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CUMMINS INC

Form 10-Q

October 30, 2018

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# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

## FORM 10-Q

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

For the Quarterly Period Ended September 30, 2018

Commission File Number 1-4949

## CUMMINS INC.

(Exact name of registrant as specified in its charter)

Indiana 35-0257090

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

500 Jackson Street

Box 3005

Columbus, Indiana 47202-3005

(Address of principal executive offices)

Telephone (812) 377-5000

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

Smaller reporting company  Emerging growth company

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

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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 September 30, 2018, there were 160,561,303 shares of common stock outstanding with a par value of \$2.50 per share.

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Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. Condensed Consolidated Financial Statements****CUMMINS INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME****(Unaudited)**

<b>In millions, except per share amounts</b>	<b>Three months ended</b>		<b>Nine months ended</b>	
	<b>September 30, 2018</b>	<b>October 1, 2017</b>	<b>September 30, 2018</b>	<b>October 1, 2017</b>
<b>NET SALES</b> <sup>(a)</sup> (Note 3)	<b>\$ 5,943</b>	\$ 5,285	<b>\$ 17,645</b>	\$ 14,952
Cost of sales	<b>4,392</b>	3,944	<b>13,454</b>	11,228
<b>GROSS MARGIN</b>	<b>1,551</b>	1,341	<b>4,191</b>	3,724
<b>OPERATING EXPENSES AND INCOME</b>				
Selling, general and administrative expenses	<b>604</b>	633	<b>1,794</b>	1,786
Research, development and engineering expenses	<b>229</b>	213	<b>658</b>	546
Equity, royalty and interest income from investees (Note 5)	<b>90</b>	95	<b>315</b>	301
Other operating income (expense), net	<b>(5)</b>	32	<b>1</b>	55
<b>OPERATING INCOME</b>	<b>803</b>	622	<b>2,055</b>	1,748
Interest income	<b>9</b>	4	<b>26</b>	11
Interest expense	<b>30</b>	18	<b>82</b>	57
Other income, net	<b>23</b>	14	<b>44</b>	67
<b>INCOME BEFORE INCOME TAXES</b>	<b>805</b>	622	<b>2,043</b>	1,769
Income tax expense (Note 6)	<b>107</b>	165	<b>466</b>	466
<b>CONSOLIDATED NET INCOME</b>	<b>698</b>	457	<b>1,577</b>	1,303
Less: Net income attributable to noncontrolling interests	<b>6</b>	4	<b>15</b>	30
<b>NET INCOME ATTRIBUTABLE TO CUMMINS INC.</b>	<b>\$ 692</b>	\$ 453	<b>\$ 1,562</b>	\$ 1,273
<b>EARNINGS PER COMMON SHARE ATTRIBUTABLE TO CUMMINS INC.</b>				
Basic	<b>\$ 4.29</b>	\$ 2.72	<b>\$ 9.57</b>	\$ 7.62
Diluted	<b>\$ 4.28</b>	\$ 2.71	<b>\$ 9.53</b>	\$ 7.60
<b>WEIGHTED AVERAGE COMMON SHARES OUTSTANDING</b>				
Basic	<b>161.3</b>	166.3	<b>163.3</b>	167.0
Dilutive effect of stock compensation awards	<b>0.5</b>	0.7	<b>0.6</b>	0.6
Diluted	<b>161.8</b>	167.0	<b>163.9</b>	167.6
<b>CASH DIVIDENDS DECLARED PER COMMON SHARE</b>	<b>\$ 1.14</b>	\$ 1.08	<b>\$ 3.30</b>	\$ 3.13

<sup>(a)</sup> Includes sales to nonconsolidated equity investees of \$314 million and \$951 million and \$285 million and \$835 million for the three and nine months ended September 30, 2018 and October 1, 2017, respectively.

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

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

In millions	Three months ended		Nine months ended	
	September 2018	October 1, 2017	September 2018	October 1, 2017
<b>CONSOLIDATED NET INCOME</b>	<b>\$ 698</b>	<b>\$ 457</b>	<b>\$1,577</b>	<b>\$ 1,303</b>
Other comprehensive income (loss), net of tax (Note 13)				
Change in pension and other postretirement defined benefit plans	<b>13</b>	16	<b>34</b>	52
Foreign currency translation adjustments	<b>(159)</b>	) 94	<b>(374)</b>	) 276
Unrealized gain on marketable securities	—	—	—	1
Unrealized gain (loss) on derivatives	<b>(3)</b>	) (1)	<b>4</b>	—
Total other comprehensive income (loss), net of tax	<b>(149)</b>	) 109	<b>(336)</b>	) 329
<b>COMPREHENSIVE INCOME</b>	<b>549</b>	566	<b>1,241</b>	1,632
Less: Comprehensive (loss) income attributable to noncontrolling interests	<b>(11)</b>	) 2	<b>(25)</b>	) 42
<b>COMPREHENSIVE INCOME ATTRIBUTABLE TO CUMMINS INC.</b>	<b>\$ 560</b>	<b>\$ 564</b>	<b>\$1,266</b>	<b>\$ 1,590</b>

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

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

In millions, except par value	September 30, 2018	December 31, 2017
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 1,222	\$ 1,369
Marketable securities (Note 7)	185	198
Total cash, cash equivalents and marketable securities	1,407	1,567
Accounts and notes receivable, net		
Trade and other	3,670	3,311
Nonconsolidated equity investees	259	307
Inventories (Note 8)	3,831	3,166
Prepaid expenses and other current assets	696	577
Total current assets	9,863	8,928
Long-term assets		
Property, plant and equipment	8,079	8,058
Accumulated depreciation	(4,209)	(4,131)
Property, plant and equipment, net	3,870	3,927
Investments and advances related to equity method investees	1,255	1,156
Goodwill	1,110	1,082
Other intangible assets, net	950	973
Pension assets	1,022	1,043
Other assets	922	966
Total assets	\$ 18,992	\$ 18,075
<b>LIABILITIES</b>		
Current liabilities		
Accounts payable (principally trade)	\$ 2,980	\$ 2,579
Loans payable (Note 9)	61	57
Commercial paper (Note 9)	800	298
Accrued compensation, benefits and retirement costs	576	811
Current portion of accrued product warranty (Note 10)	624	454
Current portion of deferred revenue (Notes 3 & 10)	500	500
Other accrued expenses (Note 11)	834	915
Current maturities of long-term debt (Note 9)	41	63
Total current liabilities	6,416	5,677
Long-term liabilities		
Long-term debt (Note 9)	1,563	1,588
Postretirement benefits other than pensions	281	289
Pensions	331	330
Other liabilities and deferred revenue (Notes 3, 10 & 11)	2,341	2,027
Total liabilities	\$ 10,932	\$ 9,911
Commitments and contingencies (Note 12)		
<b>EQUITY</b>		
Cummins Inc. shareholders' equity		

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Common stock, \$2.50 par value, 500 shares authorized, 222.4 and 222.4 shares issued	<b>\$ 2,151</b>	\$ 2,210
Retained earnings	<b>12,519</b>	11,464
Treasury stock, at cost, 61.9 and 56.7 shares	<b>(5,674)</b>	(4,905 )
Common stock held by employee benefits trust, at cost, 0.5 and 0.5 shares	<b>(6)</b>	(7 )
Accumulated other comprehensive loss (Note 13)	<b>(1,799)</b>	(1,503 )
Total Cummins Inc. shareholders' equity	<b>7,191</b>	7,259
Noncontrolling interests	<b>869</b>	905
Total equity	<b>\$ 8,060</b>	\$ 8,164
Total liabilities and equity	<b>\$ 18,992</b>	\$ 18,075

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

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

<b>In millions</b>	<b>Nine months ended</b>	
	<b>September 30,</b>	<b>October 1,</b>
	<b>2018</b>	<b>2017</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Consolidated net income	<b>\$1,577</b>	\$ 1,303
Adjustments to reconcile consolidated net income to net cash provided by operating activities		
Depreciation and amortization	<b>456</b>	433
Deferred income taxes	<b>(167)</b>	) 26
Equity in income of investees, net of dividends	<b>(156)</b>	) (166 )
Pension contributions under (in excess of) expense, net (Note 4)	<b>36</b>	) (63 )
Other post retirement benefits payments in excess of expense, net (Note 4)	<b>(8)</b>	) (4 )
Stock-based compensation expense	<b>38</b>	34
Loss contingency payments	<b>(65)</b>	) —
Translation and hedging activities	<b>(27)</b>	) 61
Changes in current assets and liabilities, net of acquisitions		
Accounts and notes receivable	<b>(429)</b>	) (722 )
Inventories	<b>(773)</b>	) (401 )
Other current assets	<b>(100)</b>	) (28 )
Accounts payable	<b>467</b>	567
Accrued expenses	<b>341</b>	369
Changes in other liabilities and deferred revenue	<b>118</b>	177
Other, net	<b>80</b>	) (115 )
Net cash provided by operating activities	<b>1,388</b>	1,471
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Capital expenditures	<b>(361)</b>	) (282 )
Investments in internal use software	<b>(55)</b>	) (59 )
Proceeds from disposals of property, plant and equipment	<b>14</b>	104
Investments in and advances to equity investees	<b>(9)</b>	) (71 )
Acquisitions of businesses, net of cash acquired (Note 14)	<b>(70)</b>	) (600 )
Investments in marketable securities—acquisitions (Note 7)	<b>(316)</b>	) (106 )
Investments in marketable securities—liquidations (Note 7)	<b>298</b>	218
Cash flows from derivatives not designated as hedges	<b>(56)</b>	) 9
Other, net	<b>36</b>	1
Net cash used in investing activities	<b>(519)</b>	) (786 )
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net borrowings of commercial paper (Note 9)	<b>502</b>	302
Payments on borrowings and capital lease obligations	<b>(54)</b>	) (38 )
Net borrowings under short-term credit agreements	<b>9</b>	19
Distributions to noncontrolling interests	<b>(30)</b>	) (29 )
Dividend payments on common stock	<b>(537)</b>	) (522 )
Repurchases of common stock (Note 2)	<b>(879)</b>	) (391 )
Other, net	<b>29</b>	59
Net cash used in financing activities	<b>(960)</b>	) (600 )
<b>EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>	<b>(56)</b>	) 85

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Net (decrease) increase in cash and cash equivalents	(147 )	170
Cash and cash equivalents at beginning of year	1,369	1,120
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<b>\$1,222</b>	<b>\$ 1,290</b>

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

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

In millions	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Common Stock Held in Trust	Accumulated Other Comprehensive Loss	Total Cummins Inc Shareholders' Equity	Noncontrolling Interests	Total Equity
<b>BALANCE AT DECEMBER 31, 2016</b>	\$ 556	\$ 1,597	\$ 11,040	\$(4,489)	\$ (8 )	\$ (1,821 )	\$ 6,875	\$ 299	\$ 7,174
Net income			1,273				1,273	30	1,303
Other comprehensive income (loss), net of tax (Note 13)						317	317	12	329
Issuance of common stock		5					5	—	5
Employee benefits trust activity		14			1		15	—	15
Repurchases of common stock				(391 )			(391 )	—	(391 )
Cash dividends on common stock			(522 )				(522 )	—	(522 )
Distributions to noncontrolling interests							—	(29 )	(29 )
Stock based awards		2		31			33	—	33
Acquisition of business							—	600	600
Other shareholder transactions		24					24	20	44
<b>BALANCE AT OCTOBER 1, 2017</b>	\$ 556	\$ 1,642	\$ 11,791	\$(4,849)	\$ (7 )	\$ (1,504 )	\$ 7,629	\$ 932	\$ 8,561