
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 June 30, 2019

Commission File Number 1-4949

CUMMINS INC.

(Exact name of registrant as specified in its charter)

IN
(State of Incorporation)

35-0257090
(IRS Employer Identification No.)

500 Jackson Street
Box 3005
Columbus, IN 47202-3005
(Address of principal executive offices)

Telephone (812) 377-5000
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading symbol(s)	Name of each exchange on which registered
Common stock, \$2.50 par value	CMI	NYSE

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 June 30, 2019, there were 157,786,322 shares of common stock outstanding with a par value of \$2.50 per share.

CUMMINS INC. AND SUBSIDIARIES
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PART I. FINANCIAL INFORMATION

ITEM 1. Condensed Consolidated Financial Statements

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

In millions, except per share amounts	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
NET SALES ^(a) (Note 3)	\$ 6,221	\$ 6,132	\$ 12,225	\$ 11,702
Cost of sales	4,580	4,692	9,052	9,062
GROSS MARGIN	1,641	1,440	3,173	2,640
OPERATING EXPENSES AND INCOME				
Selling, general and administrative expenses	629	613	1,222	1,190
Research, development and engineering expenses	251	219	488	429
Equity, royalty and interest income from investees (Note 5)	96	110	188	225
Other operating income (expense), net	(9)	4	(4)	6
OPERATING INCOME	848	722	1,647	1,252
Interest income	12	10	24	17
Interest expense	29	28	61	52
Other income, net	40	11	106	21
INCOME BEFORE INCOME TAXES	871	715	1,716	1,238
Income tax expense	186	161	362	359
CONSOLIDATED NET INCOME	685	554	1,354	879
Less: Net income attributable to noncontrolling interests	10	9	16	9
NET INCOME ATTRIBUTABLE TO CUMMINS INC.	\$ 675	\$ 545	\$ 1,338	\$ 870
EARNINGS PER COMMON SHARE ATTRIBUTABLE TO CUMMINS INC.				
Basic	\$ 4.29	\$ 3.33	\$ 8.51	\$ 5.30
Diluted	\$ 4.27	\$ 3.32	\$ 8.47	\$ 5.27
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING				
Basic	157.4	163.8	157.3	164.3
Dilutive effect of stock compensation awards	0.6	0.5	0.6	0.7
Diluted	158.0	164.3	157.9	165.0

^(a) Includes sales to nonconsolidated equity investees of \$317 million and \$602 million and \$340 million and \$637 million for the three and six months ended June 30, 2019 and July 1, 2018, respectively.

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

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

In millions	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
CONSOLIDATED NET INCOME	\$ 685	\$ 554	\$ 1,354	\$ 879
Other comprehensive income (loss), net of tax (Note 13)				
Change in pension and other postretirement defined benefit plans	7	13	(4)	21
Foreign currency translation adjustments	(99)	(299)	(15)	(215)
Unrealized gain (loss) on derivatives	(10)	—	(11)	7
Unrealized gain on marketable securities	1	—	—	—
Total other comprehensive loss, net of tax	(101)	(286)	(30)	(187)
COMPREHENSIVE INCOME	584	268	1,324	692
Less: Comprehensive income (loss) attributable to noncontrolling interests	10	(7)	19	(14)
COMPREHENSIVE INCOME ATTRIBUTABLE TO CUMMINS INC.	\$ 574	\$ 275	\$ 1,305	\$ 706

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

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

In millions, except par value	June 30, 2019	December 31, 2018
ASSETS		
Current assets		
Cash and cash equivalents	\$ 1,397	\$ 1,303
Marketable securities (Note 6)	335	222
Total cash, cash equivalents and marketable securities	1,732	1,525
Accounts and notes receivable, net		
Trade and other	3,899	3,635
Nonconsolidated equity investees	280	231
Inventories (Note 7)	3,896	3,759
Prepaid expenses and other current assets	643	668
Total current assets	10,450	9,818
Long-term assets		
Property, plant and equipment	8,424	8,319
Accumulated depreciation	(4,347)	(4,223)
Property, plant and equipment, net	4,077	4,096
Investments and advances related to equity method investees	1,274	1,222
Goodwill	1,125	1,126
Other intangible assets, net	901	909
Pension assets	960	929
Other assets	1,467	962
Total assets	\$ 20,254	\$ 19,062
LIABILITIES		
Current liabilities		
Accounts payable (principally trade)	\$ 2,991	\$ 2,822
Loans payable (Note 10)	119	54
Commercial paper (Note 10)	434	780
Accrued compensation, benefits and retirement costs	465	679
Current portion of accrued product warranty (Note 11)	809	654
Current portion of deferred revenue (Note 3)	505	498
Other accrued expenses (Note 8)	920	852
Current maturities of long-term debt (Note 10)	46	45
Total current liabilities	6,289	6,384
Long-term liabilities		
Long-term debt (Note 10)	1,624	1,597
Pensions and other postretirement benefits	522	532
Accrued product warranty (Note 11)	663	740
Deferred revenue (Note 3)	726	658
Other liabilities (Note 8)	1,234	892
Total liabilities	\$ 11,058	\$ 10,803
Commitments and contingencies (Note 12)		
EQUITY		
Cummins Inc. shareholders' equity		
Common stock, \$2.50 par value, 500 shares authorized, 222.4 and 222.4 shares issued	\$ 2,307	\$ 2,271
Retained earnings	13,897	12,917
Treasury stock, at cost, 64.6 and 64.4 shares	(6,082)	(6,028)
Common stock held by employee benefits trust, at cost, 0.3 and 0.4 shares	(4)	(5)
Accumulated other comprehensive loss (Note 13)	(1,840)	(1,807)
Total Cummins Inc. shareholders' equity	8,278	7,348
Noncontrolling interests	918	911
Total equity	\$ 9,196	\$ 8,259
Total liabilities and equity	\$ 20,254	\$ 19,062

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

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

In millions	Six months ended	
	June 30, 2019	July 1, 2018
CASH FLOWS FROM OPERATING ACTIVITIES		
Consolidated net income	\$ 1,354	\$ 879
Adjustments to reconcile consolidated net income to net cash provided by operating activities		
Depreciation and amortization	315	308
Deferred income taxes	17	(21)
Equity in income of investees, net of dividends	(43)	(163)
Pension contributions (in excess of) under expense, net (Note 4)	(45)	25
Other postretirement benefits payments in excess of expense, net (Note 4)	(10)	—
Stock-based compensation expense	28	28
Gain on corporate owned life insurance	(55)	—
Foreign currency remeasurement and transaction exposure	46	(21)
Changes in current assets and liabilities		
Accounts and notes receivable	(312)	(555)
Inventories	(125)	(475)
Other current assets	15	(42)
Accounts payable	148	442
Accrued expenses	(194)	94
Changes in other liabilities	120	5
Other, net	(39)	(31)
Net cash provided by operating activities	1,220	473
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(242)	(186)
Investments in internal use software	(34)	(35)
Investments in and advances to equity investees	(18)	(15)
Investments in marketable securities—acquisitions	(259)	(143)
Investments in marketable securities—liquidations (Note 6)	153	116
Cash flows from derivatives not designated as hedges	(26)	(9)
Other, net	15	36
Net cash used in investing activities	(411)	(236)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net (payments) borrowings of commercial paper (Note 10)	(346)	504
Payments on borrowings and finance lease obligations	(17)	(33)
Net borrowings (payments) under short-term credit agreements	57	(1)
Distributions to noncontrolling interests	(13)	(11)
Dividend payments on common stock	(358)	(355)
Repurchases of common stock	(100)	(379)
Other, net	66	22
Net cash used in financing activities	(711)	(253)
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	(4)	(35)
Net increase (decrease) in cash and cash equivalents	94	(51)
Cash and cash equivalents at beginning of year	1,303	1,369
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 1,397	\$ 1,318

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

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

In millions, except per share amounts	Three months ended								
	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
BALANCE AT MARCH 31, 2019	\$ 556	\$ 1,717	\$ 13,401	\$ (6,111)	\$ (4)	\$ (1,739)	\$ 7,820	\$ 907	\$ 8,727
Net income			675				675	10	685
Other comprehensive income, net of tax (Note 13)						(101)	(101)	—	(101)
Issuance of common stock		1					1	—	1
Employee benefits trust activity		7					7	—	7
Cash dividends on common stock, \$1.14 per share			(179)				(179)	—	(179)
Stock based awards		8		29			37	—	37
Other shareholder transactions		18					18	1	19
BALANCE AT JUNE 30, 2019	\$ 556	\$ 1,751	\$ 13,897	\$ (6,082)	\$ (4)	\$ (1,840)	\$ 8,278	\$ 918	\$ 9,196
BALANCE AT APRIL 1, 2018	\$ 556	\$ 1,661	\$ 11,641	\$ (5,061)	\$ (6)	\$ (1,397)	\$ 7,394	\$ 902	\$ 8,296
Net income			545				545	9	554
Other comprehensive income, net of tax (Note 13)						(270)	(270)	(16)	(286)
Issuance of common stock		5					5	—	5
Employee benefits trust activity		2					2	—	2
Repurchases of common stock				(216)			(216)	—	(216)
Cash dividends on common stock, \$1.08 per share			(177)				(177)	—	(177)
Stock based awards				1			1	—	1
Other shareholder transactions		15					15	—	15
BALANCE AT JULY 1, 2018	\$ 556	\$ 1,683	\$ 12,009	\$ (5,276)	\$ (6)	\$ (1,667)	\$ 7,299	\$ 895	\$ 8,194

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

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

In millions, except per share amounts	Six months ended								
	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
BALANCE AT DECEMBER 31, 2018	\$ 556	\$ 1,715	\$ 12,917	\$ (6,028)	\$ (5)	\$ (1,807)	\$ 7,348	\$ 911	\$ 8,259
Net income			1,338				1,338	16	1,354
Other comprehensive income, net of tax (Note 13)						(33)	(33)	3	(30)
Issuance of common stock		2					2	—	2
Employee benefits trust activity		20			1		21	—	21
Repurchases of common stock				(100)			(100)	—	(100)
Cash dividends on common stock, \$2.28 per share			(358)				(358)	—	(358)
Distributions to noncontrolling interests							—	(13)	(13)
Stock based awards		(3)		46			43	—	43
Other shareholder transactions		17					17	1	18
BALANCE AT JUNE 30, 2019	\$ 556	\$ 1,751	\$ 13,897	\$ (6,082)	\$ (4)	\$ (1,840)	\$ 8,278	\$ 918	\$ 9,196
BALANCE AT DECEMBER 31, 2017	\$ 556	\$ 1,654	\$ 11,464	\$ (4,905)	\$ (7)	\$ (1,503)	\$ 7,259	\$ 905	\$ 8,164
Adoption of new accounting standards ⁽¹⁾			30				30	—	30
Net income			870				870	9	879
Other comprehensive income (loss), net of tax (Note 13)						(164)	(164)	(23)	(187)
Issuance of common stock		8					8	—	8
Employee benefits trust activity		8			1		9	—	9
Repurchases of common stock				(379)			(379)	—	(379)
Cash dividends on common stock, \$2.16 per share			(355)				(355)	—	(355)
Distributions to noncontrolling interests							—	(11)	(11)
Stock based awards		(4)		8			4	—	4
Other shareholder transactions		17					17	15	32
BALANCE AT JULY 1, 2018	\$ 556	\$ 1,683	\$ 12,009	\$ (5,276)	\$ (6)	\$ (1,667)	\$ 7,299	\$ 895	\$ 8,194

⁽¹⁾ 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.

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 and six 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 second quarters of 2019 and 2018 ended on June 30 and July 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		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Options excluded	234,947	909,394	509,261	458,130

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 June 30, 2019, was \$703 million. We expect to recognize the related revenue of \$147 million over the next 12 months and \$556 million over periods up to 10 years. See NOTE 11, "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	June 30, 2019	December 31, 2018
Unbilled revenue	\$ 65	\$ 64
Deferred revenue, primarily extended warranty	1,231	1,156

We recognized revenue of \$94 million and \$203 million and \$78 million and \$206 million for the three and six months ended June 30, 2019 and July 1, 2018, respectively, that was included in the deferred revenue balance at the beginning of each year. We did not record any impairment losses on our unbilled revenues during the three and six months ended June 30, 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		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
United States	\$ 3,611	\$ 3,384	\$ 7,047	\$ 6,422
China	644	644	1,217	1,194
India	234	247	458	482
Other international	1,732	1,857	3,503	3,604
Total net sales	\$ 6,221	\$ 6,132	\$ 12,225	\$ 11,702

Segment Revenue

Engine segment external sales by market were as follows:

In millions	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Heavy-duty truck	\$ 754	\$ 730	\$ 1,477	\$ 1,344
Medium-duty truck and bus	630	714	1,240	1,341
Light-duty automotive	435	330	765	653
Total on-highway	1,819	1,774	3,482	3,338
Off-highway	254	276	575	525
Total sales	\$ 2,073	\$ 2,050	\$ 4,057	\$ 3,863

Distribution segment external sales by region were as follows:

In millions	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
North America	\$ 1,374	\$ 1,349	\$ 2,766	\$ 2,623
Asia Pacific	223	211	443	398
Europe	122	143	245	274
China	101	84	182	161
Africa and Middle East	55	62	110	123
India	49	49	96	93
Latin America	46	45	86	83
Russia	45	45	80	80
Total sales	\$ 2,015	\$ 1,988	\$ 4,008	\$ 3,835

Distribution segment external sales by product line were as follows:

In millions	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Parts	\$ 827	\$ 815	\$ 1,668	\$ 1,618
Power generation	425	345	826	670
Engines	392	460	781	828
Service	371	368	733	719
Total sales	\$ 2,015	\$ 1,988	\$ 4,008	\$ 3,835

Components segment external sales by business were as follows:

In millions	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Emission solutions	\$ 735	\$ 735	\$ 1,484	\$ 1,419
Filtration	263	257	522	514
Turbo technologies	181	201	371	398
Automated transmissions	156	141	305	258
Electronics and fuel systems	66	68	120	126
Total sales	\$ 1,401	\$ 1,402	\$ 2,802	\$ 2,715

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

In millions	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Power generation	\$ 380	\$ 390	\$ 688	\$ 700
Industrial	246	208	477	409
Generator technologies	98	93	182	177
Total sales	\$ 724	\$ 691	\$ 1,347	\$ 1,286

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		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Defined benefit pension plans				
Voluntary contribution	\$ 36	\$ 4	\$ 62	\$ 7
Mandatory contribution	8	5	15	11
Defined benefit pension contributions	<u>\$ 44</u>	<u>\$ 9</u>	<u>\$ 77</u>	<u>\$ 18</u>
Other postretirement benefit plans				
Benefit payments (rebates), net	<u>\$ 1</u>	<u>\$ (2)</u>	<u>\$ 15</u>	<u>\$ 5</u>
Defined contribution pension plans	<u>\$ 18</u>	<u>\$ 21</u>	<u>\$ 57</u>	<u>\$ 61</u>

During the remainder of 2019, we anticipate making additional defined benefit pension contributions of \$46 million for our United States (U.S.) and United Kingdom (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				Other Postretirement Benefits	
	U.S. Plans		U.K. Plans			
	Three months ended					
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Service cost	\$ 29	\$ 30	\$ 6	\$ 7	\$ —	\$ —
Interest cost	27	24	11	10	3	3
Expected return on plan assets	(48)	(49)	(18)	(18)	—	—
Amortization of prior service cost	1	—	1	—	—	—
Recognized net actuarial loss	4	9	3	8	—	—
Net periodic benefit cost	\$ 13	\$ 14	\$ 3	\$ 7	\$ 3	\$ 3

In millions	Pension					
	U.S. Plans		U.K. Plans		Other Postretirement Benefits	
	Six months ended					
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Service cost	\$ 58	\$ 60	\$ 13	\$ 15	\$ —	\$ —
Interest cost	54	49	22	21	5	5
Expected return on plan assets	(95)	(98)	(36)	(36)	—	—
Amortization of prior service cost	1	—	1	—	—	—
Recognized net actuarial loss	8	17	6	15	—	—
Net periodic benefit cost	\$ 26	\$ 28	\$ 6	\$ 15	\$ 5	\$ 5

NOTE 5. EQUITY, ROYALTY AND INTEREST INCOME FROM INVESTEEES

Equity, royalty and interest income from investees included in our *Condensed Consolidated Statements of Net Income* for the reporting periods was as follows:

In millions	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Manufacturing entities				
Beijing Foton Cummins Engine Co., Ltd.	\$ 20	\$ 24	\$ 41	\$ 45
Dongfeng Cummins Engine Company, Ltd.	16	17	30	34
Chongqing Cummins Engine Company, Ltd.	10	15	22	32
All other manufacturers	28	34	55	70
Distribution entities				
Komatsu Cummins Chile, Ltda.	7	6	13	13
All other distributors	—	—	(1)	—
Cummins share of net income	81	96	160	194
Royalty and interest income	15	14	28	31
Equity, royalty and interest income from investees	<u>\$ 96</u>	<u>\$ 110</u>	<u>\$ 188</u>	<u>\$ 225</u>

NOTE 6. MARKETABLE SECURITIES

A summary of marketable securities, all of which were classified as current, was as follows:

In millions	June 30, 2019			December 31, 2018		
	Cost	Gross unrealized gains/(losses) ⁽¹⁾	Estimated fair value	Cost	Gross unrealized gains/(losses) ⁽¹⁾	Estimated fair value
Equity securities						
Certificates of deposit	\$ 172	\$ —	\$ 172	\$ 101	\$ —	\$ 101
Debt mutual funds	140	2	142	103	1	104
Equity mutual funds	17	3	20	16	—	16
Debt securities	1	—	1	1	—	1
Total marketable securities	<u>\$ 330</u>	<u>\$ 5</u>	<u>\$ 335</u>	<u>\$ 221</u>	<u>\$ 1</u>	<u>\$ 222</u>

⁽¹⁾ Unrealized gains and losses for debt securities are recorded in other comprehensive income while unrealized gains and losses for equity securities are recorded in "Other income, net" in our *Condensed Consolidated Statements of Net Income*.

All debt securities are classified as available-for-sale. All marketable securities presented use a Level 2 fair value measure. The fair value of Level 2 securities is estimated using actively quoted prices for similar instruments from brokers and observable inputs where available, including market transactions and third-party pricing services, or net asset values provided to investors. We do not currently have any Level 3 securities and there were no transfers between Level 2 or 3 during the first half of 2019 or for the year ended December 31, 2018.

A description of the valuation techniques and inputs used for our Level 2 fair value measures is as follows:

- *Certificates of deposit* — These investments provide us with a contractual rate of return and generally range in maturity from three months to five years. The counterparties to these investments are reputable financial institutions with investment grade credit ratings. Since these instruments are not tradable and must be settled directly by us with the respective financial institution, our fair value measure is the financial institution's month-end statement.
- *Debt mutual funds* — The fair value measure for the vast majority of these investments is the daily net asset value published on a regulated governmental website. Daily quoted prices are available from the issuing brokerage and are used on a test basis to corroborate this Level 2 input.

- *Equity mutual funds* — The fair value measure for these investments is the net asset value published by the issuing brokerage. Daily quoted prices are available from reputable third party pricing services and are used on a test basis to corroborate this Level 2 input measure.
- *Debt securities* — The fair value measure for these securities is broker quotes received from reputable firms. These securities are infrequently traded on a national stock exchange and these values are used on a test basis to corroborate our Level 2 input measure.

The proceeds from sales and maturities of marketable securities were as follows:

In millions	Six months ended	
	June 30, 2019	July 1, 2018
Proceeds from sales of marketable securities	\$ 97	\$ 81
Proceeds from maturities of marketable securities	56	35
Investments in marketable securities - liquidations	<u>\$ 153</u>	<u>\$ 116</u>

NOTE 7. INVENTORIES

Inventories are stated at the lower of cost or market. Inventories included the following:

In millions	June 30, 2019	December 31, 2018
Finished products	\$ 2,431	\$ 2,405
Work-in-process and raw materials	1,591	1,487
Inventories at FIFO cost	4,022	3,892
Excess of FIFO over LIFO	(126)	(133)
Total inventories	<u>\$ 3,896</u>	<u>\$ 3,759</u>

NOTE 8. SUPPLEMENTAL BALANCE SHEET DATA

Other accrued expenses included the following:

In millions	June 30, 2019	December 31, 2018
Marketing accruals	\$ 205	\$ 199
Other taxes payable	186	196
Current portion of operating lease liabilities	125	—
Income taxes payable	75	97
Other	329	360
Other accrued expenses	<u>\$ 920</u>	<u>\$ 852</u>

Other liabilities included the following:

In millions	June 30, 2019	December 31, 2018
Operating lease liabilities	\$ 321	\$ —
Income taxes payable	293	293
Deferred income taxes	278	263
Accrued compensation	161	173
Other long-term liabilities	181	163
Other liabilities	<u>\$ 1,234</u>	<u>\$ 892</u>

NOTE 9. LEASES

Lease Accounting Pronouncement Adoption

In February 2016, the Financial Accounting Standards Board (FASB) amended its standards related to the accounting for leases. Under the new standard, lessees are now required to recognize substantially all leases on the balance sheet as both a right-of-use (ROU) asset and a liability. The standard continues to have two types of leases for income statement recognition purposes: operating leases and finance leases. Operating leases result in the recognition of a single lease expense on a straight-line basis over the lease term, similar to the treatment for operating leases under the old standard. Finance leases result in an accelerated expense similar to the accounting for capital leases under the old standard. The determination of a lease classification as operating or finance will occur in a manner similar to the old standard. The new standard also contains amended guidance regarding the identification of embedded leases in service contracts and the identification of lease and non-lease components of an arrangement.

We adopted the new standard on January 1, 2019, using a modified retrospective approach and as a result did not adjust prior periods. Adoption of the standard resulted in the recording of \$450 million of operating lease right-of-use assets and operating lease liabilities, but did not have a material impact on our net income or cash flows. The cumulative effect adjustment of adopting the new standard was not material. We elected the package of practical expedients permitted under the transition guidance within the new standard, which among other things, allowed us to carry forward the historical lease classification and to not re-evaluate existing contracts as to whether or not they contained a lease.

Lease Policies

We determine if an arrangement contains a lease in whole or in part at the inception of the contract. ROU assets represent our right to use an underlying asset for the lease term while lease liabilities represent our obligation to make lease payments arising from the lease. All leases greater than 12 months result in the recognition of a ROU asset and a liability at the lease commencement date based on the present value of the lease payments over the lease term. As most of our leases do not provide the information required to determine the implicit rate, we use our incremental borrowing rate based on the information available at commencement date in determining the present value of lease payments. This rate is determined considering factors such as the lease term, our credit standing and the economic environment of the location of the lease. We use the implicit rate when readily determinable.

Our lease terms include all non-cancelable periods and may include options to extend (or to not terminate) the lease when it is reasonably certain that we will exercise that option. Leases that have a term of 12 months or less at the commencement date are expensed on a straight-line basis over the lease term and do not result in the recognition of an asset or a liability.

Lease expense for operating leases is recognized on a straight-line basis over the lease term. Lease expense for finance leases are generally front-loaded as the finance lease ROU asset is depreciated on a straight-line basis, but interest expense on the liability is recognized utilizing the interest method that results in more expense during the early years of the lease. We have lease agreements with lease and non-lease components, primarily related to real estate, vehicle and Information Technology (IT) leases. For vehicle and real estate leases, we account for the lease and non-lease components as a single lease component. For IT leases, we allocate the payment between the lease and non-lease components based on the relative value of each component.

Leases

Our lease portfolio consists primarily of real estate and equipment leases. Our real estate leases primarily consist of office, distribution, warehousing and manufacturing facilities. These leases typically range in term from 2 to 30 years and may contain renewal options for periods up to two years at our discretion. Our equipment lease portfolio consists primarily of vehicles (including service vehicles), forklifts and IT equipment. These leases typically range in term from two years to three years and may contain renewal options. Our leases generally do not contain variable lease payments other than (1) certain foreign real estate leases which have payments indexed to inflation and (2) certain real estate executory costs (such as taxes, insurance and maintenance) which are paid based on actual expenses incurred by the lessor during the year. Our leases generally do not include residual value guarantees other than our service vehicle fleet which has a residual guarantee based on a percentage of the original cost declining over the lease term.

The components of our lease expense were as follows:

In millions	Three months ended	Six months ended
	June 30, 2019	June 30, 2019
Operating lease cost	\$ 54	\$ 104
Finance lease cost		
Amortization of right-of-use asset	4	9
Interest expense	3	6
Short-term lease cost	1	2
Variable lease cost	1	2
Total lease cost	<u>\$ 63</u>	<u>\$ 123</u>

Supplemental balance sheet information related to leases:

In millions	June 30, 2019	Balance Sheet Location
Assets		
Operating lease assets	\$ 434	Other assets
Finance lease assets ⁽¹⁾	128	Property, plant and equipment, net
Total lease assets	<u>\$ 562</u>	
Liabilities		
Current		
Operating	\$ 125	Other accrued expenses
Finance	12	Current maturities of long-term debt
Long-term		
Operating	321	Other liabilities
Finance	113	Long-term debt
Total lease liabilities	<u>\$ 571</u>	

⁽¹⁾ Finance lease assets are recorded net of accumulated amortization of \$61 million at June 30, 2019.

Supplemental cash flow and other information related to leases:

In millions	Three months ended	Six months ended
	June 30, 2019	June 30, 2019
Cash paid for amounts included in the measurement of lease liabilities:		
Operating cash flows from operating leases	\$ 41	\$ 77
Operating cash flows from finance leases	3	5
Financing cash flows from finance leases	3	7
Right-of-use assets obtained in exchange for lease obligations:		
Operating leases	60	78
Finance leases	5	6

Additional information related to leases:

	June 30, 2019
Weighted-average remaining lease term (in years)	
Operating leases	5.2
Finance leases	14.2
Weighted-average discount rate	
Operating leases	3.4%
Finance leases	4.2%

Following is a summary of the future minimum lease payments due to finance and operating leases with terms of more than one year at June 30, 2019, together with the net present value of the minimum payments due to finance leases:

In millions	Finance Leases	Operating Leases
2019	\$ 10	\$ 73
2020	19	121
2021	16	93
2022	15	69
2023	14	45
After 2023	144	96
Total minimum lease payments	\$ 218	\$ 497
Interest	(93)	(51)
Present value of net minimum lease payments	\$ 125	\$ 446

Following is a summary of the future minimum lease payments due to capital and operating leases with terms of more than one year at December 31, 2018, together with the net present value of the minimum payments due to capital leases under the previous lease standard:

In millions	Capital Leases	Operating Leases
2019	\$ 30	\$ 138
2020	21	109
2021	16	81
2022	14	60
2023	13	39
After 2023	144	81
Total minimum lease payments	\$ 238	\$ 508
Interest	(106)	
Present value of net minimum lease payments	\$ 132	

NOTE 10. DEBT

Loans Payable and Commercial Paper

Loans payable, commercial paper and the related weighted-average interest rates were as follows:

In millions	June 30, 2019	December 31, 2018
Loans payable ⁽¹⁾	\$ 119	\$ 54
Commercial paper ⁽²⁾	434	780

⁽¹⁾ Loans payable consist primarily of notes payable to various domestic and international financial institutions and it is not practicable to aggregate these notes and calculate a quarterly weighted-average interest rate.

⁽²⁾ The weighted-average interest rate, inclusive of all brokerage fees, was 2.56 percent and 2.59 percent at June 30, 2019 and December 31, 2018, respectively.

We can issue up to \$3.5 billion of unsecured, short-term promissory notes ("commercial paper") pursuant to our board authorized commercial paper programs. The programs facilitate the private placement of unsecured short-term debt through third party brokers. We intend to use the net proceeds from the commercial paper borrowings for general corporate purposes.

Revolving Credit Facilities

We have access to committed credit facilities that total \$3.5 billion, including a \$1.5 billion 364-day facility that expires August 21, 2019 and a \$2.0 billion five-year facility that expires on August 22, 2023. We intend to maintain credit facilities of a similar aggregate amount by renewing or replacing these facilities before expiration. These revolving credit facilities are maintained primarily to provide backup liquidity for our commercial paper borrowings and for general corporate purposes.

At June 30, 2019, the \$434 million of outstanding commercial paper effectively reduced the \$3.5 billion of revolving credit capacity to \$3.1 billion and had an additional \$211 million available for borrowings under our international and other domestic credit facilities.

Long-term Debt

A summary of long-term debt was as follows:

In millions	Interest Rate	June 30, 2019	December 31, 2018
Long-term debt			
Senior notes, due 2023	3.65%	\$ 500	\$ 500
Debentures, due 2027	6.75%	58	58
Debentures, due 2028	7.125%	250	250
Senior notes, due 2043	4.875%	500	500
Debentures, due 2098 ⁽¹⁾	5.65%	165	165
Other debt		83	64
Unamortized discount		(51)	(52)
Fair value adjustments due to hedge on indebtedness		40	25
Finance leases		125	132
Total long-term debt		1,670	1,642
Less: Current maturities of long-term debt		46	45
Long-term debt		\$ 1,624	\$ 1,597

⁽¹⁾ The effective interest rate on this debt is 7.48%.

Principal payments required on long-term debt during the next five years are as follows:

In millions	2019	2020	2021	2022	2023
Principal payments	\$ 37	\$ 29	\$ 43	\$ 8	\$ 507

Fair Value of Debt

Based on borrowing rates currently available to us for bank loans with similar terms and average maturities, considering our risk premium, the fair values and carrying values of total debt, including current maturities, were as follows:

In millions	June 30, 2019	December 31, 2018
Fair value of total debt ⁽¹⁾	\$ 2,535	\$ 2,679
Carrying values of total debt	2,223	2,476

⁽¹⁾ The fair value of debt is derived from Level 2 inputs.

Shelf Registration

As a well-known seasoned issuer, we filed an automatic shelf registration for an undetermined amount of debt and equity securities with the SEC on February 13, 2019. Under this shelf registration we may offer, from time to time, debt securities, common stock, preferred and preference stock, depositary shares, warrants, stock purchase contracts and stock purchase units.

NOTE 11. PRODUCT WARRANTY LIABILITY

A tabular reconciliation of the product warranty liability, including the deferred revenue related to our extended warranty coverage and accrued product campaigns was as follows:

In millions	Six months ended	
	June 30, 2019	July 1, 2018
Balance, beginning of year	\$ 2,208	\$ 1,687
Provision for base warranties issued	259	222
Deferred revenue on extended warranty contracts sold	171	139
Provision for product campaigns issued	134	403
Payments made during period	(308)	(212)
Amortization of deferred revenue on extended warranty contracts	(117)	(118)
Changes in estimates for pre-existing product warranties	(8)	10
Foreign currency translation and other	(1)	(1)
Balance, end of period	\$ 2,338	\$ 2,130

We recognized supplier recoveries of \$3 million and \$61 million and \$10 million and \$13 million for the three and six months ended June 30, 2019 and July 1, 2018, respectively.

Warranty related deferred revenues and the long-term portion of the warranty liabilities on our *Condensed Consolidated Balance Sheets* were as follows:

In millions	June 30, 2019	December 31, 2018	Balance Sheet Location
Deferred revenue related to extended coverage programs			
Current portion	\$ 224	\$ 227	Current portion of deferred revenue
Long-term portion	642	587	Deferred revenue
Total	<u>\$ 866</u>	<u>\$ 814</u>	
Product warranty			
Current portion	\$ 809	\$ 654	Current portion of accrued product warranty
Long-term portion	663	740	Accrued product warranty
Total	<u>\$ 1,472</u>	<u>\$ 1,394</u>	
Total warranty accrual	<u>\$ 2,338</u>	<u>\$ 2,208</u>	

Engine System Campaign Accrual

During 2017, the California Air Resources Board (CARB) and the U.S. Environmental Protection Agency (EPA) selected certain of our pre-2013 model year engine systems for additional emissions testing. Some of these engine systems failed CARB and EPA tests as a result of degradation of an aftertreatment component.

In the first quarter of 2018, we concluded based upon additional emission testing performed, and further discussions with the EPA and CARB that the field campaigns should be expanded to include a larger population of our engine systems that are subject to the aftertreatment component degradation, including our model years 2010 through 2015. As a result, we recorded an additional charge of \$187 million or \$0.87 per share, to cost of sales in our *Condensed Consolidated Statements of Net Income* (\$94 million recorded in the Components segment and \$93 million in the Engine segment).

In the second quarter of 2018, we reached agreement with the CARB and EPA regarding our plans to address the affected populations. In finalizing our plans, we increased the number of systems to be addressed through hardware replacement compared to our assumptions resulting in an additional charge of \$181 million, or \$0.85 per share, to cost of sales in our *Condensed Consolidated Statements of Net Income* (\$91 million recorded in the Engine segment and \$90 million in the Components segment).

The campaigns launched in the third quarter of 2018 and will be completed in phases across the affected population with a projection to be substantially complete by December 31, 2020. The total engine system campaign charge, excluding supplier recoveries, was \$410 million. At June 30, 2019, the remaining accrual balance was \$309 million.

NOTE 12. COMMITMENTS AND CONTINGENCIES

We are subject to numerous lawsuits and claims arising out of the ordinary course of our business, including actions related to product liability; personal injury; the use and performance of our products; warranty matters; product recalls; patent, trademark or other intellectual property infringement; contractual liability; the conduct of our business; tax reporting in foreign jurisdictions; distributor termination; workplace safety; and environmental matters. We also have been identified as a potentially responsible party at multiple waste disposal sites under U.S. federal and related state environmental statutes and regulations and may have joint and several liability for any investigation and remediation costs incurred with respect to such sites. We have denied liability with respect to many of these lawsuits, claims and proceedings and are vigorously defending such lawsuits, claims and proceedings. We carry various forms of commercial, property and casualty, product liability and other forms of insurance; however, such insurance may not be applicable or adequate to cover the costs associated with a judgment against us with respect to these lawsuits, claims and proceedings. We do not believe that these lawsuits are material individually or in the aggregate. While we believe we have also established adequate accruals pursuant to GAAP for our expected future liability with respect to pending lawsuits, claims and proceedings, where the nature and extent of any such liability can be

reasonably estimated based upon then presently available information, there can be no assurance that the final resolution of any existing or future lawsuits, claims or proceedings will not have a material adverse effect on our business, results of operations, financial condition or cash flows.

We conduct significant business operations in Brazil that are subject to the Brazilian federal, state and local labor, social security, tax and customs laws. While we believe we comply with such laws, they are complex, subject to varying interpretations and we are often engaged in litigation regarding the application of these laws to particular circumstances.

On April 29, 2019, we announced that we were conducting a formal internal review of our emissions certification process and compliance with emissions standards for our pick-up truck applications, following conversations with the EPA and CARB regarding certification of our engines in model year 2019 RAM 2500 and 3500 trucks. This review is being conducted with external advisors to ensure the certification and compliance processes for all of our pick-up truck applications are consistent with our internal policies, engineering standards and applicable laws. In addition, we announced that we voluntarily disclosed our formal internal review to our regulators and other agencies and were working cooperatively to ensure a complete and thorough review. During conversations with the EPA and CARB about the effectiveness of our pick-up truck applications, the agencies raised concerns that certain aspects of our emissions systems may reduce the effectiveness of our emissions control systems and did not fully comply with their requirements for certification. As a result, our internal review focuses, in part, on the agencies' concerns. We are working closely with the agencies to enhance our emission systems to improve the effectiveness of all of our pick-up truck applications and to fully address the agencies' requirements. Due to the preliminary nature of our formal review, our collaboration with our regulators to address their questions and concerns and the presence of many unknown facts and circumstances, we cannot predict the outcome of this review and process, and we cannot provide assurance that the matter will not have a materially adverse impact on our results of operations and cash flows.

Guarantees and Commitments

Periodically, we enter into guarantee arrangements, including guarantees of non-U.S. distributor financings, residual value guarantees on equipment under operating leases and other miscellaneous guarantees of joint ventures or third-party obligations. At June 30, 2019, the maximum potential loss related to these guarantees was \$52 million.

We have arrangements with certain suppliers that require us to purchase minimum volumes or be subject to monetary penalties. At June 30, 2019, if we were to stop purchasing from each of these suppliers, the aggregate amount of the penalty would be approximately \$57 million. Most of these arrangements enable us to secure supplies of critical components. We do not currently anticipate paying any penalties under these contracts.

We enter into physical forward contracts with suppliers of platinum and palladium to purchase certain volumes of the commodities at contractually stated prices for various periods, which generally fall within two years. At June 30, 2019, the total commitments under these contracts were \$64 million. These arrangements enable us to fix the prices of these commodities, which otherwise are subject to market volatility.

We have guarantees with certain customers that require us to satisfactorily honor contractual or regulatory obligations, or compensate for monetary losses related to nonperformance. These performance bonds and other performance-related guarantees were \$117 million at June 30, 2019.

Indemnifications

Periodically, we enter into various contractual arrangements where we agree to indemnify a third-party against certain types of losses. Common types of indemnities include:

- product liability and license, patent or trademark indemnifications;
- asset sale agreements where we agree to indemnify the purchaser against future environmental exposures related to the asset sold; and
- any contractual agreement where we agree to indemnify the counterparty for losses suffered as a result of a misrepresentation in the contract.

We regularly evaluate the probability of having to incur costs associated with these indemnities and accrue for expected losses that are probable. Because the indemnifications are not related to specified known liabilities and due to their uncertain nature, we are unable to estimate the maximum amount of the potential loss associated with these indemnifications.

Purchase Agreement

In June 2019, we entered into a definitive agreement to acquire, through a wholly-owned subsidiary, all of the issued and outstanding shares of fuel cell systems provider Hydrogenics Corporation, other than shares already owned by The Hydrogen Company, representing an enterprise value of approximately \$290 million, subject to customary closing conditions and shareholder approvals. The Hydrogen Company, a wholly-owned subsidiary of L'Air Liquide, S.A., and Hydrogenics' current largest equity shareholder, will maintain a non-controlling ownership interest in Hydrogenics. If Hydrogenics' shareholder approval is obtained, the transaction is expected to close in the third quarter of 2019.

NOTE 13. ACCUMULATED OTHER COMPREHENSIVE LOSS

Following are the changes in accumulated other comprehensive income (loss) by component for the three months ended:

In millions	Three months ended						
	Change in pensions and other postretirement defined benefit plans	Foreign currency translation adjustment	Unrealized gain (loss) on marketable securities	Unrealized gain (loss) on derivatives	Total attributable to Cummins Inc.	Noncontrolling interests	Total
Balance at March 31, 2019	\$ (682)	\$ (1,057)	\$ (1)	\$ 1	\$ (1,739)		
Other comprehensive income before reclassifications							
Before tax amount	1	(97)	1	(11)	(106)	\$ —	\$(106)
Tax benefit (expense)	—	(2)	—	4	2	—	2
After tax amount	1	(99)	1	(7)	(104)	—	(104)
Amounts reclassified from accumulated other comprehensive loss ⁽¹⁾	6	—	—	(3)	3	—	3
Net current period other comprehensive income (loss)	7	(99)	1	(10)	(101)	\$ —	\$(101)
Balance at June 30, 2019	\$ (675)	\$ (1,156)	\$ —	\$ (9)	\$ (1,840)		
Balance at April 1, 2018	\$ (681)	\$ (720)	\$ —	\$ 4	\$ (1,397)		
Other comprehensive income before reclassifications							
Before tax amount	—	(328)	—	4	(324)	\$ (17)	\$(341)
Tax benefit (expense)	—	45	—	(2)	43	—	43
After tax amount	—	(283)	—	2	(281)	(17)	(298)
Amounts reclassified from accumulated other comprehensive loss ⁽¹⁾	13	—	—	(2)	11	1	12
Net current period other comprehensive income (loss)	13	(283)	—	—	(270)	\$ (16)	\$(286)
Balance at July 1, 2018	\$ (668)	\$ (1,003)	\$ —	\$ 4	\$ (1,667)		

⁽¹⁾ Amounts are net of tax. Reclassifications out of accumulated other comprehensive income (loss) and the related tax effects are immaterial for separate disclosure.

Following are the changes in accumulated other comprehensive income (loss) by component for the six months ended:

In millions	Six months ended						Total
	Change in pensions and other postretirement defined benefit plans	Foreign currency translation adjustment	Unrealized gain (loss) on marketable securities	Unrealized gain (loss) on derivatives	Total attributable to Cummins Inc.	Noncontrolling interests	
Balance at December 31, 2018	\$ (671)	\$ (1,138)	\$ —	\$ 2	\$ (1,807)		
Other comprehensive income before reclassifications							
Before tax amount	(22)	(17)	—	(8)	(47)	\$ 3	\$ (44)
Tax benefit (expense)	5	(1)	—	3	7	—	7
After tax amount	(17)	(18)	—	(5)	(40)	3	(37)
Amounts reclassified from accumulated other comprehensive loss ⁽¹⁾	13	—	—	(6)	7	—	7
Net current period other comprehensive income (loss)	(4)	(18)	—	(11)	(33)	\$ 3	\$ (30)
Balance at June 30, 2019	<u>\$ (675)</u>	<u>\$ (1,156)</u>	<u>\$ —</u>	<u>\$ (9)</u>	<u>\$ (1,840)</u>		
Balance at December 31, 2017	\$ (689)	\$ (812)	\$ 1	\$ (3)	\$ (1,503)		
Other comprehensive income before reclassifications							
Before tax amount	(8)	(203)	—	15	(196)	\$ (24)	\$ (220)
Tax benefit (expense)	2	12	—	(6)	8	—	8
After tax amount	(6)	(191)	—	9	(188)	(24)	(212)
Amounts reclassified from accumulated other comprehensive loss ⁽¹⁾	27	—	(1)	(2)	24	1	25
Net current period other comprehensive income (loss)	21	(191)	(1)	7	(164)	\$ (23)	\$ (187)
Balance at July 1, 2018	<u>\$ (668)</u>	<u>\$ (1,003)</u>	<u>\$ —</u>	<u>\$ 4</u>	<u>\$ (1,667)</u>		

⁽¹⁾ Amounts are net of tax. Reclassifications out of accumulated other comprehensive income (loss) and the related tax effects are immaterial for separate disclosure.

NOTE 14. OPERATING SEGMENTS

Operating segments under GAAP are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the Chief Operating Decision Maker (CODM), or decision-making group, in deciding how to allocate resources and in assessing performance. Our CODM is the President and Chief Operating Officer.

Our reportable operating segments consist of Engine, Distribution, Components, Power Systems and Electrified Power. This reporting structure is organized according to the products and markets each segment serves. The Engine segment produces engines (15 liters and smaller) and associated parts for sale to customers in on-highway and various off-highway markets. Our engines are used in trucks of all sizes, buses and recreational vehicles, as well as in various industrial applications, including construction, agriculture, power generation systems and other off-highway applications. The Distribution segment includes wholly-owned and partially-owned distributorships engaged in wholesaling engines, generator sets and service parts, as well as performing service and repair activities on our products and maintaining relationships with various OEMs throughout the world. The Components segment sells filtration products, aftertreatment systems, turbochargers, electronics, fuel systems and transmissions. The Power Systems segment is an integrated power provider, which designs, manufactures and sells engines (16 liters and larger) for industrial applications (including mining, oil and gas, marine and rail), standby and prime power generator sets, alternators and other power components. The Electrified Power segment designs, manufactures, sells and supports electrified power systems ranging from fully electric to hybrid solutions along with innovative components and subsystems to serve all our markets as they adopt electrification, meeting the needs of our OEM partners and end customers.

We use EBITDA (defined as earnings before interest expense, income taxes, noncontrolling interests, depreciation and amortization) as the primary basis for the CODM to evaluate the performance of each of our reportable operating segments. Segment amounts exclude certain expenses not specifically identifiable to segments.

The accounting policies of our operating segments are the same as those applied in our *Condensed Consolidated Financial Statements*. We prepared the financial results of our operating segments on a basis that is consistent with the manner in which we internally disaggregate financial information to assist in making internal operating decisions. We allocate certain common costs and expenses, primarily corporate functions, among segments differently than we would for stand-alone financial information prepared in accordance with GAAP. These include certain costs and expenses of shared services, such as information technology, human resources, legal, finance and supply chain management. We do not allocate changes in cash surrender value of corporate owned life insurance to individual segments. EBITDA may not be consistent with measures used by other companies.

Summarized financial information regarding our reportable operating segments for the three months ended is shown in the table below:

In millions	Engine	Distribution	Components	Power Systems	Electrified Power	Total Segments	Intersegment Eliminations ⁽¹⁾	Total
Three months ended June 30, 2019								
External sales	\$ 2,073	\$ 2,015	\$ 1,401	\$ 724	\$ 8	\$ 6,221	\$ —	\$ 6,221
Intersegment sales	630	13	445	479	—	1,567	(1,567)	—
Total sales	2,703	2,028	1,846	1,203	8	7,788	(1,567)	6,221
Research, development and engineering expenses	88	7	75	57	24	251	—	251
Equity, royalty and interest income from investees	62	12	11	11	—	96	—	96
Interest income	4	4	2	2	—	12	—	12
Segment EBITDA	416	172	297	173	(33)	1,025	33	1,058
Depreciation and amortization ⁽²⁾	51	28	47	30	2	158	—	158
Three months ended July 1, 2018								
External sales	\$ 2,050	\$ 1,988	\$ 1,402	\$ 691	\$ 1	\$ 6,132	\$ —	\$ 6,132
Intersegment sales	646	6	485	555	—	1,692	(1,692)	—
Total sales	2,696	1,994	1,887	1,246	1	7,824	(1,692)	6,132
Research, development and engineering expenses	76	5	62	60	16	219	—	219
Equity, royalty and interest income from investees	67	11	14	18	—	110	—	110
Interest income	3	3	2	2	—	10	—	10
Segment EBITDA	362	145	237	186	(21)	909	(12)	897
Depreciation and amortization ⁽²⁾	47	27	47	32	1	154	—	154

⁽¹⁾ Includes intersegment sales, intersegment profit in inventory eliminations and unallocated corporate expenses. There were no significant unallocated corporate expenses for the three months ended June 30, 2019 and July 1, 2018.

⁽²⁾ Depreciation and amortization, as shown on a segment basis, excludes the amortization of debt discount and deferred costs included in the *Condensed Consolidated Statements of Net Income* as "Interest expense." A portion of depreciation expense is included in "Research, development and engineering expenses."

Summarized financial information regarding our reportable operating segments for the six months ended is shown in the table below:

In millions	Engine	Distribution	Components	Power Systems	Electrified Power	Total Segments	Intersegment Eliminations ⁽¹⁾	Total
Six months ended June 30, 2019								
External sales	\$ 4,057	\$ 4,008	\$ 2,802	\$ 1,347	\$ 11	\$ 12,225	\$ —	\$ 12,225
Intersegment sales	1,299	21	905	933	—	3,158	(3,158)	—
Total sales	5,356	4,029	3,707	2,280	11	15,383	(3,158)	12,225
Research, development and engineering expenses	166	14	150	113	45	488	—	488
Equity, royalty and interest income from investees	118	23	21	26	—	188	—	188
Interest income	8	8	4	4	—	24	—	24
Segment EBITDA	854	343	622	311	(62)	2,068	23	2,091
Depreciation and amortization ⁽²⁾	101	57	93	59	4	314	—	314
Six months ended July 1, 2018								
External sales	\$ 3,863	\$ 3,835	\$ 2,715	\$ 1,286	\$ 3	\$ 11,702	\$ —	\$ 11,702
Intersegment sales	1,279	12	925	1,034	—	3,250	(3,250)	—
Total sales	5,142	3,847	3,640	2,320	3	14,952	(3,250)	11,702
Research, development and engineering expenses	155	10	124	117	23	429	—	429
Equity, royalty and interest income from investees	134	24	30	37	—	225	—	225
Interest income	5	5	3	4	—	17	—	17
Segment EBITDA	648	268	464	328	(31)	1,677	(80)	1,597
Depreciation and amortization ⁽²⁾	96	54	93	62	2	307	—	307

⁽¹⁾ Includes intersegment sales, intersegment profit in inventory eliminations and unallocated corporate expenses. There were no significant unallocated corporate expenses for the six months ended June 30, 2019 and July 1, 2018.

⁽²⁾ Depreciation and amortization, as shown on a segment basis, excludes the amortization of debt discount and deferred costs included in the *Condensed Consolidated Statements of Net Income* as "Interest expense." The amortization of debt discount and deferred costs was \$1 million and \$1 million for the six months ended June 30, 2019 and July 1, 2018, respectively. A portion of depreciation expense is included in "Research, development and engineering expenses."

A reconciliation of our segment information to the corresponding amounts in the *Condensed Consolidated Statements of Net Income* is shown in the table below:

In millions	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Total EBITDA	\$ 1,058	\$ 897	\$ 2,091	\$ 1,597
Less:				
Depreciation and amortization	158	154	314	307
Interest expense	29	28	61	52
Income before income taxes	\$ 871	\$ 715	\$ 1,716	\$ 1,238

NOTE 15. RECENTLY ADOPTED AND RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Accounting Pronouncements Recently Adopted

On January 1, 2019, we adopted the new lease standard in accordance with GAAP. See NOTE 9, "LEASES," for detailed information about the adoption of this standard.

On January 1, 2019, we adopted the new FASB standard related to accounting for derivatives and hedging. The new standard allows the initial hedge effectiveness assessment to be performed by the end of the first quarter in which the hedge is designated rather than concurrently with entering into the hedge transaction. The changes also expand the use of a periodic qualitative hedge effectiveness assessment in lieu of an ongoing quantitative assessment performed throughout the life of the hedge. The revision removes the requirement to record ineffectiveness on cash flow hedges through the income statement when a hedge is considered highly effective, instead deferring all related hedge gains and losses in other comprehensive income until the hedged item impacts earnings. The modifications permit hedging the contractually-specified price of a component of a commodity purchase and revises certain disclosure requirements. We adopted the new standard on a modified retrospective basis for existing cash flow hedges and prospectively for disclosures. The amendments did not have a material effect on our *Condensed Consolidated Financial Statements* and no transition adjustment was required upon adoption. The adoption of this standard did not materially change our policies for existing hedges.

Accounting Pronouncements Issued But Not Yet Effective

In August 2018, the FASB issued a new standard that aligns the accounting for implementation costs incurred in a cloud computing arrangement accounted for as a service contract with the model currently used for internal use software costs. Under the new standard, costs that meet certain criteria will be required to be capitalized on the balance sheet and subsequently amortized over the term of the hosting arrangement. The standard is effective for us beginning on January 1, 2020, with early adoption permitted. The standard allows for either prospective or retrospective transition. We are still evaluating the impact of this standard on our financial statements.

In June 2016, the FASB amended its standards related to accounting for credit losses on financial instruments. This amendment introduces new guidance for accounting for credit losses on instruments including trade receivables and held-to-maturity debt securities. The new rules are effective for annual and interim periods beginning after December 15, 2019. Early adoption is permitted for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. We do not expect adoption of this standard to have a material impact on our *Consolidated Financial Statements*.

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Cummins Inc. and its consolidated subsidiaries are hereinafter sometimes referred to as "Cummins," "we," "our" or "us."

CAUTIONARY STATEMENTS REGARDING FORWARD-LOOKING INFORMATION

Certain parts of this quarterly report contain forward-looking statements intended to qualify for the safe harbors from liability established by the Private Securities Litigation Reform Act of 1995. Forward-looking statements include those that are based on current expectations, estimates and projections about the industries in which we operate and management's beliefs and assumptions. Forward-looking statements are generally accompanied by words such as "anticipates," "expects," "forecasts," "intends," "plans," "believes," "seeks," "estimates," "could," "should" or words of similar meaning. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions, which we refer to as "future factors," which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements. Some future factors that could cause our results to differ materially from the results discussed in such forward-looking statements are discussed below and shareholders, potential investors and other readers are urged to consider these future factors carefully in evaluating forward-looking statements. Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date hereof. Future factors that could affect the outcome of forward-looking statements include the following:

- any adverse results of our internal review into our emissions certification process and compliance with emissions standards;
- a sustained slowdown or significant downturn in our markets;
- changes in the engine outsourcing practices of significant customers;
- the development of new technologies that reduce demand for our current products and services;
- increased scrutiny from regulatory agencies, as well as unpredictability in the adoption, implementation and enforcement of emissions standards around the world;
- product recalls;
- policy changes in international trade;
- the United Kingdom's (U.K.) decision to end its membership in the European Union;
- lower than expected acceptance of new or existing products or services;
- a slowdown in infrastructure development and/or depressed commodity prices;
- supply shortages and supplier financial risk, particularly from any of our single-sourced suppliers;
- exposure to potential security breaches or other disruptions to our information technology systems and data security;
- a major customer experiencing financial distress;
- the actions of, and income from, joint ventures and other investees that we do not directly control;
- our plan to reposition our portfolio of product offerings through exploration of strategic acquisitions and divestitures and related uncertainties of entering such transactions;
- failure to realize expected results from our investment in Eaton Cummins Automated Transmission Technologies joint venture;
- competitor activity;
- increasing competition, including increased global competition among our customers in emerging markets;
- foreign currency exchange rate changes;
- variability in material and commodity costs;
- political, economic and other risks from operations in numerous countries;
- changes in taxation;
- global legal and ethical compliance costs and risks;
- aligning our capacity and production with our demand;

- product liability claims;
- increasingly stringent environmental laws and regulations;
- future bans or limitations on the use of diesel-powered products;
- the price and availability of energy;
- the performance of our pension plan assets and volatility of discount rates;
- labor relations;
- changes in accounting standards;
- our sales mix of products;
- protection and validity of our patent and other intellectual property rights;
- the outcome of pending and future litigation and governmental proceedings;
- continued availability of financing, financial instruments and financial resources in the amounts, at the times and on the terms required to support our future business; and
- other risk factors described in our [2018 Form 10-K, Part I, Item 1A. under the caption “Risk Factors.”](#)

Shareholders, potential investors and other readers are urged to consider these factors carefully in evaluating the forward-looking statements and are cautioned not to place undue reliance on such forward-looking statements. The forward-looking statements made herein are made only as of the date of this quarterly report and we undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise.

ORGANIZATION OF INFORMATION

The following Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) was prepared to provide the reader with a view and perspective of our business through the eyes of management and should be read in conjunction with our Management's Discussion and Analysis of Financial Condition and [Results of Operations section of our 2018 Form 10-K](#). Our MD&A is presented in the following sections:

- **EXECUTIVE SUMMARY AND FINANCIAL HIGHLIGHTS**
- **OUTLOOK**
- **RESULTS OF OPERATIONS**
- **OPERATING SEGMENT RESULTS**
- **LIQUIDITY AND CAPITAL RESOURCES**
- **APPLICATION OF CRITICAL ACCOUNTING ESTIMATES**
- **RECENTLY ADOPTED AND RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS**

EXECUTIVE SUMMARY AND FINANCIAL HIGHLIGHTS

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 have long-standing relationships with many of the leading manufacturers in the markets we serve, including PACCAR Inc, Navistar International Corporation, Daimler Trucks North America and Fiat Chrysler Automobiles (Chrysler). 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.

Our reportable operating segments consist of Engine, Distribution, Components, Power Systems and Electrified Power. This reporting structure is organized according to the products and markets each segment serves. The Engine segment produces engines (15 liters and smaller) and associated parts for sale to customers in on-highway and various off-highway markets. Our engines are used in trucks of all sizes, buses and recreational vehicles, as well as in various industrial applications, including construction, agriculture, power generation systems and other off-highway applications. The Distribution segment includes wholly-owned and partially-owned distributorships engaged in wholesaling engines, generator sets and service parts, as well as performing service and repair activities on our products and maintaining relationships with various OEMs throughout the world. The Components segment sells filtration products, aftertreatment systems, turbochargers, electronics, fuel systems and transmissions. The Power Systems segment is an integrated power provider, which designs, manufactures and sells engines (16 liters and larger) for industrial applications (including mining, oil and gas, marine and rail), standby and prime power generator sets, alternators and other power components. The Electrified Power segment designs, manufactures, sells and supports electrified power systems ranging from fully electric to hybrid solutions along with innovative components and subsystems to serve all our markets as they adopt electrification, meeting the needs of our OEM partners and end customers.

Our financial performance depends, in large part, on varying conditions in the markets we serve, particularly the on-highway, construction and general industrial markets. Demand in these markets tends to fluctuate in response to overall economic conditions. Our sales may also be impacted by OEM inventory levels, production schedules and stoppages. Economic downturns in markets we serve generally result in reduced sales of our products and can result in price reductions in certain products and/or markets. As a worldwide business, our operations are also affected by currency, political, economic and regulatory matters, including adoption and enforcement of environmental and emissions standards, in the countries we serve. As part of our growth strategy, we invest in businesses in certain countries that carry high levels of these risks such as China, Brazil, India, Mexico, Russia and countries in the Middle East and Africa. At the same time, our geographic diversity and broad product and service offerings have helped limit the impact from a drop in demand in any one industry or customer or the economy of any single country on our consolidated results.

Worldwide revenues increased 1 percent in the three months ended June 30, 2019, compared to the same period in 2018, as higher sales in Distribution, Engine and Electrified Power segments were partially offset by lower sales in the Power Systems and Components segments. Net sales in the United States (U.S.) and Canada improved by 7 percent primarily due to increased demand in the North American on-highway markets (mainly in the pick-up and heavy-duty truck markets) and sales of power generation equipment to data center customers. International demand (excludes the U.S. and Canada) declined by 6 percent, with lower sales in most regions. The decrease in international sales was principally due to lower on-highway demand (mainly the light commercial vehicles (LCV) market in China and truck markets in Western Europe, India and Brazil, which also negatively impacted our emission solutions and turbo technologies businesses), lower off-highway demand in construction markets in China and Western Europe and unfavorable foreign currency impacts of 5 percent of international sales (primarily the Chinese renminbi, Euro, Brazilian real, British pound, Australian dollar and Indian rupee), partially offset by increased demand in China for power generation equipment to data center customers and engines for oil and gas markets.

Worldwide revenues increased 4 percent in the six months ended June 30, 2019, compared to the same period in 2018, as higher sales in Engine, Distribution and Components segments were partially offset by lower sales in the Power Systems segment. Net sales in the U.S. and Canada improved by 10 percent, primarily due to increased demand in the North American on-highway markets (mainly in the heavy-duty and medium-duty truck and pick-up markets) and sales of power generation equipment to data center customers. International demand (excludes the U.S. and Canada) declined by 3 percent, with lower sales principally in Europe, Russia and India. The decrease in international sales was driven by lower on-highway demand (mainly in the LCV market in China and Russia and truck markets in China, Western Europe and India, which negatively impacted our emission solutions and turbo technologies businesses) and unfavorable foreign currency impacts of 5 percent of international sales (primarily the Chinese renminbi, Euro, Brazilian real, Indian rupee, Australian dollar and British pound), partially offset by increased demand in China for both power generation equipment to data center customers and engines for oil and gas markets.

The following tables contain sales and EBITDA (defined as earnings before interest expense, income taxes, noncontrolling interests, depreciation and amortization) by operating segment for the three and six months ended June 30, 2019 and July 1, 2018. See the section titled "OPERATING SEGMENT RESULTS" for a more detailed discussion of net sales and EBITDA by operating segment including the reconciliation of segment EBITDA to net income attributable to Cummins Inc.

Operating Segments	Three months ended							
	June 30, 2019			July 1, 2018			Percent change	
	Percent		EBITDA	Percent		EBITDA	2019 vs. 2018	
In millions	Sales	of Total		Sales	of Total		Sales	EBITDA
Engine	\$ 2,703	43 %	\$ 416	\$ 2,696	44 %	\$ 362	— %	15 %
Distribution	2,028	33 %	172	1,994	33 %	145	2 %	19 %
Components	1,846	30 %	297	1,887	31 %	237	(2)%	25 %
Power Systems	1,203	19 %	173	1,246	20 %	186	(3)%	(7)%
Electrified Power	8	— %	(33)	1	— %	(21)	NM	(57)%
Intersegment eliminations	(1,567)	(25)%	33	(1,692)	(28)%	(12)	(7)%	NM
Total	\$ 6,221	100 %	\$ 1,058	\$ 6,132	100 %	\$ 897	1 %	18 %

"NM" - not meaningful information

Net income attributable to Cummins was \$675 million, or \$4.27 per diluted share, on sales of \$6.2 billion for the three months ended June 30, 2019, versus the comparable prior year period net income attributable to Cummins of \$545 million, or \$3.32 per diluted share, on sales of \$6.1 billion. The increases in net income and earnings per diluted share were driven by higher net sales and increased gross margin, partially offset by higher research, development and engineering and selling, general and administrative expenses, lower equity, royalty and interest income from investees and unfavorable foreign currency fluctuations (primarily the Australian dollar, Chinese renminbi, Canadian dollar and Brazilian real). The increases in gross margin and gross margin percentage were primarily due to lower warranty costs (due to absence of the \$181 million engine system campaign accrual recorded in the second quarter of 2018), increased pricing and favorable mix, partially offset by lower volumes and tariff impacts. Gross margin was also unfavorably impacted by foreign currency (primarily the Australian dollar, Euro, Brazilian real, Canadian dollar and South African rand, partially offset by the British pound). See Note 11, "PRODUCT WARRANTY LIABILITY," to the *Condensed Consolidated Financial Statements* for additional information on the engine system campaign.

Operating Segments	Six months ended							
	June 30, 2019			July 1, 2018			Percent change	
	Percent		EBITDA	Percent		EBITDA	2019 vs. 2018	
In millions	Sales	of Total		Sales	of Total		Sales	EBITDA
Engine	\$ 5,356	44 %	\$ 854	\$ 5,142	44 %	\$ 648	4 %	32 %
Distribution	4,029	33 %	343	3,847	33 %	268	5 %	28 %
Components	3,707	30 %	622	3,640	31 %	464	2 %	34 %
Power Systems	2,280	19 %	311	2,320	20 %	328	(2)%	(5)%
Electrified Power	11	— %	(62)	3	— %	(31)	NM	(100)%
Intersegment eliminations	(3,158)	(26)%	23	(3,250)	(28)%	(80)	(3)%	NM
Total	\$12,225	100 %	\$ 2,091	\$11,702	100 %	\$ 1,597	4 %	31 %

"NM" - not meaningful information

Net income attributable to Cummins was \$1,338 million, or \$8.47 per diluted share, on sales of \$12.2 billion for the six months ended June 30, 2019, versus the comparable prior year period net income attributable to Cummins of \$870 million, or \$5.27 per diluted share, on sales of \$11.7 billion. The increases in net income and earnings per diluted share were driven by higher net sales, increased gross margin, a lower effective tax rate due to the absence of \$74 million of unfavorable discrete tax items recognized in the first half of 2018 principally due to the 2017 Tax Legislation and an increase in the cash surrender value of corporate owned life insurance, partially offset by higher research, development and engineering expenses, lower equity, royalty and interest income from investees, unfavorable foreign currency fluctuations (primarily the Australian dollar, Brazilian real, Chinese renminbi and Canadian dollar) and increased selling, general and administrative expenses. The increases in gross margin and gross margin percentage were mainly due to lower warranty costs (due to absence of the \$368 million engine system campaign accrual recorded in the first half of 2018), increased pricing, higher volumes and favorable mix, partially

offset by tariff impacts and unfavorable foreign currency impacts (primarily the Australian dollar, Brazilian real, Euro and Canadian dollar, partially offset by the British pound). See Note 11, "PRODUCT WARRANTY LIABILITY," to the *Condensed Consolidated Financial Statements* for additional information on the engine system campaign. Diluted earnings per common share for the six months ended June 30, 2019, benefited \$0.03 from fewer weighted-average shares outstanding, primarily due to the stock repurchase programs.

We generated \$1,220 million of cash from operations for the six months ended June 30, 2019, compared to \$473 million for the comparable period in 2018. Refer to the section titled "Cash Flows" in the "LIQUIDITY AND CAPITAL RESOURCES" section for a discussion of items impacting cash flows.

Our debt to capital ratio (total capital defined as debt plus equity) at June 30, 2019, was 19.5 percent, compared to 23.1 percent at December 31, 2018. The decrease was primarily due to significant net income and lower outstanding commercial paper. At June 30, 2019, we had \$1.7 billion in cash and marketable securities on hand and access to our \$3.5 billion credit facilities, if necessary, to meet currently anticipated investment and funding needs.

In July 2019, our Board of Directors authorized an increase to our quarterly dividend of 15 percent from \$1.14 per share to \$1.311 per share.

We expect our effective tax rate for the full year of 2019 to approximate 21.5 percent, excluding any discrete tax items.

Our global pension plans, including our unfunded and non-qualified plans, were 115 percent funded at December 31, 2018. Our U.S. plan, which represents approximately 54 percent of the worldwide pension obligation, was 131 percent funded and our U.K. plan was 115 percent funded. We anticipate making additional defined benefit pension contributions during the remainder of 2019 of \$46 million for our U.S. and U.K. pension plans. Approximately \$91 million of the estimated \$123 million of U.S. and U.K. pension contributions for the full year are voluntary. We expect our 2019 net periodic pension cost to approximate \$64 million.

In June 2019, we entered into a definitive agreement to acquire, through a wholly-owned subsidiary, all of the issued and outstanding shares of fuel cell systems provider Hydrogenics Corporation, other than shares already owned by The Hydrogen Company, representing an enterprise value of approximately \$290 million, subject to customary closing conditions and Hydrogenics' shareholder approval. See Note 12, "COMMITMENTS AND CONTINGENCIES," to the *Condensed Consolidated Financial Statements* for additional information on the acquisition.

On April 29, 2019, we announced that we were conducting a formal internal review of our emissions certification process and compliance with emissions standards for our pick-up truck applications, following conversations with the United States Environmental Protection Agency and the California Air Resources Board regarding certification of our engines in the model year 2019 RAM 2500 and 3500 trucks. Due to the preliminary nature of our formal review, our collaboration with our regulators to address their questions and concerns and the presence of many unknown facts and circumstances, we cannot predict the outcome of this review and process, and we cannot provide assurance that the matter will not have a materially adverse impact on our results of operations and cash flows. See Note 12, "COMMITMENTS AND CONTINGENCIES," to our *Condensed Consolidated Financial Statements* for additional information.

OUTLOOK

Our outlook reflects the following positive trends and challenges to our business that we expect could impact our revenue and earnings potential for the remainder of 2019.

Positive Trends

- We anticipate North American medium-duty and pick-up truck demand will remain strong.
- We anticipate power generation markets will remain stable, with increased demand in global data center markets.
- We expect construction markets will remain strong in North America and Europe.
- We expect demand in global mining markets will remain stable.

Challenges

- We anticipate North American heavy-duty truck demand will decline in the second half of 2019.
- Demand in truck and construction markets in China is expected to decline.
- Uncertainty in the U.K. surrounding its ability to negotiate favorable terms in its withdrawal from the European Union could have material negative impacts on our European operations in the near and long-term.
- We expect cost increases due to U.S. trade tariffs with China to continue.
- Prolonged trade disputes could negatively impact demand and trigger additional costs.
- Marine markets are expected to remain weak.
- We anticipate demand in oil and gas markets in North America will remain weak.

RESULTS OF OPERATIONS

In millions, except per share amounts	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
NET SALES	\$ 6,221	\$ 6,132	\$ 89	1 %	\$ 12,225	\$ 11,702	\$ 523	4 %
Cost of sales	4,580	4,692	112	2 %	9,052	9,062	10	— %
GROSS MARGIN	1,641	1,440	201	14 %	3,173	2,640	533	20 %
OPERATING EXPENSES AND INCOME								
Selling, general and administrative expenses	629	613	(16)	(3)%	1,222	1,190	(32)	(3)%
Research, development and engineering expenses	251	219	(32)	(15)%	488	429	(59)	(14)%
Equity, royalty and interest income from investees	96	110	(14)	(13)%	188	225	(37)	(16)%
Other operating income (expense), net	(9)	4	(13)	NM	(4)	6	(10)	NM
OPERATING INCOME	848	722	126	17 %	1,647	1,252	395	32 %
Interest income	12	10	2	20 %	24	17	7	41 %
Interest expense	29	28	(1)	(4)%	61	52	(9)	(17)%
Other income, net	40	11	29	NM	106	21	85	NM
INCOME BEFORE INCOME TAXES	871	715	156	22 %	1,716	1,238	478	39 %
Income tax expense	186	161	(25)	(16)%	362	359	(3)	(1)%
CONSOLIDATED NET INCOME	685	554	131	24 %	1,354	879	475	54 %
Less: Net income attributable to noncontrolling interests	10	9	(1)	(11)%	16	9	(7)	(78)%
NET INCOME ATTRIBUTABLE TO CUMMINS INC.	\$ 675	\$ 545	\$ 130	24 %	\$ 1,338	\$ 870	\$ 468	54 %
Diluted Earnings Per Common Share Attributable to Cummins Inc.	\$ 4.27	\$ 3.32	\$ 0.95	29 %	\$ 8.47	\$ 5.27	\$ 3.20	61 %

"NM" - not meaningful information

Percent of sales	Three months ended		Favorable/ (Unfavorable) Percentage Points	Six months ended		Favorable/ (Unfavorable) Percentage Points
	June 30, 2019	July 1, 2018		June 30, 2019	July 1, 2018	
Gross margin	26.4%	23.5%	2.9	26.0%	22.6%	3.4
Selling, general and administrative expenses	10.1%	10.0%	(0.1)	10.0%	10.2%	0.2
Research, development and engineering expenses	4.0%	3.6%	(0.4)	4.0%	3.7%	(0.3)

Net Sales

Net sales for the three months ended June 30, 2019, increased by \$89 million versus the comparable period in 2018. The primary drivers were as follows:

- Distribution segment sales increased 2 percent, primarily due to higher demand, especially in North America, and increased demand in the power generation product line.
- Engine segment sales slightly increased with higher volumes in North American heavy-duty, medium-duty and pick-up truck markets mostly offset by lower LCV demand in China and lower construction demand, primarily in China.

These increases were partially offset by:

- Unfavorable foreign currency fluctuations of 2 percent of total sales, primarily in the Chinese renminbi, Euro, Brazilian real, British pound and Australian dollar.
- Power systems sales decreased 3 percent, primarily due to lower demand in North American oil and gas markets.
- Components segment sales decreased 2 percent, primarily due to lower international truck demand in China, India and Western Europe, partially offset by higher volumes in North American heavy-duty, medium-duty and pick-up truck markets.

Net sales for the six months ended June 30, 2019, increased by \$523 million versus the comparable period in 2018. The primary drivers were as follows:

- Engine segment sales increased 4 percent, primarily due to higher volumes in most North American heavy-duty, medium-duty and pick-up truck markets.
- Distribution segment sales increased 5 percent, primarily due to higher demand in most geographic regions, especially in North America, and increased demand in the power generation product line.
- Components segment sales increased 2 percent, primarily due to higher sales volumes in North American heavy-duty, medium-duty and pick-up truck markets, partially offset by lower international truck demand in China, India and Western Europe.

These increases were partially offset by unfavorable foreign currency fluctuations of 2 percent of total sales, primarily in the Chinese renminbi, Euro, Brazilian real, Indian rupee, Australian dollar and British pound.

Sales to international markets (excluding the U.S. and Canada), based on location of customers, for the three and six months ended June 30, 2019, were 38 percent and 38 percent of total net sales compared with 41 percent and 41 percent of total net sales for the comparable periods in 2018. A more detailed discussion of sales by segment is presented in the “OPERATING SEGMENT RESULTS” section.

Cost of Sales

The types of expenses included in cost of sales are the following: parts and material consumption, including direct and indirect materials; salaries, wages and benefits; depreciation on production equipment and facilities and amortization of technology intangibles; estimated costs of warranty programs and campaigns; production utilities; production-related purchasing; warehousing, including receiving and inspection; engineering support costs; repairs and maintenance; production and warehousing facility property insurance; rent for production facilities and other production overhead.

Gross Margin

Gross margin increased \$201 million for the three months ended June 30, 2019 and increased 2.9 points as a percentage of sales, versus the comparable period in 2018. The increases in gross margin and gross margin percentage were primarily due to lower warranty costs (due to absence of the \$181 million engine system campaign accrual recorded in the second quarter of 2018), increased pricing and favorable mix, partially offset by lower volumes and tariff impacts. Gross margin was also unfavorably impacted by foreign currency (primarily the Australian dollar, Euro, Brazilian real, Canadian dollar and South African rand, partially offset by the British pound). See Note 11, “PRODUCT WARRANTY LIABILITY,” to the *Condensed Consolidated Financial Statements* for additional information.

Gross margin increased \$533 million for the six months ended June 30, 2019 and increased 3.4 points as a percentage of sales versus the comparable period in 2018. The increases in gross margin and gross margin percentage were mainly due to lower warranty costs (due to absence of the \$368 million engine system campaign accrual recorded in the first half of 2018), increased pricing, higher volumes and favorable mix, partially offset by tariff impacts and unfavorable foreign currency impacts (primarily the Australian dollar, Brazilian real, Euro and Canadian dollar, partially offset by the British pound). See Note 11, “PRODUCT WARRANTY LIABILITY,” to the *Condensed Consolidated Financial Statements* for additional information.

The provision for base warranties issued as a percent of sales for the three and six months ended June 30, 2019, was 2.1 percent and 2.1 percent, respectively, compared to 1.9 percent and 1.9 percent for the comparable periods in 2018. A detailed discussion of gross margin by segment is presented in the “OPERATING SEGMENT RESULTS” section.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased \$16 million for the three months ended June 30, 2019, versus the comparable period in 2018, primarily due to higher consulting expenses. Overall, selling, general and administrative expenses, as a percentage of sales, increased to 10.1 percent in the three months ended June 30, 2019, from 10.0 percent in the comparable period in 2018.

Selling, general and administrative expenses increased \$32 million for the six months ended June 30, 2019, versus the comparable period in 2018, primarily due to higher consulting and compensation expenses, partially offset by lower variable compensation expenses. Overall, selling, general and administrative expenses, as a percentage of sales, decreased to 10.0 percent in the six months ended June 30, 2019, from 10.2 percent in the comparable period in 2018.

Research, Development and Engineering Expenses

Research, development and engineering expenses increased \$32 million for the three months ended June 30, 2019, versus the comparable period in 2018, primarily due to decreased expense recovery and increased compensation expense driven by headcount growth, including increased staffing for the Electrified Power segment. Overall research, development and engineering expenses as a percentage of sales increased to 4.0 percent in the three months ended June 30, 2019, from 3.6 percent in the comparable period in 2018.

Research, development and engineering expenses increased \$59 million for the six months ended June 30, 2019, versus the comparable period in 2018, primarily due to increased compensation expense driven by headcount growth, including increased staffing for the Electrified Power segment, and decreased expense recovery. Overall research, development and engineering expenses as a percentage of sales increased to 4.0 percent in the six months ended June 30, 2019, from 3.7 percent in the comparable period in 2018.

Equity, Royalty and Interest Income from Investees

Equity, royalty and interest income from investees decreased \$14 million for the three months ended June 30, 2019, versus the comparable period in 2018, primarily due to lower earnings at Chongqing Cummins Engine Company, Ltd. and Beijing Foton Cummins Engine Company, Ltd.

Equity, royalty and interest income from investees decreased \$37 million for the six months ended June 30, 2019, versus the comparable period in 2018, primarily due to lower earnings at Chongqing Cummins Engine Company, Ltd., Tata Cummins Ltd., Dongfeng Cummins Emission Solutions Co., Ltd. and Beijing Foton Cummins Engine Company, Ltd.

Other Operating Income (Expense), Net

Other operating income (expense), net was as follows:

In millions	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Amortization of intangible assets	\$ (5)	\$ (5)	\$ (10)	\$ (10)
Loss on write off of assets	—	(4)	—	(4)
Gain on sale of assets, net	—	3	5	3
Royalty income, net	3	11	9	18
Other, net	(7)	(1)	(8)	(1)
Total other operating income (expense), net	<u>\$ (9)</u>	<u>\$ 4</u>	<u>\$ (4)</u>	<u>\$ 6</u>

Interest Income

Interest income for the three and six months ended June 30, 2019, increased \$2 million and \$7 million, respectively, versus the comparable periods in 2018, primarily due to higher average balances and rates of return on cash and marketable securities.

Interest Expense

Interest expense for the three and six months ended June 30, 2019, increased \$1 million and \$9 million, respectively, versus the comparable periods in 2018. The three month increase is due to higher interest rates as average short-term borrowing decreased. The six month increase is primarily due to higher interest rates and an increase in average short-term borrowing.

Other Income, Net

Other income, net was as follows:

In millions	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
Gain (loss) on corporate owned life insurance	\$ 18	\$ 1	\$ 55	\$ (3)
Non-service pension and other postretirement benefits credit	18	15	36	30
Gain on marketable securities, net	3	—	7	—
Rental income	2	2	4	4
Foreign currency loss, net	(2)	(13)	(8)	(24)
Bank charges	(3)	(2)	(6)	(5)
Other, net	4	8	18	19
Total other income, net	<u>\$ 40</u>	<u>\$ 11</u>	<u>\$ 106</u>	<u>\$ 21</u>

Income Tax Expense

Our effective tax rate for 2019 is expected to approximate 21.5 percent, excluding any discrete items that may arise.

Our effective tax rates for the three and six months ended June 30, 2019, were 21.4 percent and 21.1 percent, respectively and contained immaterial discrete items.

Our effective tax rates for the three and six months ended July 1, 2018, were 22.5 percent and 29.0 percent, respectively. The three months ended July 1, 2018, contained only immaterial discrete items. The six months ended July 1, 2018, contained \$74 million, or \$0.45 per share, of unfavorable net discrete tax items, primarily due to \$80 million of discrete items related to Tax Legislation. This includes \$45 million associated with changes related to the Tax Legislation measurement period adjustment and \$35 million associated with the one-time recognition of deferred tax charges at historical tax rates on intercompany profit in inventory.

Noncontrolling Interests

Noncontrolling interests eliminate the income or loss attributable to non-Cummins ownership interests in our consolidated entities. Noncontrolling interests in income of consolidated subsidiaries for the three and six months ended June 30, 2019, increased \$1 million and \$7 million, respectively, versus the comparable periods in 2018, primarily due to increased earnings at Eaton Cummins Joint Venture, partially offset by decreased earnings at Cummins India Limited.

Net Income Attributable to Cummins Inc. and Diluted Earnings Per Common Share Attributable to Cummins Inc.

Net income and diluted earnings per common share attributable to Cummins Inc. for the three months ended June 30, 2019, increased \$130 million and \$0.95 per diluted share, respectively, versus the comparable period in 2018, primarily due to higher net sales and increased gross margin, partially offset by higher research, development and engineering and selling, general and administrative expenses, lower equity, royalty and interest income from investees and unfavorable foreign currency fluctuations (primarily the Australian dollar, Chinese renminbi, Canadian dollar and Brazilian real).

Net income and diluted earnings per common share attributable to Cummins Inc. for the six months ended June 30, 2019, increased \$468 million and \$3.20 per diluted share, respectively, versus the comparable period in 2018, primarily due to higher net sales, increased gross margin, a lower effective tax rate due to the absence of \$74 million of unfavorable discrete tax items recognized in the first half of 2018 principally due to the 2017 Tax Legislation and an increase in the cash surrender value of corporate owned life insurance, partially offset by higher research, development and engineering expenses, lower equity, royalty and interest income from investees, unfavorable foreign currency fluctuations (primarily the Australian dollar, Brazilian real, Chinese renminbi and Canadian dollar) and increased selling, general and administrative expenses.

Comprehensive Income - Foreign Currency Translation Adjustment

The foreign currency translation adjustment was a net loss of \$99 million and \$15 million, respectively, for the three and six months ended June 30, 2019, compared to a net loss of \$299 million and \$215 million, respectively, for the three and six months ended July 1, 2018, and was driven by the following:

In millions	Three months ended			
	June 30, 2019		July 1, 2018	
	Translation adjustment	Primary currency driver vs. U.S. dollar	Translation adjustment	Primary currency driver vs. U.S. dollar
Wholly-owned subsidiaries	\$ (82)	British pound, Chinese renminbi	\$ (232)	British pound, Chinese renminbi, Indian rupee, Brazilian real
Equity method investments	(17)	Chinese renminbi	(51)	Chinese renminbi, Indian rupee, British pound
Consolidated subsidiaries with a noncontrolling interest	—		(16)	Indian rupee
Total	<u>\$ (99)</u>		<u>\$ (299)</u>	

In millions	Six months ended			
	June 30, 2019		July 1, 2018	
	Translation adjustment	Primary currency driver vs. U.S. dollar	Translation adjustment	Primary currency driver vs. U.S. dollar
Wholly-owned subsidiaries	\$ (8)	British pound offset by Indian rupee	\$ (162)	British pound, Indian rupee, Brazilian real, Chinese renminbi
Equity method investments	(10)	British pound	(29)	Chinese renminbi, Indian rupee, British pound
Consolidated subsidiaries with a noncontrolling interest	3	Indian rupee	(24)	Indian rupee
Total	<u>\$ (15)</u>		<u>\$ (215)</u>	

OPERATING SEGMENT RESULTS

Our reportable operating segments consist of the Engine, Distribution, Components, Power Systems and Electrified Power segments. This reporting structure is organized according to the products and markets each segment serves. We use segment EBITDA as a primary basis for the Chief Operating Decision Maker to evaluate the performance of each of our reportable operating segments. Segment amounts exclude certain expenses not specifically identifiable to segments. See Note 14, "OPERATING SEGMENTS," to the *Condensed Consolidated Financial Statements* for additional information.

Following is a discussion of results for each of our operating segments.

Engine Segment Results

Financial data for the Engine segment was as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
External sales	\$ 2,073	\$ 2,050	\$ 23	1 %	\$ 4,057	\$ 3,863	\$ 194	5 %
Intersegment sales	630	646	(16)	(2)%	1,299	1,279	20	2 %
Total sales	2,703	2,696	7	— %	5,356	5,142	214	4 %
Research, development and engineering expenses	88	76	(12)	(16)%	166	155	(11)	(7)%
Equity, royalty and interest income from investees	62	67	(5)	(7)%	118	134	(16)	(12)%
Interest income	4	3	1	33 %	8	5	3	60 %
Segment EBITDA	416	362	54	15 %	854	648	206	32 %
				Percentage Points				
Segment EBITDA as a percentage of total sales	15.4%	13.4%	2.0		15.9%	12.6%	3.3	

Sales for our Engine segment by market were as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
Heavy-duty truck	\$ 970	\$ 920	\$ 50	5 %	\$ 1,949	\$ 1,735	\$ 214	12 %
Medium-duty truck and bus	739	777	(38)	(5)%	1,460	1,469	(9)	(1)%
Light-duty automotive	480	444	36	8 %	862	846	16	2 %
Total on-highway	2,189	2,141	48	2 %	4,271	4,050	221	5 %
Off-highway	514	555	(41)	(7)%	1,085	1,092	(7)	(1)%
Total sales	\$ 2,703	\$ 2,696	\$ 7	— %	\$ 5,356	\$ 5,142	\$ 214	4 %
				Percentage Points				
On-highway sales as percentage of total sales	81%	79%	2		80%	79%	1	

Unit shipments by engine classification (including unit shipments to Power Systems and off-highway engine units included in their respective classification) were as follows:

	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
Heavy-duty	35,000	32,000	3,000	9 %	68,900	58,600	10,300	18 %
Medium-duty	76,400	83,500	(7,100)	(9)%	155,400	157,500	(2,100)	(1)%
Light-duty	64,100	68,500	(4,400)	(6)%	120,500	130,400	(9,900)	(8)%
Total unit shipments	175,500	184,000	(8,500)	(5)%	344,800	346,500	(1,700)	— %

Sales

Engine segment sales for the three months ended June 30, 2019, increased \$7 million versus the comparable period in 2018. The following were the primary drivers by market:

- Heavy-duty truck sales increased \$50 million, primarily due to higher volumes in the North American heavy-duty truck market with increased shipments of 9 percent.
- Light-duty automotive sales increased \$36 million, primarily due to higher pick-up sales to Chrysler, partially offset by lower LCV sales in China.

These increases were partially offset by:

- Decreased off-highway sales of \$41 million, primarily due to lower demand in international construction markets with decreased unit shipments of 20 percent, mainly in China.
- Unfavorable foreign currency fluctuations, primarily in the Chinese renminbi and Brazilian real.

Engine segment sales for the six months ended June 30, 2019, increased \$214 million versus the comparable period in 2018. The following were the primary drivers by market:

- Heavy-duty truck sales increased \$214 million, primarily due to higher volumes in the North American heavy-duty truck market with increased shipments of 18 percent.
- Light-duty automotive sales increased \$16 million, primarily due to higher pick-up sales to Chrysler, partially offset by lower LCV sales in China and Russia.

These increases were partially offset by:

- Unfavorable foreign currency fluctuations, primarily in the Brazilian real and Chinese renminbi.
- Medium-duty truck and bus sales decreased \$9 million, primarily due to decreased global bus sales and lower demand in Brazil, partially offset by increased medium-duty truck sales in North America.

Segment EBITDA

Engine segment EBITDA for the three months ended June 30, 2019, increased \$54 million versus the comparable period in 2018, primarily due to higher gross margin, partially offset by increased selling, general and administrative expenses, higher research, development and engineering expenses and lower equity, royalty and interest income from investees. The increase in gross margin was mainly due to the absence of a \$91 million engine system campaign accrual recorded in the second quarter of 2018, improved pricing and favorable mix, partially offset by tariff impacts. The increase in selling, general and administrative expenses was principally due to higher consulting expenses. The increase in research, development and engineering expenses was primarily due to lower expense recovery and higher consulting expenses. The decrease in equity, royalty and interest income from investees was largely due to lower earnings at Beijing Foton Cummins Engine Co.

Engine segment EBITDA for the six months ended June 30, 2019, increased \$206 million versus the comparable period in 2018, primarily due to higher gross margin, partially offset by increased selling, general and administrative expenses, decreased equity, royalty and interest income from investees and increased research, development and engineering expenses. The increase in gross margin was mainly due to the absence of a \$184 million engine system campaign accrual recorded in the first half of 2018, improved pricing and favorable mix, partially offset by tariff impacts. The increase in selling, general and administrative expenses was principally due to higher consulting and compensation expenses. The increase in research, development and engineering expenses was primarily due to lower expense recovery. The decrease in equity, royalty and interest income from investees was largely due to lower earnings at Tata Cummins, Ltd. and Beijing Foton Cummins Engine Co.

Distribution Segment Results

Financial data for the Distribution segment was as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
External sales	\$ 2,015	\$ 1,988	\$ 27	1 %	\$ 4,008	\$ 3,835	\$ 173	5 %
Intersegment sales	13	6	7	NM	21	12	9	75 %
Total sales	2,028	1,994	34	2 %	4,029	3,847	182	5 %
Research, development and engineering expenses	7	5	(2)	(40)%	14	10	(4)	(40)%
Equity, royalty and interest income from investees	12	11	1	9 %	23	24	(1)	(4)%
Interest income	4	3	1	33 %	8	5	3	60 %
Segment EBITDA	172	145	27	19 %	343	268	75	28 %

	Percentage Points		Percentage Points	
Segment EBITDA as a percentage of total sales	8.5%	7.3%	1.2	1.5

"NM" - not meaningful information

Sales for our Distribution segment by region were as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
North America	\$ 1,384	\$ 1,353	\$ 31	2 %	\$ 2,783	\$ 2,629	\$ 154	6 %
Asia Pacific	223	212	11	5 %	443	401	42	10 %
Europe	124	143	(19)	(13)%	247	275	(28)	(10)%
China	102	84	18	21 %	184	162	22	14 %
Africa and Middle East	55	62	(7)	(11)%	110	122	(12)	(10)%
India	49	50	(1)	(2)%	96	95	1	1 %
Latin America	46	45	1	2 %	86	83	3	4 %
Russia	45	45	—	— %	80	80	—	— %
Total sales	\$ 2,028	\$ 1,994	\$ 34	2 %	\$ 4,029	\$ 3,847	\$ 182	5 %

Sales for our Distribution segment by product line were as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
Parts	\$ 833	\$ 817	\$ 16	2 %	\$ 1,677	\$ 1,625	\$ 52	3 %
Power generation	427	346	81	23 %	830	672	158	24 %
Engines	395	461	(66)	(14)%	786	828	(42)	(5)%
Service	373	370	3	1 %	736	722	14	2 %
Total sales	\$ 2,028	\$ 1,994	\$ 34	2 %	\$ 4,029	\$ 3,847	\$ 182	5 %

Sales

Distribution segment sales for the three months ended June 30, 2019, increased \$34 million versus the comparable period in 2018. The following were the primary drivers by region:

- North American sales increased \$31 million, representing 91 percent of the total change in Distribution segment sales, primarily due to increased demand in the power generation product line mostly for improved data center orders, partially offset by decreased engine sales in oil and gas markets.

These increases were partially offset by unfavorable foreign currency fluctuations, primarily in the Australian dollar, Chinese renminbi, Euro, Canadian dollar, South African rand and Indian rupee.

Distribution segment sales for the six months ended June 30, 2019, increased \$182 million versus the comparable period in 2018. The following were the primary drivers by region:

- North American sales increased \$154 million, representing 85 percent of the total change in Distribution segment sales, primarily due to increased demand in the power generation product line mostly for improved data center orders and increased part sales, partially offset by decreased engine sales in oil and gas markets.
- Asia Pacific sales increased \$42 million, primarily due to higher volumes in whole goods.

These increases were partially offset by unfavorable foreign currency fluctuations, primarily in the Australian dollar, Euro, Chinese renminbi, Canadian dollar and Indian rupee.

Segment EBITDA

Distribution segment EBITDA for the three months ended June 30, 2019, increased \$27 million versus the comparable period in 2018, primarily due to higher gross margin and lower selling, general and administrative expenses, partially offset by unfavorable foreign currency fluctuations (primarily the Australian dollar and Canadian dollar). The increase in gross margin was mainly due to improved pricing, increased volumes and favorable mix, partially offset by increased compensation expenses and unfavorable foreign currency fluctuations (primarily in the Australian dollar, South African rand and Canadian dollar). The decrease in selling, general and administrative expenses was principally due to lower variable compensation expenses.

Distribution segment EBITDA for the six months ended June 30, 2019, increased \$75 million versus the comparable period in 2018, primarily due to higher gross margin and lower selling, general and administrative expenses, partially offset by unfavorable foreign fluctuations (primarily in the Australian dollar, South African rand, Canadian dollar and Indian rupee). The increase in gross margin was mainly due to higher volumes, improved pricing and favorable mix, partially offset by increased compensation expense and unfavorable foreign currency fluctuations (primarily in the Australian dollar, Canadian dollar, South African rand and Indian rupee).

Components Segment Results

Financial data for the Components segment was as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
External sales	\$ 1,401	\$ 1,402	\$ (1)	— %	\$ 2,802	\$ 2,715	\$ 87	3 %
Intersegment sales	445	485	(40)	(8)%	905	925	(20)	(2)%
Total sales	1,846	1,887	(41)	(2)%	3,707	3,640	67	2 %
Research, development and engineering expenses	75	62	(13)	(21)%	150	124	(26)	(21)%
Equity, royalty and interest income from investees	11	14	(3)	(21)%	21	30	(9)	(30)%
Interest income	2	2	—	— %	4	3	1	33 %
Segment EBITDA	297	237	60	25 %	622	464	158	34 %
			Percentage Points				Percentage Points	
Segment EBITDA as a percentage of total sales	16.1%	12.6%		3.5	16.8%	12.7%		4.1

Sales for our Components segment by business were as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
Emission solutions	\$ 828	\$ 841	\$ (13)	(2)%	\$ 1,682	\$ 1,616	\$ 66	4 %
Filtration	331	324	7	2 %	656	644	12	2 %
Turbo technologies	319	355	(36)	(10)%	654	695	(41)	(6)%
Electronics and fuel systems	212	226	(14)	(6)%	410	427	(17)	(4)%
Automated transmissions	156	141	15	11 %	305	258	47	18 %
Total sales	<u>\$ 1,846</u>	<u>\$ 1,887</u>	<u>\$ (41)</u>	<u>(2)%</u>	<u>\$ 3,707</u>	<u>\$ 3,640</u>	<u>\$ 67</u>	<u>2 %</u>

Sales

Components segment sales for the three months ended June 30, 2019, decreased \$41 million versus the comparable period in 2018. The following were the primary drivers by business:

- Turbo technologies sales decreased \$36 million, primarily due to weaker market demand for turbo charger products in Western Europe.
- Electronics and fuel systems sales decreased \$14 million, primarily due to lower market demand in North America, Western Europe and China.
- Emission solutions sales decreased \$13 million, primarily due to weaker demand in Western Europe, China and Asia Pacific, partially offset by stronger demand in North America.
- Unfavorable foreign currency fluctuations, primarily in the Chinese renminbi and Euro.

These changes were partially offset by increased automated transmissions sales of \$15 million, primarily due to increased heavy-duty truck demand in North America.

Components segment sales for the six months ended June 30, 2019, increased \$67 million versus the comparable period in 2018. The following were the primary drivers by business:

- Emission solutions sales increased \$66 million, primarily due to stronger demand in North America, partially offset by weaker demand in Asia Pacific, China and India.
- Automated transmissions sales increased \$47 million, primarily due to increased heavy-duty truck demand in North America.

These changes were partially offset by:

- Unfavorable foreign currency fluctuations, primarily in the Chinese renminbi, Euro and Indian rupee.
- Turbo technologies sales decreased \$41 million, primarily due to lower demand for turbochargers in Western Europe and India.

Segment EBITDA

Components segment EBITDA for the three months ended June 30, 2019, increased \$60 million versus the comparable period in 2018, as higher gross margin was partially offset by increased research, development and engineering expenses. The increase in gross margin was mainly due to the absence of a \$90 million engine system campaign accrual recorded in the second quarter of 2018 and lower material costs, partially offset by unfavorable foreign currency fluctuations (primarily in the Chinese renminbi, Brazilian real, Euro and Canadian dollar) unfavorable pricing and lower volumes. The increase in research, development and engineering expenses was primarily due to lower expense recovery and additional spending in the automated transmissions business.

Components segment EBITDA for the six months ended June 30, 2019, increased \$158 million versus the comparable period in 2018, as higher gross margin was partially offset by increased research, development and engineering expenses, unfavorable foreign currency fluctuations (primarily in the Chinese renminbi and Brazilian real) and lower equity, royalty and interest income from investees. The increase in gross margin was mainly due to the absence of a \$184 million engine system campaign accrual recorded in the first half of 2018, lower material costs and favorable mix, partially offset by lower pricing and unfavorable foreign currency fluctuations (primarily in the Chinese renminbi, Brazilian real and Canadian dollar). The increase in research, development and engineering expenses was primarily due to lower expense recovery and additional spending in the automated transmissions business. The decrease in equity, royalty and interest income from investees was largely due to lower earnings at Dongfeng Cummins Emission Solutions Co., Ltd and Shanghai Fleetguard Filter Co.

Power Systems Segment Results

Financial data for the Power Systems segment was as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
External sales	\$ 724	\$ 691	\$ 33	5 %	\$1,347	\$ 1,286	\$ 61	5 %
Intersegment sales	479	555	(76)	(14)%	933	1,034	(101)	(10)%
Total sales	1,203	1,246	(43)	(3)%	2,280	2,320	(40)	(2)%
Research, development and engineering expenses	57	60	3	5 %	113	117	4	3 %
Equity, royalty and interest income from investees	11	18	(7)	(39)%	26	37	(11)	(30)%
Interest income	2	2	—	— %	4	4	—	— %
Segment EBITDA	173	186	(13)	(7)%	311	328	(17)	(5)%
			Percentage Points				Percentage Points	
Segment EBITDA as a percentage of total sales	14.4%	14.9%	(0.5)		13.6%	14.1%	(0.5)	

Sales for our Power Systems segment by product line were as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
Power generation	\$ 668	\$ 666	\$ 2	— %	\$ 1,235	\$ 1,237	\$ (2)	— %
Industrial	432	483	(51)	(11)%	852	897	(45)	(5)%
Generator technologies	103	97	6	6 %	193	186	7	4 %
Total sales	\$ 1,203	\$ 1,246	\$ (43)	(3)%	\$ 2,280	\$ 2,320	\$ (40)	(2)%

Sales

Power Systems segment sales for the three months ended June 30, 2019, decreased \$43 million versus the comparable period in 2018. The following were the primary drivers by product line:

- Industrial sales decreased \$51 million due to lower demand in North American oil and gas markets, partially offset by higher demand in certain international markets, especially oil and gas markets in China and mining markets in North America.
- Unfavorable foreign currency fluctuations primarily in the Chinese renminbi, British pound, Indian rupee and Euro.

These decreases were partially offset by higher power generation sales of \$2 million, primarily due to stronger demand in North America, mostly offset by lower demand in Western Europe and the Middle East.

Power Systems segment sales for the six months ended June 30, 2019, decreased \$40 million versus the comparable period in 2018. The following were the primary drivers by product line:

- Industrial sales decreased \$45 million due to lower demand in North American oil and gas markets and international mining markets, partially offset by higher demand in certain international markets, especially the oil and gas market in China.
- Unfavorable foreign currency fluctuations primarily in the Indian rupee, British pound and Chinese renminbi.
- Power generation sales decreased \$2 million, primarily due to lower demand in Western Europe and Australia, mostly offset by stronger demand in North America.

Segment EBITDA

Power Systems segment EBITDA for the three months ended June 30, 2019, decreased \$13 million versus the comparable period in 2018, primarily due to lower gross margin and decreased equity, royalty and interest income from investees, partially offset by favorable foreign currency fluctuations (primarily in the British pound) and lower research, development and engineering expenses. The decrease in gross margin was mainly due to decreased volumes and unfavorable mix, partially offset by increased pricing and favorable foreign currency fluctuations (primarily in the British pound). The decrease in research, development and engineering expenses was primarily due to lower consulting expenses. The decrease in equity, royalty and interest income from investees was largely due to lower earnings at Chongqing Cummins Engine Co.

Power Systems segment EBITDA for the six months ended June 30, 2019, decreased \$17 million versus the comparable period in 2018, primarily due to lower gross margin and decreased equity, royalty and interest income from investees, partially offset by favorable foreign currency fluctuations (primarily in the British pound and Indian rupee), a gain on sale of assets and lower research, development and engineering expenses. The decrease in gross margin was mainly due to decreased volumes and unfavorable mix, partially offset by improved pricing and favorable foreign currency fluctuations (primarily in the British pound and Indian rupee). The decrease in research, development and engineering expenses was primarily due to lower consulting expenses. The decrease in equity, royalty and interest income from investees was largely due to lower earnings at Chongqing Cummins Engine Co.

Electrified Power Segment Results

The Electrified Power segment is currently in the development phase with a primary focus on research and development activities around fully electric and hybrid powertrain solutions. Financial data for the Electrified Power segment was as follows:

In millions	Three months ended		Favorable/ (Unfavorable)		Six months ended		Favorable/ (Unfavorable)	
	June 30, 2019	July 1, 2018	Amount	Percent	June 30, 2019	July 1, 2018	Amount	Percent
Total sales	\$ 8	\$ 1	\$ 7	NM	\$ 11	\$ 3	\$ 8	NM
Research, development and engineering expenses	24	16	(8)	(50)%	45	23	(22)	(96)%
Segment EBITDA	(33)	(21)	(12)	(57)%	(62)	(31)	(31)	(100)%

"NM" - not meaningful information

Reconciliation of Segment EBITDA to Net Income Attributable to Cummins Inc.

The table below reconciles the segment information to the corresponding amounts in the *Condensed Consolidated Statements of Net Income*:

In millions	Three months ended		Six months ended	
	June 30, 2019	July 1, 2018	June 30, 2019	July 1, 2018
TOTAL SEGMENT EBITDA	\$ 1,025	\$ 909	\$ 2,068	\$ 1,677
Intersegment elimination ⁽¹⁾	33	(12)	23	(80)
TOTAL EBITDA	1,058	897	2,091	1,597
Less:				
Interest expense	29	28	61	52
Depreciation and amortization ⁽²⁾	158	154	314	307
INCOME BEFORE INCOME TAXES	871	715	1,716	1,238
Less: Income tax expense	186	161	362	359
CONSOLIDATED NET INCOME	685	554	1,354	879
Less: Net income attributable to noncontrolling interest	10	9	16	9
NET INCOME ATTRIBUTABLE TO CUMMINS INC.	\$ 675	\$ 545	\$ 1,338	\$ 870

⁽¹⁾ Includes intersegment sales, intersegment profit in inventory eliminations and unallocated corporate expenses. There were no significant unallocated corporate expenses for the three and six months ended June 30, 2019 and July 1, 2018, respectively.

⁽²⁾ Depreciation and amortization, as shown on a segment basis, excludes the amortization of debt discount and deferred costs included in the *Condensed Consolidated Statements of Net Income* as "Interest expense." The amortization of debt discount and deferred costs was \$1 million and \$1 million for the six month periods ended June 30, 2019, and July 1, 2018, respectively.

LIQUIDITY AND CAPITAL RESOURCES

Key Working Capital and Balance Sheet Data

We fund our working capital with cash from operations and short-term borrowings, including commercial paper, when necessary. Various assets and liabilities, including short-term debt, can fluctuate significantly from month to month depending on short-term liquidity needs. As a result, working capital is a prime focus of management attention. Working capital and balance sheet measures are provided in the following table:

Dollars in millions	June 30, 2019	December 31, 2018
Working capital ⁽¹⁾	\$ 4,161	\$ 3,434
Current ratio	1.66	1.54
Accounts and notes receivable, net	\$ 4,179	\$ 3,866
Days' sales in receivables	60	57
Inventories	\$ 3,896	\$ 3,759
Inventory turnover	4.6	4.9
Accounts payable (principally trade)	\$ 2,991	\$ 2,822
Days' payable outstanding	60	56
Total debt	\$ 2,223	\$ 2,476
Total debt as a percent of total capital	19.5%	23.1%

⁽¹⁾ Working capital includes cash and cash equivalents.

Cash Flows

Cash and cash equivalents were impacted as follows:

In millions	Six months ended		Change
	June 30, 2019	July 1, 2018	
Net cash provided by operating activities	\$ 1,220	\$ 473	\$ 747
Net cash used in investing activities	(411)	(236)	(175)
Net cash used in financing activities	(711)	(253)	(458)
Effect of exchange rate changes on cash and cash equivalents	(4)	(35)	31
Net increase (decrease) in cash and cash equivalents	\$ 94	\$ (51)	\$ 145

Net cash provided by operating activities increased \$747 million for the six months ended June 30, 2019, versus the comparable period in 2018, primarily due to higher earnings of \$475 million, an increase in other long-term liabilities of \$115 million, higher dividends from equity investees of \$86 million and lower working capital requirements of \$68 million. During the first six months of 2019, the lower working capital requirements resulted in a cash outflow of \$468 million compared to a cash outflow of \$536 million in the comparable period in 2018.

Net cash used in investing activities increased \$175 million for the six months ended June 30, 2019, versus the comparable period in 2018, primarily due to higher net investments in marketable securities of \$79 million and increased capital expenditures of \$56 million.

Net cash used in financing activities increased \$458 million for the six months ended June 30, 2019, versus the comparable period in 2018, primarily due to lower net borrowings of commercial paper of \$850 million, partially offset by lower repurchases of common stock of \$279 million and increased net borrowings under short-term credit agreements of \$58 million.

The effect of exchange rate changes on cash and cash equivalents for the six months ended June 30, 2019, versus the comparable period in 2018, increased \$31 million primarily due to a favorable \$20 million fluctuation in the British pound.

Sources of Liquidity

We generate significant ongoing cash flow. Cash provided by operations is our principal source of liquidity with \$1,220 million provided in the six months ended June 30, 2019. Our sources of liquidity included:

In millions	June 30, 2019			Primary location of international balances
	Total	U.S.	International	
Cash and cash equivalents	\$ 1,397	\$ 325	\$ 1,072	U.K., China, Singapore, Mexico, Australia, Belgium, Canada
Marketable securities ⁽¹⁾	335	66	269	India
Total	<u>\$ 1,732</u>	<u>\$ 391</u>	<u>\$ 1,341</u>	
Available credit capacity				
Revolving credit facilities ⁽²⁾	<u>\$ 3,066</u>			
International and other uncommitted domestic credit facilities	<u>\$ 211</u>			

⁽¹⁾ The majority of marketable securities could be liquidated into cash within a few days.

⁽²⁾ The five-year credit facility for \$2.0 billion and the 364-day credit facility for \$1.5 billion, maturing August 2023 and August 2019, respectively, are maintained primarily to provide backup liquidity for our commercial paper borrowings and general corporate purposes. At June 30, 2019, we had \$434 million of commercial paper outstanding, which effectively reduced the available capacity under our revolving credit facilities to \$3.1 billion.

Cash, Cash Equivalents and Marketable Securities

A significant portion of our cash flow is generated outside the U.S. We manage our worldwide cash requirements considering available funds among the many subsidiaries through which we conduct our business and the cost effectiveness with which those funds can be accessed. As a result, we do not anticipate any local liquidity restrictions to preclude us from funding our operating needs with local resources.

Debt Facilities and Other Sources of Liquidity

We have access to committed credit facilities that total \$3.5 billion, including a \$1.5 billion 364-day facility that expires August 21, 2019 and a \$2.0 billion five-year facility that expires on August 22, 2023. We intend to maintain credit facilities of a similar aggregate amount by renewing or replacing these facilities before expiration. These revolving credit facilities are maintained primarily to provide backup liquidity for our commercial paper borrowings and for general corporate purposes.

We can issue up to \$3.5 billion of unsecured, short-term promissory notes ("commercial paper") pursuant to our board authorized commercial paper programs. The programs facilitate the private placement of unsecured short-term debt through third party brokers. We intend to use the net proceeds from the commercial paper borrowings for general corporate purposes. The total combined borrowing capacity under the revolving credit facility and commercial program should not exceed \$3.5 billion. See Note 10, "DEBT," to our *Condensed Consolidated Financial Statements* for additional information.

As a well-known seasoned issuer, we filed an automatic shelf registration for an undetermined amount of debt and equity securities with the Securities and Exchange Commission on February 13, 2019. Under this shelf registration we may offer, from time to time, debt securities, common stock, preferred and preference stock, depositary shares, warrants, stock purchase contracts and stock purchase units.

Uses of Cash

Stock Repurchases

In October 2018, our Board of Directors authorized the acquisition of up to \$2 billion of additional common stock. In the first six months of 2019, we made the following purchases under the 2018 stock repurchase program:

In millions, except per share amounts	Shares Purchased	Average Cost Per Share	Total Cost of Repurchases	Remaining Authorized Capacity ⁽¹⁾
March 31	0.7	\$ 137.80	\$ 100	\$ 1,806
June 30	—	—	—	1,806
Total	0.7	—	100	

⁽¹⁾ The remaining authorized capacity under these plans was calculated based on the cost to purchase the shares but excludes commission expenses in accordance with the authorized plan.

We intend to repurchase outstanding shares from time to time during 2019 to enhance shareholder value and to offset the dilutive impact of employee stock based compensation plans.

Dividends

In July 2019, our Board of Directors authorized an increase to our quarterly dividend of 15 percent from \$1.14 per share to \$1.311 per share.

We paid dividends of \$358 million during the six months ended June 30, 2019.

Capital Expenditures

Capital expenditures, including spending on internal use software, for the six months ended June 30, 2019, were \$276 million versus \$221 million in the comparable period in 2018. We plan to spend an estimated \$650 million to \$700 million in 2019 on capital expenditures as we continue with product launches and facility improvements. Approximately 50 percent of our capital expenditures are expected to be invested outside of the U.S. in 2019. In addition, we plan to spend an estimated \$65 million to \$75 million on internal use software in 2019.

Pensions

Our global pension plans, including our unfunded and non-qualified plans, were 115 percent funded at December 31, 2018. Our U.S. plan, which represents approximately 54 percent of the worldwide pension obligation, was 131 percent funded and our U.K. plan was 115 percent funded. The funded status of our pension plans is dependent upon a variety of variables and assumptions including return on invested assets, market interest rates and levels of voluntary contributions to the plans. In the first six months of 2019, the investment gain on our U.S. pension trust was 11.3 percent while our U.K. pension trust gain was 8.82 percent. Approximately 74 percent of our pension plan assets are held in highly liquid investments such as fixed income and equity securities. The remaining 26 percent of our plan assets are held in less liquid, but market valued investments, including real estate, private equity, venture capital, opportunistic credit and insurance contracts. We anticipate making additional defined benefit pension contributions during the remainder of 2019 of \$46 million for our U.S. and U.K. pension plans. Approximately \$91 million of the estimated \$123 million of U.S. and U.K. 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.

Current Maturities of Short and Long-Term Debt

We had \$434 million of commercial paper outstanding at June 30, 2019, that matures in less than one year. The maturity schedule of our existing long-term debt does not require significant cash outflows until 2023. Required annual principal payments range from \$8 million to \$507 million over the next five years (including the remainder of 2019). See Note 10, "DEBT," to the *Condensed Consolidated Financial Statements* for additional information.

Credit Ratings

Our ratings and outlook from each of the credit rating agencies as of the date of filing are shown in the table below.

Credit Rating Agency ⁽¹⁾	Long-Term	Short-Term	Outlook
	Senior Debt Rating	Debt Rating	
Standard and Poor's Rating Services	A+	A1	Stable
Moody's Investors Service, Inc.	A2	P1	Stable

⁽¹⁾ Credit ratings are not recommendations to buy, are subject to change, and each rating should be evaluated independently of any other rating. In addition, we undertake no obligation to update disclosures concerning our credit ratings, whether as a result of new information, future events or otherwise.

Management's Assessment of Liquidity

Our financial condition and liquidity remain strong. Our solid balance sheet and credit ratings enable us to have ready access to credit and the capital markets. We assess our liquidity in terms of our ability to generate adequate cash to fund our operating, investing and financing activities. We believe our operating cash flow and liquidity provide us with the financial flexibility needed to fund working capital, common stock repurchases, acquisitions, capital expenditures, dividend payments, projected pension obligations and debt service obligations. We continue to generate cash from operations in the U.S. and maintain access to our revolving credit facilities and commercial paper program as noted above.

APPLICATION OF CRITICAL ACCOUNTING ESTIMATES

A summary of our significant accounting policies is included in [Note 1, “SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES,” of the Notes to the Consolidated Financial Statements of our 2018 Form 10-K](#), which discusses accounting policies that we have selected from acceptable alternatives.

Our *Condensed Consolidated Financial Statements* are prepared in accordance with generally accepted accounting principles that often require management to make judgments, estimates and assumptions regarding uncertainties that affect the reported amounts presented and disclosed in the financial statements. Management reviews these estimates and assumptions based on historical experience, changes in business conditions and other relevant factors they believe to be reasonable under the circumstances. In any given reporting period, our actual results may differ from the estimates and assumptions used in preparing our *Condensed Consolidated Financial Statements*.

Critical accounting estimates are defined as follows: the estimate requires management to make assumptions about matters that were highly uncertain at the time the estimate was made; different estimates reasonably could have been used; or if changes in the estimate are reasonably likely to occur from period to period and the change would have a material impact on our financial condition or results of operations. Our senior management has discussed the development and selection of our accounting policies, related accounting estimates and the disclosures set forth below with the Audit Committee of our Board of Directors. Our critical accounting estimates disclosed in the [Form 10-K](#) address the estimation of liabilities for warranty programs, accounting for income taxes, pension benefits and goodwill impairment.

A discussion of our critical accounting estimates may be found in the [“Management’s Discussion and Analysis” section of our 2018 Form 10-K under the caption “APPLICATION OF CRITICAL ACCOUNTING ESTIMATES.”](#) Within the context of these critical accounting estimates, we are not currently aware of any reasonably likely events or circumstances that would result in different policies or estimates being reported in the first six months of 2019.

RECENTLY ADOPTED AND RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

See Note 15, "RECENTLY ADOPTED AND RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS," in the *Notes to Condensed Consolidated Financial Statements* for additional information.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

A discussion of quantitative and qualitative disclosures about market risk may be found in [Item 7A of our 2018 Form 10-K](#). There have been no material changes in this information since the filing of our [2018 Form 10-K](#).

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this Quarterly Report on Form 10-Q, we carried out an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer (CEO) and Chief Financial Officer (CFO), of the effectiveness of the design and operation of our disclosure controls and procedures as defined in Exchange Act Rules 13a-15(e) and 15d-15(e). Based upon that evaluation, our CEO and our CFO concluded that our disclosure controls and procedures were effective to ensure that the information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 is (1) recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, and (2) accumulated and communicated to management, including our CEO and CFO, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There has been no change in our internal control over financial reporting during the quarter ended June 30, 2019, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

We are subject to numerous lawsuits and claims arising out of the ordinary course of our business, including actions related to product liability; personal injury; the use and performance of our products; warranty matters; product recalls; patent, trademark or other intellectual property infringement; contractual liability; the conduct of our business; tax reporting in foreign jurisdictions; distributor termination; workplace safety; and environmental matters. We also have been identified as a potentially responsible party at multiple waste disposal sites under U.S. federal and related state environmental statutes and regulations and may have joint and several liability for any investigation and remediation costs incurred with respect to such sites. We have denied liability with respect to many of these lawsuits, claims and proceedings and are vigorously defending such lawsuits, claims and proceedings. We carry various forms of commercial, property and casualty, product liability and other forms of insurance; however, such insurance may not be applicable or adequate to cover the costs associated with a judgment against us with respect to these lawsuits, claims and proceedings. We do not believe that these lawsuits are material individually or in the aggregate. While we believe we have also established adequate accruals pursuant to U.S. generally accepted accounting principles for our expected future liability with respect to pending lawsuits, claims and proceedings, where the nature and extent of any such liability can be reasonably estimated based upon then presently available information, there can be no assurance that the final resolution of any existing or future lawsuits, claims or proceedings will not have a material adverse effect on our business, results of operations, financial condition or cash flows.

We conduct significant business operations in Brazil that are subject to the Brazilian federal, state and local labor, social security, tax and customs laws. While we believe we comply with such laws, they are complex, subject to varying interpretations and we are often engaged in litigation regarding the application of these laws to particular circumstances.

On April 29, 2019, we announced that we were conducting a formal internal review of our emissions certification process and compliance with emissions standards for our pick-up truck applications, following conversations with the U.S. Environmental Protection Agency (EPA) and California Air Resources Board (CARB) regarding certification of our engines in model year 2019 RAM 2500 and 3500 trucks. This review is being conducted with external advisors to ensure the certification and compliance processes for all of our pick-up truck applications are consistent with our internal policies, engineering standards and applicable laws. In addition, we announced that we voluntarily disclosed our formal internal review to our regulators and other agencies and were working cooperatively to ensure a complete and thorough review. During conversations with the EPA and CARB about the effectiveness of our pick-up truck applications, the agencies raised concerns that certain aspects of our emissions systems may reduce the effectiveness of our emissions control systems and did not fully comply with their requirements for certification. As a result, our internal review focuses, in part, on the agencies' concerns. We are working closely with the agencies to enhance our emission systems to improve the effectiveness of all of our pick-up truck applications and to fully address the agencies' requirements. Due to the preliminary nature of our formal review, our collaboration with our regulators to address their questions and concerns and the presence of many unknown facts and circumstances, we cannot predict the outcome of this review and process, and we cannot provide assurance that the matter will not have a materially adverse impact on our results of operations and cash flows.

ITEM 1A. Risk Factors

In addition to other information set forth in this report, you should consider other risk factors discussed in [Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2018](#), which could materially affect our business, financial condition or future results. The risks described in our [2018 Annual Report on Form 10-K](#) or the "CAUTIONARY STATEMENTS REGARDING FORWARD-LOOKING INFORMATION" in this Quarterly report are not the only risks we face. In addition, the following risk factor is provided to supplement and update the risk factors previously disclosed in [Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2018](#). Additional risks and uncertainties not currently known to us or that we currently judge to be immaterial also may materially adversely affect our business, financial condition or operating results.

We are conducting a formal internal review of our emissions certification process and compliance with emissions standards with respect to our pick-up truck applications and working with the EPA and CARB to address their questions about these applications. The results of this formal review and agency process, or the discovery of any noncompliance issues, could have a materially adverse impact on our results of operations and cash flows.

We previously announced that we are conducting a formal internal review of our emissions certification process and compliance with emissions standards with respect to all of our pick-up truck applications, following conversations with the EPA and CARB regarding certification of our engines for model year 2019 RAM 2500 and 3500 trucks. During conversations with the EPA and CARB about the effectiveness of our pick-up truck applications, the agencies raised concerns that certain

aspects of our emissions systems may reduce the effectiveness of our emissions control systems and did not fully comply with their requirements for certification. As a result, our internal review focuses, in part, on the agencies' concerns. We are working closely with the agencies to enhance our emissions systems to improve the effectiveness of all of our pick-up truck applications and to fully address the agencies' requirements. We will continue to work together closely with the relevant regulators to develop and implement recommendations for improvement as part of our ongoing commitment to compliance.

Due to the preliminary nature of the formal review, our collaboration with our regulators to address their questions and concerns and the presence of many unknown facts and circumstances, we are not yet able to estimate the financial impact of these matters. It is possible that the consequences of any remediation plans resulting from our formal review and this regulatory process could have a materially adverse impact on our results of operations and cash flows in the periods in which these emissions certification issues are addressed.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following information is provided pursuant to Item 703 of Regulation S-K:

Period	Issuer Purchases of Equity Securities			
	Total Number of Shares Purchased ⁽¹⁾	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs ⁽²⁾
April 1 - May 5	7,661	\$ 168.85	—	50,043
May 6 - June 2	1,808	165.61	—	48,857
June 3 - June 30	14,013	168.82	—	34,880
Total	23,482	168.58	—	

⁽¹⁾ Shares purchased represent shares under our Key Employee Stock Investment Plan established in 1969 (there is no maximum repurchase limitation in this plan) and our Board of Directors authorized share repurchase program.

⁽²⁾ These values reflect the sum of shares held in loan status under our Key Employee Stock Investment Plan. The repurchase program authorized by the Board of Directors does not limit the number of shares that may be purchased and was excluded from this column. The dollar value remaining available for future purchases under the 2018 program at June 30, 2019, was \$1.8 billion.

In October 2018, our Board of Directors authorized the acquisition of up to \$2 billion of additional common stock.

During the three months ended June 30, 2019, we repurchased 23,482 shares of common stock from employees in connection with the Key Employee Stock Investment Plan which allows certain employees, other than officers, to purchase shares of common stock on an installment basis up to an established credit limit. Loans are issued for five-year terms at a fixed interest rate established at the date of purchase and may be refinanced after their initial five-year period for an additional five-year period. Participants must hold shares for a minimum of six months from date of purchase. If the shares are sold before the loan is paid off, the employee must wait six months before another share purchase may be made. We hold participants' shares as security for the loans and would, in effect, repurchase shares if the participant defaulted in repayment of the loan. There is no maximum amount of shares that we may purchase under this plan.

ITEM 3. Defaults Upon Senior Securities

Not applicable.

ITEM 4. Mine Safety Disclosures

Not applicable.

ITEM 5. Other Information

Not applicable.

ITEM 6. Exhibits

The exhibits listed in the following Exhibit Index are filed as part of this Quarterly Report on Form 10-Q.

**CUMMINS INC.
EXHIBIT INDEX**

Exhibit No.	Description of Exhibit
<u>10.1</u>	<u>Cummins Inc. Employee Stock Purchase Plan, as amended (incorporated by reference to Annex B to the Company's definitive proxy statement filed with the Securities and Exchange Commission on Schedule 14A on April 1, 2019 (File No. 001-04949)).</u>
<u>10.2</u>	<u>Form of Long-Term Grant Notice under the 2012 Omnibus Incentive Plan</u>
<u>31(a)</u>	<u>Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u>
<u>31(b)</u>	<u>Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u>
<u>32</u>	<u>Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u>
101.INS	XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.

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.

Cummins Inc.

Date: July 30, 2019

By: /s/ MARK A. SMITH
 Mark A. Smith
 Vice President and Chief Financial Officer
 (Principal Financial Officer)

By: /s/ CHRISTOPHER C. CLULOW
 Christopher C. Clulow
 Vice President-Corporate Controller
 (Principal Accounting Officer)