion (ETI) as provided in the American Jobs Creation Act of 2004 along with our expected geographic mix of profits.

* * *

The information included in the Outlook section is forward looking and involves risks and uncertainties that could significantly affect expected results. A discussion of these risks and uncertainties is contained in Form 8-K filed with the Securities & Exchange Commission (SEC) on January 27, 2005.

**MANAGEMENT'S DISCUSSION AND ANALYSIS ■**

# SUPPLEMENTAL STOCKHOLDER INFORMATION

**Shareholder Services:**

***Stock Transfer Agent***
Mellon Investor Services
P.O. Box 3315
South Hackensack, NJ 07606-3315
*phone:* (866) 203-6622 (U.S. and Canada)
(201) 329-8660 (Outside U.S. and Canada)
*hearing impaired:*
(800) 231-5469 (U.S. and Canada)
(201) 329-8354 (Outside U.S. and Canada)
*Internet home page:* www.melloninvestor.com

***Caterpillar Assistant Secretary***
Laurie J. Huxtable
Assistant Secretary
Caterpillar Inc.
100 N.E. Adams Street
Peoria, IL 61629-7310
*phone:* (309) 675-4619
*fax:* (309) 675-6620
*e-mail:* **CATshareservices@cat.com**

**Stock Purchase Plan:**

Current shareholders and other interested investors may purchase Caterpillar Inc. common stock directly through the Investor Services Program sponsored and administered by our Stock Transfer Agent. Current shareholders can get more information on the program from our Transfer Agent using the contact information provided above. Non-shareholders can request program materials by calling: (800) 842-7629 (U.S. and Canada) or (201) 329-8660 (outside the U.S. and Canada). The Investor Services Program materials are available on-line from Mellon's website or linked from www.cat.com/dspp.

**Investor Relations:**

Institutional analysts, portfolio managers, and representatives of financial institutions seeking additional information about the Company should contact:

***Director of Investor Relations***
Nancy L. Snowden
Caterpillar Inc.
100 N.E. Adams Street, Peoria, IL 61629-5310
*phone:* (309) 675-4549
*fax:* (309) 675-4457
*e-mail:* **CATir@cat.com**
*Internet website:* www.cat.com/investor

**Common Stock (NYSE: CAT)**

***Listing Information:*** Caterpillar common stock is listed on the New York, Pacific and Chicago stock exchanges in the United States, and on stock exchanges in Belgium, France, Germany, Great Britain and Switzerland.

**Compliance:** In compliance with New York Stock Exchange rules, Caterpillar filed an Annual CEO Certification with the Exchange in May 2004. The certification will be included as on exhibit to our 2004 Form 10-K.

***Price Ranges:*** Quarterly price ranges of Caterpillar common stock on the New York Stock Exchange, the principal market in which the stock is traded, were:

| | **2004** | | 2003 | |
|---|---|---|---|---|
| Quarter | **High** | **Low** | High | Low |
| First | **$85.70** | **$72.51** | $53.30 | $41.24 |
| Second | **$84.76** | **$72.01** | $58.25 | $48.98 |
| Third | **$81.30** | **$68.50** | $73.97 | $53.10 |
| Fourth | **$98.72** | **$76.75** | $84.95 | $68.90 |

***Number of Stockholders:*** Stockholders of record at year end totaled 37,639, compared with 38,440 at the end of 2003. Approximately 69.71% of our issued shares are held by institutions and banks, 23.65% by individuals, and 6.64% by employees through company investment plans.

Caterpillar qualified investment plans held 20,387,316 shares at year-end, including 2,169,522 shares acquired during 2004. Non-U.S. employee stock purchase plans held an additional 2,395,759 shares at year-end, including 1,001,689 shares acquired during 2004.

**Company Information:**

***Current information:***

- phone our Information Hotline — (800) 228-7717 (U.S. and Canada) or (858) 244-2080 (outside U.S. and Canada) to request company publications by mail, listen to a summary of Caterpillar's latest financial results and current outlook, or to request a copy of results by fax or mail
- request, view, or download materials on-line or register for email alerts by visiting www.cat.com/materialsrequest

***Historical information:***

- view/download on-line at www.cat.com/historical

**Annual Meeting:**

On Wednesday, April 13, 2005, at 1:30 p.m., Central Time, the annual meeting of stockholders will be held at the Northern Trust Corporation Building in Chicago, Illinois. Proxy materials are being sent to stockholders with this report on or about March 3, 2005.

**Internet:**

Visit us on the Internet at www.cat.com.

*Information contained on our website is not incorporated by reference into this document.*

# DIRECTORS AND OFFICERS

| Directors/Committee Membership (as of December 31, 2004) | | | | |
|---|---|---|---|---|
| | Audit | Compensation | Governance | Public Policy |
| W. Frank Blount | ✔ | | ✔ | |
| John R. Brazil | | ✔ | | ✔* |
| John T. Dillon | ✔ | | ✔* | |
| Eugene V. Fife | ✔* | | | |
| Gail D. Fosler | | ✔ | | ✔ |
| Juan Gallardo | | | ✔ | ✔ |
| David R. Goode | ✔ | | ✔ | |
| Peter A. Magowan | | ✔ | ✔ | |
| William A. Osborn | | ✔* | | |
| Gordon R. Parker | ✔ | | | ✔ |
| Charles D. Powell | | ✔ | | ✔ |
| Edward B. Rust, Jr. | ✔ | | ✔ | |
| Joshua I. Smith | | ✔ | | ✔ |
| * Chairman of Committee | | | | |

**OFFICERS**

| | |
|---|---|
| James W. Owens | Chairman and CEO |
| Stuart L. Levenick | Group President |
| Douglas R. Oberhelman | Group President |
| Gerald L. Shaheen | Group President |
| Gérard R. Vittecoq | Group President |
| Steven H. Wunning | Group President |
| Kent M. Adams[3] | Vice President |
| Ali M. Bahaj | Vice President |
| Sidney C. Banwart | Vice President |
| Michael J. Baunton | Vice President |
| James S. Beard[1] | Vice President |
| Rodney C. Beeler | Vice President |
| Mary H. Bell | Vice President |
| Richard A. Benson[2] | Vice President |
| James B. Buda | Vice President, General Counsel and Secretary |
| David B. Burritt | Vice President, Chief Financial Officer |
| Rodney L. Bussell | Vice President |
| Christopher C. Curfman | Vice President |
| Paolo Fellin | Vice President |
| Thomas A. Gales | Vice President |
| Stephen A. Gosselin | Vice President |
| Hans A. Haefeli | Vice President |
| John S. Heller | Vice President |
| Richard P. Lavin | Vice President |
| Robert R. Macier | Vice President |
| F. Lynn McPheeters[2] | Vice President, Chief Financial Officer |
| Daniel M. Murphy | Vice President |
| Gerald Palmer | Vice President |
| James J. Parker | Vice President |
| Mark R. Pflederer | Vice President |
| Edward J. Rapp | Vice President |
| William J. Rohner | Vice President |
| Christiano V. Schena | Vice President |
| William F. Springer | Vice President |
| Gary A. Stroup | Vice President |
| Donald G. Western | Vice President |
| Robert T. Williams | Vice President |
| Bradley M. Halverson | Controller |
| Kevin E. Colgan | Treasurer |
| Robin D. Beran | Assistant Treasurer |
| Tinkie E. Demmin | Assistant Secretary |
| Laurie J. Huxtable | Assistant Secretary |

Note: All director/officer information is as of December 31, 2004, except as noted.

[1]*Will retire effective March 1, 2005.*

[2]*Retired effective February 1, 2005.*

[3]*Effective February 1, 2005.*

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