CITIGROUP INC
Form 424B2
March 27, 2019

The information in this preliminary pricing supplement is not complete and may be changed. A registration statement relating to these securities has been filed with the Securities and Exchange Commission. This preliminary pricing supplement and the accompanying product supplement, prospectus supplement and prospectus are not an offer to sell these securities, nor are they soliciting an offer to buy these securities, in any state where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED MARCH 27, 2019

March----, 2019

Medium-Term Senior Notes, Series N

Citigroup Global Markets Holdings Inc. **Pricing Supplement No. 2019-USNCH2190**

Filed Pursuant to Rule 424(b)(2)

Registration Statement Nos. 333-224495 and 333-224495-03

Autocallable Equity Linked Securities Based on the Worst Performing of the Common Stock of Advanced Micro Devices, Inc. and the Common Stock of Electronic Arts Inc. Due October 2, 2019

The securities offered by this pricing supplement are unsecured senior debt securities issued by Citigroup Global Markets Holdings Inc. and guaranteed by Citigroup Inc. The securities offer a monthly coupon payment at a per annum rate that is generally higher than the rate we would pay on conventional debt securities of the same maturity. In exchange for this higher coupon, you must be willing to accept the risks that (i) the securities may be automatically redeemed prior to maturity in the circumstances described below and (ii) if the securities are not automatically redeemed prior to maturity and a downside event (as described below) occurs, what you receive at maturity will be worth significantly less than the stated principal amount of your securities, and possibly worth nothing. Each of these risks will depend on the performance of the **worst performing** of the shares of common stock of Advanced Micro Devices, Inc. and the shares of common stock of Electronic Arts Inc. (each, the "underlying shares"), as described below. You will be subject to risks associated with each of the underlying shares and will be negatively affected by adverse movements in any of the underlying shares regardless of the performance of any other underlying shares. Although you will be exposed to downside risk with respect to the worst performing underlying shares, you will not participate in any appreciation of the underlying shares or receive any dividends paid on the underlying shares.

Investors in the securities must be willing to accept (i) an investment that may have limited or no liquidity and (ii) the risk of not receiving any payments due under the securities if we and Citigroup Inc. default on our obligations. **All payments on the securities are subject to the credit risk of Citigroup Global Markets Holdings Inc. and Citigroup Inc.**

KEY TERMS

Issuer: Citigroup Global Markets Holdings Inc., a wholly owned subsidiary of Citigroup Inc.

Guarantee: All payments due on the securities are fully and unconditionally guaranteed by Citigroup Inc.

Underlying shares:

Underlying shares	Initial share price*	Downside threshold price**	Equity ratio***
Shares of common stock of Advanced Micro Devices, Inc.	$25.69	$19.268	38.92565
Shares of common stock of Electronic Arts Inc.	$102.32	$76.740	9.77326

* For each of the underlying shares, their closing price on the strike date

** For each of the underlying shares, 75% of their initial share price

*** For each of the underlying shares, the stated principal amount of $1,000 *divided by* their initial share price

Aggregate stated principal amount:	$
Stated principal amount:	$1,000 per security
Strike date:	March 26, 2019
Pricing date:	March 27, 2019
Issue date:	March 29, 2019
Valuation date:	September 27, 2019, subject to postponement if such date is not a scheduled trading day for any of the underlying shares or if certain market disruption events occur with respect to any of the underlying shares
Maturity date:	Unless earlier redeemed, October 2, 2019
Coupon payments:	1.9875% of the stated principal amount (approximately 23.85% per annum, or 11.925% for the term of the securities) paid on each monthly coupon payment date, subject to automatic early redemption
Coupon payment dates:	May 6, 2019, June 4, 2019, July 5, 2019, August 5, 2019, September 4, 2019 and the maturity date
Payment at maturity:	If the securities have not been earlier redeemed, for each $1,000 stated principal amount security you hold at maturity, you will be entitled to receive the final coupon payment *plus:* If a downside event occurs: a fixed number of the worst performing underlying shares on the valuation date equal to the applicable equity ratio (or, if we exercise our cash election right, the cash value of those shares based on their final share price) If a downside event does not occur: $1,000 **If the securities have not been automatically redeemed prior to maturity and a downside event occurs, you will receive a number of the worst performing underlying shares (or, in our sole discretion, cash) worth less than 75% of the stated principal amount of your securities, and possibly nothing, at maturity. You should not invest in the securities unless you are willing and able to bear the risk of losing a significant portion, and up to all, of your investment. The number of full underlying shares and any cash in lieu of a fractional underlying share that you receive at maturity will be calculated based on the aggregate number of securities you then hold.**
Downside event:	A downside event will occur if the final share price of the worst performing underlying shares on the valuation date is less than their downside threshold price.
Final share price:	For each of the underlying shares, their closing price on the valuation date
Worst performing underlying shares:	For any date, the underlying shares with the lowest underlying return on that date
Listing:	The securities will not be listed on any securities exchange
Underwriter:	Citigroup Global Markets Inc. (“CGMI”), an affiliate of the issuer, acting as principal

Underwriting fee and issue price:	**Issue price(1)(2)**	**Underwriting fee(3)**	**Proceeds to issuer(4)**
Per security:	$1,000	$25	$975

Total:	$	$	$

(Key Terms continued on next page)

(1) Citigroup Global Markets Holdings Inc. currently expects that the estimated value of the securities on the pricing date will be at least $933.50 per security, which will be less than the issue price. The estimated value of the securities is based on CGMI's proprietary pricing models and our internal funding rate. It is not an indication of actual profit to CGMI or other of our affiliates, nor is it an indication of the price, if any, at which CGMI or any other person may be willing to buy the securities from you at any time after issuance. See "Valuation of the Securities" in this pricing supplement.

(2) The issue price for investors purchasing the securities in fee-based advisory accounts will be $975 per security, assuming no custodial fee is charged by a selected dealer, and up to $980 per security, assuming the maximum custodial fee is charged by a selected dealer. See "Supplemental Plan of Distribution" in this pricing supplement.

(3) CGMI will receive an underwriting fee of up to $25 for each security sold in this offering. The total underwriting fee and proceeds to issuer in the table above give effect to the actual total underwriting fee. For more information on the distribution of the securities, see "Supplemental Plan of Distribution" in this pricing supplement. In addition to the underwriting fee, CGMI and its affiliates may profit from expected hedging activity related to this offering, even if the value of the securities declines. See "Use of Proceeds and Hedging" in the accompanying prospectus.

(4) The per security proceeds to issuer indicated above represent the minimum per security proceeds to issuer for any security, assuming the maximum per security underwriting fee. As noted above, the underwriting fee is variable.

Investing in the securities involves risks not associated with an investment in conventional debt securities. See "Summary Risk Factors" beginning on page PS-4.

Neither the Securities and Exchange Commission (the "SEC") nor any state securities commission has approved or disapproved of the securities or determined that this pricing supplement and the accompanying product supplement, prospectus supplement and prospectus is truthful or complete. Any representation to the contrary is a criminal offense. ***You should read this pricing supplement together with the accompanying product supplement, prospectus supplement and prospectus, each of which can be accessed via the hyperlinks below:***

Product Supplement No. ES-01-07 dated March 8, 2019 **Prospectus Supplement and Prospectus each dated May 14, 2018**

The securities are not bank deposits and are not insured or guaranteed by the Federal Deposit Insurance Corporation or any other governmental agency, nor are they obligations of, or guaranteed by, a bank.

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KEY TERMS (continued)

Automatic early redemption:	If, on any potential autocall date, the closing price of the worst performing underlying shares on that potential autocall date is greater than or equal to their initial share price, each security you then hold will be automatically redeemed on the coupon payment date immediately following that potential autocall date for an amount in cash equal to $1,000 *plus* the related coupon payment. **If the securities are automatically redeemed prior to maturity, you will not receive any further coupon payments following the redemption.**
Potential autocall dates:	June 27, 2019, July 29, 2019, and August 27, 2019, each subject to postponement on the same basis as if it were the valuation date
Underlying return:	For each of the underlying shares on any date, (i) their closing price on that date *minus* their initial share price *divided by* (ii) their initial share price
CUSIP / ISIN:	17324XFY1 / US17324XFY13

Additional Information

General. The terms of the securities are set forth in the accompanying product supplement, prospectus supplement and prospectus, as supplemented by this pricing supplement. The accompanying product supplement, prospectus supplement and prospectus contain important disclosures that are not repeated in this pricing supplement. For example, certain events may occur that could affect your payment at maturity or, in the case of a delisting of the underlying shares, could give us the right to call the securities prior to maturity for an amount that may be less than the stated principal amount. These events, including market disruption events and other events affecting the underlying shares, and their consequences are described in the accompanying product supplement in the sections "Description of the Securities—Consequences of a Market Disruption Event; Postponement of the Valuation Date," "—Dilution and Reorganization Adjustments" and "—Delisting of Underlying Shares (Other than Shares of an ETF)," and not in this pricing supplement. It is important that you read the accompanying product supplement, prospectus supplement and prospectus together with this pricing supplement before deciding whether to invest in the securities. Certain terms used but not defined in this pricing supplement are defined in the accompanying product supplement.

Postponement of a potential autocall date. If a scheduled potential autocall date is not a scheduled trading day for any of the underlying shares or if a market disruption event occurs or is continuing with respect to any of the underlying shares on a scheduled potential autocall date, that potential autocall date will be subject to postponement as if it were the valuation date as described in the accompanying product supplement in the section "Description of the Securities—Consequences of a Market Disruption Event; Postponement of the Valuation Date." If a scheduled potential autocall date is postponed, the closing price of each of the underlying shares in respect of that potential autocall date will be determined based on (i) for any underlying shares for which the originally scheduled potential autocall date is a scheduled trading day and as to which a market disruption event does not occur on the originally scheduled potential autocall date, the closing price of such underlying shares on the originally scheduled potential autocall date and (ii) for any other underlying shares, the closing price of such underlying shares on the potential autocall date as postponed (or, if earlier, the first scheduled trading day for such underlying shares following the originally scheduled potential autocall date on which a market disruption event did not occur with respect to such underlying shares).

Postponement of a coupon payment date. If the potential autocall date that immediately precedes a coupon payment date is postponed, that coupon payment date will be postponed to the fifth business day after that potential autocall date as postponed.

Dilution and reorganization adjustments. With respect to each of the underlying shares, the initial share price, the downside threshold price and the equity ratio are subject to adjustment upon the occurrence of certain events as described in the section "Description of the Securities—Dilution and Reorganization Adjustments" in the accompanying product supplement.

Coupon payments. The provisions of the accompanying product supplement describing the computation of each coupon payment do not apply and are superseded by this pricing supplement.

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Hypothetical Examples of the Payment at Maturity on the Securities

The examples below illustrate how to determine what you will receive at maturity of the securities, assuming the securities have not been previously redeemed. You should understand that the term of the securities, and your opportunity to receive the coupon payments on the securities, may be limited to as short as approximately three months by the automatic early redemption feature of the securities, which is not reflected in the examples below. The outcomes illustrated below are not exhaustive, and your actual payment at maturity on the securities (if the securities are not earlier automatically redeemed) may differ from any example illustrated below. For ease of analysis, figures below have been rounded.

The examples below are based on the following hypothetical values and assumptions in order to illustrate how the securities work and do not reflect the actual initial share price, downside threshold price or equity ratio of any of the underlying shares or the coupon payment rate of the securities:

Underlying shares	**Hypothetical initial share price***	**Hypothetical downside threshold price****	**Equity ratio*****
Shares of common stock of Advanced Micro Devices, Inc.	$100.00	$75.000	10.00000
Shares of common stock of Electronic Arts Inc.	$100.00	$75.000	10.00000
Coupon payment rate:	23.85% of the stated principal amount per annum, or 11.925% for the term of the securities, paid monthly, subject to automatic early redemption		

* For each of the underlying shares, their actual initial share price will be their closing price on the strike date.

** For each of the underlying shares, their actual downside threshold price will be equal to 75% of their initial share price.

*** For each of the underlying shares, their actual equity ratio will be equal to the stated principal amount of $1,000 *divided by* their initial share price.

The following examples illustrate the hypothetical payment at maturity on the securities determined based on the following hypothetical final share prices of each of the underlying shares, assuming the securities have not been earlier automatically redeemed.

	Hypothetical final share price of the shares of common stock of Advanced Micro Devices, Inc.	Hypothetical final share price of the shares of common stock of Electronic Arts Inc.	Hypothetical value received[1] at maturity per security (excluding final coupon payment)
Example 1	\$110.00 (underlying return = 10%)	\$130.00 (underlying return = 30%)	**\$1,000.00**
Example 2	\$120.00 (underlying return = 20%)	\$30.00 (underlying return = -70%)	**\$300.00**
Example 3	\$0.00 (underlying return = -100%)	\$160.00 (underlying return = 60%)	**\$0.00**

[1] Assumes that the closing price of the worst performing underlying shares on the valuation date is the same as their closing price on the maturity date.

Example 1: In this example, the shares of common stock of Advanced Micro Devices, Inc. have the lowest underlying return (based on their final share price) and are therefore the worst performing underlying shares on the valuation date. In this scenario, the final share price of the worst performing underlying shares on the valuation date is greater than their downside threshold price and, as a result, a downside event does not occur. Accordingly, at maturity, you would receive the stated principal amount of the securities *plus* the final coupon payment. You would not participate in the appreciation of any of the underlying shares, even though each of the underlying shares have appreciated from their initial share price in this example.

Example 2: In this example, the shares of common stock of Electronic Arts Inc. have the lowest underlying return (based on their final share price) and are therefore the worst performing underlying shares on the valuation date. In this scenario, the final share price of the worst performing underlying shares on the valuation date is less than their downside threshold price and, as a result, a downside event occurs. Accordingly, at maturity, you would receive a fixed number of the worst performing underlying shares on the valuation date equal to the applicable equity ratio (or, at our option, the cash value thereof) per security, *plus* the final coupon payment.

In this example, the value of a number of the worst performing underlying shares on the valuation date equal to the applicable equity ratio, based on their final share price, would be \$300.00. Therefore, in this scenario, the value of the worst performing underlying shares (or, in our discretion, cash) you receive at maturity would be significantly less than the stated principal amount of your securities. You would incur a loss based on the performance of the worst performing underlying shares on the valuation date, even though the final share prices of the other underlying shares are greater than their downside threshold prices.

If the final share price of the worst performing underlying shares on the valuation date is less than their downside threshold price, we will have the option to deliver to you on the maturity date either a number of the worst performing underlying shares on the valuation date equal to the applicable equity ratio or the cash value of those shares based on their final share price. The value of these shares on the maturity date may be different than their final share price.

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Example 3: In this example, the ordinary shares of Advanced Micro Devices, Inc. have the lowest underlying return (based on their final share price) and are therefore the worst performing underlying shares on the valuation date. In this scenario, the final share price of the worst performing underlying shares on the valuation date is less than their downside threshold price and, as a result, a downside event occurs. Accordingly, at maturity, you would receive a fixed number of the worst performing underlying shares on the valuation date equal to the applicable equity ratio (or, at our option, the cash value thereof) per security, *plus* the final coupon payment.

In this scenario, because the worst performing underlying shares on the valuation date are worthless, you would lose your entire investment in the securities.

Summary Risk Factors

An investment in the securities is significantly riskier than an investment in conventional debt securities. The securities are subject to all of the risks associated with an investment in our conventional debt securities (guaranteed by Citigroup Inc.), including the risk that we and Citigroup Inc. may default on our obligations under the securities, and are also subject to risks associated with each of the underlying shares. Accordingly, the securities are suitable only for investors who are capable of understanding the complexities and risks of the securities. You should consult your own financial, tax and legal advisors as to the risks of an investment in the securities and the suitability of the securities in light of your particular circumstances.

The following is a summary of certain key risk factors for investors in the securities. You should read this summary together with the more detailed description of risks relating to an investment in the securities contained in the section "Risk Factors Relating to the Securities" beginning on page ES-4 in the accompanying product supplement. You should also carefully read the risk factors included in the accompanying prospectus supplement and in the documents incorporated by reference in the accompanying prospectus, including Citigroup Inc.'s most recent Annual Report on Form 10-K and any subsequent Quarterly Reports on Form 10-Q, which describe risks relating to the business of Citigroup Inc. more generally.

You may lose some or all of your investment. Unlike conventional debt securities, the securities do not provide for the repayment of the stated principal amount at maturity in all circumstances. If the securities are not automatically redeemed prior to maturity, your payment at maturity will depend on the performance of the worst performing underlying shares on the valuation date. If the closing price of the worst performing underlying shares on the valuation date is less than their downside threshold price, a downside event will occur and you will not receive the stated principal amount of your securities at maturity and, instead, will receive a number of the worst performing underlying shares on the valuation date (or, in our sole discretion, cash based on the value thereof) that are expected to be worth less than 75% of the stated principal amount and may be worth nothing. There is no minimum payment at maturity on the securities, and you may lose up to all of your investment.

We may elect, in our sole discretion, to pay you cash at maturity in lieu of delivering any underlying shares. If we elect to pay you cash at maturity in lieu of delivering any underlying shares, the amount of that cash may be less than the market value of the underlying shares on the maturity date because the market value will likely fluctuate between the final valuation date and the maturity date. Conversely, if we do not exercise our cash election right and instead deliver underlying shares to you on the maturity date, the market value of such underlying shares may be less than the cash amount you would have received if we had exercised our cash election right. We will have no obligation to take your interests into account when deciding whether to exercise our cash election right.

The initial share prices, which have been set on the strike date, may be higher than the closing prices of the underlying shares on the pricing date. If the closing prices of the underlying shares on the pricing date are less than the initial share prices that were set on the strike date, the terms of the securities may be less favorable to you than the terms of an alternative investment that may be available to you that offers a similar payout as the securities but with the initial share prices set on the pricing date.

Your opportunity to receive coupon payments may be limited by the automatic early redemption feature. Beginning approximately three months after issuance, the securities will be automatically redeemed following a monthly potential autocall date if the closing price of the worst performing underlying shares on that date is greater than or equal to their initial share price. If the securities are automatically redeemed prior to maturity, you will not receive any additional coupon payments following the redemption and may not be able to reinvest your funds in another investment that offers comparable terms or returns. The term of the securities, and your opportunity to receive the coupon payments on the securities, may be limited to as short as three months.

Higher coupon payment rates are associated with greater risk. The securities offer coupon payments at a per annum rate that is higher than the rate we would pay on conventional debt securities of the same maturity. In exchange for this higher coupon payment rate, investors in the securities will be subject to significantly greater risk than investors in our conventional debt securities, including the risk that the securities may not be redeemed and you may lose a significant portion, and up to all, of your investment at maturity. The volatility of and the correlation among the underlying shares are important factors affecting these risks. In general, the higher the expected volatility of the underlying shares, and the lower the expected correlation among the underlying shares, the greater the coupon payment rate on the securities. However, higher expected volatility and lower expected correlation would also represent a greater expected likelihood as of the pricing date that (i) the closing price of the worst performing underlying shares on each potential autocall date will be less than their initial share price, resulting in the securities not being automatically redeemed and (ii) the final share price of the worst performing underlying shares on the valuation date will be less than their downside threshold price, resulting in a downside event and a significant loss at maturity.

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The securities are subject to the risks of all of the underlying shares and will be negatively affected if any of the underlying shares perform poorly, even if the other underlying shares perform well. You are subject to risks associated with all of the underlying shares. If any of the underlying shares perform poorly, you will be negatively affected, even if the other underlying shares perform well. The securities are not linked to a basket composed of the underlying shares, where the better performance of some could ameliorate the poor performance of the other. Instead, you are subject to the full risks of whichever of the underlying shares are the worst performing underlying shares.

You will not benefit in any way from the performance of the better performing underlying shares. The return on the securities depends solely on the performance of the worst performing underlying shares, and you will not benefit in any way from the performance of the better performing underlying shares. The securities may underperform a similar investment in all of the underlying shares or a similar alternative investment linked to a basket composed of the underlying shares, since in either such case the performance of the better performing underlying shares would be blended with the performance of the worst performing underlying shares, resulting in a better return than the return of the worst performing underlying shares.

You will be subject to risks relating to the relationship among the underlying shares. It is preferable from your perspective for the underlying shares to be correlated with each other, in the sense that they tend to increase or decrease at similar times and by similar magnitudes. By investing in the securities, you assume the risk that the underlying shares will not exhibit this relationship. The less correlated the underlying shares, the more likely it is that any one of the underlying shares will perform poorly over the term of the securities. All that is necessary for the securities to perform poorly is for one of the underlying shares to perform poorly; the performance of the underlying shares that are not the worst performing underlying shares is not relevant to your return on the securities. It is impossible to predict what the relationship among the underlying shares will be over the term of the securities.

The securities offer downside exposure to the underlying shares, but no upside exposure to the underlying shares. You will not participate in any appreciation in the price of any of the underlying shares over the term of the securities. Consequently, any positive return on the securities will be limited to the coupon payments and may be significantly less than the return on any of the underlying shares over the term of the securities. In addition, you will not receive any dividends or other distributions or any other rights with respect to any of the underlying shares.

The performance of the securities will depend on the closing price of the worst performing underlying shares solely on the potential autocall dates and the valuation date, which makes the securities particularly sensitive to volatility of the worst performing underlying shares. If the securities are not automatically redeemed prior to maturity, the amount you receive at maturity will depend solely on the closing price of the worst performing underlying shares on the valuation date. Whether your securities will be automatically redeemed prior to maturity depends solely on the closing price of the worst performing underlying shares on each potential autocall date. As a result, the performance of the securities will be sensitive to the volatility of the worst performing underlying shares. You should understand that each of the underlying shares have historically been highly volatile.

The securities are subject to the credit risk of Citigroup Global Markets Holdings Inc. and Citigroup Inc. If we default on our obligations under the securities and Citigroup Inc. defaults on its guarantee obligations, you may not receive any amounts owed to you under the securities.

The securities will not be listed on any securities exchange and you may not be able to sell them prior to maturity. The securities will not be listed on any securities exchange. Therefore, there may be little or no secondary market for the securities. CGMI currently intends to make a secondary market in relation to the securities and to provide an indicative bid price for the securities on a daily basis. Any indicative bid price for the securities provided by CGMI will be determined in CGMI's sole discretion, taking into account prevailing market conditions and other relevant factors, and will not be a representation by CGMI that the securities can be sold at that price, or at all. CGMI may suspend or terminate making a market and providing indicative bid prices without notice, at any time and for any reason. If CGMI suspends or terminates making a market, there may be no secondary market at all for the securities because it is likely that CGMI will be the only broker-dealer that is willing to buy your securities prior to maturity. Accordingly, an investor must be prepared to hold the securities until maturity.

The estimated value of the securities on the pricing date, based on CGMI's proprietary pricing models and our internal funding rate, will be less than the issue price. The difference is attributable to certain costs associated with selling, structuring and hedging the securities that are included in the issue price. These costs include (i) the selling concessions paid in connection with the offering of the securities, (ii) hedging and other costs incurred by us and our affiliates in connection with the offering of the securities and (iii) the expected profit (which may be more or less than actual profit) to CGMI or other of our affiliates in connection with hedging our obligations under the securities. These costs adversely affect the economic terms of the securities because, if they were lower, the economic terms of the securities would be more favorable to you. The economic terms of the securities are also likely to be adversely affected by the use of our internal funding rate, rather than our secondary market rate, to price the securities. See "The estimated value of the securities would be lower if it were calculated based on our secondary market rate" below.

The estimated value of the securities was determined for us by our affiliate using proprietary pricing models. CGMI derived the estimated value disclosed on the cover page of this pricing supplement from its proprietary pricing models. In doing so, it may have made discretionary judgments about the inputs to its models, such as the volatility of and correlation among the underlying shares, the dividend yields on the underlying shares and interest rates. CGMI's views on these inputs may differ from your or others' views, and as an underwriter in this offering, CGMI's interests may conflict with yours. Both the models and the inputs to the models may prove to be wrong and therefore not an accurate reflection of the value of the securities. Moreover, the estimated value of the securities set forth on the cover page of this pricing supplement may differ from the value that we or our affiliates may determine for the securities for other purposes, including for accounting purposes. You should not invest in the securities because of the estimated value of the securities. Instead, you should be willing to hold the securities to maturity irrespective of the initial estimated value.

The estimated value of the securities would be lower if it were calculated based on our secondary market rate. The estimated value of the securities included in this pricing supplement is calculated based on our internal funding rate, which is the rate at which we are willing to borrow funds through the issuance of the securities. Our internal funding rate is generally lower than our secondary market rate, which is the rate that CGMI will use in determining the value of the securities for purposes of any purchases of the securities from you in the secondary market. If the estimated value included in this pricing supplement were based on our secondary market rate, rather than our internal funding rate, it would likely be lower. We determine our internal funding rate based on factors such as the costs associated with the securities, which are generally higher than the costs associated with conventional debt securities, and our liquidity needs and preferences. Our internal funding rate is not the same as the coupon that is payable on the securities.

Because there is not an active market for traded instruments referencing our outstanding debt obligations, CGMI determines our secondary market rate based on the market price of traded instruments referencing the debt obligations of Citigroup Inc., our parent company and the guarantor of all payments due on the securities, but subject to adjustments that CGMI makes in its sole discretion. As a result, our secondary market rate is not a market-determined measure of our creditworthiness, but rather reflects the market’s perception of our parent company’s creditworthiness as adjusted for discretionary factors such as CGMI’s preferences with respect to purchasing the securities prior to maturity.

The estimated value of the securities is not an indication of the price, if any, at which CGMI or any other person may be willing to buy the securities from you in the secondary market. Any such secondary market price will fluctuate over the term of the securities based on the market and other factors described in the next risk factor. Moreover, unlike the estimated value included in this pricing supplement, any value of the securities determined for purposes of a secondary market transaction will be based on our secondary market rate, which will likely result in a lower value for the securities than if our internal funding rate were used. In addition, any secondary market price for the securities will be reduced by a bid-ask spread, which may vary depending on the aggregate stated principal amount of the securities to be purchased in the secondary market transaction, and the expected cost of unwinding related hedging transactions. As a result, it is likely that any secondary market price for the securities will be less than the issue price.

The value of the securities prior to maturity will fluctuate based on many unpredictable factors. The value of your securities prior to maturity will fluctuate based on the price and volatility of the underlying shares and a number of other factors, including the correlation among the underlying shares, dividend yields on the underlying shares, interest rates generally, the time remaining to maturity and our and Citigroup Inc.’s creditworthiness, as reflected in our secondary market rate. Changes in the prices of the underlying shares may not result in a comparable change in the value of your securities. You should understand that the value of your securities at any time prior to maturity may be significantly less than the issue price.

Immediately following issuance, any secondary market bid price provided by CGMI, and the value that will be indicated on any brokerage account statements prepared by CGMI or its affiliates, will reflect a temporary upward adjustment. The amount of this temporary upward adjustment will steadily decline to zero over the temporary adjustment period. See “Valuation of the Securities” in this pricing supplement.

Our offering of the securities is not a recommendation of any of the underlying shares. The fact that we are offering the securities does not mean that we believe that investing in an instrument linked to any of the underlying shares is likely to achieve favorable returns. In fact, as we are part of a global financial institution, our affiliates may have positions (including short positions) in the underlying shares or in instruments related to the underlying shares and may publish research or express opinions, that in each case are inconsistent with an investment linked to the underlying shares. These and other of our affiliates’ activities may affect the prices of the underlying shares in a way that has a negative impact on your interests as a holder of the securities.

The prices of the underlying shares may be adversely affected by our or our affiliates’ hedging and other trading activities. We expect to hedge our obligations under the securities through CGMI or other of our affiliates, who may take positions directly in the underlying shares and other financial instruments related to the underlying shares and may adjust such positions during the term of the securities. Our affiliates also trade the underlying shares and other financial instruments related to the underlying shares on a regular basis (taking long or short positions or both), for their accounts, for other accounts under their management or to facilitate transactions on behalf of customers. These activities could affect the prices of the underlying shares in a way that negatively affects the value of the securities. They could also result in substantial returns for us or our affiliates while the value of the securities declines.

We and our affiliates may have economic interests that are adverse to yours as a result of our affiliates’ business activities. Our affiliates may currently or from time to time engage in business with any underlying share issuer, including extending loans to, making equity investments in or providing advisory services to those issuers. In the course of this business, we or our affiliates may acquire non-public information about the underlying share issuers, which we will not disclose to you. Moreover, if any of our affiliates is or becomes a creditor of any such issuer, they may exercise any remedies against that issuer that are available to them without regard to your interests.

You will have no rights and will not receive dividends with respect to any of the underlying shares unless and until you receive underlying shares at maturity. As of March 26, 2019, Advanced Micro Devices, Inc. and Electronic Arts Inc. do not pay regular dividends. However, that may change, and if Advanced Micro Devices, Inc. or Electronic Arts Inc. starts to pay dividends during the term of the securities, you should understand that you will not receive such dividend payments under the securities. If any change to any of the underlying shares is proposed, such as an amendment to any underlying share issuer's organizational documents, you will not have the right to vote on such change, but you will be subject to such change in the event you receive the applicable underlying shares at maturity. Any such change may adversely affect the market price of the applicable underlying shares.

Even if any underlying share issuer pays a dividend that it identifies as special or extraordinary, no adjustment will be required under the securities for that dividend unless it meets the criteria specified in the accompanying product supplement. In general, an adjustment will not be made under the terms of the securities for any cash dividend paid on any of the underlying shares unless the amount of the dividend per share, together with any other dividends paid in the same fiscal quarter, exceeds the dividend paid per share in the most recent fiscal quarter by an amount equal to at least 10% of the closing price of the applicable shares on the date of declaration of the dividend. Any dividend will reduce the closing price of the applicable underlying shares by the amount of the dividend per share. If the applicable underlying share issuer pays any dividend for which an adjustment is not made under the terms of the securities, holders of the securities may be adversely affected. See "Description of the Securities—Dilution and Reorganization Adjustments—Certain Extraordinary Cash Dividends" in the accompanying product supplement.

The securities will not be adjusted for all events that could affect the price of any of the underlying shares. For example, we will not make any adjustment for ordinary dividends or extraordinary dividends that do not meet the criteria described above, partial tender offers or additional public offerings of the underlying shares. Moreover, the adjustments we do make may not fully offset the dilutive or adverse effect of the particular event. Investors in the securities may be adversely affected by such an event in a circumstance in which a direct holder of any of the underlying shares would not.

If any of the underlying shares are delisted, we may call the securities prior to maturity for an amount that may be less than the stated principal amount. If we exercise this call right, you will receive the amount described under "Description of the Securities—Delisting of Underlying Shares (Other than Shares of an ETF)" in the accompanying product supplement. This amount may be less, and possibly significantly less, than the stated principal amount of the securities.

The securities may become linked to shares of an issuer other than any original underlying share issuer upon the occurrence of a reorganization event or upon the delisting of any of the underlying shares. For example, if any underlying share issuer enters into a merger agreement that provides for holders of the applicable underlying shares to receive stock of another entity, the stock of such other entity will become the applicable underlying shares for all purposes of the securities upon consummation of the merger. Additionally, if the applicable underlying shares are delisted and we do not exercise our call right, the calculation agent may, in its sole discretion, select shares of another issuer to be the applicable underlying shares. See "Description of the Securities—Dilution and Reorganization Adjustments" and "—Delisting of Underlying Shares (Other than Shares of an ETF)" in the accompanying product supplement.

The calculation agent, which is an affiliate of ours, will make important determinations with respect to the securities. If certain events occur, such as market disruption events, corporate events with respect to any of the underlying share issuers that may require a dilution adjustment or the delisting of any underlying shares, CGMI, as calculation agent, will be required to make discretionary judgments that could significantly affect what you receive at maturity. In making these judgments, the calculation agent's interests as an affiliate of ours could be adverse to your interests as a holder of the securities.

The U.S. federal tax consequences of an investment in the securities are unclear. There is no direct legal authority regarding the proper U.S. federal tax treatment of the securities, and we do not plan to request a ruling from the Internal Revenue Service (the "IRS"). Consequently, significant aspects of the tax treatment of the securities are uncertain, and the IRS or a court might not agree with the treatment of the securities as described in "United States Federal Tax Considerations" below. If the IRS were successful in asserting an alternative treatment, the tax consequences of ownership and disposition of the securities might be materially and adversely affected. As described in the accompanying product supplement under "United States Federal Tax Considerations," in 2007 the U.S. Treasury Department and the IRS released a notice requesting comments on various issues regarding the U.S. federal income tax treatment of "prepaid forward contracts" and similar instruments. While it is not clear whether the securities would be viewed as similar to the typical prepaid forward contract described in the notice, it is possible that any Treasury regulations or other guidance promulgated after consideration of these issues could materially and adversely affect the tax consequences of an investment in the securities, including the character and timing of income or loss and the degree, if any, to which income realized by non-U.S. persons should be subject to withholding tax, possibly with retroactive effect. You should read carefully the discussion under "United States Federal Tax Considerations" and "Risk Factors Relating to the Securities" in the accompanying product supplement and "United States Federal Tax Considerations" in this pricing supplement. You should also consult your tax adviser regarding the U.S. federal tax consequences of an investment in the securities, as well as tax consequences arising under the laws of any state, local or non-U.S. taxing jurisdiction.

As described in "United States Federal Tax Considerations" below, in connection with any information reporting requirements we may have in respect of the securities under applicable law, we intend to treat a portion of each coupon payment as attributable to interest and the remainder to option premium. However, in light of the uncertain treatment of the securities, it is possible that other persons having withholding or information reporting responsibility in respect of the securities may treat a security differently, for instance, by treating the entire coupon payment as ordinary income at the time received or accrued by a holder and/or treating some or all of each coupon payment on a security to a non-U.S. investor as subject to withholding tax at a rate of 30%.

If withholding applies to the securities, we will not be required to pay any additional amounts with respect to amounts withheld.

Citigroup Global Markets Holdings Inc.
Autocallable Equity Linked Securities Based on the Worst Performing of the Common Stock of Advanced Micro Devices, Inc. and the Common Stock of Electronic Arts Inc. Due October 2, 2019

Information About Advanced Micro Devices, Inc.

Advanced Micro Devices, Inc. is a semiconductor company. The common stock of Advanced Micro Devices, Inc. is registered under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Information provided to or filed with the SEC by Advanced Micro Devices, Inc. pursuant to the Exchange Act can be located by reference to the SEC file number 001-07882 through the SEC's website at http://www.sec.gov. In addition, information regarding Advanced Micro Devices, Inc. may be obtained from other sources including, but not limited to, press releases, newspaper articles and other publicly disseminated documents. The common stock of Advanced Micro Devices, Inc. trades on the Nasdaq Global Select Market under the ticker symbol "AMD."

This pricing supplement relates only to the securities offered hereby and does not relate to the common stock of Advanced Micro Devices, Inc. or other securities of Advanced Micro Devices, Inc. We have derived all disclosures contained in this pricing supplement regarding Advanced Micro Devices, Inc. from the publicly available documents described above. In connection with the offering of the securities, none of Citigroup Global Markets Holdings Inc., Citigroup Inc. or CGMI has participated in the preparation of such documents or made any due diligence inquiry with respect to Advanced Micro Devices, Inc.

The securities represent obligations of Citigroup Global Markets Holdings Inc. (guaranteed by Citigroup Inc.) only. Advanced Micro Devices, Inc. is not involved in any way in this offering and has no obligation relating to the securities or to holders of the securities.

Neither we nor any of our affiliates make any representation to you as to the performance of the shares of common stock of Advanced Micro Devices, Inc.

Historical Information

The graph below shows the closing price of the shares of common stock of Advanced Micro Devices, Inc. for each day such price was available from January 2, 2015 to March 26, 2019. The table that follows shows the high and low closing prices of, and dividends paid on, the shares of common stock of Advanced Micro Devices, Inc. for each quarter in that same period. We obtained the closing prices and other information below from Bloomberg L.P., without independent verification. If certain corporate transactions occurred during the historical period shown below, including, but not limited to, spin-offs or mergers, then the closing prices of the shares of common stock of Advanced Micro Devices, Inc. shown below for the period prior to the occurrence of any such transaction have been adjusted by Bloomberg L.P. as if any such transaction had occurred prior to the first day in the period shown below. **You should**

not take the historical prices of the shares of common stock of Advanced Micro Devices, Inc. as an indication of future performance.

Common Stock of Advanced Micro Devices, Inc. – Historical Closing Prices

January 2, 2015 to March 26, 2019

* The red line indicates the downside threshold price with respect to the shares of common stock of Advanced Micro Devices, Inc. of $19.268, equal to 75% of the applicable initial share price.

Citigroup Global Markets Holdings Inc.
Autocallable Equity Linked Securities Based on the Worst Performing of the Common Stock of Advanced Micro Devices, Inc. and the Common Stock of Electronic Arts Inc. Due October 2, 2019

Common Stock of Advanced Micro Devices, Inc.	High	Low	Dividends
2015			
First Quarter	$3.31	$2.24	$0.00000
Second Quarter	$2.87	$2.22	$0.00000
Third Quarter	$2.53	$1.62	$0.00000
Fourth Quarter	$3.00	$1.74	$0.00000
2016			
First Quarter	$2.93	$1.80	$0.00000
Second Quarter	$5.45	$2.62	$0.00000
Third Quarter	$7.67	$4.96	$0.00000
Fourth Quarter	$12.07	$6.30	$0.00000
2017			
First Quarter	$15.20	$9.75	$0.00000
Second Quarter	$14.64	$10.04	$0.00000
Third Quarter	$14.76	$12.05	$0.00000
Fourth Quarter	$14.26	$9.90	$0.00000
2018			
First Quarter	$13.74	$9.81	$0.00000
Second Quarter	$17.11	$9.53	$0.00000
Third Quarter	$32.72	$15.00	$0.00000
Fourth Quarter	$31.42	$16.65	$0.00000
2019			
First Quarter (through March 26, 2019)	$27.89	$17.05	$0.00000

The closing price of the shares of common stock of Advanced Micro Devices, Inc. on March 26, 2019 was $25.69.

We make no representation as to the amount of dividends, if any, that may be paid on the shares of common stock of Advanced Micro Devices, Inc. in the future. In any event, as an investor in the securities, you will not be entitled to receive dividends, if any, that may be payable on the shares of common stock of Advanced Micro Devices, Inc.

Citigroup Global Markets Holdings Inc.
Autocallable Equity Linked Securities Based on the Worst Performing of the Common Stock of Advanced Micro Devices, Inc. and the Common Stock of Electronic Arts Inc. Due October 2, 2019

Information About Electronic Arts Inc.

Electronic Arts Inc. develops, markets, publishes and distributes games, content and services that can be played on a variety of platforms, including game consoles, PCs, mobile phones and tablets. The common stock of Electronic Arts Inc. is registered under the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Information provided to or filed with the SEC by Electronic Arts Inc. pursuant to the Exchange Act can be located by reference to the SEC file number 000-17948 through the SEC’s website at http://www.sec.gov. In addition, information regarding Electronic Arts Inc. may be obtained from otheleft;font-size:10pt;">

Net earnings
172.9

105.9

501.6

395.8

Net earnings attributable to the noncontrolling interest, net of tax
6.1

4.8

18.7

16.1

Net earnings attributable to BorgWarner Inc.
$
166.8

$
101.1

$
482.9

$
379.7

Earnings per share — basic
$
1.47

$
0.88

$
4.21

$
3.40

Earnings per share — diluted
$
1.45

$
0.85

$
4.16

$

3.15

Weighted average shares outstanding:

Basic
113.819

114.299

114.584

111.619

Diluted
115.238

118.499

115.968

122.571

Dividends declared per share

$
0.25

$
—

$
0.25

$
—

See accompanying Notes to Condensed Consolidated Financial Statements.

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BORGWARNER INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(millions of dollars)	2013	2012	2013	2012
Net earnings attributable to BorgWarner Inc.	$166.8	$101.1	$482.9	$379.7
Other comprehensive income				
Foreign currency translation adjustments	94.5	64.2	4.7	18.3
Hedge instruments	0.4	(3.7)	14.0	7.3
Defined benefit postretirement plans	1.9	1.5	11.1	4.1
Other	—	—	0.5	0.5
Total other comprehensive income attributable to BorgWarner Inc.	96.8	62.0	30.3	30.2
Comprehensive income attributable to BorgWarner Inc.	263.6	163.1	513.2	409.9
Comprehensive income attributable to the noncontrolling interest	2.7	1.3	0.4	1.4
Comprehensive income	$266.3	$164.4	$513.6	$411.3

See accompanying Notes to Condensed Consolidated Financial Statements.

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BORGWARNER INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Nine Months Ended September 30,	
(millions of dollars)	2013	2012
OPERATING		
Net earnings	$501.6	$395.8
Adjustments to reconcile net earnings to net cash flows from operations:		
Non-cash charges (credits) to operations:		
Depreciation and tooling amortization	202.4	189.8
Amortization of intangible assets and other	20.1	21.5
Loss from disposal activities, net of cash paid	—	31.7
Restructuring expense, net of cash paid	—	25.5
Bond amortization	—	5.3
Stock-based compensation expense	29.3	41.0
Deferred income tax benefit	(9.0)	(0.4)
Equity in affiliates' earnings, net of dividends received, and other	(28.2)	(15.9)
Net earnings adjusted for non-cash charges to operations	716.2	694.3
Changes in assets and liabilities:		
Receivables	(195.3)	(81.5)
Inventories	(13.0)	(38.5)
Prepayments and other current assets	(39.7)	(18.9)
Accounts payable and accrued expenses	85.5	(2.1)
Income taxes payable	(25.9)	25.7
Other non-current assets and liabilities	(13.0)	(36.4)
Net cash provided by operating activities	514.8	542.6
INVESTING		
Capital expenditures, including tooling outlays	(297.9)	(283.0)
Net proceeds from asset disposals	22.8	3.9
Net proceeds from sale of business	—	56.8
Net cash used in investing activities	(275.1)	(222.3)
FINANCING		
Net increase in notes payable	14.3	34.7
Additions to long-term debt, net of debt issuance costs	272.0	313.9
Repayments of long-term debt, including current portion	(76.9)	(203.6)
Payments for purchase of treasury stock	(225.5)	(200.3)
Proceeds from stock options exercised, including the tax benefit	25.3	49.9
Taxes paid on employees' restricted stock award vestings	(29.2)	(17.8)
Purchase of noncontrolling interest	—	(7.4)
Dividends paid to BorgWarner stockholders	(28.5)	—
Dividends paid to noncontrolling stockholders	(10.7)	(20.5)
Net cash used in financing activities	(59.2)	(51.1)
Effect of exchange rate changes on cash	24.2	(7.3)
Net increase in cash	204.7	261.9
Cash at beginning of year	715.7	359.6
Cash at end of period	$920.4	$621.5

SUPPLEMENTAL CASH FLOW INFORMATION		
Net cash paid during the period for:		
Interest	$37.6	$44.7
Income taxes	$197.6	$122.0

See accompanying Notes to Condensed Consolidated Financial Statements.

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BORGWARNER INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

(1) Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements of BorgWarner Inc. and Consolidated Subsidiaries (the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes necessary for a comprehensive presentation of financial position, results of operations and cash flow activity required by GAAP for complete financial statements. In the opinion of management, all normal recurring adjustments necessary for a fair presentation of results have been included. Operating results for the three and nine months ended September 30, 2013 are not necessarily indicative of the results that may be expected for the year ending December 31, 2013. The balance sheet as of December 31, 2012 was derived from the audited financial statements as of that date. For further information, refer to the Consolidated Financial Statements and Footnotes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012.

Management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and accompanying notes, as well as, the amounts of revenues and expenses reported during the periods covered by those financial statements and accompanying notes. Actual results could differ from these estimates.

(2) Research and Development Expenditures

The Company's net Research & Development ("R&D") expenditures are included in selling, general and administrative expenses of the Condensed Consolidated Statements of Operations. Customer reimbursements are netted against gross R&D expenditures as they are considered a recovery of cost. Customer reimbursements for prototypes are recorded net of prototype costs based on customer contracts, typically either when the prototype is shipped or when it is accepted by the customer. Customer reimbursements for engineering services are recorded when performance obligations are satisfied in accordance with the contract and accepted by the customer. Financial risks and rewards transfer upon shipment, acceptance of a prototype component by the customer or upon completion of the performance obligation as stated in the respective customer agreement.

The following table presents the Company’s gross and net expenditures on R&D activities:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(millions of dollars)	2013	2012	2013	2012
Gross R&D expenditures	$84.7	$75.6	$250.9	$228.5
Customer reimbursements	(12.9)	(11.2)	(34.7)	(29.8)
Net R&D expenditures	$71.8	$64.4	$216.2	$198.7

The Company has contracts with several customers at the Company's various R&D locations. No such contract exceeded 5% of annual net R&D expenditures in any of the periods presented.

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(3) Other (Income) Expense

Items included in other (income) expense consist of:

(millions of dollars)	Three Months Ended September 30, 2013	2012	Nine Months Ended September 30, 2013	2012
Program termination agreement	$—	$—	$11.3	$—
Retirement related obligations	—	—	5.9	—
Loss from disposal activities	—	1.8	—	39.7
Restructuring expense	—	27.4	—	27.4
Other	(3.7)	0.5	(6.4)	0.3
Other (income) expense	$(3.7)	$29.7	$10.8	$67.4

During the first quarter of 2013, the Company recorded an $11.3 million expense related to a program termination agreement, which was paid in the second and third quarters of 2013.

During the fourth quarter of 2012, the Company waived the forfeiture provision associated with future restricted stock grants made to certain retiring Named Executive Officers. The Company recorded a $5.9 million retirement related obligation primarily related to a first quarter 2013 grant of restricted stock awards to these Named Executive Officers.

During the second quarter of 2012, the Company signed a Master Purchase Agreement to sell its spark plug business to Federal-Mogul Corporation. As a result, the Company recorded expense of $39.7 million primarily to write-down prior purchase price accounting adjustments included within the disposal group. These purchase price accounting adjustments were originally recorded in the Engine segment and related to the BERU acquisition.The Company also recorded restructuring expense of $27.4 million in the third quarter of 2012 primarily associated with the disposal and future requirements of BERU's on-going business, which included $16.9 million of employee termination benefits and $10.5 million of other charges, primarily related to the write-down of certain assets.

(4) Income Taxes

The Company's provision for income taxes is based upon an estimated annual tax rate for the year applied to federal, state and foreign income. On a quarterly basis, the annual effective tax rate is adjusted, as appropriate, based upon changed facts and circumstances, if any, as compared to those forecasted at the beginning of the fiscal year and each interim period thereafter.

At September 30, 2013, the Company estimates its U.S. GAAP effective tax rate to be approximately 26% for the year ending December 31, 2013, which includes tax benefits of $3.8 million and $2.1 million related to the program termination agreement and retirement related obligations discussed in the Other (Income) Expense footnote. This rate also includes a net tax benefit of $7.3 million, which is comprised of tax benefits of $6.6 million related to the extension of the federal research and development credit and other international tax provisions resulting from the retroactive impact of U.S. legislation enacted in January 2013, $3.1 million related to 2012 provision to return adjustments and $2.5 million related to the reversal of certain deferred tax asset valuation allowances, partially offset by a $4.9 million tax expense related to a comprehensive income adjustment.

At September 30, 2012, the Company estimated its U.S. GAAP effective tax rate to be approximately 31% for the year ending December 31, 2012. This rate included net tax expense of $3.5 million associated with the loss from disposal activities and restructuring expense recorded during the third quarter of 2012. The $3.5 million net expense was comprised of $11.2 million tax expense resulting from the completion of the disposal, partially offset by a tax benefit of $7.7 million associated with the restructuring expense. For

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the nine months ended September 30, 2012, the net tax benefit associated with the loss from disposal activities and restructuring expense was $2.0 million. The 31% U.S. GAAP effective tax rate also included additional tax expense of $15.9 million resulting from other tax adjustments. These other tax adjustments included $8.2 million of tax expense primarily resulting from the settlement of certain tax audits and $7.7 million of tax expense associated with the Company's second quarter 2012 decision to change its cash repatriation assertion for some of its foreign subsidiaries.

The annual effective tax rates differ from the U.S. statutory rate primarily due to foreign rates which differ from those in the U.S., the realization of certain business tax credits, including foreign tax credits, and favorable permanent differences between book and tax treatment for certain items, including equity in affiliates' earnings.

(5) Inventories, net

Inventories are valued at the lower of cost or market. The cost of U.S. inventories is determined by the last-in, first-out (“LIFO”) method, while the operations outside the U.S. use the first-in, first-out (“FIFO”) or average-cost methods. Inventories consisted of the following:

(millions of dollars)	September 30, 2013	December 31, 2012
Raw material and supplies	$284.2	$264.0
Work in progress	79.8	82.0
Finished goods	106.1	117.6
FIFO inventories	470.1	463.6
LIFO reserve	(15.4)	(16.0)
Inventories, net	$454.7	$447.6

(6) Property, Plant and Equipment, net

(millions of dollars)	September 30, 2013	December 31, 2012
Land, land use rights and buildings	$738.6	$717.2
Machinery and equipment	1,848.0	2,282.4
Capital leases	2.4	2.3
Construction in progress	265.0	243.7
Total property, plant and equipment, gross	2,854.0	3,245.6
Less: accumulated depreciation	(1,086.5)	(1,567.0)
Property, plant and equipment, net, excluding tooling	1,767.5	1,678.6
Tooling, net of amortization	107.9	109.4
Property, plant and equipment, net	$1,875.4	$1,788.0

As of September 30, 2013 and December 31, 2012, accounts payable of $35.8 million and $39.8 million, respectively, were related to property, plant and equipment purchases.

Interest costs capitalized for the nine months ended September 30, 2013 and 2012 were $8.5 million and $13.5 million, respectively.

(7) Product Warranty

The Company provides warranties on some, but not all, of its products. The warranty terms are typically from one to three years. Provisions for estimated expenses related to product warranty are made at the time products are sold. These estimates are established using historical information about the nature,

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frequency and average cost of warranty claim settlements as well as product manufacturing and industry developments and recoveries from third parties. Management actively studies trends of warranty claims and takes action to improve product quality and minimize warranty claims. Management believes that the warranty accrual is appropriate; however, actual claims incurred could differ from the original estimates, requiring adjustments to the accrual.

The following table summarizes the activity in the product warranty accrual accounts:

(millions of dollars)	2013	2012
Beginning balance, January 1	$64.9	$72.7
Provisions	29.1	23.1
Payments	(28.3)	(31.9)
Translation adjustment	0.7	0.2
Ending balance, September 30	$66.4	$64.1

The product warranty liability is classified in the Condensed Consolidated Balance Sheets as follows:

(millions of dollars)	September 30, 2013	December 31, 2012
Accounts payable and accrued expenses	$33.3	$33.1
Other non-current liabilities	33.1	31.8
Total product warranty liability	$66.4	$64.9

(8) Notes Payable and Long-Term Debt

As of September 30, 2013 and December 31, 2012, the Company had short-term and long-term debt outstanding as follows:

(millions of dollars)	September 30, 2013	December 31, 2012
Short-term debt		
Short-term borrowings	$143.4	$129.1
Receivables securitization	110.0	110.0
Total short-term debt	$253.4	$239.1
Long-term debt		
5.75% Senior notes due 11/01/16 ($150 million par value)	$149.6	$149.6
8.00% Senior notes due 10/01/19 ($134 million par value)	133.9	133.9
4.625% Senior notes due 09/15/20 ($250 million par value)	248.1	247.9
7.125% Senior notes due 02/15/29 ($121 million par value)	119.4	119.4
Multi-currency revolving credit facility	320.0	140.0
Term loan facilities and other	30.7	17.1
Unamortized portion of debt derivatives	17.2	20.2
Total long-term debt	1,018.9	828.1
Less: current portion	0.3	4.3
Long-term debt, net of current portion	$1,018.6	$823.8

The weighted average interest rate on all borrowings outstanding as of September 30, 2013 and December 31, 2012 was 3.6% and 4.0%, respectively.

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The Company's multi-currency revolving credit facility includes a feature that allows the Company's borrowings to be increased to $1 billion. Utilizing this feature, on April 12, 2013, the Company increased its multi-currency revolving credit facility from $650 million to $750 million. The credit facility provides for borrowings through June 30, 2016 and is guaranteed by the Company's material domestic subsidiaries. The credit facility has two key financial covenants, a debt compared to EBITDA (“Earnings Before Interest, Taxes, Depreciation and Amortization”) test and an interest coverage test. The Company was in compliance with all covenants at September 30, 2013 and expects to remain compliant in future periods. At September 30, 2013 and December 31, 2012, the Company had outstanding borrowings of $320.0 million and $140.0 million, respectively, under this facility.

As of September 30, 2013 and December 31, 2012, the estimated fair values of the Company’s senior unsecured notes totaled $738.4 million and $770.3 million, respectively. The estimated fair values were $87.4 million and $119.5 million higher than their carrying value at September 30, 2013 and December 31, 2012, respectively. Fair market values of the senior unsecured notes are developed using observable values for similar debt instruments, which are considered Level 2 inputs as defined by ASC Topic 820. The carrying value of the Company's multi-currency revolving credit facility is equal to its fair value. The fair value estimates do not necessarily reflect the values the Company could realize in the current markets.

The Company had outstanding letters of credit of $27.1 million and $59.1 million at September 30, 2013 and December 31, 2012, respectively. The letters of credit typically act as guarantees of payment to certain third parties in accordance with specified terms and conditions.

(9) Fair Value Measurements

ASC Topic 820 emphasizes that fair value is a market-based measurement, not an entity specific measurement. Therefore, a fair value measurement should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering market participant assumptions in fair value measurements, ASC Topic 820 establishes a fair value hierarchy, which prioritizes the inputs used in measuring fair values as follows:

Level 1: Observable inputs such as quoted prices for identical assets or liabilities in active markets;
Level 2: Inputs, other than quoted prices in active markets, that are observable either directly or indirectly; and
Level 3: Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

Assets and liabilities measured at fair value are based on one or more of the following three valuation techniques noted in ASC Topic 820:

A. Market approach: Prices and other relevant information generated by market transactions involving identical or comparable assets, liabilities or a group of assets or liabilities, such as a business.
B. Cost approach: Amount that would be required to replace the service capacity of an asset (replacement cost).
C. Income approach: Techniques to convert future amounts to a single present amount based upon market expectations (including present value techniques, option-pricing and excess earnings models).

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The following tables classify assets and liabilities measured at fair value on a recurring basis as of September 30, 2013 and December 31, 2012:

		Basis of fair value measurements			
(millions of dollars)	Balance at September 30, 2013	Quoted prices in active markets for identical items (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Valuation technique
Assets:					
Foreign currency contracts	$2.6	$—	$2.6	$—	A
Other non-current assets (insurance settlement agreement note receivable)	$35.5	$—	$35.5	$—	C
Liabilities:					
Foreign currency contracts	$6.7	$—	$6.7	$—	A
Net investment hedge contracts	$36.2	$—	$36.2	$—	A

		Basis of fair value measurements			
(millions of dollars)	Balance at December 31, 2012	Quoted prices in active markets for identical items (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Valuation technique
Assets:					
Foreign currency contracts	$5.9	$—	$5.9	$—	A
Other non-current assets (insurance settlement agreement note receivable)	$41.0	$—	$41.0	$—	C
Liabilities:					
Foreign currency contracts	$9.8	$—	$9.8	$—	A
Net investment hedge contracts	$58.1	$—	$58.1	$—	A

(10) Financial Instruments

The Company's financial instruments include cash and marketable securities. Due to the short-term nature of these instruments, their book value approximates their fair value. The Company's financial instruments also include long-term debt, interest rate and cross-currency swaps, commodity derivative contracts and foreign currency derivatives. All derivative contracts are placed with counterparties that have an S&P, or equivalent, investment grade credit rating at the time of the contracts' placement. At September 30, 2013 and December 31, 2012, the Company had no derivative contracts that contained credit risk related contingent features.

The Company selectively uses cross-currency swaps to hedge the foreign currency exposure associated with our net investment in certain foreign operations (net investment hedges). At September 30, 2013 and December 31, 2012, the following cross-currency swaps were outstanding:

	Cross-currency swaps		
(in millions)	Notional in USD	Notional in local currency	Duration
Floating $ to floating €	$75.0	€58.5	Oct - 19
Floating $ to floating ¥	$150.0	¥17,581.5	Nov - 16

The Company uses certain commodity derivative contracts to protect against commodity price changes related to forecasted raw material and supplies purchases. The Company primarily utilizes forward and option contracts, which are designated as cash flow hedges. The Company did not have any commodity derivative contracts outstanding at September 30, 2013 and December 31, 2012.

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The Company uses foreign currency forward and option contracts to protect against exchange rate movements for forecasted cash flows, including capital expenditures, purchases, operating expenses or sales transactions designated in currencies other than the functional currency of the operating unit. Foreign currency derivative contracts require the Company, at a future date, to either buy or sell foreign currency in exchange for the operating units' local currency.

At September 30, 2013 and December 31, 2012, the following foreign currency derivative contracts were outstanding:

Foreign currency derivatives (in millions)

Functional currency	Traded currency	Notional in traded currency September 30, 2013	Notional in traded currency December 31, 2012	Duration
Brazilian real	US dollar	21.9	—	Dec - 14
British pound	Euro	14.4	28.8	Dec - 13
Chinese yuan	Japanese yen	737.0	—	Feb - 14
Chinese yuan	US dollar	17.5	—	Dec - 14
Euro	British pound	4.2	4.7	Dec - 14
Euro	Hungarian forint	2,325.0	9,300.0	Nov - 13
Euro	Japanese yen	5,762.5	6,760.0	Dec - 14
Euro	Polish zloty	16.3	87.4	Dec - 13
Euro	US dollar	35.0	15.2	Dec - 14
Hungarian forint	Euro	1.7	—	Dec - 13
Japanese yen	Chinese yuan	84.0	—	Dec - 14
Japanese yen	US dollar	2.5	9.5	Dec - 13
Korean won	Euro	25.3	32.4	Dec - 14
Korean won	Japanese yen	162.9	—	Jun - 14
Korean won	US dollar	4.2	17.5	Dec - 13
Mexican peso	US dollar	7.4	20.9	Dec - 13
Swedish krona	Euro	13.0	—	Dec - 13
US dollar	Indian rupee	9.4	111.1	Oct - 13
US dollar	Japanese yen	3,311.2	3,000.0	Dec - 13

At September 30, 2013 and December 31, 2012, the following amounts were recorded in the Condensed Consolidated Balance Sheets as being payable to or receivable from counterparties under ASC Topic 815:

(millions of dollars)	Assets			Liabilities		
Contract Type	Location	September 30, 2013	December 31, 2012	Location	September 30, 2013	December 31, 2012
Foreign currency contracts	Prepayments and other current assets	$2.4	$5.7	Accounts payable and accrued expenses	$6.5	$9.8
	Other non-current assets	$0.2	$0.2	Other non-current liabilities	$0.2	$—
Net investment hedge contracts	Other non-current assets	$—	$—	Other non-current liabilities	$36.2	$58.1

Effectiveness for cash flow and net investment hedges is assessed at the inception of the hedging relationship and quarterly, thereafter. To the extent that derivative instruments are deemed to be effective, gains and losses arising from these contracts are deferred into accumulated other comprehensive income (loss) ("AOCI") and reclassified into income as the underlying operating transactions are recognized. These realized gains or losses offset the hedged transaction and are recorded on the same line in the statement

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of operations. To the extent that derivative instruments are deemed to be ineffective, gains or losses are recognized into income.

The table below shows deferred gains (losses) reported in AOCI as well as the amount expected to be reclassified to income in one year or less. The amount expected to be reclassified to income in one year or less assumes no change in the current relationship of the hedged item at September 30, 2013 market rates.

(millions of dollars)	Deferred gain (loss) in AOCI at		Gain (loss) expected to be reclassified to income in one year or less
Contract Type	September 30, 2013	December 31, 2012	
Foreign currency	$(4.6)	$(3.5)	$(4.6)
Net investment hedges	(32.6)	(54.5)	—
Total	$(37.2)	$(58.0)	$(4.6)

Derivative instruments designated as hedging instruments as defined by ASC Topic 815 held during the period resulted in the following gains and losses recorded in income:

(millions of dollars)		Gain (loss) reclassified from AOCI to income (effective portion) Three Months Ended			Gain (loss) recognized in income (ineffective portion) Three Months Ended	
Contract Type	Location	September 30, 2013	September 30, 2012	Location	September 30, 2013	September 30, 2012
Foreign currency	Sales	$0.7	$2.4	SG&A expense	$—	$—
Foreign currency	Cost of goods sold	$(4.1)	$1.4	SG&A expense	$(0.1)	$—
Foreign currency	SG&A expense	$(0.1)	$—	SG&A expense	$—	$—
Cross-currency swap	N/A			Interest expense	$0.4	$3.9

(millions of dollars)		Gain (loss) reclassified from AOCI to income (effective portion) Nine Months Ended			Gain (loss) recognized in income (ineffective portion) Nine Months Ended	
Contract Type	Location	September 30, 2013	September 30, 2012	Location	September 30, 2013	September 30, 2012
Foreign currency	Sales	$1.6	$3.9	SG&A expense	$0.2	$—
Foreign currency	Cost of goods sold	$(10.1)	$2.5	SG&A expense	$(0.8)	$—
Foreign currency	SG&A expense	$(0.2)	$—	SG&A expense	$—	$—
Cross-currency swap	N/A			Interest expense	$0.1	$1.7

At September 30, 2013, derivative instruments that were not designated as hedging instruments as defined by ASC Topic 815 were immaterial.

(11) Retirement Benefit Plans

The Company has a number of defined benefit pension plans and other postretirement benefit plans covering eligible salaried and hourly employees and their dependents. The estimated contributions to the Company's defined benefit pension plans for 2013 range from $15 million to $25 million, of which $15.1 million has been contributed through the first nine months of the year. The other postretirement benefit plans, which provide medical and life insurance benefits, are unfunded plans.

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The components of net periodic benefit cost recorded in the Condensed Consolidated Statements of Operations are as follows:

	Pension benefits				Other post-retirement benefits	
(millions of dollars)	2013		2012		2013	2012
Three Months Ended September 30,	US	Non-US	US	Non-US		
Service cost	$—	$3.1	$—	$2.2	$0.1	$0.1
Interest cost	2.9	4.2	3.6	4.2	1.7	2.5
Expected return on plan assets	(4.6)	(2.8)	(4.7)	(2.3)	—	—
Amortization of unrecognized prior service benefit	(0.2)	—	(0.2)	—	(1.6)	(1.6)
Amortization of unrecognized loss	2.1	1.3	2.0	0.4	1.2	1.8
Net periodic benefit cost	$0.2	$5.8	$0.7	$4.5	$1.4	$2.8

	Pension benefits				Other post-retirement benefits	
(millions of dollars)	2013		2012		2013	2012
Nine Months Ended September 30,	US	Non-US	US	Non-US		
Service cost	$—	$9.3	$—	$6.8	$0.3	$0.4
Interest cost	8.7	12.4	10.8	12.9	5.1	7.6
Expected return on plan assets	(13.7)	(8.2)	(14.1)	(6.9)	—	—
Amortization of unrecognized prior service benefit	(0.6)	—	(0.6)	—	(4.8)	(4.8)
Amortization of unrecognized loss	6.2	3.9	6.1	0.9	3.7	5.2
Net periodic benefit cost	$0.6	$17.4	$2.2	$13.7	$4.3	$8.4

(12) Stock-Based Compensation

Under the Company's 1993 Stock Incentive Plan ("1993 Plan"), the Company granted options to purchase shares of the Company's common stock at the fair market value on the date of grant. The options vested over periods up to three years and have a term of 10 years from date of grant. As of December 31, 2003, there were no options available for future grants under the 1993 Plan. The 1993 Plan expired at the end of 2003 and was replaced by the Company's 2004 Stock Incentive Plan. Under this Plan, 12.5 million shares are authorized for grant, of which approximately 1.6 million shares are available for future issuance.

Stock options A summary of the Company's stock option activity for the nine months ended September 30, 2013 is as follows:

	Shares under option (thousands)	Weighted average exercise price	Weighted average remaining contractual life (in years)	Aggregate intrinsic value (in millions)
Outstanding and exercisable at December 31, 2012	1,436	$30.65	3.4	$58.8
Exercised	(81)	$28.43		
Outstanding and exercisable at March 31, 2013	1,355	$30.78	3.2	$63.1
Exercised	(201)	$27.56		
Outstanding and exercisable at June 30, 2013	1,154	$31.34	3.1	$63.2
Exercised	(103)	$30.12		
Outstanding and exercisable at September 30, 2013	1,051	$31.46	2.8	$73.5

Restricted stock At its November 2007 meeting, the Company's Compensation Committee decided that restricted common stock awards and stock units ("restricted stock") would be awarded in place of stock options for long-term incentive award grants to employees. Restricted stock granted to employees vests

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50% after two years and the remainder after three years from the date of grant. Restricted stock granted to non-employee directors generally vests on the anniversary date of the grant.

The value of restricted stock is determined by the market value of the Company's common stock at the date of grant. In 2013, restricted stock in the amount of 373,197 and 14,140 shares was granted to employees and non-employee directors, respectively, under the 2004 Stock Incentive Plan. The value of the awards is recorded as unearned compensation within capital in excess of par value in equity and is amortized as compensation expense over the restriction periods.

The Company recorded restricted stock compensation expense of $4.9 million and $20.8 million for the three and nine months ended September 30, 2013, respectively, and $5.0 million and $14.9 million for the three and nine months ended September 30, 2012, respectively.

During the fourth quarter of 2012, the Company waived the forfeiture provision associated with future restricted stock grants made to certain retiring Named Executive Officers. The expense of $20.8 million for the nine months ended September 30, 2013 includes $5.5 million of expense related to the grant of restricted stock awards to these Named Executive Officers.

A summary of the Company's restricted stock activity for the nine months ended September 30, 2013 is as follows:

	Shares subject to restriction (thousands)	Weighted average price
Outstanding at December 31, 2012	1,032	$58.77
Granted	372	$75.41
Vested	(331)	$47.69
Forfeited	(19)	$68.14
Outstanding at March 31, 2013	1,054	$67.71
Granted	15	$75.32
Vested	(65)	$72.93
Forfeited	(12)	$75.68
Outstanding at June 30, 2013	992	$67.37
Granted	—	$—
Vested	(6)	$42.23
Forfeited	(21)	$75.56
Outstanding at September 30, 2013	965	$67.36

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(13) Accumulated Other Comprehensive (Loss) Income

The following table summarizes the activity within accumulated other comprehensive (loss) income during the nine months ended September 30, 2013:

(millions of dollars)	Foreign currency translation adjustments	Hedge instruments	Defined benefit postretirement plans	Other	Total
Beginning Balance, December 31, 2012	$140.8	$(37.2)	$(225.8)	$0.9	$(121.3)
Comprehensive (loss) income before reclassifications	4.7	12.1	1.4	0.5	18.7
Income taxes associated with comprehensive (loss) income before reclassifications	—	(8.5)	—	—	(8.5)
Reclassification from accumulated other comprehensive (loss) income	—	8.7	8.4	—	17.1
Income taxes reclassified into net earnings	—	1.7	1.3	—	3.0
Ending Balance September 30, 2013	$145.5	$(23.2)	$(214.7)	$1.4	$(91.0)

(14) Contingencies

In the normal course of business, the Company is party to various commercial and legal claims, actions and complaints, including matters involving warranty claims, intellectual property claims, general liability and various other risks. It is not possible to predict with certainty whether or not the Company will ultimately be successful in any of these commercial and legal matters or, if not, what the impact might be. The Company's environmental and product liability contingencies are discussed separately below. The Company's management does not expect that an adverse outcome in any of these commercial and legal claims, actions and complaints would have a material adverse effect on the Company's overall results of operations, financial position or cash flows, although it could be material to results of operations in a particular quarter.

Litigation

In January 2006, BorgWarner Diversified Transmission Products Inc. ("DTP"), a subsidiary of the Company, filed a declaratory judgment action in United States District Court, Southern District of Indiana (Indianapolis Division) against the United Automobile, Aerospace, and Agricultural Implements Workers of America (“UAW”) Local No. 287 and Gerald Poor, individually and as the representative of a defendant class. DTP sought the Court's affirmation that DTP did not violate the Labor-Management Relations Act or the Employee Retirement Income Security Act (ERISA) by unilaterally amending certain medical plans effective April 1, 2006 and October 1, 2006, prior to the expiration of the then-current collective bargaining agreements. On September 10, 2008, the Court found that DTP's reservation of the right to make such amendments reducing the level of benefits provided to retirees was limited by its collectively bargained health insurance agreement with the UAW, which did not expire until April 24, 2009. Thus, the amendments were untimely. In 2008, the Company recorded a charge of $4.0 million as a result of the Court's decision.

DTP filed a declaratory judgment action in the United States District Court, Southern District of Indiana (Indianapolis Division) against the UAW Local No. 287 and Jim Barrett and others, individually and as representatives of a defendant class, on February 26, 2009 again seeking the Court's affirmation that DTP did not violate the Labor-Management Relations Act or ERISA by modifying the level of benefits provided retirees to make them comparable to other Company retiree benefit plans after April 24, 2009. Certain retirees, on behalf of themselves and others, filed a mirror-image action in the United States District Court, Eastern District of Michigan (Southern Division) on March 11, 2009, for which a class has been certified. During the last quarter of 2009, the action pending in Indiana was dismissed, while the action in Michigan is continuing. The Company is vigorously defending against the suit. This contingency is subject to many

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uncertainties, therefore based on the information available to date, the Company cannot reasonably estimate the amount or the range of potential loss, if any. A decision on the merits of the suit could be rendered sometime in 2013.

Environmental

The Company and certain of its current and former direct and indirect corporate predecessors, subsidiaries and divisions have been identified by the United States Environmental Protection Agency and certain state environmental agencies and private parties as potentially responsible parties (“PRPs”) at various hazardous waste disposal sites under the Comprehensive Environmental Response, Compensation and Liability Act (“Superfund”) and equivalent state laws and, as such, may presently be liable for the cost of clean-up and other remedial activities at 32 such sites. Responsibility for clean-up and other remedial activities at a Superfund site is typically shared among PRPs based on an allocation formula.

The Company believes that none of these matters, individually or in the aggregate, will have a material adverse effect on its results of operations, financial position or cash flows. Generally, this is because either the estimates of the maximum potential liability at a site are not material or the liability will be shared with other PRPs, although no assurance can be given with respect to the ultimate outcome of any such matter.

Based on information available to the Company (which in most cases includes: an estimate of allocation of liability among PRPs; the probability that other PRPs, many of whom are large, solvent public companies, will fully pay the cost apportioned to them; currently available information from PRPs and/or federal or state environmental agencies concerning the scope of contamination and estimated remediation and consulting costs; and remediation alternatives), the Company has an accrual for indicated environmental liabilities of $4.7 million and $3.9 million at September 30, 2013 and at December 31, 2012, respectively. The Company expects to pay out substantially all of the amounts accrued for environmental liability over the next five years.

In connection with the sale of Kuhlman Electric Corporation (“Kuhlman Electric”), the Company agreed to indemnify the buyer and Kuhlman Electric for certain environmental liabilities, then unknown to the Company, relating to certain operations of Kuhlman Electric that pre-date the Company's 1999 acquisition of Kuhlman Electric. The Company previously settled or obtained dismissals of various lawsuits that were filed against Kuhlman Electric and others, including the Company, on behalf of plaintiffs alleging personal injury relating to alleged environmental contamination at its Crystal Springs, Mississippi plant. The Company filed a lawsuit against Kuhlman Electric and a related entity challenging the validity of the indemnity and the defendants filed counterclaims and a related lawsuit. In addition, two lawsuits by plaintiffs alleging environmental contamination relating to Kuhlman Electric's Crystal Springs plant are still pending and the Company may in the future become subject to further legal proceedings.

Product Liability

Like many other industrial companies who have historically operated in the U.S., the Company (or parties the Company is obligated to indemnify) continues to be named as one of many defendants in asbestos-related personal injury actions. We believe that the Company's involvement is limited because, in general, these claims relate to a few types of automotive friction products that were manufactured many years ago and contained encapsulated asbestos. The nature of the fibers, the encapsulation and the manner of use lead the Company to believe that these products are highly unlikely to cause harm. As of both September 30, 2013 and December 31, 2012, the Company had approximately 16,000 pending asbestos-related product liability claims, respectively. Of the approximately 16,000 outstanding claims at September 30, 2013, approximately half were pending in jurisdictions that have undergone significant tort and judicial reform activities subsequent to the filing of these claims.

The Company's policy is to vigorously defend against these lawsuits and the Company has been successful in obtaining dismissal of many claims without any payment. The Company expects that the vast

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majority of the pending asbestos-related product liability claims where it is a defendant (or has an obligation to indemnify a defendant) will result in no payment being made by the Company or its insurers. In 2013, of the approximately 1,200 claims resolved, 217 (18%) resulted in payment being made to a claimant by or on behalf of the Company. In the full year of 2012, of the approximately 2,400 claims resolved, 308 (13%) resulted in any payment being made to a claimant by or on behalf of the Company.

Prior to June 2004, the settlement and defense costs associated with all claims were paid by the Company's primary layer insurance carriers under a series of funding arrangements. In addition to the primary insurance available for asbestos-related claims, the Company has substantial excess insurance coverage available for potential future asbestos-related product claims. In June 2004, primary layer insurance carriers notified the Company of the alleged exhaustion of their policy limits.

A declaratory judgment action was filed in January 2004 in the Circuit Court of Cook County, Illinois by Continental Casualty Company and related companies against the Company and certain of its historical general liability insurers. The court has issued a number of interim rulings and discovery is continuing. The Company has entered into settlement agreements with some of its insurance carriers, resolving their coverage disputes by agreeing to pay specified amounts to the Company. The Company is vigorously pursuing the litigation against the remaining insurers.

In August 2013, the Los Angeles Superior Court entered a jury verdict against the Company in an asbestos-related personal injury action with damages of $35.0 million, $32.5 million of which was non-compensatory and will not be recoverable through insurance if the verdict is upheld. The Company intends to vigorously defend against this action and to appeal the verdict. The Company cannot predict the outcome of this pending litigation and therefore cannot reasonably estimate the amount of possible loss, if any, that could result from this action.
Although it is impossible to predict the outcome of pending or future claims or the impact of tort reform legislation that may be enacted at the state or federal levels, due to the encapsulated nature of the products, the Company's experience in vigorously defending and resolving claims in the past, and the Company's significant insurance coverage with solvent carriers as of the date of this filing, management does not believe that asbestos-related product liability claims are likely to have a material adverse effect on the Company's results of operations, financial position or cash flows.

To date, the Company has paid and accrued $264.6 million in defense and indemnity in advance of insurers' reimbursement and has received $124.8 million in cash and notes from insurers. The net balance of $139.8 million, is expected to be fully recovered, of which approximately $20.0 million is expected to be recovered within one year. Timing of recovery is dependent on final resolution of the declaratory judgment action referred to above or additional negotiated settlements. At December 31, 2012, insurers owed $111.0 million in association with these claims.

In addition to the $139.8 million net balance relating to past settlements and defense costs, the Company has estimated a liability of $109.0 million for claims asserted, but not yet resolved and their related defense costs at September 30, 2013. The Company also has a related asset of $109.0 million to recognize proceeds from the insurance carriers, which is expected to be fully recovered. Receipt of these proceeds is not expected prior to the resolution of the declaratory judgment action referred to above, which, more-likely-than-not, will occur subsequent to September 30, 2014. At December 31, 2012, the comparable value of the accrued liability and associated insurance asset was $85.6 million.

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The amounts recorded in the Condensed Consolidated Balance Sheets related to the estimated future settlement of existing claims are as follows:

(millions of dollars)	September 30, 2013	December 31, 2012
Assets:		
Prepayments and other current assets	$—	$—
Other non-current assets	109.0	85.6
Total insurance assets	$109.0	$85.6
Liabilities:		
Accounts payable and accrued expenses	$44.1	$36.5
Other non-current liabilities	64.9	49.1
Total accrued liabilities	$109.0	$85.6

The 2013 increase in the accrued liability and associated insurance asset is primarily due to an expected higher rate of claim settlement based on recent litigation claim activity.

The Company cannot reasonably estimate possible losses, if any, in excess of those for which it has accrued, because it cannot predict how many additional claims may be brought against the Company (or parties the Company has an obligation to indemnify) in the future, the allegations in such claims, the possible outcomes, or the impact of tort reform legislation that may be enacted at the state or federal levels.

(15) Earnings Per Share

The Company presents both basic and diluted earnings per share of common stock ("EPS") amounts. Basic EPS is calculated by dividing net earnings attributable to BorgWarner Inc. by the weighted average shares of common stock outstanding during the reporting period. Diluted EPS is calculated by dividing net earnings attributable to BorgWarner Inc. by the weighted average shares of common stock and common equivalent stock outstanding during the reporting period.

The dilutive impact of stock-based compensation is calculated using the treasury stock method. The treasury stock method assumes that the Company uses the assumed proceeds from the exercise of awards to repurchase common stock at the average market price during the period. The assumed proceeds under the treasury stock method include the purchase price that the grantee will pay in the future, compensation cost for future service that the Company has not yet recognized and any windfall/(shortfall) tax benefits that would be credited/(debited) to capital in excess of par value when the award generates a tax deduction. Options are only dilutive when the average market price of the underlying common stock exceeds the exercise price of the options.

Prior to the April 2012 settlement of the Company's 3.50% convertible senior notes, the potential common shares associated with these notes were reflected in diluted EPS using the "if-converted" method. Under this method, if dilutive, the common shares were assumed issued as of the beginning of the reporting period and included in calculating diluted EPS. In addition, if dilutive, interest expense, net of tax, related to the convertible senior notes was added back to the numerator in calculating diluted EPS.

In conjunction with the convertible senior note offering, the Company entered into a bond hedge overlay, including both call options and warrants. Prior to the April 2012 settlement of the call option portion of the bond hedge overlay, the call options were anti-dilutive if the Company's weighted average share price exceeded $32.82 per share. Prior to third and fourth quarter 2012 settlements of the warrant portion of the bond hedge overlay, the warrants were dilutive to the Company's earnings if the Company's weighted-average share price exceeded $38.61 per share.

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The following table reconciles the numerators and denominators used to calculate basic and diluted earnings per share of common stock:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions, except per share amounts)	2013	2012	2013	2012
Basic earnings per share:				
Net earnings attributable to BorgWarner Inc.	$166.8	$101.1	$482.9	$379.7
Weighted average shares of common stock outstanding	113.819	114.299	114.584	111.619
Basic earnings per share of common stock	$1.47	$0.88	$4.21	$3.40
Diluted earnings per share:				
Net earnings attributable to BorgWarner Inc.	$166.8	$101.1	$482.9	$379.7
Adjustment for net interest expense on convertible notes	—	—	—	5.8
Diluted net earnings attributable to BorgWarner Inc.	$166.8	$101.1	$482.9	$385.5
Weighted average shares of common stock outstanding	113.819	114.299	114.584	111.619
Effect of 3.50% convertible senior notes	—	—	—	4.429
Effect of warrant	—	2.208	—	4.507
Effect of stock-based compensation	1.419	1.992	1.384	2.016
Total dilutive effect on weighted average shares of common stock outstanding	1.419	4.200	1.384	10.952
Weighted average shares of common stock outstanding including dilutive shares	115.238	118.499	115.968	122.571
Diluted earnings per share of common stock	$1.45	$0.85	$4.16	$3.15
Total anti-dilutive shares:				
Call options	—	—	—	2.586

(16) Reporting Segments

The Company's business is comprised of two reporting segments: Engine and Drivetrain. These segments are strategic business groups, which are managed separately as each represents a specific grouping of related automotive components and systems.

The Company allocates resources to each segment based upon the projected after-tax return on invested capital ("ROIC") of its business initiatives. ROIC is comprised of Adjusted EBIT after deducting notional taxes compared to the projected average capital investment required. Adjusted EBIT is comprised of earnings before interest, income taxes and noncontrolling interest (“EBIT") adjusted for restructuring, goodwill impairment charges, affiliates' earnings and other items not reflective of on-going operating income or loss.

Adjusted EBIT is the measure of segment income or loss used by the Company. The Company believes Adjusted EBIT is most reflective of the operational profitability or loss of our reporting segments. The following tables show segment information and Adjusted EBIT for the Company's reporting segments.

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Net Sales by Reporting Segment

(millions of dollars)	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Engine	$1,210.3	$1,168.0	$3,756.1	$3,745.8
Drivetrain	604.0	534.4	1,818.9	1,739.7
Inter-segment eliminations	(8.1)	(7.2)	(23.8)	(21.4)
Net sales	$1,806.2	$1,695.2	$5,551.2	$5,464.1

Adjusted Earnings Before Interest, Income Taxes and Noncontrolling Interest (“Adjusted EBIT”)

(millions of dollars)	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Engine	$195.5	$184.1	$618.1	$604.4
Drivetrain	65.9	44.1	181.7	159.9
Adjusted EBIT	261.4	228.2	799.8	764.3
Program termination agreement	—	—	11.3	—
Retirement related obligations	—	—	5.9	—
Loss from disposal activities	—	1.8	—	39.7
Restructuring expense	—	27.4	—	27.4
Corporate, including equity in affiliates' earnings and stock-based compensation	25.4	24.9	83.9	82.2
Interest income	(1.3)	(1.0)	(3.3)	(3.7)
Interest expense and finance charges	8.1	5.0	26.6	32.7
Earnings before income taxes and noncontrolling interest	229.2	170.1	675.4	586.0
Provision for income taxes	56.3	64.2	173.8	190.2
Net earnings	172.9	105.9	501.6	395.8
Net earnings attributable to the noncontrolling interest, net of tax	6.1	4.8	18.7	16.1
Net earnings attributable to BorgWarner Inc.	$166.8	$101.1	$482.9	$379.7

Total Assets

(millions of dollars)	September 30, 2013	December 31, 2012
Engine	$3,514.0	$3,299.2
Drivetrain	1,826.7	1,652.2
Total	5,340.7	4,951.4
Corporate (a)	1,623.6	1,449.4
Total assets	$6,964.3	$6,400.8

(a) Corporate assets include investments and advances and deferred income taxes.

(17) New Accounting Pronouncements

In July 2013, the Financial Accounting Standards Board amended ASC Topic 740, "Income Taxes," requiring an unrecognized tax benefit, or a portion of an unrecognized tax benefit, to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward. This guidance is effective prospectively for interim and annual periods beginning after December 15, 2013. The Company anticipates the adoption of this guidance will not have a material impact to its Consolidated Financial

Statements.

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Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations
INTRODUCTION

BorgWarner Inc. and Consolidated Subsidiaries (the “Company”) is a leading global supplier of highly engineered automotive systems and components primarily for powertrain applications. Our products help improve vehicle performance, fuel efficiency, stability and air quality. These products are manufactured and sold worldwide, primarily to original equipment manufacturers (“OEMs”) of light vehicles (passenger cars, sport-utility vehicles ("SUVs"), vans and light trucks). The Company's products are also sold to other OEMs of commercial vehicles (medium-duty trucks, heavy-duty trucks and buses) and off-highway vehicles (agricultural and construction machinery and marine applications). We also manufacture and sell our products to certain Tier One vehicle systems suppliers and into the aftermarket for light, commercial and off-highway vehicles. The Company operates manufacturing facilities serving customers in the Americas, Europe and Asia and is an original equipment supplier to every major automotive OEM in the world.

The Company's products fall into two reporting segments: Engine and Drivetrain. The Engine segment's products include turbochargers, timing devices and chain products, emissions systems, thermal systems, diesel coldstart, gasoline ignition technology and cabin heaters. The Drivetrain segment's products include transmission components and systems and all-wheel drive torque management systems.

RESULTS OF OPERATIONS

Three Months Ended September 30, 2013 vs. Three Months Ended September 30, 2012

Net sales for the three months ended September 30, 2013 totaled $1,806.2 million, a 6.5% increase from the three months ended September 30, 2012. Excluding the impact of 2012 dispositions and strengthening foreign currencies, primarily the Euro, net sales increased approximately 6%. Estimated light vehicle production was up 4% worldwide, primarily driven by a 6% increase in North America, a 4% increase in Asia and a 2% increase in Europe from the three months ended September 30, 2012.

Cost of sales as a percentage of net sales decreased to 79.0% in the three months ended September 30, 2013 from 79.7% in the three months ended September 30, 2012. Gross profit and gross margin were $379.6 million and 21.0% in the three months ended September 30, 2013 compared to $343.7 million and 20.3% in the three months ended September 30, 2012. The Company's material cost of sales was approximately 50% of net sales in both the three months ended September 30, 2013 and 2012. The Company's remaining cost to convert raw material to finished product (conversion cost) decreased compared to the three months ended September 30, 2012.

Selling, general and administrative ("SG&A") expenses for the three months ended September 30, 2013 increased $6.7 million to $157.7 million from $151.0 million in the three months ended September 30, 2012. SG&A as a percentage of was 8.7% in the three months ended September 30, 2013 down from 8.9% in the three months ended September 30, 2012. Research and Development ("R&D") expenses, which are included in SG&A expenses, increased $7.4 million to $71.8 million from $64.4 million as compared to the three months ended September 30, 2012. As a percentage of net sales, R&D expenses were 4.0% and 3.8% in the three months ended September 30, 2013 and 2012, respectively. Our continued investment in a number of cross-business R&D programs, as well as other key programs, is necessary for the Company’s short- and long-term growth.

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Other expense of $29.7 million for the three months ended September 30, 2012 includes $1.8 million of expense primarily related to working capital adjustments associated with the completion of the Company's sale of its spark plug business and $27.4 million of restructuring expense primarily associated with the disposal and future requirements of BERU's on-going business, which included $16.9 million of employee termination benefits and $10.5 million of other charges, primarily related to the write-down of certain assets.

Equity in affiliates’ earnings of $10.4 million decreased $0.7 million as compared with the three months ended September 30, 2012 primarily due to lower earnings from the Company's 50% interest in NSK-Warner.

Interest expense and finance charges of $8.1 million increased $3.1 million as compared with the three months ended September 30, 2012 primarily due to income from the Company's cross-currency swaps in the third quarter of 2012.

At September 30, 2013, the Company estimated its U.S. GAAP effective tax rate to be approximately 26% for the year ending December 31, 2013, which includes tax benefits of $3.8 million and $2.1 million related to the program termination agreement and retirement related obligations discussed in the Other (Income) Expense footnote. This rate also includes a net tax benefit of $7.3 million, which is comprised of tax benefits of $6.6 million related to the extension of the federal research and development credit and other international tax provisions resulting from the retroactive impact of U.S. legislation enacted in January 2013, $3.1 million related to 2012 provision to return adjustments and $2.5 million related to the reversal of certain deferred tax asset valuation allowances, partially offset by a $4.9 million tax expense related to a comprehensive income adjustment. Excluding the impact of these non-comparable items, the Company has estimated its annual effective tax rate associated with ongoing operations to be approximately 27% for the year ending December 31, 2013.

At September 30, 2012, the Company estimated its U.S. GAAP effective tax rate to be approximately 31% for the year ending December 31, 2012. This rate included net tax expense of $3.5 million associated with the loss from disposal activities and restructuring expense recorded during the third quarter of 2012. The $3.5 million net expense is comprised of $11.2 million tax expense resulting from the completion of the disposal, partially offset by a tax benefit of $7.7 million associated with the restructuring expense. For the nine months ended September 30, 2012, the net tax benefit associated with the loss from disposal activities and restructuring expense was $2.0 million. The 31% U.S. GAAP effective tax rate also includes additional tax expense of $15.9 million resulting from other tax adjustments. These other tax adjustments include $8.2 million of tax expense primarily resulting from the settlement of certain tax audits and $7.7 million of tax expense associated with the Company's second quarter 2012 decision to change its cash repatriation assertion for some of its foreign subsidiaries. Excluding the impact of these non-comparable items, the Company estimated its annual effective tax rate associated with ongoing operations to be approximately 27% for the year ending December 31, 2012.

The Company’s earnings per diluted share were $1.45 and $0.85 for the three months ended September 30, 2013 and 2012, respectively. The Company believes the following table is useful in highlighting non-comparable items that impacted its earnings per diluted share.

	Three Months Ended September 30, 2013	2012
Non-comparable items:		
Loss from disposal activities	$—	$(0.11)
Restructuring expense	—	(0.17)
Tax adjustments	0.05	(0.06)
Total impact of non-comparable items per share — diluted	$0.05	$(0.34)

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Nine Months Ended September 30, 2013 vs. Nine Months Ended September 30, 2012

Net sales for the nine months ended September 30, 2013 totaled $5,551.2 million, a 1.6% increase from the nine months ended September 30, 2012. Excluding the impact of 2012 dispositions and strengthening foreign currencies, primarily the Euro, net sales increased approximately 2%. Estimated light vehicle production was up 2% worldwide, primarily driven by a 5% increase in North America and a 3% increase in Asia, partially offset by a 1% decrease in Europe from the nine months ended September 30, 2012.

Cost of sales as a percentage of net sales decreased to 79.3% in the nine months ended September 30, 2013 from 79.5% in the nine months ended September 30, 2012. Gross profit and gross margin were $1,150.9 million and 20.7% in the nine months ended September 30, 2013 compared to $1,122.7 million and 20.5% in the nine months ended September 30, 2012. The Company's material cost of sales was approximately 50% of net sales in both the nine months ended September 30, 2013 and 2012. The Company's remaining cost to convert raw material to finished product (conversion cost) decreased compared to the nine months ended September 30, 2012.

SG&A expenses for the nine months ended September 30, 2013 decreased $0.5 million to $472.6 million from $473.1 million and decreased as a percentage of net sales to 8.5% from 8.7% in the nine months ended September 30, 2012. The decrease in SG&A is primarily due to lower stock-based compensation expense during the nine months ended September 30, 2013. R&D expenses, which are included in SG&A expenses, increased $17.5 million to $216.2 million from $198.7 million as compared to the nine months ended September 30, 2012. As a percentage of net sales, R&D expenses were 3.9% and 3.6% in the nine months ended September 30, 2013 and 2012, respectively. Our continued investment in a number of cross-business R&D programs, as well as other key programs, is necessary for the Company’s short- and long-term growth.

Other expense of $10.8 million for the nine months ended September 30, 2013 is primarily related to an $11.3 million expense associated with a program termination agreement and a $5.9 million retirement related obligation related to a first quarter 2013 grant of restricted stock awards to certain retiring Named Executive Officers, which resulted from the Company's fourth quarter 2012 decision to waive the forfeiture provision associated with future restricted stock grants made to these Named Executive Officers. These items were partially offset by gains on asset disposals.

Other expense of $67.4 million for the nine months ended September 30, 2012 includes a $39.7 million loss from disposal activities as a result of the Company's sale of its spark plug business to Federal-Mogul Corporation. This loss primarily relates to purchase price accounting adjustments originally recorded in the Engine segment and related to the BERU acquisition. During the third quarter of 2012, the Company recorded $27.4 million of restructuring expense primarily associated with the disposal and future requirements of BERU's on-going business, which included $16.9 million of employee termination benefits and $10.5 million of other charges, primarily related to the write-down of certain assets.

Equity in affiliates’ earnings was $31.2 million and $32.8 million in the nine months ended September 30, 2013 and 2012, respectively.

Interest expense and finance charges of $26.6 million decreased $6.1 million as compared with the nine months ended September 30, 2012 primarily due to the April 2012 settlement of the Company's convertible senior notes.

At September 30, 2013, the Company estimated its U.S. GAAP effective tax rate to be approximately 26% for the year ending December 31, 2013, which includes tax benefits of $3.8 million and $2.1 million related to the program termination agreement and retirement related obligations discussed in the Other (Income) Expense footnote. This rate also includes a net tax benefit of $7.3 million, which is comprised of

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tax benefits of $6.6 million related to the extension of the federal research and development credit and other international tax provisions resulting from the retroactive impact of U.S. legislation enacted in January 2013, $3.1 million related to 2012 provision to return adjustments and $2.5 million related to the reversal of certain deferred tax asset valuation allowances, partially offset by a $4.9 million tax expense related to a comprehensive income adjustment. Excluding the impact of these non-comparable items, the Company has estimated its annual effective tax rate associated with ongoing operations to be approximately 27% for the year ending December 31, 2013.

At September 30, 2012, the Company estimated its U.S. GAAP effective tax rate to be approximately 31% for the year ending December 31, 2012. This rate includes net tax expense of $3.5 million associated with the loss from disposal activities and restructuring expense recorded during the third quarter of 2012. The $3.5 million net expense is comprised of $11.2 million tax expense resulting from the completion of the disposal, partially offset by a tax benefit of $7.7 million associated with the restructuring expense. For the nine months ended September 30, 2012, the net tax benefit associated with the loss from disposal activities and restructuring expense was $2.0 million. The 31% U.S. GAAP effective tax rate also includes additional tax expense of $15.9 million resulting from other tax adjustments. These other tax adjustments include $8.2 million of tax expense primarily resulting from the settlement of certain tax audits and $7.7 million of tax expense associated with the Company's second quarter 2012 decision to change its cash repatriation assertion for some of its foreign subsidiaries. Excluding the impact of these non-comparable items, the Company estimated its annual effective tax rate associated with ongoing operations to be approximately 27% for the year ending December 31, 2012.

The Company’s earnings per diluted share were $4.16 and $3.15 for the nine months ended September 30, 2013 and 2012, respectively. The Company believes the following table is useful in highlighting non-comparable items that impacted its earnings per diluted share.

	Nine Months Ended September 30,	
	2013	2012
Non-comparable items:		
Program termination agreement	$(0.06)	$—
Retirement related obligations	(0.03)	—
Loss from disposal activities	—	(0.37)
Restructuring expense	—	(0.17)
Tax adjustments	0.06	(0.13)
Total impact of non-comparable items per share — diluted	$(0.03)	$(0.67)

Reporting Segments

The Company's business is comprised of two reporting segments: Engine and Drivetrain. These segments are strategic business groups, which are managed separately as each represents a specific grouping of related automotive components and systems.

The Company allocates resources to each segment based upon the projected after-tax return on invested capital ("ROIC") of its business initiatives. ROIC is comprised of Adjusted EBIT after deducting notional taxes compared to the projected average capital investment required. Adjusted EBIT is comprised of earnings before interest, income taxes and noncontrolling interest (“EBIT") adjusted for restructuring, goodwill impairment charges, affiliates' earnings and other items not reflective of on-going operating income or loss.

Adjusted EBIT is the measure of segment income or loss used by the Company. The Company believes Adjusted EBIT is most reflective of the operational profitability or loss of our reporting segments. The following tables show segment information and Adjusted EBIT for the Company's reporting segments.

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Net Sales by Reporting Segment

	Three Months Ended September 30,		Nine Months Ended September 30,	
(millions of dollars)	2013	2012	2013	2012
Engine	$1,210.3	$1,168.0	$3,756.1	$3,745.8
Drivetrain	604.0	534.4	1,818.9	1,739.7
Inter-segment eliminations	(8.1)	(7.2)	(23.8)	(21.4)
Net sales	$1,806.2	$1,695.2	$5,551.2	$5,464.1

Adjusted Earnings Before Interest, Income Taxes and Noncontrolling Interest (“Adjusted EBIT”)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(millions of dollars)	2013	2012	2013	2012
Engine	$195.5	$184.1	$618.1	$604.4
Drivetrain	65.9	44.1	181.7	159.9
Adjusted EBIT	261.4	228.2	799.8	764.3
Program termination agreement	—	—	11.3	—
Retirement related obligations	—	—	5.9	—
Loss from disposal activities	—	1.8	—	39.7
Restructuring expense	—	27.4	—	27.4
Corporate, including equity in affiliates' earnings and stock-based compensation	25.4	24.9	83.9	82.2
Interest income	(1.3)	(1.0)	(3.3)	(3.7)
Interest expense and finance charges	8.1	5.0	26.6	32.7
Earnings before income taxes and noncontrolling interest	229.2	170.1	675.4	586.0
Provision for income taxes	56.3	64.2	173.8	190.2
Net earnings	172.9	105.9	501.6	395.8
Net earnings attributable to the noncontrolling interest, net of tax	6.1	4.8	18.7	16.1
Net earnings attributable to BorgWarner Inc.	$166.8	$101.1	$482.9	$379.7

Three Months Ended September 30, 2013 vs. Three Months Ended September 30, 2012

The Engine segment net sales increased $42.3 million, or 3.6%, from the three months ended September 30, 2012. Excluding the impact of 2012 dispositions and strengthening foreign currencies, primarily the Euro, net sales increased approximately 4% primarily due to higher sales of turbochargers variable cam timing devices and exhaust gas recirculation coolers around the world. The Engine segment Adjusted EBIT margin was 16.2% in the three months ended September 30, 2013 up from 15.8% in the three months ended September 30, 2012.

The Drivetrain segment net sales increased $69.6 million, or 13.0%, from the three months ended September 30, 2012. Excluding the impact of strengthening foreign currencies, primarily the Euro, net sales increased approximately 10% primarily due to higher sales of all-wheel drive systems and transmission components in North America and Korea. The Drivetrain segment Adjusted EBIT margin was 10.9% in the three months ended September 30, 2013 up from 8.3% in the three months ended September 30, 2012.

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Nine Months Ended September 30, 2013 vs. Nine Months Ended September 30, 2012

The Engine segment net sales increased $10.3 million, or 0.3%, from the nine months ended September 30, 2012. Excluding the impact of 2012 dispositions and strengthening foreign currencies, primarily the Euro, net sales increased approximately 2% from the nine months ended September 30, 2012. Higher sales of variable cam timing systems in Japan, turbochargers, exhaust gas recirculation coolers and engine timing systems in China and turbochargers in Brazil were partially offset by lower light vehicle production in Europe. The Engine segment Adjusted EBIT margin was 16.5% in the nine months ended September 30, 2013 up from 16.1% in the nine months ended September 30, 2012.

The Drivetrain segment net sales increased $79.2 million, or 4.6%, from the nine months ended September 30, 2012. Excluding the impact of strengthening foreign currencies, primarily the Euro, net sales increased approximately 3% from the nine months ended September 30, 2012. Higher sales of all-wheel drive systems and transmission components in North America and Korea, were partially offset by lower light vehicle production in Europe. The Drivetrain segment Adjusted EBIT margin was 10.0% in the nine months ended September 30, 2013 up from 9.2% in the nine months ended September 30, 2012. The Company continues to review the consistency of the Drivetrain segment's financial performance.

Outlook for 2013

Based on uncertain global economic conditions our outlook for the remainder of 2013 is cautious. The Company expects global production volumes to be slightly higher in 2013 compared with 2012. In Europe, our largest market, we expect production volumes to decline in 2013 compared with 2012. However, we expect that higher adoption rates of BorgWarner products around the world will result in sales growth for the Company in 2013.

The Company maintains a positive long-term outlook for its global business and is committed to new product development and strategic capital investments to enhance its product leadership strategy. The trends that are driving our long-term growth are expected to continue, including the growth of direct injection diesel and gasoline engines worldwide, the increased adoption of automated transmissions in Europe and Asia-Pacific, and the move to variable cam and chain engine timing systems in Europe and Asia-Pacific.

FINANCIAL CONDITION AND LIQUIDITY

The Company maintains various liquidity sources including cash and cash equivalents and the unused portion of our multi-currency revolving credit agreement. At September 30, 2013, the Company had $920.4 million of cash, including $916.8 million of cash held by our subsidiaries outside of the United States. Cash held by these subsidiaries is used to fund foreign operational activities and future investments, including acquisitions. The vast majority of cash held outside the United States is available for repatriation, however, doing so could result in increased foreign and U.S. federal, state and local income taxes. A deferred tax liability has been recorded for the portion of these funds anticipated to be repatriated to the United States.

The Company's multi-currency revolving credit facility includes a feature that allows the Company's borrowings to be increased to $1 billion. Utilizing this feature, on April 12, 2013, the Company increased its multi-currency revolving credit facility from $650 million to $750 million. The credit facility provides for borrowings through June 30, 2016 and is guaranteed by the Company's material domestic subsidiaries. The credit facility has two key financial covenants, a debt compared to EBITDA (“Earnings Before Interest, Taxes, Depreciation and Amortization”) test and an interest coverage test. The Company was in compliance with all covenants at September 30, 2013 and expects to remain compliant in future periods. At September 30, 2013 and December 31, 2012, the Company had outstanding borrowings of $320.0 million and $140.0 million, respectively, under this facility.

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On October 18, 2013 and July 24, 2013, the Company's Board of Directors declared a quarterly cash dividend of $0.25 per share of common stock. The fourth quarter dividend is payable on November 15, 2013 to shareholders of record on November 1, 2013. The third quarter dividend was paid on August 15, 2013 to shareholders of record on August 5, 2013.

The Company's debt net of cash to capital ratio was 9.3% at September 30, 2013 versus 10.0% at December 31, 2012.

In addition to the credit facility, the Company's universal shelf registration with the Securities and Exchange Commission has an unlimited amount of various debt and equity instruments which could be issued.

From a credit quality perspective, the Company has a credit rating of Baa2 from Moody's and BBB+ from both Standard & Poor’s and Fitch Ratings. The current outlook from Moody's, Standard & Poor’s and Fitch Ratings is stable. None of the Company’s debt agreements require accelerated repayment in the event of a downgrade in credit ratings.

Net cash provided by operating activities decreased $27.8 million to $514.8 million in the first nine months of 2013 from $542.6 million in the first nine months of 2012. This decrease primarily reflects a reduction in dividends received from affiliates and higher cash paid for income taxes, partially offset by lower stock-based compensation compared with the first nine months of 2012.

Net cash used in investing activities increased $52.8 million to $275.1 million in the first nine months of 2013 from $222.3 million in the first nine months of 2012. This increase is primarily driven by cash received in the third quarter of 2012 from the Company's spark plug business sale.

Net cash used in financing activities increased $8.1 million to $59.2 million in the first nine months of 2013 from $51.1 million in the first nine months of 2012. This increase is primarily driven by a reduction in proceeds from stock option exercises, including the tax benefit and increased payments for treasury stock purchases and dividends, partially offset by increased net borrowings.

We believe that the combination of cash from operations, cash balances, available credit facilities, and the remaining shelf registration capacity will be sufficient to satisfy our cash needs for our current level of operations and our planned operations for the foreseeable future. We will continue to balance our needs for internal growth, external growth, debt reduction and cash conservation.

CONTINGENCIES

In the normal course of business, the Company is party to various commercial and legal claims, actions and complaints, including matters involving warranty claims, intellectual property claims, general liability and various other risks. It is not possible to predict with certainty whether or not the Company will ultimately be successful in any of these commercial and legal matters or, if not, what the impact might be. The Company's environmental and product liability contingencies are discussed separately below. The Company's management does not expect that an adverse outcome in any of these commercial and legal claims, actions and complaints would have a material adverse effect on the Company's overall results of operations, financial position or cash flows, although it could be material to results of operations in a particular quarter.

Litigation

In January 2006, BorgWarner Diversified Transmission Products Inc. ("DTP"), a subsidiary of the Company, filed a declaratory judgment action in United States District Court, Southern District of Indiana (Indianapolis Division) against the United Automobile, Aerospace, and Agricultural Implements Workers of

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America ("UAW") Local No. 287 and Gerald Poor, individually and as the representative of a defendant class. DTP sought the Court's affirmation that DTP did not violate the Labor-Management Relations Act or the Employee Retirement Income Security Act (ERISA) by unilaterally amending certain medical plans effective April 1, 2006 and October 1, 2006, prior to the expiration of the then-current collective bargaining agreements. On September 10, 2008, the Court found that DTP's reservation of the right to make such amendments reducing the level of benefits provided to retirees was limited by its collectively bargained health insurance agreement with the UAW, which did not expire until April 24, 2009. Thus, the amendments were untimely. In 2008, the Company recorded a charge of $4.0 million as a result of the Court's decision.

DTP filed a declaratory judgment action in the United States District Court, Southern District of Indiana (Indianapolis Division) against the UAW Local No. 287 and Jim Barrett and others, individually and as representatives of a defendant class, on February 26, 2009 again seeking the Court's affirmation that DTP did not violate the Labor-Management Relations Act or ERISA by modifying the level of benefits provided retirees to make them comparable to other Company retiree benefit plans after April 24, 2009. Certain retirees, on behalf of themselves and others, filed a mirror-image action in the United States District Court, Eastern District of Michigan (Southern Division) on March 11, 2009, for which a class has been certified. During the last quarter of 2009, the action pending in Indiana was dismissed, while the action in Michigan is continuing. The Company is vigorously defending against the suit. This contingency is subject to many uncertainties, therefore based on the information available to date, the Company cannot reasonably estimate the amount or the range of potential loss, if any. A decision on the merits of the suit could be rendered sometime in 2013.

Environmental

The Company and certain of its current and former direct and indirect corporate predecessors, subsidiaries and divisions have been identified by the United States Environmental Protection Agency and certain state environmental agencies and private parties as potentially responsible parties ("PRPs") at various hazardous waste disposal sites under the Comprehensive Environmental Response, Compensation and Liability Act ("Superfund") and equivalent state laws and, as such, may presently be liable for the cost of clean-up and other remedial activities at 32 such sites. Responsibility for clean-up and other remedial activities at a Superfund site is typically shared among PRPs based on an allocation formula.

The Company believes that none of these matters, individually or in the aggregate, will have a material adverse effect on its results of operations, financial position or cash flows. Generally, this is because either the estimates of the maximum potential liability at a site are not material or the liability will be shared with other PRPs, although no assurance can be given with respect to the ultimate outcome of any such matter.

Based on information available to the Company (which in most cases includes: an estimate of allocation of liability among PRPs; the probability that other PRPs, many of whom are large, solvent public companies, will fully pay the cost apportioned to them; currently available information from PRPs and/or federal or state environmental agencies concerning the scope of contamination and estimated remediation and consulting costs; and remediation alternatives), the Company has an accrual for indicated environmental liabilities of $4.7 million and $3.9 million at September 30, 2013 and at December 31, 2012, respectively. The Company expects to pay out substantially all of the amounts accrued for environmental liability over the next five years.

In connection with the sale of Kuhlman Electric Corporation ("Kuhlman Electric"), the Company agreed to indemnify the buyer and Kuhlman Electric for certain environmental liabilities, then unknown to the Company, relating to certain operations of Kuhlman Electric that pre-date the Company's 1999 acquisition of Kuhlman Electric. The Company previously settled or obtained dismissals of various lawsuits that were filed against Kuhlman Electric and others, including the Company, on behalf of plaintiffs alleging personal injury relating to alleged environmental contamination at its Crystal Springs, Mississippi plant. The Company filed a lawsuit against Kuhlman Electric and a related entity challenging the validity of the indemnity and the defendants filed counterclaims and a related lawsuit. In addition, two lawsuits by plaintiffs alleging

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environmental contamination relating to Kuhlman Electric's Crystal Springs plant are still pending and the Company may in the future become subject to further legal proceedings.

Product Liability

Like many other industrial companies who have historically operated in the U.S., the Company (or parties the Company is obligated to indemnify) continues to be named as one of many defendants in asbestos-related personal injury actions. We believe that the Company's involvement is limited because, in general, these claims relate to a few types of automotive friction products that were manufactured many years ago and contained encapsulated asbestos. The nature of the fibers, the encapsulation and the manner of use lead the Company to believe that these products are highly unlikely to cause harm. As of both September 30, 2013 and December 31, 2012, the Company had approximately 16,000 pending asbestos-related product liability claims, respectively. Of the approximately 16,000 outstanding claims at September 30, 2013, approximately half were pending in jurisdictions that have undergone significant tort and judicial reform activities subsequent to the filing of these claims.

The Company's policy is to vigorously defend against these lawsuits and the Company has been successful in obtaining dismissal of many claims without any payment. The Company expects that the vast majority of the pending asbestos-related product liability claims where it is a defendant (or has an obligation to indemnify a defendant) will result in no payment being made by the Company or its insurers. In 2013, of the approximately 1,200 claims resolved, 217 (18%) resulted in payment being made to a claimant by or on behalf of the Company. In the full year of 2012, of the approximately 2,400 claims resolved, 308 (13%) resulted in any payment being made to a claimant by or on behalf of the Company.

Prior to June 2004, the settlement and defense costs associated with all claims were paid by the Company's primary layer insurance carriers under a series of funding arrangements. In addition to the primary insurance available for asbestos-related claims, the Company has substantial excess insurance coverage available for potential future asbestos-related product claims. In June 2004, primary layer insurance carriers notified the Company of the alleged exhaustion of their policy limits.

A declaratory judgment action was filed in January 2004 in the Circuit Court of Cook County, Illinois by Continental Casualty Company and related companies against the Company and certain of its historical general liability insurers. The court has issued a number of interim rulings and discovery is continuing. The Company has entered into settlement agreements with some of its insurance carriers, resolving their coverage disputes by agreeing to pay specified amounts to the Company. The Company is vigorously pursuing the litigation against the remaining insurers.

In August 2013, the Los Angeles Superior Court entered a jury verdict against the Company in an asbestos-related personal injury action with damages of $35.0 million, $32.5 million of which was non-compensatory and will not be recoverable through insurance if the verdict is upheld. The Company intends to vigorously defend against this action and to appeal the verdict. The Company cannot predict the outcome of this pending litigation and therefore cannot reasonably estimate the amount of possible loss, if any, that could result from this action.

Although it is impossible to predict the outcome of pending or future claims or the impact of tort reform legislation that may be enacted at the state or federal levels, due to the encapsulated nature of the products, the Company's experience in vigorously defending and resolving claims in the past, and the Company's significant insurance coverage with solvent carriers as of the date of this filing, management does not believe that asbestos-related product liability claims are likely to have a material adverse effect on the Company's results of operations, financial position or cash flows.

To date, the Company has paid and accrued $264.6 million in defense and indemnity in advance of insurers' reimbursement and has received $124.8 million in cash and notes from insurers. The net balance

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of $139.8 million, is expected to be fully recovered, of which approximately $20.0 million is expected to be recovered within one year. Timing of recovery is dependent on final resolution of the declaratory judgment action referred to above or additional negotiated settlements. At December 31, 2012, insurers owed $111.0 million in association with these claims.

In addition to the $139.8 million net balance relating to past settlements and defense costs, the Company has estimated a liability of $109.0 million for claims asserted, but not yet resolved and their related defense costs at September 30, 2013. The Company also has a related asset of $109.0 million to recognize proceeds from the insurance carriers, which is expected to be fully recovered. Receipt of these proceeds is not expected prior to the resolution of the declaratory judgment action referred to above, which, more-likely-than-not, will occur subsequent to June 30, 2014. At December 31, 2012, the comparable value of the accrued liability and associated insurance asset was $85.6 million.

The amounts recorded in the Condensed Consolidated Balance Sheets related to the estimated future settlement of existing claims are as follows:

(millions of dollars)	September 30, 2013	December 31, 2012
Assets:		
Prepayments and other current assets	$—	$—
Other non-current assets	109.0	85.6
Total insurance assets	$109.0	$85.6
Liabilities:		
Accounts payable and accrued expenses	$44.1	$36.5
Other non-current liabilities	64.9	49.1
Total accrued liabilities	$109.0	$85.6

The 2013 increase in the accrued liability and associated insurance asset is primarily due to an expected higher rate of claim settlement based on recent litigation claim activity.

The Company cannot reasonably estimate possible losses, if any, in excess of those for which it has accrued, because it cannot predict how many additional claims may be brought against the Company (or parties the Company has an obligation to indemnify) in the future, the allegations in such claims, the possible outcomes, or the impact of tort reform legislation that may be enacted at the state or federal levels.

New Accounting Pronouncements

In July 2013, the Financial Accounting Standards Board amended ASC Topic 740, "Income Taxes," requiring an unrecognized tax benefit, or a portion of an unrecognized tax benefit, to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward. This guidance is effective prospectively for interim and annual periods beginning after December 15, 2013. The Company anticipates the adoption of this guidance will not have a material impact to its Consolidated Financial Statements.

CAUTIONARY STATEMENTS FOR FORWARD-LOOKING STATEMENTS

Statements contained in this Form 10-Q (including Management's Discussion and Analysis of Financial Condition and Results of Operations) may contain forward-looking statements as contemplated by the 1995 Private Securities Litigation Reform Act (the “Act”) that are based on management's current outlook, expectations, estimates and projections. Words such as "anticipates," "believes," "continues," "could," "designed," "effect," "estimates," "evaluates," "expects," "forecasts," "goal," "initiative," "intends," "outlook," "plans," "potential," "project," "pursue," "seek," "should," "target," "when," "would," variations of such words

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and similar expressions are intended to identify such forward-looking statements. All statements, other than statements of historical fact contained or incorporated by reference in this Form 10-Q, that we expect or anticipate will or may occur in the future regarding our financial position, business strategy and measures to implement that strategy, including changes to operations, competitive strengths, goals, expansion and growth of our business and operations, plans, references to future success and other such matters, are forward-looking statements. Accounting estimates, such as those described under the heading "Critical Accounting Policies" in Item 7 of our most recent Annual Report on Form 10-K, are inherently forward-looking. These statements are based on assumptions and analysis made by us in light of our experience and our perception of historical trends, current conditions and expected future developments, as well as other factors we believe are appropriate in the circumstances. Forward-looking statements are not guarantees of performance and the Company's actual results may differ materially from those expressed, projected or implied in or by the forward-looking statements.

You should not place undue reliance on these forward-looking statements, which speak only as of the date of this Quarterly Report. Forward-looking statements are subject to risks and uncertainties, many of which are difficult to predict and generally beyond our control. Such risks and uncertainties include: fluctuations in domestic or foreign vehicle production, the continued use by original equipment manufacturers of outside suppliers, fluctuations in demand for vehicles containing our products, changes in general economic conditions, as well as the other risks noted under Item 1A, “Risk Factors,” of our Annual Report on Form 10-K and in other reports that we file with the Securities and Exchange Commission. We do not undertake any obligation to update or announce publicly any updates to or revision to any of the forward-looking statements in this Form 10-Q to reflect any change in our expectations or any change in events, conditions, circumstances, or assumptions underlying the statements.

This section is intended to provide meaningful cautionary statements for purposes of the safe harbor provisions of the Act. This should not be construed as a complete list of all of the economic, competitive, governmental, technological and other factors that could adversely affect our expected consolidated financial position, results of operations or liquidity. Additional risks and uncertainties not currently known to us or that we currently believe are immaterial also may impair our business, operations, liquidity, financial condition and prospects.

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Item 3.Quantitative and Qualitative Disclosure About Market Risk

There have been no material changes to the information concerning our exposures to market risk as stated in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012.

Item 4.Controls and Procedures

The Company maintains disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) that are designed to provide reasonable assurance that the information required to be disclosed in the reports it files with the Securities and Exchange Commission is collected and then processed, summarized and disclosed within the time periods specified in the rules of the Securities and Exchange Commission. Under the supervision and with the participation of the Company’s management, including the Company’s Chief Executive Officer and Chief Financial Officer, the Company has evaluated the effectiveness of the design and operation of its disclosure controls and procedures as of the end of the period covered by this report. Based on such evaluation, the Company’s Chief Executive Officer and Chief Financial Officer have concluded that these procedures are effective. There have been no changes in internal control over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company is subject to a number of claims and judicial and administrative proceedings (some of which involve substantial amounts) arising out of the Company’s business or relating to matters for which the Company may have a contractual indemnity obligation. See Note 14 — Contingencies to the Condensed Consolidated Financial Statements for a discussion of environmental, product liability and other litigation, which is incorporated herein by reference.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds (Repurchases and Authorization of Equity Securities)

The Company's Board of Directors authorized the purchase of up to 29.8 million shares of the Company's common stock. As of September 30, 2013, the Company had repurchased 24,290,805 shares under the Common Stock Repurchase Program. All shares purchased under this authorization have been and will continue to be repurchased in the open market at prevailing prices and at times and in amounts to be determined by management as market conditions and the Company's capital position warrant. The Company may use Rule 10b5-1 plans to facilitate share repurchases. Repurchased shares will be deemed common stock held in treasury and may subsequently be reissued for general corporate purposes.

Employee transactions include shares withheld to offset statutory minimum tax withholding that occurs upon vesting of performance and restricted shares. The BorgWarner Inc. Amended and Restated 2004 Stock Incentive Plan provides that the withholding obligations be settled by the Company retaining stock that is part of the Award. Withheld shares will be deemed common stock held in treasury and may subsequently be reissued for general corporate purposes.

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The following table provides information about the Company's purchases of its equity securities that are registered pursuant to Section 12 of the Exchange Act during the quarter ended September 30, 2013:

Issuer Repurchases of Equity Securities

Period	Total number of shares repurchased	Average price per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number of shares that may yet be purchased
Month Ended July 31, 2013				
Common Stock Repurchase Program	—	$—	—	6,275,495
Employee transactions	1,965	$88.27	—	
Month Ended August 31, 2013				
Common Stock Repurchase Program	390,000	$97.36	—	5,885,495
Employee transactions	—	$—	—	—
Month Ended September 30, 2013				
Common Stock Repurchase Program	376,300	$98.37	—	5,509,195
Employee transactions	160	$96.81	—	—

Item 6. Exhibits

Exhibit 31.1	Rule 13a-14(a)/15d-14(a) Certification of the Principal Executive Officer.*
Exhibit 31.2	Rule 13a-14(a)/15d-14(a) Certification of the Principal Financial Officer.*
Exhibit 32.1	Section 1350 Certifications.*
Exhibit 101.INS	XBRL Instance Document.
Exhibit 101.SCH	XBRL Taxonomy Extension Schema Document.
Exhibit 101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
Exhibit 101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
Exhibit 101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.
Exhibit 101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.

*Filed herewith.

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SIGNATURES

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

BorgWarner Inc.

(Registrant)

By /s/ Steven G. Carlson
(Signature)

Steven G. Carlson

Vice President and Controller
(Principal Accounting Officer)

Date: October 30, 2013