

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934

CUMMINS ENGINE COMPANY, INC.

For the Quarter Ended June 25, 2000 Commission File Number 1-4949

Indiana

35-0257090

(State or Other Jurisdiction of
Incorporation or Organization)

(IRS Employer Identification No.)

500 Jackson Street, Box 3005,

Columbus, Indiana

47202-3005

(Address of Principal Executive Offices)

(Zip Code)

812-377-5000

(Registrant's Telephone Number)

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 proceeding 12 months and (2) has been subject to such filing requirements for the past 90 days:

Yes
No

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date:

As of June 25, 2000, the number of shares outstanding of the registrant's only class of common stock was 41.5 million.

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CUMMINS ENGINE COMPANY, INC.
CONSOLIDATED STATEMENT OF EARNINGS
FOR THE SECOND QUARTER AND FIRST HALF
ENDED JUNE 25, 2000 AND JUNE 27, 1999
Unaudited

Millions, except per share amounts	Second Quarter		First Half	
	2000	1999	2000	1999
Net sales	\$1,769	\$1,667	\$3,417	\$3,172
Cost of goods sold	1,418	1,296	2,731	2,500
Gross profit	351	371	686	672
Selling & administrative expenses	190	200	384	378
Research & engineering expenses	59	60	118	114
Net (income) expense from joint ventures and alliances	(3)	5	(4)	12
Interest expense	21	19	40	38
Other (income) expense, net	(2)	3	-	10
Earnings before income taxes	86	84	148	120
Provision for income taxes	22	25	39	35
Minority interest	3	1	6	3
Net earnings	\$ 61	\$ 58	\$ 103	\$ 82
Basic earnings per share	\$ 1.62	\$ 1.51	\$ 2.71	\$ 2.14
Diluted earnings per share	1.62	1.50	2.70	2.13
Cash dividends declared per share	.30	.275	.60	.55

CUMMINS ENGINE COMPANY, INC.
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
Unaudited

Millions, except per share amounts	6/25/2000	12/31/1999
Assets		
Current assets:		
Cash and cash equivalents	\$ 74	\$ 74
Receivables, net of allowance of \$9	1,138	1,026
Inventories	822	787
Other current assets	294	293
	2,328	2,180
Investments and other assets	346	274
Property, plant & equipment less accumulated depreciation of \$1,542 and \$1,490	1,602	1,630
Goodwill, net of amortization of \$33 and \$28	359	364
Other intangibles, deferred taxes and deferred charges	258	249
Total assets	\$4,893	\$4,697
Liabilities and shareholders' investment		
Current liabilities:		
Loans payable	\$ 68	\$ 113
Current maturities of long-term debt	9	10
Accounts payable	463	411
Other current liabilities	770	780
	1,310	1,314
Long-term debt	1,255	1,092
Other liabilities	788	788

Minority interest	79	74
Shareholders' investment:		
Common stock, \$2.50 par value, 48.7 and 48.3 shares issued	121	121
Additional contributed capital	1,140	1,129
Retained earnings	839	760
Accumulated other comprehensive income	(158)	(109)
Common stock in treasury, at cost, 7.2 and 6.8 shares	(290)	(274)
Common stock held in trust for employee benefit plans, 3.4 shares	(158)	(163)
Unearned compensation (ESOP)	(33)	(35)
	<u>1,461</u>	<u>1,429</u>
Total liabilities and shareholders' investment	<u>\$4,893</u>	<u>\$4,697</u>

CUMMINS ENGINE COMPANY, INC.
CONSOLIDATED STATEMENT OF CASH FLOWS
Unaudited

Millions	First Half Ended	
	6/25/2000	6/27/1999
Cash flows from operating activities:		
Net earnings	\$103	\$ 82
Adjustments to reconcile net earnings to net cash from operating activities:		
Depreciation and amortization	117	114
Restructuring actions	(5)	(11)
Accounts receivable	(144)	(188)
Inventories	(38)	(28)
Accounts payable and accrued expenses	55	200
Income taxes payable	(5)	8
Equity in losses of joint ventures and alliances	4	16
Other	(28)	(10)
Total adjustments	<u>(44)</u>	<u>101</u>
Net cash provided by operating activities	<u>59</u>	<u>183</u>
Cash flows from investing activities:		
Property, plant and equipment:		
Additions	(84)	(80)
Disposals	16	21
Investments in joint ventures and alliances	(36)	(37)
Acquisition and disposition of businesses	(35)	3
Other	-	2
Net cash used in investing activities	<u>(139)</u>	<u>(91)</u>
Net cash flows (used in) provided by operating and investing activities	<u>(80)</u>	<u>92</u>
Cash flows from financing activities:		
Proceeds from borrowings	168	-
Payments on borrowings	(7)	(17)
Net payments under short-term credit agreements	(40)	(10)
Repurchases of common stock	(16)	(10)
Dividend payments	(25)	(23)
Other	1	(3)
Net cash provided by (used in) financing activities	<u>81</u>	<u>(63)</u>
Effect of exchange rate changes on cash	<u>(1)</u>	<u>-</u>
Net change in cash and cash equivalents	-	29
Cash & cash equivalents at beginning of the year	74	38

Cash & cash equivalents at end of the first half	\$ 74	\$ 67
	—	—
	—	—

CUMMINS ENGINE COMPANY, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Unaudited

Note 1. Accounting Policies: The Consolidated Financial Statements for the interim periods ended June 25, 2000 and June 27, 1999 have been prepared in accordance with the accounting policies described in the Company's Annual Report to Shareholders and Form 10-K. Management believes the statements include all adjustments of a normal recurring nature necessary to present fairly the results of operations for the interim periods. Inventory values at interim reporting dates are based upon estimates of the annual adjustments for taking physical inventory and for the change in cost of LIFO inventories.

Note 2. Income Taxes: Income tax expense is reported during the interim reporting periods on the basis of the estimated annual effective tax rate for the taxable jurisdictions in which the Company operates.

Note 3. Earnings per Share: Basic earnings per share of common stock are computed by dividing net earnings by the weighted-average number of common shares outstanding during the period. Diluted earnings per share are computed by dividing net earnings by the weighted-average number of shares, assuming the exercise of stock options. Shares of stock held by the employee benefits trust are not included in outstanding shares for EPS until distributed from the trust.

Millions, except per share amounts	Second Quarter		
	Net Earnings	Weighted Average Shares	Per-Share Amount
<hr/>			
2000			
Basic	\$61	38.1	\$1.62
Options	-	-	
Diluted	<u>\$61</u>	<u>38.1</u>	\$1.62
	—	—	
1999			
Basic	\$58	38.5	\$1.51
Options	-	.2	
Diluted	<u>\$58</u>	<u>38.7</u>	\$1.50
	—	—	
	—	—	

Millions, except per share amounts	First Half		
	Net Earnings	Weighted Average Shares	Per-Share Amount
<hr/>			
2000			
Basic	\$103	38.2	\$2.71
Options	-	-	
Diluted	<u>\$103</u>	<u>38.2</u>	\$2.70
	—	—	
1999			
Basic	\$82	38.5	\$2.14
Options	-	.2	
Diluted	<u>\$82</u>	<u>38.7</u>	\$2.13
	—	—	
	—	—	

Note 4. Comprehensive Income: Comprehensive income, which includes net income and all other non-owner changes in equity during a period, is as follows:

Millions	Second Quarter Ended	
	June 25, 2000	June 27, 1999
Net income	\$ 61	\$ 58
Unrealized gain on securities	1	-
Translation loss, net of tax	(35)	(7)
Comprehensive income	<u>\$ 27</u>	<u>\$ 51</u>

Millions	First Half Ended	
	June 25, 2000	June 27, 1999
Net income	\$103	\$ 82
Unrealized gain on securities	-	1
Translation loss, net of tax	(49)	(7)
Comprehensive income	<u>\$ 54</u>	<u>\$ 76</u>

Note 5. Segment Information: Operating segment information is as follows:

Millions	Engine	Power Generation	Filtration And Other	Total
Second Quarter Ended June 25, 2000				
Net sales	\$1,107	\$368	\$294	\$1,769
Earnings before interest and income taxes	42	30	35	107
Net assets	1,160	578	845	2,583
Second Quarter Ended June 27, 1999				
Net sales	\$1,095	\$305	\$267	\$1,667
Earnings before interest and income taxes	59	11	33	103
Net assets	974	509	815	2,298
First Half Ended June 25, 2000				
Net sales	\$2,152	\$697	\$568	\$3,417
Earnings before interest and income taxes	70	53	65	188
First Half Ended June 27, 1999				
Net sales	\$2,095	\$556	\$521	\$3,172
Earnings before interest and income taxes	86	13	59	158

Reconciliation to Consolidated Financial Statements:

Millions	Second Quarter Ended	
	6/25/2000	6/27/1999
Earnings before interest and income taxes for reportable segments	\$ 107	\$ 103
Interest expense	21	19
Income tax expense	22	25
Minority interest	3	1
Net earnings	<u>\$ 61</u>	<u>\$ 58</u>
Net assets for reportable segments	\$2,583	\$2,298
Liabilities deducted in arriving at net assets	1,971	2,116
Deferred tax assets not allocated to segments	320	334

Debt-related costs not allocated to segments	19	22
Total assets	<u>\$4,893</u>	<u>\$4,770</u>

Millions	First Half Ended	
	6/25/2000	6/27/1999
Earnings before interest and income taxes for reportable segments	\$ 188	\$ 158
Interest expense	40	38
Income tax expense	39	35
Minority interest	6	3
Net earnings	<u>\$ 103</u>	<u>\$ 82</u>

Note 6. Restructuring and Other Non-Recurring Charges: In the third quarter of 1998, the Company recorded charges of \$125 million, comprised of \$100 million for costs to reduce the worldwide workforce by approximately 1,100 people, as well as costs associated with streamlining certain majority-owned and international joint venture operations and \$25 million for a civil penalty to be paid by the Company as a result of an agreement reached with the U.S. Environmental Protection Agency (EPA) regarding diesel engine emissions. In addition, the Company recorded special charges of \$14 million for inventory write-downs associated with restructuring actions.

The Company is continuing the restructuring plan implemented in the third quarter of 1998. As of June 25, 2000, approximately \$91 million has been charged against the liabilities associated with these actions. The Company has funded the restructuring actions using cash generated from operations. The remaining actions to be completed consist primarily of the outsourcing of certain manufacturing operations and payment of severance commitments to terminated employees. The program is expected to be essentially complete in 2000, and the Company does not currently anticipate any material changes in the original charges recorded for these actions.

Activity in the major components of these charges is as follows:

\$ Millions	Original Provision	Charges				Balance 6/25/00
		1998	1999	Q1 2000	Q2 2000	
Restructuring of majority-owned operations:						
Workforce reductions	\$ 38	\$(12)	\$(14)	\$(3)	\$(1)	\$ 8
Asset impairment loss	22	-	(7)	(2)	(1)	12
Facility consolidations and other	17	(8)	(4)	(2)	(1)	2
	<u>77</u>	<u>(20)</u>	<u>(25)</u>	<u>(7)</u>	<u>(3)</u>	<u>22</u>
Restructuring of joint venture operations:						
Workforce reductions	11	-	(10)	-	-	1
Tax asset impairment loss	7	-	(7)	-	-	-
Facility & equipment-related costs	5	-	(5)	-	-	-
	<u>23</u>	<u>-</u>	<u>(22)</u>	<u>-</u>	<u>-</u>	<u>1</u>
Inventory write-downs associated with restructuring actions	14	(5)	(9)	-	-	-
Total restructuring charges	<u>114</u>	<u>(25)</u>	<u>(56)</u>	<u>(7)</u>	<u>(3)</u>	<u>23</u>
EPA penalty	25	-	(8)	-	-	17
Total	<u>\$139</u>	<u>\$(25)</u>	<u>\$(64)</u>	<u>\$(7)</u>	<u>\$(3)</u>	<u>\$40</u>

Overview

Net sales were \$1.77 billion in the second quarter of 2000, the second highest sales quarter ever, and 6 percent higher than the second quarter of 1999. Earnings before interest and taxes in the second quarter of 2000 matched an all-time record for the Company of \$107 million, or 6.0 percent of sales. This compares to \$103 million, or 6.2% of sales, in the second quarter of 1999. Net earnings were \$61 million, or \$1.62 per share, compared to \$58 million, or \$1.50 per share, in the second quarter of 1999. Net earnings for the first half of 2000 were \$103 million, or \$2.70 per share, compared to \$82 million, or \$2.13 per share, in the first half of 1999.

Results of Operations

Net Sales:

Revenues from sales of engines were 54 percent of the Company's net sales in the second quarter of 2000, with engine revenues 2 percent higher than second-quarter 1999 and unit shipments 8 percent higher. Unit shipments increased more than revenue due to lower heavy-duty engine sales, primarily in the North American heavy-duty truck market.

Unit Shipments	Second Quarter		First Half	
	2000	1999	2000	1999
Midrange Engines	89,100	76,600	168,000	150,300
Heavy-duty Engines	25,800	30,600	53,200	57,400
High-horsepower Engines	3,000	2,200	5,500	4,200
	<u>117,900</u>	<u>109,400</u>	<u>226,700</u>	<u>211,900</u>

Revenues from non-engine products, which were 46 percent of net sales in the second quarter of 2000, were 12 percent higher than the second quarter of 1999. The major increases included higher sales of gensets and filtration products and revenues from international distributors.

The Company's sales for each of its key businesses during the comparative periods were:

\$ Millions	Second Quarter		First Half	
	2000	1999	2000	1999
Automotive markets	\$ 810	\$ 820	\$1,586	\$1,580
Industrial markets	297	275	566	515
Engine Business	<u>1,107</u>	<u>1,095</u>	<u>2,152</u>	<u>2,095</u>
Power Generation Business	368	305	697	556
Filtration Business & Other	294	267	568	521
	<u>\$1,769</u>	<u>\$1,667</u>	<u>\$3,417</u>	<u>\$3,172</u>

In the second quarter of 2000, engine business revenues of \$1.1 billion increased 1 percent as compared to the second quarter of 1999, despite a 28 percent decrease in shipments to the North American heavy-duty truck market. The Company expects a further decline in the North American heavy-duty truck market during the second half of 2000 as compared to the first half of the year.

Sales of \$810 million in the second quarter of 2000 for automotive markets were 1 percent lower than the second quarter of 1999. Heavy-duty truck revenues decreased 14 percent from the second quarter of 1999, with the market decline in North America partially offset by increased demand in Mexican automotive markets.

Medium-duty truck revenues were essentially flat with the second quarter of 1999, despite an 11 percent increase in unit shipments. This variance reflected a mix shift towards engines with a lower selling price and margin. Unit shipments to North America declined 19 percent, while international shipments increased 38 percent, primarily in Brazil.

Revenues of the bus and light commercial vehicle market were 26 percent higher than the second quarter of 1999. In the second quarter of 2000, Cummins shipped a record 32,100 engines to DaimlerChrysler, 36 percent higher than the second-quarter 1999 level. Shipments to the North American bus and recreational vehicle market were 11 percent higher than the year-ago quarter, and shipments for international bus markets increased 92 percent from the second quarter of 1999, due to higher sales into China and Mexico.

Sales to industrial markets were 8 percent higher than the second quarter of 1999, due to increased volume and a shift in product mix. Engine revenues for this market were up 9 percent on a 3-percent increase in units. Construction equipment business was flat compared to second quarter 1999, while agricultural equipment demand declined 11 percent from the prior year's quarter. Sales to marine markets increased 11 percent from second quarter 1999, with growth in Europe and North America. Mining market sales increased 38 percent as compared to the second quarter of 1999, reflecting higher high-horsepower engine volumes.

In the second quarter of 2000, sales for the Company's power generation business increased 21 percent compared to second quarter 1999. Sales of the Company's generator sets were 37 percent above second quarter last year with continued strength in North American markets. Engine sales to generator set assemblers were up 24 percent from the second quarter of 1999, primarily in Europe and Turkey. Generator set sales for the recreational vehicle market in North America were essentially flat with the year-ago quarter.

Filtration business and other sales were \$294 million in the second quarter of 2000, an increase of 10 percent from the second quarter of 1999. Sales of filtration products reflected gains in North America and Europe and strong increases in Latin America, Mexico and Asia. Sales of international company-owned distributors and the Holset turbocharger business included in this segment also increased compared to the second quarter of 1999.

In total, international markets represented 41 percent of the Company's revenues in the second quarter of 2000, with increases in most of the international markets in which the Company participates. Sales to Europe and the CIS, representing 13 percent of the Company's sales in the second quarter of 2000, were 12 percent higher than the prior year's quarter. Business in Mexico, Brazil and Latin America represented 7 percent of sales in the second quarter of 2000, with revenues 32 percent above the year-ago levels. Asia and Australian markets, in total, representing 13 percent of sales in the second quarter of 2000, were 20 percent higher than the prior year's quarter. Sales to Canada, representing 6 percent of sales in the second quarter of 2000, were 25 percent lower than the second quarter of 1999 due to the decline in the heavy-duty truck market.

Gross Margin:

The Company's gross margin percentage was 19.8 percent in the second quarter of 2000, compared to 22.3 percent in the prior year's quarter. The decreased margin in 2000 was due to higher product coverage costs and changes in product mix. Contributing to the increased product coverage costs is the ISX engine family, which continues to have higher coverage costs than the N14 product it replaces. The Company currently anticipates this increased level of product coverage expense to continue for the next three to four quarters. The impact on gross

margin from changes in product mix resulted from the mix shift from the N14 to the ISX engines, as well as mix changes in the power generation business and in the Company's international distributor revenue. For the first half of 2000, gross margin percentage was 20.1 percent, compared to 21.2 percent in the first half of 1999.

Operating Expenses:

Selling and administrative expenses as a percent of sales were 10.8 percent in the second quarter of 2000, compared to 12.0 percent in the second quarter of 1999, with total spending decreasing \$10 million on a 6-percent increase in sales. Research and engineering expenses declined from 3.6 percent of sales in the second quarter of 1999 to 3.3 percent in the second quarter of 2000. These improvements are primarily a result of the Company's cost reduction initiatives.

The Company is continuing the restructuring plan implemented in the third quarter of 1998. During the second quarter of 2000, \$3 million was charged against the liabilities associated with these actions. The Company expects to complete the restructuring in 2000 and does not

currently anticipate any material changes in the original charges recorded for these actions.

The Company's income from joint ventures and alliances was \$3 million in the second quarter of 2000 as compared to losses of \$5 million in the second quarter of 1999 due to the termination of the Company's joint venture with Wartsila, which had losses of \$7 million in the second quarter of 1999.

Other:

Interest expense was \$21 million in the second quarter of 2000, compared to \$19 million in the prior year's quarter due to increased levels of borrowings and lower interest capitalization. Other income was \$2 million in the second quarter of 2000 compared to expense of \$3 million in the second quarter of 1999, with the variance resulting primarily from increased earnings from distributors and from non-recurring transactions recorded in the prior year.

Provision for Income Taxes:

In the second quarter, the estimated effective tax rate for 2000 was reduced to 26 percent for the year. The Company's tax rate for the second quarter was 25 percent to reflect the year-to-date adjustment to the lower 2000 effective tax rate. The effective tax rate for the second quarter and first half of 1999 was 29 percent.

Cash Flow and Financial Condition

Key elements of cash flows were:

\$ Millions	First Half	
	2000	1999
Net cash provided by operating activities	\$ 59	\$183
Net cash used in investing activities	(139)	(91)
Net cash provided by (used in) financing activities	81	(63)
Effect of exchange rate changes on cash	(1)	-
Net change in cash and cash equivalents	\$ -	\$ 29

In the first half of 2000, net cash provided by operating activities was \$59 million, reflecting the Company's strong net earnings and the non-cash effect of depreciation and amortization, reduced by increases in working capital. Net cash requirements for investing activities of \$139 million included capital expenditures of \$84 million in the first half of 2000, compared to capital expenditures of \$80 million in the first half of 1999. Net cash provided by financing activities was \$81

million in the first half of 2000. This included proceeds from increased borrowings, reduced by cash used for dividend payments and repurchases of the Company's stock.

FORWARD-LOOKING STATEMENTS

When used herein, the terms "expect, plan, anticipate, believe" or similar expressions, as they relate to the Company or its management, are intended to identify forward-looking statements.

The Company has included certain forward-looking statements in this Management's Discussion and Analysis of Results of Operations, Cash Flow and Financial Condition and in the Company's press releases, teleconferences and other external communications. These statements are based on current expectations, estimates and projections about the industries in which the Company operates, management's beliefs and various assumptions made by management which are difficult to predict. Among the factors that could affect the outcome of the statements are general industry and market conditions and growth rates. Therefore, actual outcomes and their impact on the Company may differ materially from what is expressed or forecasted. The Company undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

Item 6. Exhibits and Reports on Form 8-K:

- (a) See the Index to Exhibits on page 14 for a list of exhibits filed herewith.
- (b) The Company was not required to file a Form 8-K during the second quarter of 2000.

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 ENGINE COMPANY, INC.

By: /s/Robert C. Crane

Robert C. Crane
Vice President - Corporate Controller
(Chief Accounting Officer)

July 31, 2000

CUMMINS ENGINE COMPANY, INC.

INDEX TO EXHIBITS

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