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CUMMINS INC

Form 10-Q

April 30, 2019

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

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

**For the Quarterly Period Ended March 31, 2019**

**Commission File Number 1-4949**

**CUMMINS INC.**

(Exact name of registrant as specified in its charter)

**Indiana 35-0257090**

(State of Incorporation) (IRS Employer Identification No.)

**500 Jackson Street**

**Box 3005**

**Columbus, Indiana 47202-3005**

(Address of principal executive offices)

**Telephone (812) 377-5000**

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that registrant was required to submit such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

Smaller reporting company  Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

As of March 31, 2019, there were 157,492,272 shares of common stock outstanding with a par value of \$2.50 per share.

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In millions, except per share amounts	Three months ended	
	March 31, 2019	April 1, 2018
<b>NET SALES</b> <sup>(a)</sup> (Note 3)	<b>\$ 6,004</b>	\$ 5,570
Cost of sales	<b>4,472</b>	4,370
<b>GROSS MARGIN</b>	<b>1,532</b>	1,200
<b>OPERATING EXPENSES AND INCOME</b>		
Selling, general and administrative expenses	<b>593</b>	577
Research, development and engineering expenses	<b>237</b>	210
Equity, royalty and interest income from investees (Note 5)	<b>92</b>	115
Other operating income (expense), net	<b>5</b>	2
<b>OPERATING INCOME</b>	<b>799</b>	530
Interest income	<b>12</b>	7
Interest expense	<b>32</b>	24
Other income, net	<b>66</b>	10
<b>INCOME BEFORE INCOME TAXES</b>	<b>845</b>	523
Income tax expense	<b>176</b>	198
<b>CONSOLIDATED NET INCOME</b>	<b>669</b>	325
Less: Net income attributable to noncontrolling interests	<b>6</b>	—
<b>NET INCOME ATTRIBUTABLE TO CUMMINS INC.</b>	<b>\$ 663</b>	\$ 325
<b>EARNINGS PER COMMON SHARE ATTRIBUTABLE TO CUMMINS INC.</b>		
Basic	<b>\$ 4.22</b>	\$ 1.97
Diluted	<b>\$ 4.20</b>	\$ 1.96
<b>WEIGHTED AVERAGE COMMON SHARES OUTSTANDING</b>		
Basic	<b>157.2</b>	164.9
Dilutive effect of stock compensation awards	<b>0.5</b>	0.8
Diluted	<b>157.7</b>	165.7

<sup>(a)</sup> Includes sales to nonconsolidated equity investees of \$285 million and \$297 million for the three months ended March 31, 2019 and April 1, 2018, respectively.

*The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.*

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**CUMMINS INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
**(Unaudited)**

In millions	Three months ended	
	March 31, 2019	April 1, 2018
<b>CONSOLIDATED NET INCOME</b>	<b>\$ 669</b>	<b>\$ 325</b>
Other comprehensive income (loss), net of tax (Note 13)		
Change in pension and other postretirement defined benefit plans	(11 )	8
Foreign currency translation adjustments	84	84
Unrealized (loss) gain on derivatives	(1 )	7
Unrealized loss on marketable securities	(1 )	—
Total other comprehensive (loss) income, net of tax	71	99
<b>COMPREHENSIVE INCOME</b>	<b>740</b>	<b>424</b>
Less: Comprehensive income (loss) attributable to noncontrolling interests	9	(7 )
<b>COMPREHENSIVE INCOME ATTRIBUTABLE TO CUMMINS INC.</b>	<b>\$ 731</b>	<b>\$ 431</b>

*The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.*



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**CUMMINS INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(Unaudited)**

<b>In millions, except par value</b>	<b>March 31,</b>	<b>December 31,</b>
	<b>2019</b>	<b>2018</b>
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	<b>\$ 1,328</b>	\$ 1,303
Marketable securities (Note 6)	<b>246</b>	222
Total cash, cash equivalents and marketable securities	<b>1,574</b>	1,525
Accounts and notes receivable, net		
Trade and other	<b>3,765</b>	3,635
Nonconsolidated equity investees	<b>260</b>	231
Inventories (Note 7)	<b>3,893</b>	3,759
Prepaid expenses and other current assets	<b>599</b>	668
Total current assets	<b>10,091</b>	9,818
Long-term assets		
Property, plant and equipment	<b>8,349</b>	8,319
Accumulated depreciation	<b>(4,283)</b>	(4,223)
Property, plant and equipment, net	<b>4,066</b>	4,096
Investments and advances related to equity method investees	<b>1,303</b>	1,222
Goodwill	<b>1,125</b>	1,126
Other intangible assets, net	<b>895</b>	909
Pension assets	<b>939</b>	929
Other assets	<b>1,427</b>	962
Total assets	<b>\$ 19,846</b>	\$ 19,062
<b>LIABILITIES</b>		
Current liabilities		
Accounts payable (principally trade)	<b>\$ 3,018</b>	\$ 2,822
Loans payable (Note 9)	<b>70</b>	54
Commercial paper (Note 9)	<b>709</b>	780
Accrued compensation, benefits and retirement costs	<b>364</b>	679
Current portion of accrued product warranty (Note 10)	<b>762</b>	654
Current portion of deferred revenue (Note 3)	<b>509</b>	498
Other accrued expenses (Note 11)	<b>958</b>	852
Current maturities of long-term debt (Note 9)	<b>37</b>	45
Total current liabilities	<b>6,427</b>	6,384
Long-term liabilities		
Long-term debt (Note 9)	<b>1,605</b>	1,597
Pensions and other postretirement benefits	<b>520</b>	532
Accrued product warranty (Note 10)	<b>682</b>	740
Deferred revenue (Note 3)	<b>697</b>	658
Other liabilities (Note 11)	<b>1,188</b>	892
Total liabilities	<b>\$ 11,119</b>	\$ 10,803

Commitments and contingencies (Note 12)

**EQUITY**

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Cummins Inc. shareholders' equity		
Common stock, \$2.50 par value, 500 shares authorized, 222.4 and 222.4 shares issued	<b>\$2,273</b>	\$ 2,271
Retained earnings	<b>13,401</b>	12,917
Treasury stock, at cost, 64.9 and 64.4 shares	<b>(6,111 )</b>	(6,028 )
Common stock held by employee benefits trust, at cost, 0.3 and 0.4 shares	<b>(4 )</b>	(5 )
Accumulated other comprehensive loss (Note 13)	<b>(1,739 )</b>	(1,807 )
Total Cummins Inc. shareholders' equity	<b>7,820</b>	7,348
Noncontrolling interests	<b>907</b>	911
Total equity	<b>\$8,727</b>	\$ 8,259
Total liabilities and equity	<b>\$19,846</b>	\$ 19,062

*The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.*

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**CUMMINS INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited)**

<b>In millions</b>	<b>Three months ended</b>	
	<b>March 31,</b>	<b>April 1,</b>
	<b>2019</b>	<b>2018</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Consolidated net income	<b>\$ 669</b>	\$ 325
Adjustments to reconcile consolidated net income to net cash provided by (used in) operating activities		
Depreciation and amortization	<b>157</b>	154
Deferred income taxes	<b>11</b>	(27 )
Equity in income of investees, net of dividends	<b>(64)</b>	(95 )
Pension contributions (in excess of) under expense, net (Note 4)	<b>(17)</b>	) 13
Other postretirement benefits payments in excess of expense, net (Note 4)	<b>(12)</b>	) (5 )
Stock-based compensation expense	<b>9</b>	9
(Gain) loss on corporate owned life insurance	<b>(37)</b>	) 3
Foreign currency remeasurement and transaction exposure	<b>79</b>	38
Changes in current assets and liabilities		
Accounts and notes receivable	<b>(135)</b>	) (217 )
Inventories	<b>(107)</b>	) (259 )
Other current assets	<b>67</b>	56
Accounts payable	<b>166</b>	246
Accrued expenses	<b>(293)</b>	) (337 )
Changes in other liabilities	<b>64</b>	27
Other, net	<b>(145)</b>	) (48 )
Net cash provided by (used in) operating activities	<b>412</b>	(117 )
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Capital expenditures	<b>(109)</b>	) (72 )
Investments in internal use software	<b>(20)</b>	) (15 )
Investments in and advances to equity investees	<b>(10)</b>	) (16 )
Investments in marketable securities—acquisitions (Note 6)	<b>(121)</b>	) (67 )
Investments in marketable securities—liquidations (Note 6)	<b>103</b>	82
Cash flows from derivatives not designated as hedges	<b>55</b>	27
Other, net	<b>31</b>	25
Net cash used in investing activities	<b>(71)</b>	) (36 )
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net (payments) borrowings of commercial paper (Note 9)	<b>(71)</b>	) 295
Payments on borrowings and finance lease obligations	<b>(10)</b>	) (16 )
Distributions to noncontrolling interests	<b>(13)</b>	) (11 )
Dividend payments on common stock	<b>(179)</b>	) (178 )
Repurchases of common stock	<b>(100)</b>	) (163 )
Other, net	<b>26</b>	21
Net cash used in financing activities	<b>(347)</b>	) (52 )
<b>EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>		
Net increase (decrease) in cash and cash equivalents	<b>25</b>	(162 )
Cash and cash equivalents at beginning of year	<b>1,303</b>	1,369
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<b>\$ 1,328</b>	\$ 1,207

*The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.*

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**CUMMINS INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**  
**(Unaudited)**

In millions, except per share amounts	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Common Stock Held in Trust	Accumulated Other Comprehensive Loss	Total Cummins Inc Shareholders' Equity	Noncontrolling Interests	Total Equity
<b>BALANCE AT DECEMBER 31, 2017</b>	\$ 556	\$ 1,654	\$ 11,464	\$(4,905)	\$ (7)	\$(1,503)	\$ 7,259	\$ 905	\$ 8,164
Adoption of new accounting standards <sup>(1)</sup>			30				30	—	30
Net income			325				325	—	325
Other comprehensive income (loss), net of tax (Note 13)						106	106	(7)	99
Issuance of common stock		3					3	—	3
Employee benefits trust activity		6			1		7	—	7
Repurchases of common stock				(163)			(163)	—	(163)
Cash dividends on common stock, \$1.08 per share			(178)				(178)	—	(178)
Distributions to noncontrolling interests							—	(11)	(11)
Stock based awards		(4)	7				3	—	3
Other shareholder transactions		2					2	15	17
<b>BALANCE AT APRIL 1, 2018</b>	\$ 556	\$ 1,661	\$ 11,641	\$(5,061)	\$ (6)	\$(1,397)	\$ 7,394	\$ 902	\$ 8,296
<b>BALANCE AT DECEMBER 31, 2018</b>	\$ 556	\$ 1,715	\$ 12,917	\$(6,028)	\$ (5)	\$(1,807)	\$ 7,348	\$ 911	\$ 8,259
Net income			663				663	6	669
Other comprehensive income, net of tax (Note 13)						68	68	3	71
Issuance of common stock		1					1	—	1
Employee benefits trust activity		13			1		14	—	14
Repurchases of common stock				(100)			(100)	—	(100)
Cash dividends on common stock, \$1.14 per share			(179)				(179)	—	(179)
Distributions to noncontrolling interests							—	(13)	(13)
Stock based awards		(11)	17				6	—	6
Other shareholder transactions		(1)					(1)	—	(1)
<b>BALANCE AT MARCH 31, 2019</b>	\$ 556	\$ 1,717	\$ 13,401	\$(6,111)	\$ (4)	\$(1,739)	\$ 7,820	\$ 907	\$ 8,727

<sup>(1)</sup> Includes \$28 million related to adoption of the revenue recognition standard and \$2 million related to adoption of the accounting for certain financial instruments standard. See Note 1, "SUMMARY OF

SIGNIFICANT ACCOUNTING POLICIES - Recently Adopted and Recently Issued Accounting Pronouncements" of the Notes to the Consolidated Financial Statements of our 2018 Form 10-K for additional information.

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

Table of Contents**CUMMINS INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)****NOTE 1. NATURE OF OPERATIONS**

Cummins Inc. (“Cummins,” “we,” “our” or “us”) was founded in 1919 as Cummins Engine Company, a corporation in Columbus, Indiana, and one of the first diesel engine manufacturers. In 2001, we changed our name to Cummins Inc. We are a global power leader that designs, manufactures, distributes and services diesel and natural gas engines and powertrain-related component products, including filtration, aftertreatment, turbochargers, fuel systems, controls systems, air handling systems, transmissions, electric power generation systems, batteries and electrified power systems. We sell our products to original equipment manufacturers (OEMs), distributors, dealers and other customers worldwide. We serve our customers through a network of approximately 600 wholly-owned and independent distributor locations and over 7,600 dealer locations in more than 190 countries and territories.

**NOTE 2. BASIS OF PRESENTATION****Interim Condensed Financial Statements**

The unaudited *Condensed Consolidated Financial Statements* reflect all adjustments which, in the opinion of management, are necessary for a fair statement of the results of operations, financial position and cash flows. All such adjustments are of a normal recurring nature. The *Condensed Consolidated Financial Statements* have been prepared in accordance with accounting principles in the United States of America (GAAP) pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) for interim financial information. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with GAAP have been condensed or omitted as permitted by such rules and regulations.

These interim condensed financial statements should be read in conjunction with the *Consolidated Financial Statements* included in our Annual Report on Form 10-K for the year ended December 31, 2018. Our interim period financial results for the three month periods presented are not necessarily indicative of results to be expected for any other interim period or for the entire year. The year-end *Condensed Consolidated Balance Sheet* data was derived from audited financial statements, but does not include all disclosures required by GAAP.

**Reclassifications**

Certain amounts for prior year periods have been reclassified to conform to the presentation of the current year.

**Use of Estimates in Preparation of Financial Statements**

Preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect reported amounts presented and disclosed in our *Condensed Consolidated Financial Statements*. Significant estimates and assumptions in these *Condensed Consolidated Financial Statements* require the exercise of judgment. Due to the inherent uncertainty involved in making estimates, actual results reported in future periods may be different from these estimates.

**Reporting Period**

Our reporting period usually ends on the Sunday closest to the last day of the quarterly calendar period. The first quarters of 2019 and 2018 ended on March 31 and April 1, respectively. Our fiscal year ends on December 31, regardless of the day of the week on which December 31 falls.

**Weighted-Average Diluted Shares Outstanding**

The weighted-average diluted common shares outstanding excludes the anti-dilutive effect of certain stock options since such options had an exercise price in excess of the monthly average market value of our common stock. The options excluded from diluted earnings per share were as follows:

	Three months ended	
	March 31,	April 1,
	2019	2018
Options excluded	<b>783,576</b>	6,867



Table of Contents**NOTE 3. REVENUE RECOGNITION****Long-term Contracts**

Most of our contracts are for a period of less than one year. We have certain long-term maintenance agreements, construction contracts and extended warranty coverage arrangements that span a period in excess of one year. The aggregate amount of the transaction price for long-term maintenance agreements and construction contracts allocated to performance obligations that have not been satisfied as of March 31, 2019, was \$705 million. We expect to recognize the related revenue of \$205 million over the next 12 months and \$500 million over periods up to 10 years. See NOTE 10, "PRODUCT WARRANTY LIABILITY," for additional disclosures on extended warranty coverage arrangements. Our other contracts generally are for a duration of less than one year, include payment terms that correspond to the timing of cost incurred when providing goods and services to our customers or represent sale-based royalties.

**Deferred and Unbilled Revenue**

The following is a summary of our unbilled and deferred revenue and related activity:

In millions	March 31, December 31,	
	2019	2018
Unbilled revenue	\$ 46	\$ 64
Deferred revenue, primarily extended warranty	1,206	1,156

Revenue recognized was \$109 million and \$128 million for the three months ended March 31, 2019 and April 1, 2018, respectively. These amounts relate to year-to-date revenues recognized from amounts included in deferred revenue at the beginning of the year. We did not record any impairment losses on our unbilled revenues during the three months ended March 31, 2019.

**Disaggregation of Revenue****Consolidated Revenue**

The table below presents our consolidated sales by geographic area. Net sales attributed to geographic areas were based on the location of the customer.

In millions	Three months ended	
	March 31, 2019	April 1, 2018
United States	\$3,436	\$3,038
China	573	550
India	224	235
Other international	1,771	1,747
Total net sales	\$6,004	\$5,570

**Segment Revenue**

Engine segment external sales by market were as follows:

In millions	Three months ended	
	March 31, 2019	April 1, 2018
Heavy-duty truck	\$723	\$614
Medium-duty truck and bus	610	627
Light-duty automotive	330	323
Total on-highway	1,663	1,564
Off-highway	321	249
Total sales	\$1,984	\$1,813





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Distribution segment external sales by region were as follows:

In millions	Three months ended	
	March 31, 2019	April 1, 2018
North America	<b>\$ 1,392</b>	\$ 1,274
Asia Pacific	<b>220</b>	187
Europe	<b>123</b>	131
China	<b>81</b>	77
Africa and Middle East	<b>55</b>	61
India	<b>47</b>	44
Latin America	<b>40</b>	38
Russia	<b>35</b>	35
Total sales	<b>\$ 1,993</b>	\$ 1,847

Distribution segment external sales by product line were as follows:

In millions	Three months ended	
	March 31, 2019	April 1, 2018
Parts	<b>\$ 841</b>	\$ 803
Power generation	<b>401</b>	325
Engines	<b>389</b>	368
Service	<b>362</b>	351
Total sales	<b>\$ 1,993</b>	\$ 1,847

Components segment external sales by business were as follows:

In millions	Three months ended	
	March 31, 2019	April 1, 2018
Emission solutions	<b>\$ 749</b>	\$ 684
Filtration	<b>259</b>	257
Turbo technologies	<b>190</b>	197
Automated transmissions	<b>149</b>	117
Electronics and fuel systems	<b>54</b>	58
Total sales	<b>\$ 1,401</b>	\$ 1,313

Power Systems segment external sales by product line were as follows:

In millions	Three months ended	
	March 31, 2019	April 1, 2018
Power generation	<b>\$ 308</b>	\$ 310
Industrial	<b>231</b>	201
Generator technologies	<b>84</b>	84
Total sales	<b>\$ 623</b>	\$ 595

Table of Contents**NOTE 4. PENSIONS AND OTHER POSTRETIREMENT BENEFITS**

We sponsor funded and unfunded domestic and foreign defined benefit pension and other postretirement benefit plans. Contributions to these plans were as follows:

In millions	Three months ended	
	March 31, 2019	April 1, 2018
Defined benefit pension plans		
Voluntary contribution	\$ 26	\$ 3
Mandatory contribution	7	6
Defined benefit pension contributions	\$ 33	\$ 9
Other postretirement benefit plans		
Benefit payments, net	\$ 14	\$ 7
Defined contribution pension plans	\$ 39	\$ 40

We anticipate making additional defined benefit pension contributions during the remainder of 2019 of \$90 million for our U.S. and U.K. pension plans. Approximately \$91 million of the estimated \$123 million of pension contributions for the full year are voluntary. These contributions may be made from trusts or company funds either to increase pension assets or to make direct benefit payments to plan participants. We expect our 2019 net periodic pension cost to approximate \$64 million.

The components of net periodic pension and other postretirement benefit costs under our plans were as follows:

In millions	Pension					
	U.S. Plans		U.K. Plans		Other Postretirement Benefits	
	Three months ended					
	March 31, 2019	April 1, 2018	March 31, 2019	April 1, 2018	March 31, 2019	April 1, 2018
Service cost	\$29	\$ 30	\$7	\$ 8	\$ —	\$ —
Interest cost	27	25	11	11	2	2
Expected return on plan assets	(47)	(49)	(18)	(18)	—	—
Recognized net actuarial loss	4	8	3	7	—	—
Net periodic benefit cost	\$13	\$ 14	\$3	\$ 8	\$ 2	\$ 2

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**NOTE 5. EQUITY, ROYALTY AND INTEREST INCOME FROM INVESTEEES**