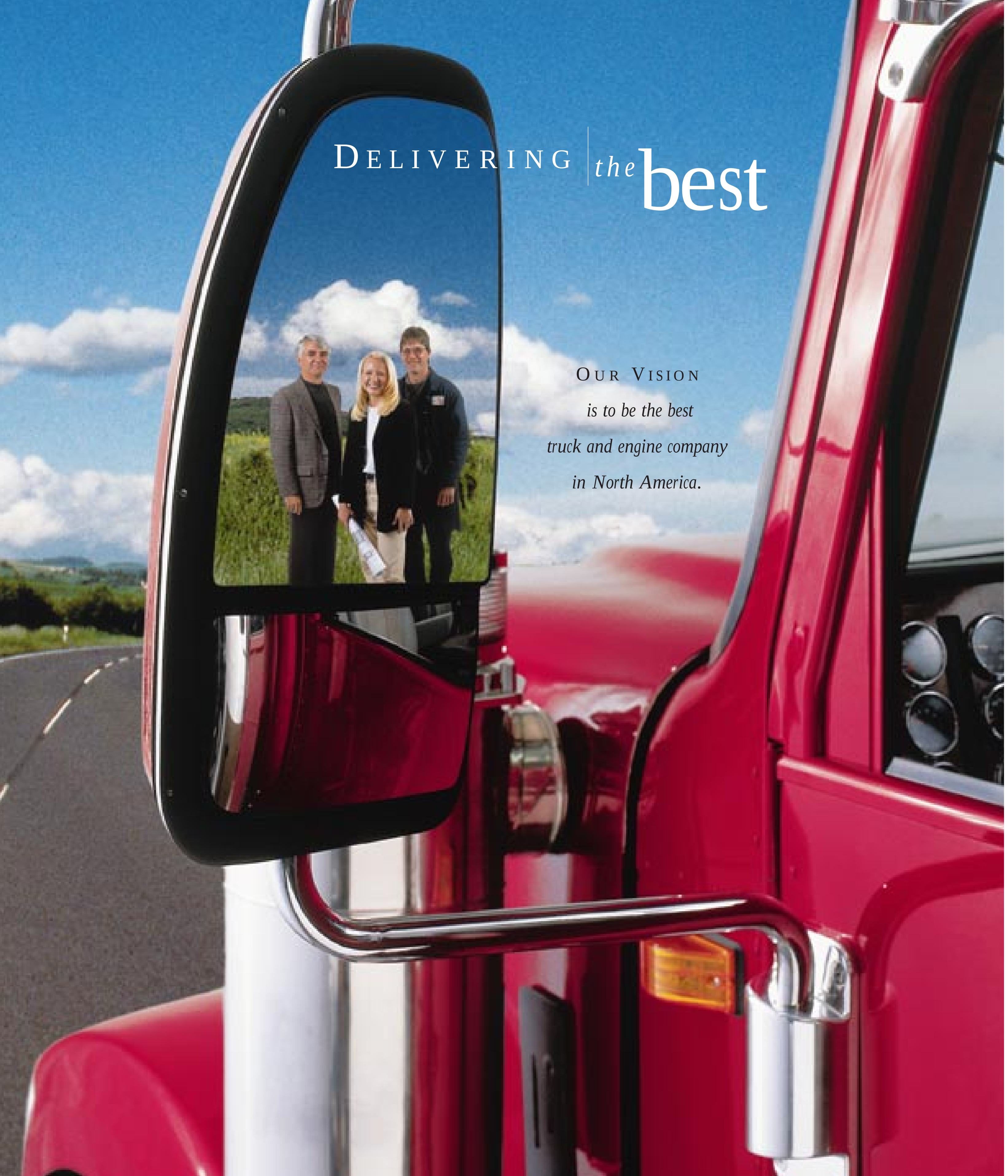


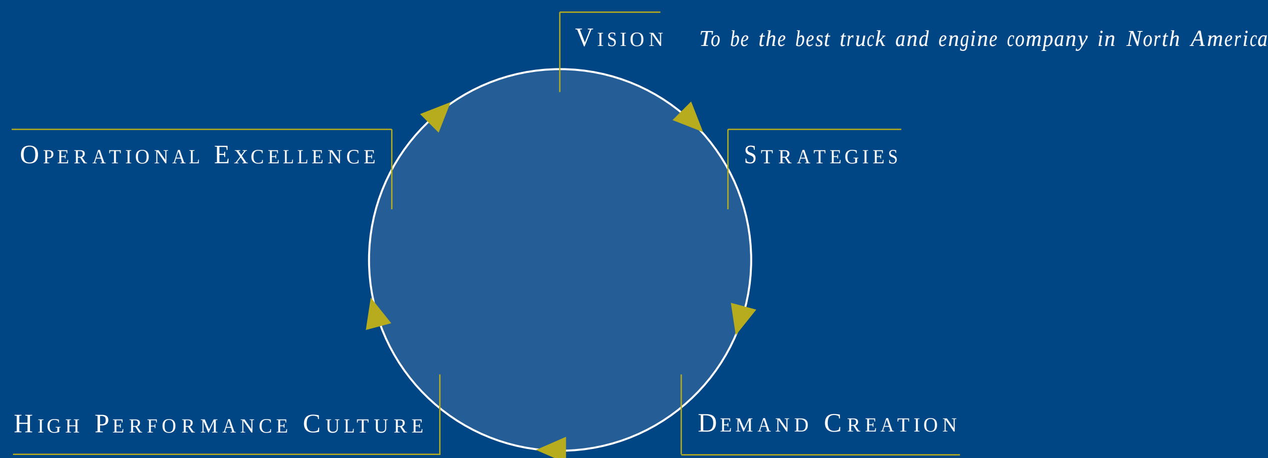
DELIVERING *the* best

OUR VISION
is to be the best
truck and engine company
in North America.

NAVISTAR

Annual *report* FOR 1997

Our Business | Model



Overview *of our* Business

HEAVY TRUCK (CLASS 8) Navistar produces premium conventional tractors for long-haul, over-the-highway usage; cabover trucks; regular conventional trucks for local and regional delivery; and severe service trucks for construction, mining, oil field and other rugged applications.

MEDIUM TRUCK (CLASS 5-7) Navistar is the market share leader in the United States and Canada. Applications include regional delivery, beverage, recycling, refrigerated, utility, construction, towing, municipal and emergency rescue.

SCHOOL BUS Navistar is the market share leader in the United States and Canada, and offers a range of small capacity and full-size conventional models. In addition, through AmTran, a wholly owned subsidiary, the company produces the Genesis® and AmTran nameplates.

SERVICE PARTS To support customers of the truck and bus business, Navistar has the largest truck service parts distribution network in the United States, Canada and Mexico with nearly 1,000 International® dealer locations and eight parts distribution centers, offering more than 350,000 truck, engine and trailer aftermarket parts. Navistar also offers 24-hour availability of service parts and guaranteed national pricing on parts and service under its Fleet Charge® system.

ENGINE DIVISION Navistar is a leader in the production of mid-range diesel engines, ranging from 160 to 300 horsepower. International® engines are featured in all of the company's medium trucks, school buses and some heavy trucks. International engines are sold to other original equipment manufacturers (OEMs) in North America and export markets for use in agricultural and industrial applications.

FINANCIAL SERVICES Navistar Financial Corporation (NFC) provides wholesale, retail and lease financing for International dealers and retail customers, and provides commercial physical damage and liability insurance coverage through its wholly owned subsidiary, Harco National Insurance Company.

ON THE COVER

Three employees who are delivering the best in new truck design, development and production are (left to right): Tom Osborn, chief engineer, line haul products, Ft. Wayne; Cortney Guzlas, chassis systems design engineer, Ft. Wayne; Wade Myers, assembly line operator, Chatham.

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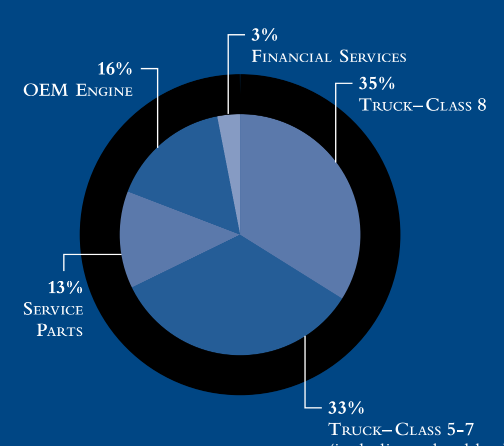


Percent of Sales and Revenues

Financial | Summary

For the Years Ended October 31

(MILLIONS OF DOLLARS, EXCEPT PER SHARE DATA)

	1997	1996
Sales and revenues	$6,371	$5,754
Income before income taxes	$ 242	$ 105
Net income	$ 150	$ 65
Net income per common share	$ 1.65	$ .49
Manufacturing gross margin	14.2%	12.5%
Return on equity	14.7%	7.1%
Cash and marketable securities	$ 965	$ 881

Achievements *of* 1997

INCREASED the share price of Navistar common stock 147%, from $9 3/8 to $23 3/16, at the close of the fiscal year, contributing nearly $1 billion to shareowner value.

ALIGNED the interests of management with shareowners through an executive stock purchase plan, giving 30 senior executives a personal stake in increasing shareowner value, and by linking 450 managers' incentive compensation directly to improvements in return on equity.

REACHED a landmark agreement with the United Auto Workers to extend the master contract through 2002, enabling Navistar to reinstate the next generation truck and bus (NGT) program, focus assembly operations, achieve more competitive productivity levels and ensure competitiveness of foundry operations.

LAUNCHED the NGT program, which includes world-class vehicles, assembly processes and operations, and a new cab and stamping facility.

SIMPLIFIED the process of ordering medium trucks with the extension of Diamond SPEC™, exceeding pilot program expectations by 120%.

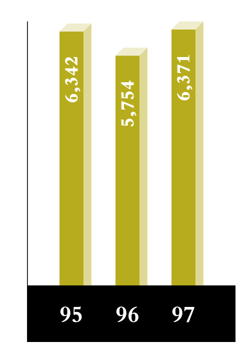
HEIGHTENED the company's presence in Mexico by capturing an 11.5% market share, expanding to a 38-dealer network, and continuing on-schedule construction of an assembly facility in Escobedo, Nuevo Leon.

SIGNED a ten-year agreement with Ford Motor Company to supply a new, advanced technology diesel engine for use in its over 8500 lb. trucks and vans.

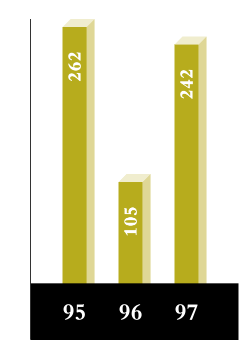
DEMONSTRATED industry-leading productivity and quality levels in the engine division, exceeding ROA targets, while increasing OEM shipments to 184,000 units, a 13% increase over the previous year.

INTRODUCED all 16,000 employees to the values and guiding behaviors of a high-performance culture, established an annual all-employee survey to measure progress, and developed 22 specific action plans to improve performance.

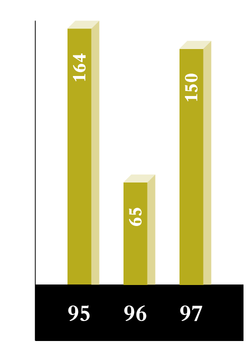
RANKED No. 1 for the third year in a row by American Truck Dealers survey, where dealers rate major manufacturers on truck product lines, service and support.



Sales and Revenues
$ MILLIONS



Income before Income Taxes
$ MILLIONS



Net Income
$ MILLIONS

Our vision is to be *the best* TRUCK AND ENGINE company in North America.

LEADERSHIP

In 1997, we continued to add new talent to our leadership team. Gary Diaz, with 17 years of leadership in product development and general management, has joined Navistar as group vice president of truck engineering, reliability and quality and chief technical officer. He is accountable for continuous improvement in quality—from vehicle concept and development, through engineering and the manufacturing process, and into field support.

Anthony Hines joined us as vice president of manufacturing for our truck business. He is spearheading our drive for excellence in truck operations.

In our engine division, we added the talent of Jim Marcoux, vice president of worldwide sales and marketing, and Bob Rath, vice president, reliability, service and new products.

We welcomed to our board of directors Allen Krowe, former vice chairman of Texaco, Inc., who adds financial expertise to our team and is a member of the audit and finance committee. And John Grigsby, former chairman and chief executive officer of Allis-Chalmers Corporation, joined the board replacing Richard Celeste, who resigned to take a post as Ambassador to India. John's relevant industry experience and financial expertise add strength to our public policy and audit committees.

To our shareowners:

This past year was truly a turning point in our drive to make Navistar the best truck and engine company in North America. Our strategic focus of the past three years began to pay off in very tangible ways, including:

- growth in net income of 130% to $150 million
- gross margins of 14.2%, up from last year's 12.5%
- return on equity of 14.7%, up from 7.1%

Certainly we were helped by a strong economy overall, as well as better-than-expected demand in the truck industry, which contributed to increased revenues of $6.37 billion. But those factors alone do not account for our success. A major part of our improvement in gross margin was related directly to performance improvements—higher levels of productivity and first-time quality resulting from specific initiatives to drive operational excellence through the organization.

Of course, the one measure most visible to the widest cross-section of stakeholders was the dramatic increase in the value of our stock, which increased 147%. From November 1, 1996 to the fiscal year end, our performance created nearly $1 billion in value for our shareowners.

The stock performance is especially significant since most of the increase occurred well before the announcement of the year's two most important achievements: the breakthrough labor agreement with the United Auto Workers (UAW), and the long-term contract with Ford that extends our partnership through the year 2012.

The landmark UAW contract, after years of strained management/labor relations, removes many of the obstacles standing in the way of our competitiveness. We now have a solid foundation of understanding that allows us to tap the expertise of the most experienced workforce in the industry.

We are extremely proud that our record of bringing superior diesel engine technology to market was rewarded by the Ford Motor Company, laying the foundation for the long-term success of our engine division.

Certainly, these were the "big wins." But what really captured the attention of investors and analysts and truly contributed to our stock growth, was the steady progress we reported against our five-point truck strategy and engine strategies. It was our continued strategic focus that Wall Street recognized and rewarded.

We moved product out of our plants to reduce complexity, expanded our operations in Mexico and other international markets, and rejuvenated our product line, particularly in heavy truck. And Wall Street saw clear evidence that we were improving our manufacturing processes, with quality and productivity initiatives on the factory floor.

For me, the year's biggest achievement does not show up on the bottom line or in the balance sheet. It's one of those "intangibles" that defies measurement but can make all the difference in the world. That is, for the first time in many years, we as a team learned how to win.

This was a major, fundamental cultural shift. It didn't happen overnight. It developed gradually over the past several years with each new success. One-by-one, we tore down obstacles and overcame hurdles that would have defied us in years past.

When people doubted we could go into Mexico, we proved them wrong, capturing a stunning 11.5% market share in the first year of operation.

As domestic competitors fled the "low-tech" foundry industry, we invested and focused and turned our Indianapolis foundry into a world-class operation that sets the standard for quality and productivity.

EXECUTIVE TEAM

Pictured below are the team members of the Executive Committee. In the front row are Donald DeFosset, Jr., executive vice president and president, truck group; John R. Horne, chairman, president and chief executive officer; and Robert C. Lannert, executive vice president and chief financial officer. From left to right are: Robert A. Boardman, senior vice president, general counsel; Maril G. MacDonald, vice president, corporate communications; Thomas M. Hough, vice president, treasurer; Daniel C. Ustian, vice president, general manager, engine and foundry; J. Steven Keate, vice president, controller; Joseph V. Thompson, senior vice president, employee relations and administration; and John J. Bongiorno, vice president, general manager, financial services.

And when our customers called for new product, we brought a new heavy truck on line in record time—four months from concept to rollout.

These are the results that come from winners. These are the accomplishments made possible by believers—by people who continuously challenge themselves, raise their own expectations for performance, and set the bar ever higher.

Instead of explaining why they can't, our people are stepping up and saying, "bring it on, we'll find a way."

Next year will be our hardest year ever. Not because of any obstacles we face, but because we're going to demand even more from ourselves. Last year, in a dramatic vote of confidence in the company's strategies and direction, our top 30 executives put themselves on the line. We agreed to purchase large quantities of stock, at amounts as high as three times our salary level. And we tied the incentive compensation of the rest of our 450 managers directly to achieving return on equity targets. This essentially said to our shareowners: we are with you—your risks are our risks and your rewards are ours as well.

This year we're taking another critical step in aligning the interests of our executives and shareowners—that is, putting our money where our mouth is. Because delivering the best is continuously redefining what "the best" means. In 1998, if we perform according to plan, our senior-most executives will not receive a significant portion of their bonus. Instead, we've once again raised the bar. We must. Because our challenges are still great and our competition is not standing still. So we have established a higher, "distinguished" level of financial performance for the company. Only when we hit these higher targets for return on equity will our top management be rewarded, as it should be.

These are exciting times. The year ahead poses many challenges, not the least of which is a likely leveling off of truck demand. But we have many exciting opportunities in 1998.

Our brand new plant in Mexico—our first new manufacturing facility in 20 years—goes on line in the spring.

We are fundamentally restructuring our truck group to better align it with customer needs and drive greater accountability for profits.

We're hiring hundreds of new engineers to develop our next generation of trucks and buses. And, we're planning a major capacity increase at our Indianapolis engine facility to meet continued increases in demand.

As I look ahead to 1998, I am more excited than ever before. All the pieces, as represented in our business model, are coming together: a clear vision for the future and solid strategies to get us there; marketing and branding strategies aimed at demand creation; high standards of excellence in our operations—all fueled by a high performance culture and captured in a never-ending process of continuous improvement.

Let our competition be on notice: this is a new Navistar—a company of believers, a team of winners.

John R. Horne

John R. Horne
Chairman, President and Chief Executive Officer

To achieve our vision, every decision we make will be based on improving SHAREOWNER VALUE, CUSTOMER SATISFACTION and employee motivation and pride.

To achieve our vision and deliver the best, Navistar defines performance by how well we serve shareowners, customers and employees. This past year, we delivered measurable improvement in shareowner value. Our progress toward our strategies, coupled with strong industry demand, resulted in a 147% increase in stock price by year end.

Throughout the year, we focused our short-term plans on meeting expectations for financial performance. Net income rose 130% to $150 million, manufacturing gross margin improved 1.7 percentage points to 14.2%, and earnings per share increased to $1.65 compared to $.49 a year ago (which included a one-time pretax charge of $35 million for termination of our next generation truck and bus (NGT) program).

To ensure that we are accountable for achieving a 15% return on assets and a 17.5% after tax return on equity over the cycle, we aligned the interests of senior executives and top management with shareowners. Under Navistar's new executive stock ownership program, our top 30 executives are required to invest personal funds in Navistar common stock at the current market price in an amount equal to three-quarters to three times their base salary, depending upon their management level—making a significant personal investment to achieve real value for our shareowners. Each executive has met or exceeded the plan's investment requirements.

In addition, we introduced a new management incentive plan this year tied directly to improvements in ROE. Now the performance of all 450 of our top management employees is directly linked to increasing shareowner value. Moreover, the majority of our employees participate in profit sharing, which provides an incentive for improving the company's performance.

Our new annual incentive plan has been designed to address the cyclicality of the truck industry. As total demand for trucks and buses in North America increased from our original estimates of 313,500 units, the targeted ROE performance level increased dramatically. At the end of the year, we achieved the ROE target.

Over the past year we moved aggressively to improve customer satisfaction. We maintained our position as market leader in the U.S. and Canada for medium, heavy trucks and school buses achieving a 28.6% share, 1.1 percentage points higher than a year ago. Our share of heavy trucks increased to 18.6%, compared to 17.1% last year, while we continued our leadership in the medium truck and school bus market with a 36.8% and 59.6% share, respectively. And our engine division continued its success among OEM customers. In 1997, we shipped a record 184,000 engines, a 13% increase over 1996.

We also measure how well we're doing by the expectations of our employees. Our employees take pride in our company and its achievements. Our challenge is to continue to focus that pride on driving change to deliver results. As a result, we established a benchmark in 1996 to gauge how well we're living our values. And we created an environment in which our employees can respond to changing market conditions and customer needs.

VISION

MAKING IT HAPPEN

It takes all of us working together to achieve our vision. Making it happen at the Springfield, Ohio assembly plant are (foreground) Willie Randle, line quality team member, and (background) Dan Roberts, first shift team leader.

HIGHLIGHTS

- Increased Navistar stock price from $9⅜ to $23³⁄₁₆ at the close of the year, a 147% increase—the greatest stock price gain among select industry peers and five times greater than the S&P 500 average.
- Aligned interests of management with shareowners through an executive stock purchase plan, giving 30 senior executives a personal stake in increasing shareowner value and linking 450 managers' incentive compensation directly to improvements in return on equity.

We have sound, AGGRESSIVE strategies that address our CURRENT AND FUTURE *opportunities.*

UNITY

Unity at Springfield made possible by a dedicated labor/management team, four of whom are pictured here. From left to right are: Ron Rhine, International representative, region 2B, UAW; Jack Kitchen, chairman, bargaining committee, UAW local 658; Tom Hennigan, director of human resources, truck manufacturing; and Larry Bayless, chairman, bargaining committee, UAW local 402.

STRATEGIES

With our new competitive labor contract, we have surpassed a significant hurdle and are now positioned to forge ahead on all elements of our five-point truck strategy, and to drive for even greater performance in our engine business.

The contract extension, coupled with our new 10-year agreement with Ford, helps ensure solid growth in our V-8 and I-6 engine product lines. V-8 engine shipments to Ford alone increased by 13% for the year to 176,000 engines. Total division shipments were up 11% to 258,000 engines. We also established agreements with two distribution partners for our I-6 engines, securing greater opportunities to grow that business in markets outside of North America. And this growth is wholly attainable: With production expected to reach record highs in 1998, the engine group is demonstrating solid improvements in quality and productivity.

The new labor agreement enables our truck and engine businesses to become more competitive from a total labor cost standpoint. We can now build NGT at our Springfield assembly plant, and keep our Indianapolis foundry cost-competitive. Of equal importance, we have built a new partnership with our employees and are jointly committed to tackling our challenges together.

At the same time, with approval to move ahead on NGT, we can forge a more competitive product line-up. Over the next six years, we will invest $350 million in capital spending and $300 million in development toward our world-class medium and heavy trucks and school buses. Development and design of NGT are now aggressively underway and on target for the first truck and bus roll-out by mid-2001, with additional new vehicles to follow approximately every six months through 2003.

In addition to driving product innovations into the future, this year we continued to build a comprehensive, winning product line-up for our customers. We launched the International® 9100 to meet the needs of local and regional operators, taking it from design to the road in a record four months. We also initiated production of the Pro Sleeper® Sky-Rise™ integrated sleeper to target the long-haul customers.

We took additional strides in 1997 to reduce complexity in our manufacturing operations. Production of the Paystar® severe service trucks began at SST Truck Company, in Garland, Texas. By moving Paystar from our Chatham, Ontario facility, the company freed up 20% more floor space, allowing that facility to boost production of heavy conventional trucks to 100 per day. Chatham can now focus on International® and Eagle® 9000 heavy trucks, and SST can focus exclusively on assembling the severe service Paystar trucks.

And, with NGT reinstated, plans are now underway for an aggressive transformation of our Springfield assembly plant into a focused, world-class medium truck manufacturing facility, with new tooling and equipment and a new stamping and cab assembly operation. These changes will result in reductions in costs and unsurpassed quality.

In our international operations, we continued our expansion into Mexico, growing to 38 dealer outlets and an 11.5% market share. And construction of our new assembly facility in Escobedo, Nuevo Leon, continued through the year and is on target for full production in mid-1998. We also established Navistar do Brasil, a commercial company, and signed an agreement with a Brazilian equipment manufacturer to assemble commercial trucks. Establishing a presence in Brazil will enable us to target growing markets like Brazil and Argentina that were previously inaccessible due to trade barriers.

HIGHLIGHTS

- **Reached landmark agreement with the UAW to extend master contract through 2002, enabling Navistar to build NGT.**
- **Launched the NGT program which includes world-class vehicles, assembly processes and operations.**
- **Signed ten-year agreement with Ford Motor Company to supply advanced technology diesel engines.**
- **Expanded growth of V-8 and I-6 engine product lines by 11% to 258,000 engines.**
- **Streamlined assembly facilities, with Chatham, Ontario now focused on heavy conventionals; SST Truck, Garland, Texas producing Paystar® severe service trucks.**
- **Heightened presence in Mexico, growing to 38 dealer outlets and 11.5% market share; established commercial company in Brazil and signed contract assembly agreement.**

Designing and building innovative

TRUCKS AND ENGINES

that target customers best will

CREATE GREATER DEMAND

and improve financial performance.

Demand creation has been designed to increase profitable growth by anticipating customer needs. It means focusing on our competitive advantages, targeting markets where Navistar can truly excel, then delivering products and services that exceed customer expectations.

Our ability to anticipate and exceed customers' changing needs has been continuously demonstrated by our engine division—and, ultimately, rewarded by our customers. This is evidenced by our new agreement with Ford Motor Company to supply a newly designed, advanced technology diesel engine through the year 2012. Our next generation diesel engine will set new standards for performance, quality and emission control.

In our truck business, we already offer our customers superior value through our Diamond SPEC™ ordering system, which we launched last year for our International® and Eagle® 9000 tractors. Under this program, we're giving customers an effective and efficient way to get the best trucks suited to their application requirements, along with providing them guaranteed reliability, unprecedented service and warranty options. This year, we expanded Diamond SPEC and launched a pilot program in 11 key markets for medium trucks. Pilot results exceeded original projections for orders by 120%. Once again, our customers have responded resoundingly to our efforts to anticipate their needs for improved uptime.

All of our U.S. and Canadian dealers offer Diamond SPEC on all International 4000 medium-duty trucks. Customers choose from 16 pre-engineered component modules, rather than 1,250 individual components. They are guaranteed a faster, simpler order process, improved quality and enhanced overall vehicle performance. Indications are that Diamond SPEC for medium will meet the needs of more than two-thirds of our current customers.

Moreover, with plans approved for NGT, we will give our customers a best-in-class driver environment, the lowest cost of operation, and most advanced visibility and maneuverability. And, with a common chassis platform, we can ensure our customers get even higher quality and delivery integrity.

To deliver the best to customers, Navistar's North American distribution system includes a 1,000-location strong International dealer organization in the U.S., Canada and Mexico, a comprehensive service parts network, and an expanding used truck organization. Navistar gives its customers a branded product and service package unmatched in the industry.

Our collaborative approach and commitment to our dealers was once again recognized as Navistar was ranked number one for the third year in a row by the annual American Truck Dealers (ATD) Dealer Attitude Survey. The survey evaluates original equipment manufacturers (OEMs) on quality and performance issues related to products, parts, policies and service.

DEMAND *creation*

INNOVATION BRINGS REWARDS

Engine division innovation rewarded by Ford. Pictured are a few of the Navistar team members. From left to right: James T. Marcoux, vice president, worldwide sales and marketing; Patrick E. Charbonneau, vice president, engineering; Milan E. Zlock, manager, advanced vee engines; and Stephen K. Guillaume, Ford national accounts manager.

HIGHLIGHTS

- **Signed ten-year agreement with Ford Motor Company to supply newly designed, advanced technology diesel engines through the year 2012.**
- **Expanded Diamond SPEC™ truck ordering process, which now accounts for 40% of all conventional Class 8 truck orders, more than 80% of conventional Class 8 stock trucks ordered by dealers. The program has now been extended to medium trucks, exceeding pilot program expectations by 120%.**

This is a changing company.

We are working to

BUILD A NEW CULTURE

of cooperation and participation based on

RESPECT AND PERFORMANCE

POOLING TOGETHER

Chatham employees focus on relentless pursuit of quality on the line. Pictured clockwise are: assembly line operators, Rick Cowden, Carlo Roman (stockman), Jim Revell, Bonny Authier and Jack Bakker.

HIGH PERFORMANCE *culture*

The progress Navistar has made this year in achieving its performance goals is due to the efforts of our employees. They are the engine that makes the company run. They will be the source of our future success.

One of the most critical imperatives we have as a company is to mobilize employees so our company can set new standards of performance—in customer satisfaction, in product design, in quality and productivity, in our stock price. Our employees are the most experienced designers, producers and marketers of trucks and engines on the planet. The more each contributes, the greater will be Navistar's success. It's a fundamental strength that can't be readily duplicated by competition.

In the last few years, management has rededicated itself to tapping the reservoir of talent of all of our 16,000 employees. We articulated a focused vision—to be the best truck and engine company in North America—as a way to reignite the pride our people feel in the strong heritage of their company. We accompanied that vision with a new set of core values to drive performance.

These values are designed to provide a greater opportunity for every employee to contribute to his or her fullest, and to ensure that we serve the interests of shareowners, employees and customers.

To make the vision and values a reality, we trained nearly 4,000 non-represented employees to bring the values to life in the workplace. We are working with front-line supervisors and employees to develop the best way to share the training with all our employees in 1998.

Supporting this training is an ongoing communications program designed to re-build understanding and trust between management and employees, and to drive the vision and values across our company. We utilize frequent and direct face-to-face meetings with senior executives and employees.

Twice annually, the company's 450 leaders and senior management gather to review the challenges Navistar faces and their role in addressing those challenges. Also at these leadership conferences, managers work through issues to make the vision and values a reality for every employee in the company.

In 1997, for the first time in many years, we reached out to employees in face-to-face meetings. Once a month a key executive visits each of our main sites. Employees are encouraged to ask difficult but important questions. Our executives are answering in a very open, forthright manner. We are listening—and putting our newly gained knowledge into action.

To drive the new values through the company, we conducted an all-employee survey to provide a baseline to measure how well we work by our values. This survey indicated considerable need for improvement in the areas of respect for people and accountability.

Based on this survey, every functional area of the company developed action plans to improve performance. We will measure the impact of these plans with a follow-up survey, and managers will be held accountable for our progress.

In addition, we introduced a measurement tool to 4,000 employees trained in our values. It measures how well each employee lives and works by the values and squarely places accountability for progress on the shoulders of each individual.

Navistar is a changing company. Our challenges are significant. The results achieved in 1997 demonstrate clearly that working together we can create the kind of company we need to deliver the best to our shareowners, customers and employees. Because we really always had two options; win together, or lose apart. Our choice, our imperative: win together.

HIGHLIGHTS

- **Established a new standard of management, moving from a "command-and-control" approach to a "win/win" style designed to tap the immense energies and talents of all Navistar employees.**
- **Created an environment in which employees are accountable for results—enabling us to respond rapidly to changing market conditions and customer needs.**
- **Created the foundation for a new relationship with the UAW based on open communication, respect for people and increased accountability at all levels of the company.**
- **Created seven core values to drive performance and improve results: respect for people; customer focus; relentless pursuit of quality; speed, simplicity and agility; innovation; accountability; and communication.**

Quality and productivity together are the keys to DELIVERING MEASURABLE, SUSTAINABLE performance over the *long haul*.

RAISING THE BAR

Navistar Financial raises the bar on productivity: 100 new 9300 trucks financed in 1997 for Elite Express, Inc. through Ohio dealer, Center City International Trucks, Inc. Pictured here from left to right are: Doug Abel, president, Elite Express, Inc.; Jerry Wahoff, president, Center City International Trucks, Inc.; Chuck Koenig, vice president, Elite Express, Inc.; Patricia Brault, NFC area account executive.

Our focus in accelerating operational excellence is twofold: improve day-to-day operations, and drive changes that deliver improved, long-term performance.

We have seen dramatic results in our engine business, achieving industry-leading levels of productivity and quality while raising capacity to record levels. Hours-per-engine and uptime are among the best in the industry. First-time quality on both the I-6 and V-8 engines is close to 100%, and hours per unit improved by 25% over the last two years. Through asset management—increasing inventory and receivable turns—cash flow improved by $30 million.

With quality and productivity at all-time highs, our Indianapolis engine plant produced its 500,000th engine—two years ahead of schedule. This achievement reflects the engine's superior design and performance and high demand in the marketplace. It confirms the value of having employees directly accountable for and involved in engine quality.

Our truck business implemented the Navistar Production System (NPS) to improve quality and reduce manufacturing complexity. NPS will help us to reduce waste and increase efficiency at all locations.

To drive and support operational excellence, we implemented activity based management (ABM) across our truck business. ABM is a management information system that will help us focus on improvement initiatives that have the greatest impact on profitability. ABM more accurately measures the cost of our products and processes. We've been able to look at product profitability in an entirely new way, linking operational performance with long-term strategies and generating better information for decision making.

With ABM in place, our truck business launched an immediate drive to improve productivity and quality. For example, more than 100 employees from across the company were trained in "six sigma" tools and measurements, becoming internal "Black Belt" experts charged with identifying and eliminating sources of waste and variation within the manufacturing process. Each project they tackle is targeted to deliver 50% improvement and average cost savings of $75,000 from productivity and quality enhancements. By fiscal-year end, our employees were addressing more than 200 Black Belt projects which are expected to deliver a total savings of $15 million through fiscal 1998.

At Springfield, employees have systematically remapped each work station on the assembly line to eliminate unnecessary waste and streamline processes. At Chatham, we have changed the way work is assigned and raised overall productivity. We also launched the 20 Keys program, to improve performance measurements in 20 critical areas, including cleanliness, quality, productivity and technology.

Our best-in-class ergonomics program has served as a benchmark for OSHA, National Institute of Occupational Safety & Health and the General Accounting Office on the relationship between ergonomic improvements and advances in productivity, quality and employee morale. In 1997, we saw a 19% improvement from all operations in worker compensation costs, a 27% drop in incidence frequency rate, and a 33% improvement in our lost time case rate—showing the payoff of better ergonomics, accident prevention and case management programs.

OPERATIONAL *excellence*

HIGHLIGHTS

- **Attained record production levels in engine and foundry division, with total shipments up 11% to 258,000 engines, while achieving close to 100% first-time yield.**
- **Reduced production material and freight costs company-wide by 1.1% or $40.7 million, versus a plan of $33.2 million or 0.9%.**
- **Reduced workers compensation costs by 19% through best-in-class ergonomics program; reduced injury rates by 27% and improved lost time cases by 33% through aggressive prevention and case management programs.**

Certain statements under this caption constitute "forward-looking statements" under the Reform Act, which involve risks and uncertainties. Navistar International Corporation's actual results may differ significantly from the results discussed in such forward-looking statements. Factors that might cause such a difference include, but are not limited to, those discussed under the caption "Business Environment."

Navistar International Corporation is a holding company and its principal operating subsidiary is Navistar International Transportation Corp. (Transportation). In this discussion and analysis, "company" refers to Navistar International Corporation and its consolidated subsidiaries. The company's manufacturing operations are engaged in the manufacture and marketing of Class 5 through 8 trucks, including school buses, mid-range diesel engines and service parts primarily in the United States and Canada. These products are also sold to distributors in selected export markets. The financial services operations of the company provide wholesale, retail and lease financing, and commercial physical damage and liability insurance coverage to the company's dealers and retail customers and to the general public through an independent insurance agency system.

The discussion and analysis reviews the operating and financial results, and liquidity and capital resources of manufacturing operations and financial services operations. Manufacturing operations include the financial results of the financial services operations included on a one-line basis under the equity method of accounting. Financial services operations include Navistar Financial Corporation (NFC), its domestic insurance subsidiary as well as the company's foreign finance and insurance companies. See Note 1 to the Financial Statements.

Results of Operations

The company reported net income of $150 million for 1997, or $1.65 per common share, reflecting higher sales of manufactured products. Net income was $65 million, or $.49 per common share, in 1996 and $164 million, or $1.83 per common share, in 1995. Net income in 1996 included a one-time $35 million pretax charge for costs related to the termination of the next generation truck (NGT) program. In August 1997, the company and the United Auto Workers reached agreement on a master contract extension that enabled the company to reinstate this program. The remaining accrual for the 1996 charge at the time of the announcement was not material.

The company's manufacturing operations reported income before income taxes of $164 million in 1997 compared with pretax income of $22 million in 1996 and $200 million in 1995. The increase in 1997 reflects higher sales of trucks and diesel engines as well as the effects of improved pricing and various cost improvement initiatives. The decrease in 1996 from 1995 reflects a decline in demand for trucks as well as the charge for termination of the company's next generation truck program.

The company's financial services operations had income before income taxes of $78 million, $83 million and $62 million in 1997, 1996 and 1995, respectively.

NFC's pretax income in 1997 was $75 million, a 7% decrease from $81 million in 1996. The change is primarily a result of lower income on sales of retail receivables and a decline in wholesale financing activity. The reduced gains on sales resulted from lower margins on retail notes reflecting higher market interest rates prior to the date of sale. NFC's pretax income increased $22 million in 1996 from the $59 million reported in 1995 primarily due to higher income on sales of retail notes and an increased volume of wholesale financing.

Earnings from the foreign finance and insurance subsidiaries were $3 million, $2 million and $3 million in 1997, 1996 and 1995, respectively.

Sales and Revenues. Industry retail sales of Class 5 through 8 trucks totaled 347,400 units in 1997, a 2% increase from the 341,200 units sold in 1996, but 9% lower than the 380,600 units sold in 1995. Class 8 heavy truck sales totaled 196,800 units, comparable to the 195,400 units sold in 1996 but a decrease of 14% from the 228,800 units sold in 1995. Industry sales of Class 5, 6 and 7 medium trucks, including school buses, totaled 150,600 units in 1997, a 3% increase from 1996 when 145,800 units were sold, and comparable to the 151,800 units sold in 1995. Industry sales of school buses, which accounted for 22% of the medium truck market, increased slightly from 1996 to 33,200 units.

Sales and revenues of $6,371 million in 1997 were 11% higher than the $5,754 million reported in 1996 and comparable to the $6,342 million reported in 1995. Sales of trucks, mid-range diesel engines and service parts totaled $6,147 million in 1997, 12% above the $5,508 million reported for 1996 and comparable to the $6,125 million reported in 1995.

The company maintained its position as sales leader in the combined United States and Canadian Class 5 through 8 truck market in 1997 with a 28.6% market share, an increase from the 27.5% share in 1996 and the 26.7% share in 1995. (Sources: American Automobile Manufacturer's Association, the United States Motor Vehicle Manufacturer's Association and R. L. Polk & Company.) In 1997, the company's share of the Class 8 heavy truck market increased to 18.6% from 17.1% in 1996 and 18.4% in 1995.

Shipments of mid-range diesel engines by the company to other original equipment manufacturers during 1997 were a record 184,000 units, a 13% increase from 1996 and a 19% improvement over 1995. Higher shipments to Ford Motor Company to meet consumer demand for the light trucks and vans which use this engine was the primary reason for the increase.

Service parts sales of $806 million in 1997 increased from the $760 million reported in 1996 and were 10% higher than the $730 million reported in 1995 as a result of dealer and national account volume growth.

Finance and insurance revenue for 1997 was $174 million, 12% lower than the $197 million reported in 1996 primarily as a result of a decline in wholesale financing activity. Revenues from financial services operations increased 18% between 1996 and 1995 primarily as a result of higher income on sales of retail notes.

Costs and Expenses. Manufacturing gross margin was 14.2% of sales in 1997, compared with 12.5% in 1996 and 13.8% in 1995. The increase in gross margin is primarily due to lower production costs and improved pricing offset by a provision for employee profit sharing. Factors which contributed to the change in gross margin between 1996 and 1995 included lower sales volumes, more competitive pricing and the costs of terminating the next generation truck program.

Engineering and research expense was $124 million in 1997, $129 million in 1996 and $113 million in 1995, reflecting continuing investment in new truck and engine products as well as improvements to existing products.

Marketing and administrative expense was $365 million in 1997 compared with $319 million in 1996 and $307 million in 1995. The change between 1997 and 1996 is the result of higher sales and distribution costs, and an increase in the provision for payment to employees as provided by the company's performance incentive programs. The $12 million increase in the expense between 1996 and 1995 reflects investment in the implementation of the company's strategy to reduce costs and complexity in its manufacturing processes.

Interest expense decreased to $74 million in 1997 from $83 million in 1996 and $87 million in 1995. The decreases in 1997 and 1996 were the result of lower wholesale note funding requirements and declining interest rates.

Finance service charges on sold receivables were $23 million in 1997, 4% lower than in 1996 and 21% lower than in 1995.

Liquidity and Capital Resources

Cash flow is generated from the manufacture and sale of trucks, mid-range diesel engines and service parts as well as product financing and insurance coverage provided to Transportation's dealers and retail customers by the financial services operations.

Historically, funds to finance Transportation's products are obtained from a combination of commercial paper, short- and long-term bank borrowings, medium- and long-term debt issues, sales of finance receivables and equity capital. NFC's current debt ratings have made bank borrowings and sales of finance receivables the most economic sources of cash. Insurance operations are funded through internal operations.

Total cash, cash equivalents and marketable securities of the company amounted to $965 million at October 31, 1997, $881 million at October 31, 1996 and $1,040 million at October 31, 1995.

Cash provided by operations during 1997 totaled $380 million, primarily from net income of $150 million, $82 million of noncash deferred income taxes, and $59 million of other noncash items, principally depreciation and a net change in operating assets and liabilities of $89 million. Income tax expense for 1997 was $92 million, of which $10 million was cash payments to federal and certain state and local governments, while the remaining $82 million of federal and other taxes reduced the deferred tax asset.

The net change in operating assets and liabilities of $89 million includes a $195 million increase in receivables, reflecting continued strong demand for the company's products, offset by a $288 million increase in accounts payable as a result of increased production in the fourth quarter.

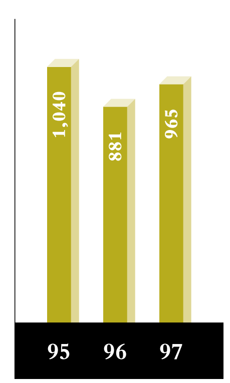
Investment programs included a net decrease in marketable securities, as sales of securities exceeded purchases by $45 million. During 1997, the purchase of $970 million of retail notes and lease receivables was funded with $958 million in proceeds from the sale of receivables and principal collections of $94 million. Other investment activities used $42 million for an increase in property and equipment leased to others and $172 million to fund capital expenditures. Capital expenditures included $82 million for construction of a truck assembly facility in Mexico, $42 million to increase mid-range diesel engine capacity and additional funds for truck product improvements.

Financing activities used cash to pay $29 million in dividends on the Series G Preferred shares, $46 million for principal payments on long-term debt, and $285 million to reduce notes and debt outstanding under the bank revolving credit facility and asset-backed and other commercial paper programs offset by an increase of $209 million in long-term debt.

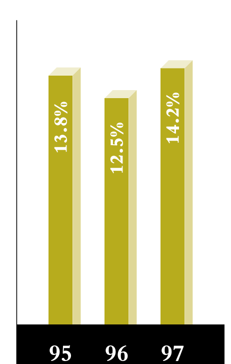
During 1997 and 1996, NFC supplied 94% of the wholesale financing of new trucks sold to Transportation's dealers compared with 93% in 1995. NFC's share of the retail financing of new trucks sold in the United States decreased to 13% in 1997 from 16% in 1996 and 14% in 1995 due to the highly competitive commercial financing market.

The sale of finance receivables is a significant source of funding for the financial services operations. During 1997, 1996 and 1995, NFC sold $987 million, $985 million and $740 million, respectively, of retail notes through Navistar Financial Retail Receivables Corporation (NFRRC), a wholly owned subsidiary. The net proceeds from these sales were used for general working capital purposes. In November 1997, NFC sold an additional $500 million of retail notes through NFRRC.

NFRRC has filed registration statements with the Securities and Exchange Commission which provide for the issuance of up to $5,000 million of asset-backed securities. At October 31, 1997, the remaining shelf registration available to NFRRC for issuance of asset-backed securities was $1,473 million. See Note 8 to the Financial Statements.



Cash and Marketable Securities
$ millions



Gross Margin

NFC has a $925 million contractually committed bank revolving credit facility and a $400 million asset-backed commercial paper program supported by a bank liquidity facility which mature in March 2001. NFC also utilizes a $600 million revolving wholesale note trust that provides for the continuous sale of eligible wholesale notes on a daily basis. The trust is comprised of two $100 million tranches of investor certificates maturing serially from 1998 to 1999, and two $200 million tranches maturing in 2003 and 2004. At October 31, 1997, the remaining shelf registration available for issuance of investor certificates was $200 million.

At October 31, 1997, available funding under NFC's amended and restated credit facility and the asset-backed commercial paper facility was $532 million and $14 million, respectively, of which $141 million was used to back short-term debt at October 31, 1997.

The company finances capital expenditures principally through internally generated cash. Capital leasing is used to fund selected projects based on economic and operating factors. The company had outstanding capital commitments of $137 million at October 31, 1997 primarily for increased manufacturing capacity at the Indianapolis engine plant and construction of a truck assembly facility in Mexico.

The company has announced plans for approximately $350 million in capital spending over the next six years for the NGT program. Capital expenditures for 1998 are expected to be approximately double the current year's level. Approximately $25 million is to be spent in 1998 for the NGT program. Additional capital expenditures are planned for the completion of the truck assembly facility in Mexico, increased manufacturing capacity at the Indianapolis engine plant, commencement of truck operations in Brazil and improvements to existing facilities and products. The company's investment in the NGT program will also include $300 million in development expense over the next six years, of which approximately $50 million is planned for 1998.

In November 1997, the company contributed $200 million to the Retiree Health Care Base Plan Trust and contributed $100 million to the hourly pension plan.

NFC's maximum exposure under all receivable sale recourse provisions at October 31, 1997 was $246 million; however, management believes that the allowance for credit losses on sold receivables is adequate.

At October 31, 1997, the Canadian operating subsidiary was contingently liable for retail customers' contracts and leases financed by a third party. The company is subject to maximum recourse of $261 million on retail contracts and $13 million on retail leases. In addition, as of October 31, 1997, the company is contingently liable for approximately $49 million for various guarantees and buyback programs; however, based on historical loss trends, the company's exposure is not considered material.

The Canadian operating subsidiary, NFC and certain other subsidiaries included in financial services operations are parties to agreements which result in the restriction of amounts which can be distributed to Transportation in the form of dividends, loans or advances. At October 31, 1997, the maximum amount of dividends which were available for distribution under the most restrictive covenants was $62 million.

The company and Transportation are obligated under certain agreements with public and private lenders of NFC to maintain the subsidiary's income before interest expense and income taxes at not less than 125% of its total interest expense. No income maintenance payments were required for the three years ended October 31, 1997.

During November 1997, the company arranged financing for $125 million of funds denominated in U.S. dollars and Mexican pesos to be used for development of the company's Mexican operations.

Management continues to evaluate current and forecasted cash flow as a basis for financing operating requirements, capital expenditures and anticipated payments of preferred dividends. Management believes that collections on the outstanding receivables portfolios as well as funds available from various funding sources will permit the financial services operations to meet the financing requirements of the company's dealers and customers.

Environmental Matters

In the fourth quarter of 1994, Transportation recorded a $20 million charge, net of $13 million of income taxes, as a loss of discontinued operations related to environmental liabilities at production facilities of two formerly owned businesses, Wisconsin Steel and Solar Turbine, Inc. Included in the charge was an anticipated $11 million payment to the Economic Development Administration, a division of the U.S. Department of Commerce, in settlement of commercial and environmental disputes related to the Wisconsin Steel property. In 1997, the U.S. Department of Justice and Transportation approved the final consent decree related to the Wisconsin Steel property and the company paid $11 million to the Economic Development Administration.

The company has been named a potentially responsible party (PRP), in conjunction with other parties, in a number of cases arising under an environmental protection law known as the Superfund law. These cases involve sites which allegedly have received wastes from current or former company locations. Based on information available to the company, which in most cases consists of data related to quantities and characteristics of material generated at or shipped to each site as well as cost estimates from PRPs and/or federal or state regulatory agencies for the cleanup of these sites, a reasonable estimate is calculated of the company's share, if any, of the probable costs and is provided for in the financial statements. These obligations generally are recognized no later than completion of the remedial feasibility study and are not discounted to their present value. The company reviews its accruals on a regular basis and believes that, based on these calculations, its share of the potential additional costs for the cleanup of each site will not have a material effect on the company's financial results.

Derivative Financial Instruments

As disclosed in Notes 1 and 10 to the Financial Statements, the company uses derivative financial instruments to transfer or reduce the risks of foreign exchange and interest rate volatility, and potentially increase the return on invested funds. Company policy does not allow the use of derivatives for speculative purposes.

The company's manufacturing operations, as conditions warrant, hedge foreign exchange exposure on the purchase of parts and materials from foreign countries and its exposure from sales of manufactured products in other countries. Contracted purchases of commodities for manufacturing may be hedged up to one year. The manufacturing operations had no foreign exchange exposure at October 31, 1997.

NFC uses interest rate caps, interest rate swaps and forward interest rate contracts when needed to convert floating rate funds to fixed and vice versa to match its asset portfolio. NFC also uses forward interest rate contracts to manage its exposure to fluctuations in funding costs from the anticipated securitization and sale of retail notes. During 1997, NFC entered into $500 million of interest rate hedge agreements in anticipation of the November 1997 sale of retail receivables. These hedge agreements were closed in conjunction with the pricing of the sale, and the loss at October 31, 1997, which was not material, was deferred and reduced the gain recognized on the sale of receivables in November 1997.

Both manufacturing operations and NFC purchase collateralized mortgage obligations that have relatively stable cash flow patterns in relation to interest rate changes.

Year 2000

The company has made and will make certain investments in its software systems and applications to ensure that the company is Year 2000 compliant. The financial impact to the company has not been and is not anticipated to be material to its financial position or results of operations.

New Accounting Pronouncements

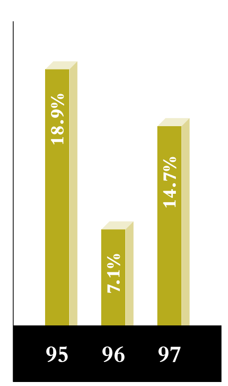
In February 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 128, "Earnings Per Share." This statement specifies the computation, presentation and disclosure requirements for earnings per share and is effective for financial statements issued for periods ending after December 15, 1997. The standard is not expected to have a material effect on the company's net income per common share computation.

In June 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" (SFAS 130), and Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information" (SFAS 131). SFAS 130 establishes standards for reporting and display of comprehensive income and its components. SFAS 131 establishes standards for reporting information about operating segments, and related disclosures about products and services, geographic areas and major customers. These statements are effective for fiscal years beginning after December 15, 1997. These standards expand or modify disclosures and, accordingly, will have no impact on the company's reported financial position, results of operations and cash flows. The company is assessing the impact of SFAS 131 on its reported segments.

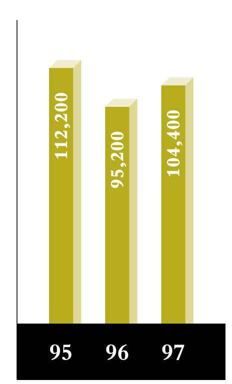
Income Taxes

The Statement of Financial Condition at October 31, 1997 and 1996 includes a deferred tax asset of $934 million and $1,030 million, respectively, net of valuation allowances of $309 million related to future tax benefits. The deferred tax assets are net of valuation allowances since it is more likely than not that some portion of the deferred tax asset may not be realized in the future.

The deferred tax asset includes the tax benefits associated with cumulative tax losses of $1,808 million and temporary differences, which represent the cumulative expense of $1,413 million recorded in the Statement of Income that has not been deducted on the company's tax returns. The valuation allowance at October 31, 1997 assumes that it is more likely than not that approximately $815 million of cumulative tax losses will not be realized before their expiration date. Realization of the net deferred tax asset is dependent on the generation of approximately $2,500 million of future taxable income, of which an average of approximately $75 million would need to be generated annually for the 14-year period 1998 through 2011. The remaining taxable income, which represents the realization of tax benefits associated with temporary differences, does not need to be generated until subsequent to 2011. Until the company has utilized its significant



Return on Equity



Company Shipments
units (class 5-8)

NOL carryforwards, the cash payment of federal income taxes will be minimal. See Note 3 to the Financial Statements.

Extensive analysis is performed to determine the amount of the deferred tax asset. Such analysis is based on the premise that the company is and will continue to be a going concern and that it is more likely than not that deferred tax benefits will be realized through the generation of future taxable income. Management reviews all available evidence, both positive and negative, to assess the long-term earnings potential of the company using a number of alternatives to evaluate financial results in economic cycles at various industry volume conditions based upon the company's current operating structure. Other factors considered are the company's 17-consecutive-year leadership in the combined market share of Class 5 through 8 trucks and recognition as a worldwide leading producer of mid-range diesel engines. The projected availability of taxable income to realize the tax benefit from net operating loss carryforwards and the reversal of temporary differences before expiration of these benefits are also considered. The valuation allowance may be adjusted in the future as a result of changes in business and industry conditions, operating structure, company strategies or other significant transactions. Management believes that, with the combination of available tax planning strategies and the maintenance of significant market share, earnings are achievable in order to realize the net deferred tax asset of $934 million.

Reconciliation of the company's income before income taxes for financial statement purposes to United States taxable income for the years ended October 31 is as follows:

MILLIONS OF DOLLARS	1997	1996	1995
Income before income taxes	$242	$ 105	$262
Exclusion of (income) loss of foreign subsidiaries	(3)	3	(11)
State income taxes	(2)	(2)	(2)
Temporary differences	151	(284)	69
Other	6	–	(4)
Taxable income (loss)	$394	$(178)	$314

The company contributed approximately $215 million to its hourly and salaried pension plans in fiscal 1997. The timing of these contributions allowed for their deduction on the company's 1996 tax return, which resulted in a tax loss of $178 million as compared to the $37 million of taxable income previously reported.

Business Environment

Sales of Class 5 through 8 trucks are cyclical, with demand affected by such economic factors as industrial production, construction, demand for consumer durable goods, interest rates and the earnings and cash flow of dealers and customers. Reflecting the stability of the general economy, demand for new trucks remained strong during 1997. An improvement in the number of new truck orders has increased the company's order backlog to 45,300 units at October 31, 1997 from 20,900 units at October 31, 1996. Retail deliveries in 1998 continue to be highly dependent on the rate at which new truck orders are received. The company will evaluate order receipts and backlog throughout the year and will balance production with demand as appropriate.

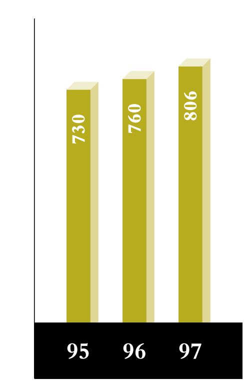
The company currently projects 1998 United States and Canadian Class 8 heavy truck demand to be 195,000 units, a slight decrease from 1997. Class 5, 6 and 7 medium truck demand, excluding school buses, is forecast at 116,000 units, slightly lower than in 1997. Demand for school buses is expected to decrease 8% in 1998 to 30,500 units. Mid-range diesel engine shipments by the company to original equipment manufacturers in 1998 are expected to be 215,700 units, 17% higher than in 1997. The company's service parts sales are projected to grow 9% to approximately $875 million.

An independent trust, created in 1993 for the benefit of the company's current and future retirees and administered by a five person trust committee, owned all of the outstanding Class B Common Stock at October 31, 1997 which is approximately one-third of the company's outstanding common stock. The Class B Common Stock has restricted voting rights and transfer provisions but, on July 1, 1998, will convert into Common Stock with full voting rights and no transfer restrictions.

During August 1997, the company's current master contract with the United Auto Workers (UAW) was extended through October 1, 2002. This contract allows the company to focus its assembly plants, simplify current product lines, invest in new product development and achieve more competitive wage, benefit and productivity levels.

During 1997, the company entered into a ten-year agreement, effective with model year 2003, to supply newly designed, advanced technology engines through the year 2012 to Ford Motor Company for use in its diesel-powered light trucks and vans. The company's current engine agreement with Ford was extended through model year 2002.

OEM Diesel Engine Shipments
units



Parts Sales
$ millions

Statement *of* Financial Reporting Responsibility

Management of Navistar International Corporation and its subsidiaries is responsible for the preparation and for the integrity and objectivity of the accompanying financial statements and other financial information in this report. The financial statements have been prepared in accordance with generally accepted accounting principles and include amounts that are based on management's estimates and judgments.

The accompanying financial statements have been audited by Deloitte & Touche LLP, independent auditors, whose appointment is ratified by shareowner vote at the Annual Meeting. Management has made available to Deloitte & Touche LLP all the company's financial records and related data, as well as the minutes of the Board of Directors' meetings. Management believes that all representations made to Deloitte & Touche LLP during its audit were valid and appropriate.

Management is responsible for establishing and maintaining a system of internal controls throughout its operations that provides reasonable assurance as to the integrity and reliability of the financial statements, the protection of assets from unauthorized use and the execution and recording of transactions in accordance with management's authorization. The system of internal controls which provides for appropriate division of responsibility is supported by written policies and procedures that are updated by management, as necessary. The system is tested and evaluated regularly by the company's internal auditors as well as by the independent auditors in connection with their annual audit of the financial statements. The independent auditors conduct their audit in accordance with generally accepted auditing standards and perform such tests of transactions and balances as they deem necessary. Management considers the recommendations of its internal auditors and independent auditors concerning the company's system of internal controls and takes the necessary actions that are cost-effective in the circumstances to respond appropriately to the recommendations presented. Management believes that the company's system of internal controls accomplishes the objectives set forth in the first sentence of this paragraph.

The Audit Committee of the Board of Directors, composed of six non-employee Directors, meets periodically with the independent auditors, management, general counsel and internal auditors to satisfy itself that such persons are properly discharging their responsibilities regarding financial reporting and auditing. In carrying out these responsibilities, the Committee has full access to the independent auditors, internal auditors, general counsel and financial management in scheduled joint sessions or private meetings as in the Committee's judgment seem appropriate. Similarly, the company's independent auditors, internal auditors, general counsel and financial management have full access to the Committee and to the Board of Directors and each is responsible for bringing before the Committee or its Chair, in a timely manner, any matter deemed appropriate to the discharge of the Committee's responsibility.

John R. Horne

JOHN R. HORNE
Chairman, President and Chief Executive Officer

Robert C. Lannert

ROBERT C. LANNERT
Executive Vice President and Chief Financial Officer

Independent Auditors' Report

Deloitte & Touche LLP

Navistar International Corporation,
Its Directors and Shareowners:

We have audited the Statement of Financial Condition of Navistar International Corporation and Consolidated Subsidiaries as of October 31, 1997 and 1996, and the related Statements of Income and of Cash Flow for each of the three years in the period ended October 31, 1997. These consolidated financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Navistar International Corporation and Consolidated Subsidiaries at October 31, 1997 and 1996, and the results of their operations and their cash flow for each of the three years in the period ended October 31, 1997, in conformity with generally accepted accounting principles.

Deloitte & Touche LLP

DELOITTE & TOUCHE LLP
December 15, 1997
Chicago, Illinois

Statement *of* Income

Navistar International Corporation and Consolidated Subsidiaries

For the Years Ended October 31

(MILLIONS OF DOLLARS, EXCEPT PER SHARE DATA)	1997	1996	1995
SALES AND REVENUES			
Sales of manufactured products	$6,147	$5,508	$6,125
Finance and insurance revenue	174	197	167
Other income	50	49	50
Total sales and revenues	6,371	5,754	6,342
COSTS AND EXPENSES			
Cost of products and services sold	5,292	4,827	5,288
Postretirement benefits	215	220	206
Engineering and research expense	124	129	113
Marketing and administrative expense	365	319	307
Interest expense	74	83	87
Financing charges on sold receivables	23	24	29
Insurance claims and underwriting expense	36	47	50
Total costs and expenses	6,129	5,649	6,080
Income before income taxes	242	105	262
Income tax expense	92	40	98
NET INCOME	150	65	164
Less dividends on Series G preferred stock	29	29	29
Net income applicable to common stock	$ 121	$ 36	$ 135
NET INCOME PER COMMON SHARE	$ 1.65	$ .49	$ 1.83
Average number of common and dilutive common equivalent shares outstanding (millions)	73.6	73.8	74.3

See Notes to Financial Statements.

Navistar International Corporation and Consolidated Subsidiaries

As of October 31

(MILLIONS OF DOLLARS)

	1997	1996
ASSETS		
Cash and cash equivalents	$ 609	$ 487
Marketable securities	356	394
	965	881
Receivables, net	1,755	1,655
Inventories	483	463
Property and equipment, net	835	770
Investments and other assets	332	213
Intangible pension assets	212	314
Deferred tax asset, net	934	1,030
Total assets	$5,516	$5,326
LIABILITIES AND SHAREOWNERS' EQUITY		
LIABILITIES		
Accounts payable, principally trade	$1,100	$ 820
Debt:		
Manufacturing operations	92	115
Financial services operations	1,224	1,305
Postretirement benefits liability	1,186	1,351
Other liabilities	894	819
Total liabilities	4,496	4,410
Commitments and contingencies		
SHAREOWNERS' EQUITY		
Series G convertible preferred stock (liquidation preference $240 million)	240	240
Series D convertible junior preference stock (liquidation preference $4 million)	4	4
Common stock (52.2 million and 51.0 million shares issued)	1,659	1,642
Class B Common stock (23.1 million and 24.3 million shares issued)	471	491
Retained earnings (deficit)—balance accumulated after the deficit reclassification as of October 31, 1987	(1,301)	(1,431)
Common stock held in treasury, at cost (2.9 million and 1.6 million shares held)	(53)	(30)
Total shareowners' equity	1,020	916
Total liabilities and shareowners' equity	$5,516	$5,326

See Notes to Financial Statements.

Navistar International Corporation and Consolidated Subsidiaries

For the Years Ended October 31

(MILLIONS OF DOLLARS)

	1997	1996	1995
CASH FLOW FROM OPERATIONS			
Net income	$ 150	$ 65	$ 164
ADJUSTMENTS TO RECONCILE NET INCOME TO CASH PROVIDED BY OPERATIONS:			
Depreciation and amortization	120	105	86
Deferred income taxes	82	37	89
Other, net	(61)	(13)	(9)
CHANGE IN OPERATING ASSETS AND LIABILITIES:			
Receivables	(195)	186	(91)
Inventories	(25)	(47)	35
Prepaid and other current assets	4	1	10
Accounts payable	288	(110)	63
Other liabilities	17	(106)	70
Cash provided by operations	380	118	417
CASH FLOW FROM INVESTMENT PROGRAMS			
Purchase of retail notes and lease receivables	(970)	(1,108)	(1,099)
Collections/sales of retail notes and lease receivables	1,052	1,107	850
Purchase of marketable securities	(512)	(585)	(722)
Sales or maturities of marketable securities	557	752	480
Capital expenditures	(172)	(117)	(139)
Property and equipment leased to others	(42)	(73)	(19)
Other investment programs, net	3	(8)	8
Cash used in investment programs	(84)	(32)	(641)
CASH FLOW FROM FINANCING ACTIVITIES			
Issuance of debt	209	—	—
Principal payments on debt	(46)	(136)	(121)
Net increase (decrease) in notes and debt outstanding under bank revolving credit facility and asset-backed and other commercial paper programs	(285)	81	312
Dividends paid	(29)	(29)	(29)
Repurchase of common stock	(23)	—	(10)
Cash (used in) provided by financing activities	(174)	(84)	152
CASH AND CASH EQUIVALENTS			
Increase (decrease) during the year	122	2	(72)
At beginning of the year	487	485	557
Cash and cash equivalents at end of the year	$ 609	$ 487	$ 485

See Notes to Financial Statements.

1 SUMMARY OF ACCOUNTING POLICIES

Basis of Consolidation

Navistar International Corporation is a holding company, whose principal operating subsidiary is Navistar International Transportation Corp. (Transportation). As used hereafter, "company" refers to Navistar International Corporation and its consolidated subsidiaries. The consolidated financial statements include the results of the company's manufacturing operations and its wholly owned financial services subsidiaries. The effects of transactions between the manufacturing and financial services operations have been eliminated to arrive at the consolidated totals. The distinction between current and long-term assets and liabilities in the Statement of Financial Condition is not meaningful when finance, insurance and manufacturing operations are combined; therefore, the company has adopted an unclassified presentation. Certain 1996 and 1995 amounts have been reclassified to conform with the presentation used in the 1997 financial statements.

The company operates in two principal industry segments: manufacturing and financial services. Manufacturing operations are responsible for the manufacture and marketing of medium and heavy trucks, including school buses, mid-range diesel engines and service parts primarily in the United States and Canada as well as in selected export markets. Based on assets and revenues, manufacturing operations represent the majority of the company's business activities. The financial services operations consist of Navistar Financial Corporation (NFC), its domestic insurance subsidiary and the company's foreign finance and insurance subsidiaries. NFC's primary business is the retail and wholesale financing of products sold by the manufacturing operations and its dealers within the United States and the providing of commercial physical damage and liability insurance to the manufacturing operations' dealers and retail customers and to the general public through an independent insurance agency system.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Revenue Recognition

Manufacturing operations recognize shipments of new trucks and service parts to independent dealers and retail customers as sales. Price allowances, expected in the normal course of business, and the cost of special incentive programs are recorded at the time of sale. Engine sales are recognized at the time of shipment to original equipment manufacturers. An allowance for losses on receivables is maintained at an amount that management considers appropriate in relation to the outstanding receivables portfolio and it is charged when receivables are determined to be uncollectible.

Financial services operations recognize finance charges on retail notes and finance leases as income over the term of the receivables utilizing the interest method. Interest due from interest-bearing notes and accounts is recognized on the accrual basis. Operating lease revenues are recognized on a straight-line basis over the life of the lease. Selected receivables are sold and securitized to public and private investors with limited recourse. Gains or losses on sales of receivables are credited or charged to revenue in the period in which the sale occurs. Financial services operations continue to service the sold receivables and receive a fee for such services from the investor. An allowance for losses is maintained at a level deemed appropriate based on such factors as overall portfolio quality, historical loss experience and current economic conditions.

Insurance premiums are earned on a prorata basis over the terms of the policies. Underwriting losses and outstanding loss reserve balances are based on individual case estimates of the ultimate cost of settlement, including actual losses, and determinations of amounts required for losses incurred but not reported.

Cash and Cash Equivalents

All highly liquid financial instruments with maturities of three months or less from date of purchase, consisting primarily of bankers' acceptances, commercial paper, United States government securities and floating rate notes, are classified as cash equivalents in the Statement of Financial Condition and Statement of Cash Flow.

Marketable Securities

Marketable securities are classified as available-for-sale securities and are reported at fair value. The difference between amortized cost and fair value is recorded as an adjustment to shareowners' equity, net of applicable deferred taxes.

Inventories

Inventories are valued at the lower of average cost or market.

Property and Other Long-Lived Assets

Significant expenditures for replacement of equipment, tooling and pattern equipment, and major rebuilding of machine tools are capitalized. Depreciation and amortization are generally provided on the straight-line basis over the estimated useful lives of the assets, which average 35 years for buildings and improvements and eight years for machinery and equipment. Gains and losses on property disposals are included in other income and expense. The carrying amount of all long-lived assets is evaluated periodically to determine if adjustment to the depreciation and amortization period or to the unamortized balance is warranted. Such evaluation is based principally on the expected utilization of the long-lived assets and the projected, undiscounted cash flows of the operations in which the long-lived assets are deployed.

1 SUMMARY OF ACCOUNTING POLICIES *(continued)*

Engineering and Research Expense

Engineering and research expense includes research and development expenses and routine ongoing costs associated with improving existing products and manufacturing processes. Research and development expenses, which include activities for the introduction of new truck and diesel engine products and major improvements to existing products and processes, totaled $92 million, $101 million and $91 million in 1997, 1996 and 1995, respectively.

Product Related Costs

The company accrues warranty expense at the time of end product sale. Product liability expense is accrued based on the estimate of total future payments to settle product liability claims.

Derivative Financial Instruments

The company uses derivatives to transfer or reduce risks of foreign exchange and interest rate volatility and to potentially increase the return on invested funds. NFC, a wholly owned subsidiary of Transportation, uses derivatives such as forward contracts and interest rate swaps to reduce its exposure to interest rate volatility. NFC's primary use of such financial instruments is to hedge the fair value of its fixed rate receivables against changes in market interest rates in anticipation of securitization and sale of such receivables. The anticipated transactions are probable of occurrence and their significant terms and characteristics have been identified.

All derivative financial instruments are held for purposes other than trading, and company policy prohibits the use of derivatives for speculative purposes. Gains or losses related to hedges of anticipated sales of receivables are deferred and are recognized in income when the receivables are sold. At all times, the principal balance of receivables owned and expected to be sold by NFC exceeds the notional amount of open derivative contracts.

Stock-Based Compensation

Effective November 1, 1996, the company adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" (SFAS 123). Accordingly, the company elected to continue to account for stock-based compensation plans consistent with prior years.

New Accounting Pronouncements

In February 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 128, "Earnings Per Share." This statement specifies the computation, presentation and disclosure requirements for earnings per share and is effective for financial statements issued for periods ending after December 15, 1997. The standard is not expected to have a material effect on the company's net income per common share computation.

In June 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" (SFAS 130), and Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information" (SFAS 131). SFAS 130 establishes standards for reporting and display of comprehensive income and its components. SFAS 131 establishes standards for reporting information about operating segments and related disclosures about products and services, geographic areas and major customers. These statements are effective for fiscal years beginning after December 15, 1997. These standards expand or modify current disclosures and, accordingly, will have no impact on the company's reported financial position, results of operations and cash flows. The company is assessing the impact of SFAS 131 on its reported segments.

2 POSTRETIREMENT BENEFITS

The company provides postretirement benefits to substantially all of its employees. Costs associated with postretirement benefits include pension expense for employees, retirees and surviving spouses, and postretirement health care and life insurance expense for employees, retirees, surviving spouses and dependents. In addition, as part of the 1993 restructured retiree health care and life insurance plans, profit sharing payments to an independent retiree trust are required. The cost of postretirement benefits is segregated as a separate component in the Statement of Income and is as follows:

MILLIONS OF DOLLARS	1997	1996	1995
Pension expense	$129	$160	$110
Health/life insurance	66	60	70
Profit sharing provision to Trust	20	—	26
Total postretirement benefits expense	$215	$220	$206

In the Statement of Financial Condition, the postretirement benefits liability of $1,186 million in 1997 and $1,351 million in 1996 includes $445 million and $607 million, respectively, for pension and $741 million and $744 million, respectively, for postretirement health care and life insurance benefits. Included in investments and other assets in the Statement of Financial Condition is a prepaid pension asset of $120 million in 1997 and $38 million in 1996.

2 POSTRETIREMENT BENEFITS *(continued)*

Pension Benefits

Generally, the pension plans are noncontributory with benefits related to an employee's length of service and compensation rate. The company's policy is to fund its pension plans in accordance with applicable United States and Canadian government regulations and to make additional payments as funds are available to achieve full funding of the vested accumulated benefit obligation. The pension plans vary in the extent to which they are funded, but, for plan years which ended during the current year, all legal funding requirements have been met. Plan assets are invested primarily in dedicated portfolios of long-term fixed income securities with more recent contributions invested in equity securities.

Pension Expense

Net pension expense included in the Statement of Income is composed of the following:

MILLIONS OF DOLLARS	1997	1996	1995
Service cost for benefits earned during the period	$ 34	$ 34	$ 24
Interest on projected benefit obligation	238	231	232
Net amortization costs and other	99	104	57
Less expected return on assets	(242)	(209)	(203)
Net pension expense	$ 129	$ 160	$ 110
Actual return on assets	$ 505	$ 188	$ 398

"Amortization costs" include amortization of cumulative gains and losses over the expected remaining service life of employees, amortization of the initial transition liability over 15 years, the expense related to yearly lump-sum payments to retirees required by negotiated labor contracts and amortization of plan amendments, recognized over the remaining service life of employees, except for those plan amendments arising from negotiated labor contracts, which are amortized over the length of the contract.

Pension Assets and Liabilities

Included in the Statement of Financial Condition is the minimum pension liability for certain unfunded pension plans. The adjustment for the minimum pension liability in the amounts of $504 million and $623 million are offset by intangible pension assets of $212 million and $314 million and accumulated reductions in shareowners' equity of $195 million and $206 million at October 31, 1997 and October 31, 1996, respectively. The changes in shareowners' equity are net of deferred income taxes of $97 million at October 31, 1997 and $103 million at October 31, 1996. The minimum pension liability will change from year to year as a result of revisions to actuarial assumptions, experience gains or losses and settlement rate changes.

The funded status of the company's plans as of October 31, 1997 and 1996 and a reconciliation with amounts recognized in the Statement of Financial Condition are provided below.

	PLANS IN WHICH ASSETS EXCEED ACCUMULATED BENEFITS		PLANS IN WHICH ACCUMULATED BENEFITS EXCEED ASSETS	
MILLIONS OF DOLLARS	1997	1996	1997	1996
ACTUARIAL PRESENT VALUE OF:				
Vested benefits	$(1,122)	$(59)	$(1,857)	$(2,672)
Nonvested benefits	(80)	(7)	(207)	(270)
Accumulated benefit obligation	(1,202)	(66)	(2,064)	(2,942)
Effect of projected future compensation levels	(30)	(3)	(3)	(23)
Projected benefit obligation	(1,232)	(69)	(2,067)	(2,965)
Plan assets at fair value	1,279	91	1,621	2,336
Funded status at October 31	47	22	(446)	(629)
UNAMORTIZED PENSION COSTS:				
Net losses	29	11	293	332
Prior service costs	12	6	77	113
(Asset) liability at date of transition	32	(1)	135	200
Adjustment for the minimum liability	—	—	(504)	(623)
Net asset (liability)	$ 120	$ 38	$ (445)	$ (607)

The weighted average rate assumptions used in determining pension costs and the projected benefit obligation were:

	1997	1996	1995
Discount rate used to determine present value of projected benefit obligation at end of year	7.3%	8.1%	7.8%
Expected long-term rate of return on plan assets for the year	9.8%	9.0%	9.9%
Expected rate of increase in future compensation levels	3.5%	3.5%	3.5%

2 POSTRETIREMENT BENEFITS *(continued)*

Other Postretirement Benefits

In addition to providing pension benefits, the company provides health care and life insurance for a majority of its retired employees, spouses and certain dependents in the United States and Canada.

In 1993, a trust was established to provide a vehicle for funding the health care liability through company contributions and retiree premiums. The funds in this trust are invested primarily in equity securities. The company was required to make a prefunding contribution of $200 million to the trust on or prior to June 30, 1998. This contribution was made during November 1997.

The components of expense for other postretirement benefits included in the Statement of Income are as follows:

MILLIONS OF DOLLARS	1997	1996	1995
Service cost for benefits earned during the year	$ 13	$ 14	$ 10
Interest cost on the accumulated benefit obligation and other	96	84	90
Less expected return on assets	(43)	(38)	(30)
Net other postretirement benefits expense	$ 66	$ 60	$ 70
Actual return on assets	$102	$ 46	$ 65

The funded status of other postretirement benefits as of October 31 is as follows:

MILLIONS OF DOLLARS	1997	1996
ACCUMULATED OTHER POSTRETIREMENT BENEFIT OBLIGATION (APBO):		
Retirees and their dependents	$ (952)	$ (773)
Active employees eligible to retire	(221)	(244)
Other active participants	(201)	(208)
Total APBO	(1,374)	(1,225)
Plan assets at fair value	486	401
APBO in excess of plan assets	(888)	(824)
Unamortized prior service cost	(5)	(6)
Unrecognized net loss	152	86
Net liability	$ (741)	$ (744)

The weighted average expected return on plan assets was 11.1% for 1997, 10.5% for 1996 and 10% for 1995. The weighted average of discount rates used to determine the accumulated other postretirement benefit obligation was 7.4% and 8.2% at October 31, 1997 and 1996, respectively. For 1998, the weighted average rate of increase in the per capita cost of covered health care benefits is projected to be 8.2%. The rate is projected to decrease to 5.0% by the year 2004 and remain at that level each year thereafter. If the cost trend rate assumptions were increased by one percentage point for each year, the accumulated postretirement benefit obligation would increase by approximately $167 million and the associated expense recognized for the year ended October 31, 1997 would increase by an estimated $16 million.

3 INCOME TAXES

The domestic and foreign components of income (loss) before income taxes consist of the following:

MILLIONS OF DOLLARS	1997	1996	1995
Domestic	$ 239	$ 108	$ 251
Foreign	3	(3)	11
Total income before income taxes	$ 242	$ 105	$ 262

The components of income tax expense consist of the following:

MILLIONS OF DOLLARS	1997	1996	1995
CURRENT:			
Federal	$ 8	$ 1	$ 7
State and local	2	2	2
Total current expense	10	3	9
DEFERRED:			
Federal	71	32	77
State and local	11	5	12
Total deferred expense	82	37	89
Total income tax expense	$92	$40	$98

The deferred tax expense does not represent cash payment of income taxes and was primarily generated by the utilization of net operating loss (NOL) carryforwards and the increase of temporary differences, and will not require future cash payments. Consolidated tax payments made during 1997, 1996 and 1995 were $10 million, $3 million and $9 million, respectively.

The relationship of the tax expense to income before taxes for 1997, 1996 and 1995 differs from the U.S. statutory rate (35%) because of state income taxes and the benefit of NOLs in foreign countries. The effective tax rates for the years 1997, 1996 and 1995 were 38.0%, 38.1% and 37.4%, respectively.

Undistributed earnings of foreign subsidiaries were $35 million and $30 million at October 31, 1997 and 1996, respectively. Taxes have not been provided on these earnings because no withholding taxes are applicable upon repatriation and U.S. tax would be substantially offset by utilization of NOL carryforwards.

3 Income Taxes *(continued)*

Taxpaying entities of the company offset all deferred tax assets and liabilities within each tax jurisdiction and present them in a single amount in the Statement of Financial Condition. The components of the deferred tax asset (liability) at October 31 are as follows:

MILLIONS OF DOLLARS	1997	1996
United States		
DEFERRED TAX ASSETS:		
Net operating loss carryforwards	$ 680	$ 753
Alternative minimum tax	19	11
Product liability and warranty	97	100
Other liabilities	168	143
Postretirement benefits	353	363
Total deferred tax assets	1,317	1,370
DEFERRED TAX LIABILITIES:		
Prepaid pension assets	(58)	(12)
Depreciation	(37)	(40)
Total deferred tax liabilities	(95)	(52)
Total deferred tax asset	1,222	1,318
Less valuation allowance	(288)	(288)
Net deferred tax asset	$ 934	$1,030
Foreign		
DEFERRED TAX ASSETS:		
Net operating loss carryforwards	$ 2	$ 2
Postretirement benefits	19	19
Total deferred tax assets	21	21
Less valuation allowance	(21)	(21)
Net deferred tax assets	—	—
Deferred tax liabilities— prepaid pension assets	(16)	(16)
Net deferred tax liabilities	$ (16)	$ (16)

A valuation allowance has been provided for those NOL carryforwards and temporary differences which are estimated to expire before they are utilized. Because the foreign tax carryforward period is relatively short, an allowance has been provided against the total deferred tax assets.

At October 31, 1997, the company had $1,802 million of domestic and $6 million of foreign NOL carryforwards available to offset future taxable income. Such carryforwards reflect income tax losses incurred which will expire as follows, in millions of dollars:

2000	$ 174
2001	143
2002	47
2004	238
2005	7
2006 through 2011	1,199
Total	$1,808

Additionally, the reversal of net temporary differences of $1,413 million as of October 31, 1997 will create net tax deductions which, if not utilized previously, will expire subsequent to 2011.

4 Marketable Securities

The fair value of marketable securities is estimated based on quoted market prices, when available. If a quoted price is not available, fair value is estimated using quoted market prices for similar financial instruments.

Information related to the company's marketable securities at October 31 is as follows:

	1997		1996	
MILLIONS OF DOLLARS	AMORTIZED COST	FAIR VALUE	AMORTIZED COST	FAIR VALUE
Corporate securities	$150	$150	$127	$126
U.S. government securities	88	89	152	152
Mortgage and asset-backed securities	86	86	94	94
Foreign government securities	10	10	5	5
Total debt securities	334	335	378	377
Equity securities	16	21	14	17
Total marketable securities	$350	$356	$392	$394

4 Marketable Securities *(continued)*

Contractual maturities of marketable debt securities at October 31 are as follows:

	1997		1996	
MILLIONS OF DOLLARS	AMORTIZED COST	FAIR VALUE	AMORTIZED COST	FAIR VALUE
Due in one year or less	$113	$114	$ 66	$ 66
Due after one year through five years	100	100	189	188
Due after five years through 10 years	25	25	23	23
Due after 10 years	10	10	6	6
	248	249	284	283
Mortgage and asset-backed securities	86	86	94	94
Total debt securities	$334	$335	$378	$377

Gross gains and losses realized on sales or maturities of marketable securities were not material for each of the two years. At October 31, 1997 and 1996, a domestic insurance subsidiary had $15 million and $17 million, respectively, of marketable securities which were on deposit with various state departments of insurance or otherwise not available. These securities are included in total marketable securities balances at October 31, 1997 and 1996.

5 Receivables

Receivables at October 31 are summarized by major classification as follows:

MILLIONS OF DOLLARS	1997	1996
Accounts receivable	$ 671	$ 560
Retail notes and lease financing	706	733
Wholesale notes	46	101
Amounts due from sales of receivables	233	264
Notes receivable	101	—
Other	29	28
Allowance for losses	(31)	(31)
Total receivables, net	$1,755	$1,655

NFC purchases the majority of the wholesale notes receivable and some retail notes and accounts receivable arising from Transportation's operations in the United States.

A portion of NFC's funding for retail and wholesale notes comes from sales of receivables by NFC to third parties with limited recourse. Proceeds from sales of retail notes receivable, net of underwriting costs, were $958 million in 1997, $982 million in 1996 and $727 million in 1995. Uncollected sold retail and wholesale receivable balances totaled $1,968 million and $1,866 million as of October 31, 1997 and 1996, respectively.

Contractual maturities of accounts receivable, retail notes and lease financing and wholesale notes, including unearned finance income, at October 31, 1997 were: 1998—$950 million, 1999—$195 million, 2000—$161 million, 2001—$131 million, 2002—$91 million, and 2003 and thereafter—$18 million. Unearned finance income totaled $123 million at October 31, 1997. Notes receivable are due upon demand from a limited partnership that invests in S&P 500 stock index arbitrage.

6 Inventories

Inventories at October 31 are as follows:

MILLIONS OF DOLLARS	1997	1996
Finished products	$212	$242
Work in process	106	97
Raw materials and supplies	165	124
Total inventories	$483	$463

7 Property and Equipment

At October 31, property and equipment includes the following:

MILLIONS OF DOLLARS	1997	1996
Land	$ 18	$ 12
BUILDINGS, MACHINERY AND EQUIPMENT AT COST:		
Plants	1,200	1,241
Distribution	86	79
Construction in progress	117	58
Other	261	222
Subtotal	1,664	1,600
Total property	1,682	1,612
Less accumulated depreciation and amortization	(847)	(842)
Total property and equipment, net	$ 835	$ 770

Total property includes property under capitalized lease obligations of $25 million at October 31, 1997 and 1996. In addition, other property includes vehicles under operating leases to third parties of $150 million at October 31, 1997 and $116 million at October 31, 1996.

8 DEBT

MILLIONS OF DOLLARS	1997	1996
MANUFACTURING OPERATIONS		
Notes payable and current maturities of long-term debt	$ 13	$ 14
9% Sinking Fund Debentures, due 2004	45	53
8% Secured Note, due 2002, secured by plant assets	21	26
Capitalized leases and other	13	22
Total long-term debt	79	101
Manufacturing operations debt	92	115
FINANCIAL SERVICES OPERATIONS		
Commercial paper	141	99
Capitalized leases	13	—
Total short-term debt	154	99
Asset-backed commercial paper program, variable rate, due 2001	400	402
Bank revolver, variable rate, due 2001	393	704
Total senior debt	793	1,106
8⅞% Subordinated Senior Notes due 1998	94	100
9% Subordinated Senior Notes due 2002	100	—
Total subordinated term debt	194	100
Capitalized leases, 5.2% to 5.6%, due 2002	83	—
Total long-term debt	1,070	1,206
Financial services operations debt	1,224	1,305
Total debt	$1,316	$1,420

The effective annual interest rate on Manufacturing notes payable was 8.3% in 1997 and 8.9% in 1996. Consolidated interest payments were $66 million, $83 million and $82 million in 1997, 1996 and 1995, respectively.

NFC issues commercial paper with varying terms and has short-term borrowings with various banks on a noncommitted basis. Compensating cash balances and commitment

The aggregate annual maturities and sinking fund requirements for debt for the years ended October 31 are as follows:

MILLIONS OF DOLLARS	MANUFACTURING OPERATIONS	FINANCIAL SERVICES OPERATIONS	TOTAL
1998	$ 13	$ 154	$ 167
1999	15	111	126
2000	15	25	40
2001	15	820	835
2002	14	114	128
Thereafter	20	—	20
WEIGHTED AVERAGE INTEREST RATE ON TOTAL DEBT, INCLUDING SHORT-TERM, AND THE EFFECT OF DISCOUNTS AND RELATED AMORTIZATION FOR THE YEARS ENDED:			
October 31, 1997	10.3%	6.4%	6.8%
October 31, 1996	9.7%	6.5%	6.8%

At October 31, 1997, NFC has a $925 million contractually committed bank revolving credit facility and a $400 million asset-backed commercial paper (ABCP) program supported by a bank liquidity facility. Available funding under the ABCP program is comprised of a $400 million liquidity facility plus $14 million of trust certificates issued in connection with the formation of the ABCP trust.

Available funding under the amended and restated credit facility and the ABCP program was $546 million, of which $141 million provided funding backup for the outstanding short-term debt at October 31, 1997. The remaining $405 million when combined with unrestricted cash and cash equivalents made $416 million available to fund the general business purposes of NFC at October 31, 1997.

NFC's wholly owned subsidiaries, Navistar Financial Retail Receivables Corporation (NFRRC) and Navistar Financial Securities Corporation (NFSC), have a limited purpose of purchasing retail and wholesale receivables, respectively, and transferring an undivided ownership interest in such notes to investors in exchange for pass-through notes and certificates. The subsidiaries have limited recourse on the sold receivables and their assets are available to satisfy the claims of their creditors prior to such assets becoming available to NFC or affiliated companies.

NFSC has in place a $600 million revolving wholesale note trust that provides for the continuous sale of eligible wholesale notes on a daily basis. The trust is comprised of two $100 million tranches of investor certificates maturing in 1998 and 1999 and two $200 million tranches maturing in 2003. At October 31, 1997, the remaining shelf registration available to NFSC for issuance of investor certificates was $200 million.

8 DEBT *(continued)*

During 1997, NFC sold $987 million of retail notes, net of unearned finance income, through NFRRC to two individual owner trusts. The owner trusts in turn sold notes and certificates to investors. The net proceeds, after underwriting costs and credit enhancements, were used by NFC for general working capital purposes. At October 31, 1997, the remaining shelf registration available to NFRRC for issuance of asset-backed securities was $1,473 million.

In November 1997, NFC sold $500 million of retail notes, net of unearned finance income, through NFRRC. The net proceeds were used for general working capital purposes.

During 1997, NFC entered into sale/leaseback agreements involving vehicles that were already subject to retail finance and operating leases with end users. The remaining balance as of October 31, 1997 is classified under Financial Services operations as capitalized leases. These agreements grant a security interest in the underlying vehicles and lease receivables to the purchasers.

During November 1997, the company arranged financing for $125 million of funds denominated in U.S. dollars and Mexican pesos to be used for development of the company's Mexican operations.

9 OTHER LIABILITIES

Major classifications of other liabilities at October 31 are as follows:

MILLIONS OF DOLLARS	1997	1996
Product liability and warranty	$285	$293
Loss reserves and unearned premiums	99	113
Employee incentive programs	93	10
Payroll, commissions and employee related benefits	83	73
Long-term disability and workers' compensation	54	55
Taxes	59	44
Environmental	27	23
Interest	13	9
Other	181	199
Total other liabilities	$894	$819

During the fourth quarter of 1996, the company recorded a one-time $35 million pretax charge for costs related to the termination of its next generation truck program. In August 1997, the company and the United Auto Workers reached agreement on a master contract extension that enabled the company to reinstate its next generation truck program. The remaining accrual at the time of the announcement was not material.

10 FINANCIAL INSTRUMENTS

Fair Value of Financial Instruments

The carrying amounts of financial instruments, as reported in the Statement of Financial Condition and described in various Notes to the Financial Statements, and their fair values at October 31 are as follows:

	1997		1996	
MILLIONS OF DOLLARS	CARRYING AMOUNT	FAIR VALUE	CARRYING AMOUNT	FAIR VALUE
Receivables, net	$1,755	$1,764	$1,655	$1,658
Investments and other assets	332	343	213	221
Debt	1,316	1,321	1,420	1,414

Cash and cash equivalents approximate fair value. The cost and fair value of marketable securities are disclosed in Note 4.

Customer receivables, wholesale notes, retail and wholesale accounts, notes receivable, and other variable-rate retail notes approximate fair value as a result of the short-term maturities of the financial instruments. The fair value of truck retail notes is estimated based on quoted market prices of similar sold receivables. The fair value of amounts due from sales of receivables is estimated by discounting expected cash flows at estimated current market rates.

The fair value of investments and other assets is estimated based on quoted market prices or by discounting future cash flows.

The short-term debt and variable-rate borrowings under NFC's bank revolving credit agreement, which is repriced frequently, approximate fair value. The fair value of long-term debt is estimated based on quoted market prices, when available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar financial instruments or discounting future cash flows.

Derivatives Held or Issued for Purposes Other Than Trading

The company uses derivatives to transfer or reduce risks of foreign exchange and interest rate volatility and to potentially increase the return on invested funds.

NFC manages its exposure to fluctuations in interest rates by limiting the amount of fixed rate assets funded with variable rate debt, by selling fixed rate retail receivables on a fixed rate basis and, to a lesser extent, by utilizing derivative financial instruments. These instruments may include interest rate swaps, interest rate caps and forward interest rate contracts. NFC manages exposure to counter-party credit risk by entering into derivative financial instruments with major financial institutions that can be expected to fully perform under the terms of such agreements. Notional amounts are used to measure the volume of derivative financial instruments and do not represent exposure to credit loss.

NFC enters into forward interest rate contracts to manage its exposure to fluctuations in the fair value and resulting funding costs from the anticipated securitization and sale of retail notes.

10 FINANCIAL INSTRUMENTS *(continued)*

NFC manages interest rate risk by entering into either forward contracts to sell fixed debt securities or interest rate swaps whose fair values are highly correlated with the fair value of NFC's receivables. Gains or losses incurred with the closing of these agreements are included as a component of the gain or loss on sale of receivables.

During 1997, NFC entered into $500 million of interest rate hedge agreements in anticipation of the November 1997 sale of retail receivables. These hedge agreements were closed in conjunction with the pricing of the sale, and the loss at October 31, 1997, which was not material, was deferred and reduced the gain recognized on the sale of receivables in November 1997.

11 COMMITMENTS, CONTINGENCIES, RESTRICTED ASSETS, CONCENTRATIONS AND LEASES

Commitments, Contingencies and Restricted Assets

At October 31, 1997, commitments for capital expenditures in progress were approximately $137 million.

NFC's maximum exposure under all receivable sale recourse provisions at October 31, 1997 was $246 million; however, management believes that the allowance for credit losses on sold receivables is adequate.

At October 31, 1997, the Canadian operating subsidiary was contingently liable for retail customers' contracts and leases financed by a third party. The company is subject to maximum recourse of $261 million on retail contracts and $13 million on retail leases. In addition, as of October 31, 1997, the company is contingently liable for approximately $49 million for various guarantees and buyback programs; however, based on historical loss trends, the company's exposure is not considered material.

The Canadian operating subsidiary, NFC and certain other subsidiaries included in financial services operations are parties to agreements that may result in the restriction of amounts which can be distributed to Transportation in the form of dividends or loans and advances. At October 31, 1997, the maximum amount of dividends which were available for distribution under the most restrictive covenants was $62 million.

The company and Transportation are obligated under certain agreements with public and private lenders of NFC to maintain the subsidiary's income before interest expense and income taxes at not less than 125% of its total interest expense. No income maintenance payments were required for the three years ended October 31, 1997.

Concentrations

At October 31, 1997, the company employed 10,593 hourly workers and 5,434 salaried workers in the United States and Canada. Approximately 93% of the hourly employees and 23% of the salaried employees are represented by unions. Of these represented employees, 91% of the hourly workers and 94% of the salaried workers are represented by the United Automobile, Aerospace, and Agricultural Implement Workers of America (UAW) or the National Automobile, Aerospace, and Agricultural Implement Workers of Canada (CAW). During August 1997, the company's current master contract with the UAW was extended from October 1, 1998 to October 1, 2002. The collective bargaining agreement with the CAW expires on October 24, 1999.

Reflecting higher consumer demand for light trucks and vans, sales of mid-range diesel engines to Ford Motor Company were 14% of consolidated sales and revenues in 1997 and 1996 and 12% in 1995. During 1997, the company entered into a ten-year agreement, effective with model year 2003, to continue supplying Ford Motor Company with diesel engines for use in its diesel-powered light trucks and vans.

Leases

The company has long-term noncancellable leases for use of various equipment and facilities. Lease terms are generally for five to 25 years and, in many cases, provide for renewal options. The company is generally obligated for the cost of property taxes, insurance and maintenance. The company leases office buildings, distribution centers, furniture and equipment, machinery and equipment, and computer equipment.

The majority of the company's lease payments are for operating leases. At October 31, 1997, future minimum lease payments under operating leases having lease terms in excess of one year are: 1998—$36 million, 1999—$34 million, 2000—$33 million, 2001—$20 million, 2002—$15 million and thereafter—$42 million. Total operating lease expense was $40 million in 1997, $35 million in 1996 and $42 million in 1995. Income received from sublease rentals was $6 million in 1997, 1996 and 1995, respectively.

12 LEGAL PROCEEDINGS

The company and its subsidiaries are subject to various claims arising in the ordinary course of business, and are parties to various legal proceedings which constitute ordinary routine litigation incidental to the business of the company and its subsidiaries. In the opinion of the company's management, none of these proceedings or claims is material to the business or the financial condition of the company.

13 ENVIRONMENTAL MATTERS

In the fourth quarter of 1994, Transportation recorded a $20 million charge, net of $13 million of income taxes, as a loss of discontinued operations related to environmental liabilities at production facilities of two formerly owned businesses, Wisconsin Steel and Solar Turbine, Inc. Included in the charge was an anticipated $11 million payment to the Economic Development Administration, a division of the U.S. Department of Commerce, in settlement of commercial and environmental disputes related to the Wisconsin Steel property. In 1997, the U.S. Department of Justice and Transportation approved the final consent decree related to the Wisconsin Steel property and the company paid the $11 million to the Economic Development Administration.

13 ENVIRONMENTAL MATTERS *(continued)*

The company has been named a potentially responsible party (PRP), in conjunction with other parties, in a number of cases arising under an environmental protection law known as the Superfund law. These cases involve sites which allegedly have received wastes from current or former company locations. Based on information available to the company, which in most cases consists of data related to quantities and characteristics of material generated at or shipped to each site as well as cost estimates from PRPs and/or federal or state regulatory agencies for the cleanup of these sites, a reasonable estimate is calculated of the company's share, if any, of the probable costs and is provided for in the financial statements. These obligations generally are recognized no later than completion of the remedial feasibility study and are not discounted to their present value. The company reviews its accruals on a regular basis and believes that, based on these calculations, its share of the potential additional costs for the cleanup of each site will not have a material effect on the company's financial results.

14 INDUSTRY SEGMENT DATA

Information concerning operations by industry segment is as follows:

MILLIONS OF DOLLARS	MANUFACTURING OPERATIONS	FINANCIAL SERVICES OPERATIONS	CONSOLIDATED
OCTOBER 31, 1997			
Total sales and revenues	$6,191	$239	$6,371
Operating profit	873	101	924
Depreciation and amortization	97	23	120
Capital expenditures	172	—	172
Identifiable assets	4,111	1,857	5,516
OCTOBER 31, 1996			
Total sales and revenues	$5,550	$258	$5,754
Operating profit	690	109	755
Depreciation and amortization	90	15	105
Capital expenditures	117	—	117
Identifiable assets	3,815	1,843	5,326
OCTOBER 31, 1995			
Total sales and revenues	$6,168	$235	$6,342
Operating profit	845	80	870
Depreciation and amortization	75	11	86
Capital expenditures	139	—	139
Identifiable assets	4,018	1,922	5,566

Intersegment sales and revenues were not material in 1997, 1996 or 1995. Transactions between manufacturing operations and financial services operations have been eliminated from the consolidated column.

15 PREFERRED AND PREFERENCE STOCKS

The company's Nonconvertible Junior Preference Stock Series A is held for the Retiree Supplemental Benefit Program by the Supplemental Trust which is currently entitled to elect two members to the company's Board of Directors. The UAW holds the Nonconvertible Junior Preference Stock Series B and is currently entitled to elect one member of the company's Board of Directors. At October 31, 1997, there was one share each of Series A and Series B Preference stock authorized and outstanding. The value of the preference shares is minimal.

Other information pertaining to preferred and preference stocks outstanding is summarized as follows:

	SERIES G CONVERTIBLE CUMULATIVE PREFERRED	SERIES D CONVERTIBLE JUNIOR PREFERENCE
Number authorized and issued	4,800,000	3,000,000
Number outstanding	4,800,000	175,000
Optional redemption price and liquidation preference	$50 per share plus accrued dividends	$25 per share plus accrued dividends
Conversion rate per share into Common Stock (subject to adjustment in certain circumstances)	0.133 shares	0.3125 shares
Ranking as to dividends and upon liquidation	Senior to all other equity securities	Senior to Common; junior to Series G
Dividend rate	Annual rate of $6.00 per share, payable quarterly	120% of the cash dividends on Common Stock as declared on a common equivalent basis.

Dividends may be paid out of surplus as defined under Delaware corporation law. At October 31, 1997, the company had such defined surplus of $1,007 million.

16 COMMON SHAREOWNERS' EQUITY

Changes in the common shareowners' equity accounts are as follows:

MILLIONS OF DOLLARS	1997	1996	1995
COMMON STOCK			
Beginning of year	$ 1,642	$ 1,641	$ 1,628
Conversion of Class B Common Stock and other	17	1	13
End of year	$ 1,659	$ 1,642	$ 1,641
CLASS B COMMON STOCK			
Beginning of year	$ 491	$ 491	$ 501
Repurchase of stock	(20)	—	(10)
End of year	$ 471	$ 491	$ 491
RETAINED EARNINGS (DEFICIT)			
Beginning of year	$(1,431)	$(1,478)	$(1,538)
Net income	150	65	164
Preferred dividends	(29)	(29)	(22)
Minimum pension liability adjustments and other	9	11	(82)
End of year	$(1,301)	$(1,431)	$(1,478)
COMMON STOCK HELD IN TREASURY			
Beginning of year	$ (30)	$ (28)	$ (18)
Repurchase of Common Stock and other	(23)	(2)	(10)
End of year	$ (53)	$ (30)	$ (28)

Common Stock

The company has authorized 110 million shares of Common Stock with a par value of $.10 per share and 26 million shares of Class B Common Stock with a par value of $.10 per share and restricted voting rights and transfer provisions. At October 31, 1997 and 1996, there were 49.3 million and 49.4 million shares of Common Stock outstanding, net of Common Stock held in Treasury, respectively. The number of shares of Class B Common Stock outstanding at October 31, 1997 and 1996 was 23.1 million and 24.3 million, respectively. The remaining Class B Common Stock will convert into Common Stock on July 1, 1998.

17 STOCK COMPENSATION PLANS

The company has stock-based compensation plans, approved by the Committee on Organization of the Board of Directors, which provide for granting of stock options to employees for purchase of Common Stock at the fair market value of the stock on the date of grant. The grants are generally exercisable after one year and generally have a ten-year life.

The company has elected to continue to account for stock option grants in accordance with Accounting Principles Board Opinion No. 25 and related Interpretations. Accordingly, no compensation cost has been recognized for fixed stock options because the exercise prices of the stock options equal the market value of the company's Common Stock at the date of grant. Had compensation cost for the plans been determined based upon the fair value at the grant date consistent with SFAS 123, pro forma net income would have been $147 million in 1997 and $63 million in 1996 and pro forma earnings per share would have been $1.61 in 1997 and $0.46 in 1996. The pro forma effect on net income for 1997 and 1996 may not be representative of the pro forma effect on net income of future years because it does not take into consideration pro forma compensation expense relating to grants made prior to November 1, 1995.

The weighted-average fair values at date of grant for options granted during 1997 and 1996 were $5.71 and $5.34, respectively, and were estimated using the Black-Scholes option-pricing model with the following assumptions:

	1997	1996
Risk-free interest rate	6.6%	6.1%
Dividend yield	0%	0%
Expected volatility	29.8%	30.9%
Expected life in years	10	10

17 STOCK COMPENSATION PLANS *(continued)*

The following summarizes stock option activity for the years ended October 31:

SHARES IN THOUSANDS	1997 SHARES	1997 WEIGHTED AVERAGE EXERCISE PRICE	1996 SHARES	1996 WEIGHTED AVERAGE EXERCISE PRICE	1995 SHARES	1995 WEIGHTED AVERAGE EXERCISE PRICE
Options outstanding at beginning of period	2,346	$20.34	1,762	$24.25	1,163	$30.08
Granted	876	10.13	718	10.45	642	13.58
Exercised	(715)	12.45	—	—	—	—
Canceled	(77)	28.52	(134)	18.75	(43)	22.46
Options outstanding at year end	2,430	$18.73	2,346	$20.34	1,762	$24.25
Options exercisable at year end	1,579	$23.35	1,682	$24.25	1,140	$30.07
Options available for grant at year end	—		—		—	

The following table summarizes information about stock options outstanding and exercisable at October 31, 1997.

	OUTSTANDING OPTIONS			OPTIONS EXERCISABLE	
RANGE OF EXERCISE PRICES	NUMBER OUTSTANDING (IN THOUSANDS)	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED AVERAGE EXERCISE PRICE	NUMBER EXERCISABLE (IN THOUSANDS)	WEIGHTED AVERAGE EXERCISE PRICE
$ 9.31–$13.75	1,448	8.5	$10.70	649	$12.11
17.40– 25.63	686	6.5	23.52	642	23.93
27.96– 37.50	113	5.5	36.78	105	37.43
43.75– 61.88	156	3.5	49.49	156	49.49
68.12– 91.25	27	1.1	73.09	27	73.09

18 SELECTED QUARTERLY FINANCIAL DATA *(Unaudited)*

(MILLIONS OF DOLLARS, EXCEPT PER SHARE DATA)	1ST QUARTER 1997	1ST QUARTER 1996	2ND QUARTER 1997	2ND QUARTER 1996	3RD QUARTER 1997	3RD QUARTER 1996	4TH QUARTER 1997	4TH QUARTER 1996
Sales and revenues	$1,296	$1,432	$1,551	$1,480	$1,586	$1,391	$1,938	$1,451
Manufacturing gross margin	13.6%	12.2%	13.8%	13.7%	13.8%	12.6%	15.2%	11.6%
Net income	$ 15	$ 22	$ 30	$ 26	$ 35	$ 17	$ 70	$ —
Net income (loss) per common share	$ .10	$ .20	$ .31	$ .26	$ .38	$ .13	$ .85	$ (.10)
Market price range—Common Stock								
High	$ 10⅜	$ 12⅛	$ 11⅜	$ 12	$ 21 5/16	$ 12	$ 29½	$ 10⅜
Low	$ 9	$ 9½	$ 9⅛	$ 9½	$ 11¼	$ 9⅛	$ 17¼	$ 8½

Net income per common share is computed independently based on the weighted average number of Common and Class B Common shares at the end of each quarter.

19 SUPPLEMENTAL FINANCIAL INFORMATION AS OF OCTOBER 31 AND FOR THE YEARS THEN ENDED *(Unaudited)*

Navistar International Corporation (with financial services operations on an equity basis) in millions of dollars:

CONDENSED STATEMENT OF INCOME	1997	1996	1995
Sales of manufactured products	$6,147	$5,508	$6,125
Other income	44	42	43
Total sales and revenues	6,191	5,550	6,168
Cost of products sold	5,274	4,818	5,280
Postretirement benefits	214	219	205
Engineering and research expense	124	129	113
Marketing and administrative expense	332	282	277
Other expenses	83	80	93
Total costs and expenses	6,027	5,528	5,968
INCOME BEFORE INCOME TAXES			
Manufacturing operations	164	22	200
Financial services operations	78	83	62
Income before income taxes	242	105	262
Income tax expense	92	40	98
Net income	$ 150	$ 65	$ 164

CONDENSED STATEMENT OF FINANCIAL CONDITION	1997	1996
Cash, cash equivalents and marketable securities	$ 802	$ 707
Inventories	483	463
Property and equipment, net	706	666
Equity in nonconsolidated subsidiaries	322	306
Other assets	864	643
Deferred tax asset, net	934	1,030
Total assets	$4,111	$3,815
Accounts payable	$1,060	$ 771
Postretirement benefits liabilities	1,178	1,344
Other liabilities	853	784
Shareowners' equity	1,020	916
Total liabilities and shareowners' equity	$4,111	$3,815

CONDENSED STATEMENT OF CASH FLOW	1997	1996	1995
Cash flow from operations			
Net income	$ 150	$ 65	$ 164
ADJUSTMENTS TO RECONCILE NET INCOME TO CASH PROVIDED BY OPERATIONS:			
Depreciation and amortization	97	90	75
Equity in earnings of nonconsolidated companies, net of dividends received	(8)	(24)	(28)
Deferred income taxes	82	37	89
Other, net	(26)	4	(66)
Change in operating assets and liabilities	143	(172)	166
Cash provided by operations	438	—	400
Cash flow from investment programs			
Purchase of marketable securities	(428)	(501)	(646)
Sales or maturities of marketable securities	454	665	399
Capital expenditures	(172)	(117)	(139)
Loan to NFC	(99)	—	—
Other investment programs, net	4	(8)	8
Cash (used in) provided by investment programs	(241)	39	(378)
Cash flow from financing activities	(76)	(48)	(60)
Cash and cash equivalents			
Increase (decrease) during the year	121	(9)	(38)
At beginning of the year	452	461	499
Cash and cash equivalents at end of the year	$ 573	$ 452	$ 461

For the Years Ended October 31

(MILLIONS OF DOLLARS, EXCEPT PER SHARE DATA, MARKET SHARE, AND UNITS SHIPPED)

	1997	1996	1995	1994	1993
RESULTS OF OPERATIONS					
Total sales and revenues	$6,371	$5,754	$6,342	$5,337	$4,721
Income (loss) of continuing operations	150	65	164	102	(273)
Net income (loss) (a)	150	65	164	82	(501)
Income (loss) per common share of continuing operations	1.65	.49	1.83	.99	(8.63)
Net income (loss) per common share	1.65	.49	1.83	.72	(15.19)
Average number of Common, Class B Common and dilutive common equivalent shares outstanding (millions)	73.6	73.8	74.3	74.6	34.9
FINANCIAL DATA					
Total assets	$5,516	$5,326	$5,566	$5,047	$5,060
DEBT					
Manufacturing operations	92	115	127	127	175
Financial services operations	1,224	1,305	1,330	1,091	1,199
Total debt	1,316	1,420	1,457	1,218	1,374
Shareowners' equity	1,020	916	870	817	775
Total manufacturing operations debt as a percent of total manufacturing capitalization	8.3%	11.2%	12.7%	13.4%	18.4%
Return on equity (b)	14.7%	7.1%	18.9%	12.5%	(35.2)%
SUPPLEMENTAL DATA					
Capital expenditures	$ 172	$ 117	$ 139	$ 87	$ 110
Engineering and research expense	124	129	113	97	94
OPERATING DATA					
United States and Canadian market share (c)	28.6%	27.5%	26.7%	27.0%	27.6%
UNIT SHIPMENTS					
Trucks	104,400	95,200	112,200	95,000	87,200
OEM engines	184,000	163,200	154,200	130,600	118,200
Service parts sales	$ 806	$ 760	$ 730	$ 714	$ 632

(a) In the third quarter of 1993, the company adopted SFAS 106 and SFAS 109 retroactive to November 1, 1992.

(b) Return on equity is calculated based on income of continuing operations.

(c) Based on retail deliveries of medium trucks (Classes 5, 6 and 7), including school buses, and heavy trucks (Class 8).

ABOUT YOUR STOCK

Navistar International Corporation Common Stock is listed on the New York, Chicago and Pacific Stock Exchanges and is quoted as "Navistar" in stock table listings in daily newspapers. The abbreviated stock symbol is "NAV."

The stock transfer agent who can answer inquiries about your Navistar International Corporation Common Stock such as name changes, changes of address or missing certificates is: Harris Trust and Savings Bank, 311 West Monroe Street, 11th Floor, Chicago, Illinois 60606; Telephone: (312) 360-5101.

For information about other shareowner matters, contact: Investor Relations, Navistar International Corporation, 455 North Cityfront Plaza Drive, Chicago, Illinois 60611; Telephone: (312) 836-2143.

There were approximately 57,949 owners of Common Stock at October 31, 1997.

ANNUAL MEETING

The 1998 Annual Meeting of Shareowners is scheduled to take place at 10:15 a.m., CST on March 24, 1998, at the Art Institute of Chicago in the Arthur Rubloff Auditorium.

Shareowners are invited to attend this meeting, take part in discussions of company affairs and meet personally with the directors and officers responsible for the operations of Navistar.

A Proxy Statement and Form of Proxy will be mailed to each shareowner on or about February 2, 1998.

COMMITMENT TO EQUAL EMPLOYMENT OPPORTUNITY

Navistar International Corporation has a long-standing commitment to equal employment opportunity dating back to 1919 when the company issued its first written statement against discrimination in the workplace.

Today, Navistar continues to be a leader in the industry in complying with all state and federal laws, local municipal laws and regulations governing employment. Navistar has continuously and aggressively implemented measures to ensure that all individuals regardless of age, race, sex, religion, national origin, disability, or veteran status are not discriminated against in regard to career opportunities within the company.

Navistar has adopted policy standards and assurances for all employees and qualified applicants, pledging terms and conditions of employment to be equal for all individuals.

CORPORATE HEADQUARTERS

The corporate offices of Navistar International Corporation and its principal subsidiary, Navistar International Transportation Corp., are located at 455 North Cityfront Plaza Drive, Chicago, Illinois 60611; Telephone: (312) 836-2000.

REPORTS AND PUBLICATIONS

A copy of the company's 1997 Annual Report on Form 10-K to the Securities and Exchange Commission will be provided, without charge, to shareowners upon written request to the Corporate Secretary, Corporate Headquarters, after January 31, 1998.

In order to provide shareowners with immediate access to financial information and news about the company, Navistar distributes its corporate news releases through PR Newswire, an electronic news service, and files its financial statements with the Securities and Exchange Commission electronically through the EDGAR system. PR Newswire and EDGAR can be accessed by computer via the Internet, and through such services as America On-Line and CompuServe. In addition, this information can be accessed through such databases and information services as Lexis/Nexus, Dow Jones and Bloomberg which frequently are available at libraries and brokerage firms.

Navistar also offers a toll-free, "Company News on Call" service, which allows shareowners to receive copies of recent Navistar corporate news releases via telefax. To access this service, call (800) 758-5804, and enter Navistar's six digit code when prompted: 103895. Using a touch-tone phone, shareowners can select from a menu of news releases and request specific news releases to be faxed directly to them.

Navistar encourages shareowners to take advantage of these electronic databases and the "Company News on Call" service to access the company's quarterly financial results on the same day that the results are announced. Navistar's 1998 quarterly financial results will be announced on the following dates:

FIRST QUARTER	February 12, 1998
SECOND QUARTER	May 14, 1998
THIRD QUARTER	August 13, 1998
FOURTH QUARTER	December 3, 1998

News releases, Form 10-Qs, Navistar's Annual Environmental Health & Safety Report, and other publications are available by writing: Corporate Communications, Navistar International Corporation, 455 North Cityfront Plaza Drive, Chicago, Illinois 60611.

Navistar also encourages shareowners to visit its home page on the World Wide Web at http://www.navistar.com.

TRADEMARKS

Navistar logotype and Navistar are registered trademarks of Navistar International Corporation. The Diamond Road symbol and International are registered trademarks of Navistar International Transportation Corp. Additional registered trademarks include Eagle, Fleet Charge, Fleetrite, Skyrise, Paystar and Pro Sleeper. Diamond SPEC, Diamond PLUS and Diamond Services are trademarks of Navistar International Transportation Corp.

Navistar International Corporation as of December 19, 1997

Board of Directors

JOHN R. HORNE
Chairman, President and Chief Executive Officer
Navistar International Corporation
Committees: 1 [Chair]

WILLIAM F. ANDREWS
Chairman
Schrader-Bridgeport International Inc.
Manufacturer of Tire Valves and Valve Accessories
Chairman
Scovill Fasteners, Inc.
Manufacturers of Apparel and Industrial Fasteners
Committees: 1, 2, 3 [Chair]

DR. ANDREW F. BRIMMER
President
Brimmer & Company, Inc.
Economic and Financial Consulting
Committees: 1, 3, 4 [Chair], 5

JOHN D. CORRENTI
Chief Executive Officer, President and Vice Chairman
Nucor Corporation
Steel Manufacturer
Committees: 2, 4

WILLIAM C. CRAIG
Former Executive Vice President
Mack Trucks
Manufacturer of Trucks
Committees: 1, 2, 3

JERRY E. DEMPSEY
Retired Chairman and Chief Executive Officer
PPG Industries, Inc.
Diversified Global Manufacturer of Glass, Protective Coatings and Chemicals
Committees: 1, 2 [Chair], 3

JOHN F. FIEDLER
Chairman, President and Chief Executive Officer
Borg-Warner Automotive, Inc.
Supplier of Engineered Components and Systems
Committees: 2, 5

MARY GARST
Manager, Cattle Division
Garst Company
Agri-Business Company
Committees: 1, 4, 5 [Chair]

JOHN T. GRIGSBY
President
John Grigsby & Associates, Inc.
Provider of Strategic and Operational Consulting to Financially Distressed Companies
Committees: 4, 5

MICHAEL N. HAMMES
Former Chairman and Chief Executive Officer
The Coleman Company, Inc.
Manufacturer and Distributor of Camping and Outdoor Recreational Products and Hardware/Home Products
Committees: 3, 5

ALLEN J. KROWE
Retired Vice Chairman
Texaco, Inc.
Global Energy Company
Committees: 3, 4

ROBERT C. LANNERT
Executive Vice President and Chief Financial Officer
Navistar International Corporation

WALTER J. LASKOWSKI
International Vice President of the UAW
Committees: 1, 3, 4

WILLIAM F. PATIENT
Chairman of the Board, President and Chief Executive Officer
The Geon Company
Manufacturer of Polyvinyl Chloride (PVC) Resins and Compounds
Committees: 2, 4

Principal Officers

JOHN R. HORNE
Chairman, President and Chief Executive Officer

DONALD DEFOSSET, JR.
Executive Vice President and President, Truck Group

ROBERT C. LANNERT
Executive Vice President and Chief Financial Officer

ROBERT A. BOARDMAN
Senior Vice President and General Counsel

THOMAS M. HOUGH
Vice President and Treasurer

J. STEVEN KEATE
Vice President and Controller

STEVEN K. COVEY
Corporate Secretary

Committees:
1 Executive
2 Organization
3 Finance
4 Audit
5 Public Policy

Navistar International Transportation Corp.

Principal Officers

JOHN R. HORNE
Chairman, President and Chief Executive Officer

DONALD DEFOSSET, JR.
Executive Vice President and President Truck Group

ROBERT C. LANNERT
Executive Vice President and Chief Financial Officer

Group Vice Presidents

JOHN J. BONGIORNO
General Manager
Financial Services

R. GARY DIAZ
Chief Technical Officer
Truck Group

DAVID J. JOHANNESON
Truck Businesses

JAMES T. O'DARE, JR.
Sales and Distribution

DANIEL C. USTIAN
General Manager
Engine and Foundry

DENNIS W. WEBB
International Operations

Senior Vice Presidents

ROBERT A. BOARDMAN
General Counsel

JOSEPH V. THOMPSON
Employee Relations and Administration

Vice Presidents

THOMAS M. HOUGH
Treasurer

J. STEVEN KEATE
Controller

JAMES L. SIMONTON
Purchasing and Supplier Development

BRIAN B. WHALEN
Public Affairs

Secretary

GREGORY LENNES

Company | PROFILE

Navistar International Corporation manufactures and markets medium and heavy trucks, school buses and mid-range diesel engines in North America and selected export markets. Navistar has led the U.S. and Canadian markets in combined sales of medium and heavy trucks and school buses for 17 consecutive years, and the company is the leading supplier of mid-range diesel engines in the 160 to 300 horsepower range.

The company's products, parts and services are sold through a network of 1,000 International® dealer outlets in the United States, Canada and Mexico, more than 80 dealers in 75 countries, eight parts distribution centers and 16 used truck centers. Navistar also provides financing for its customers and distributors principally through its wholly owned subsidiary, Navistar Financial Corporation.

Company | LOCATIONS

CORPORATE HEADQUARTERS
Chicago, Illinois

MANUFACTURING FACILITIES

American Transportation Corporation
SCHOOL BUS ASSEMBLY
Conway, Arkansas

Chatham Assembly Plant
HEAVY TRUCK ASSEMBLY
Chatham, Ontario

Indianapolis Casting Corporation
PRECISION GREY IRON CASTINGS
Indianapolis, Indiana

Indianapolis Engine Plant
MID-RANGE DIESEL ENGINES
Indianapolis, Indiana

Melrose Park Engine Plant
MID-RANGE DIESEL ENGINES
Melrose Park, Illinois

Mexico Assembly Operation
(A contract manufacturing agreement)
MEDIUM AND HEAVY TRUCK ASSEMBLY
Monterrey, Nuevo Leon

Mexico Assembly Operation
(Scheduled to be in operation mid-1998)
MEDIUM AND HEAVY TRUCK ASSEMBLY
Escobedo, Nuevo Leon

Springfield Assembly Plant
SCHOOL BUS, MEDIUM AND HEAVY TRUCK ASSEMBLY
Springfield, Ohio

Springfield Body Plant
FABRICATED TRUCK COMPONENTS
Springfield, Ohio

SST Truck Company
(A Navistar joint venture)
SEVERE SERVICE TRUCK ASSEMBLY
Garland, Texas

Waukesha Manufacturing Facility
DUCTILE IRON CASTINGS AND MACHINING
Waukesha, Wisconsin

ENGINEERING AND TECHNICAL CENTERS

TRUCK ENGINEERING
Fort Wayne, Indiana

ENGINE ENGINEERING
Melrose Park, Illinois

PURCHASING AND SUPPLIER DEVELOPMENT
Westchester, Illinois

PARTS OPERATIONS
Westchester, Illinois
Marshfield, Missouri
Shawnee Mission, Kansas

PARTS DISTRIBUTION CENTERS
Baltimore, Maryland
Burlington, Ontario
Cuautitlan, Mexico
Dallas, Texas
East Point, Georgia
Edmonton, Alberta
Richmond, California
West Chicago, Illinois

REGIONAL SALES OFFICES
Atlanta, Georgia
Dallas, Texas
Hamilton, Ontario
Mt. Laurel, New Jersey
Oakbrook Terrace, Illinois
San Ramon, California

EXPORT SALES OFFICES
Dubai, United Arab Emirates
Johannesburg, South Africa
Miami, Florida

USED TRUCK CENTERS
Baltimore, Maryland
Charlotte, North Carolina
Conley, Georgia
Dallas, Texas
Denver, Colorado
Etna, Ohio
Houston, Texas
Indianapolis, Indiana
Kansas City, Missouri
Liverpool, New York
Melrose Park, Illinois
Nashville, Tennessee
Oakland, California
Philadelphia, Pennsylvania
Tampa, Florida
Taylor, Michigan

NAVISTAR FINANCIAL CORPORATION
Rolling Meadows, Illinois

NAVISTAR INTERNATIONAL CORPORATION CANADA
Hamilton, Ontario

NAVISTAR INTERNATIONAL CORPORATION MEXICO, S.A. DE C.V.
Mexico City, D.F.

Our | DEALER NETWORK

With over 400 principal locations representing 1,000 retail outlets throughout North America, the International® truck dealer distribution network has long been recognized as one of Navistar's greatest competitive strengths.

Dealers have taken a leading role in implementing an industry-leading customer satisfaction process (CSP) to significantly enhance the value of Navistar's products and services in the marketplace. The success of this collaborative effort was recently rewarded by J.D. Power and Associates, recognizing Navistar in 1997 for achieving the highest medium truck service satisfaction rating.

EXECUTIVE MEMBERS OF THE INTERNATIONAL TRUCK DEALER COUNCIL

Pictured left to right: Bill Ward, Ward International Trucks; Blaine Roberts, Roberts Truck Center, Inc.; Ed Wise, Wise International Trucks, Inc.

Navistar International Corporation
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Chicago, Illinois 60611

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