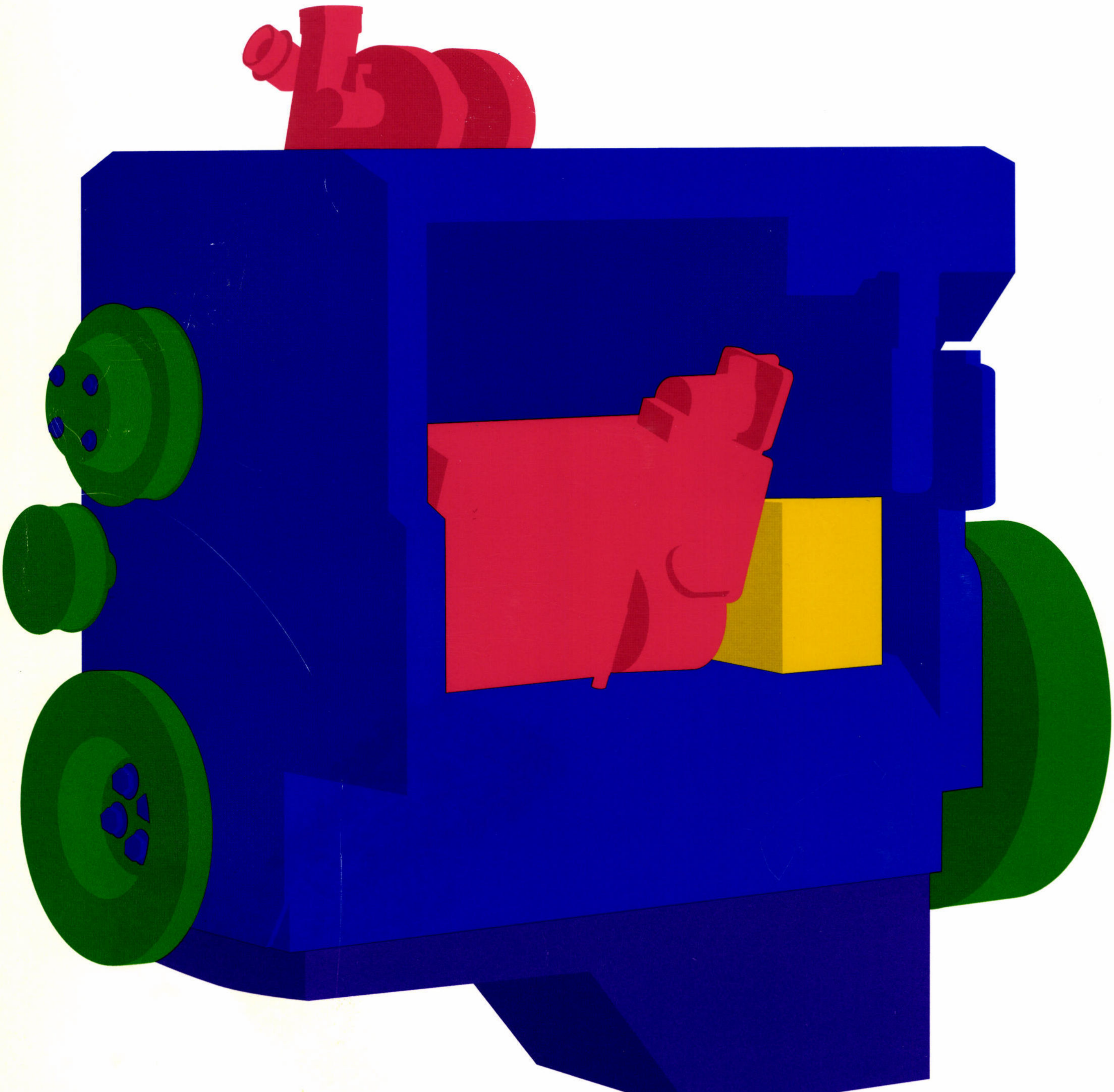
Annual Report 1996



CUMMINS ENGINE COMPANY, INC.

500 JACKSON STREET, BOX 3005, COLUMBUS, INDIANA 47202-3005

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

To the Shareholders of
CUMMINS ENGINE COMPANY, INC.

NOTICE IS HEREBY GIVEN that the Annual Meeting of the Shareholders of Cummins Engine Company, Inc. will be held at the Columbus East High School Auditorium, 230 South Marr Road, Columbus, Indiana, on Tuesday, April 1, 1997, at 10:30 a.m., local time, for the following purposes:

1. to elect twelve directors of the Company for the ensuing year;
2. to ratify the appointment of Arthur Andersen LLP as auditors for the year 1997;
3. to transact any other business that may properly come before the meeting or any adjournment thereof.

Only shareholders of Common Stock of the Company of record at the close of business on February 14, 1997, are entitled to notice of and to vote at the meeting.

Shareholders of Common Stock who do not expect to be present in person at the meeting are urged to complete, sign and date the enclosed proxy and return it promptly to the undersigned in the envelope provided.

The proxy may be revoked by the shareholder giving it at any time before the voting. Any shareholders entitled to vote at the meeting who attend the meeting will be entitled to cast their votes in person.

MARK R. GERSTLE,
Secretary

March 1, 1997

CUMMINS ENGINE COMPANY, INC.

500 JACKSON STREET, BOX 3005, COLUMBUS, INDIANA 47202-3005

PROXY STATEMENT

This proxy statement is being furnished in connection with the solicitation by the Board of Directors of Cummins Engine Company, Inc. (the ''Company'' or ''Cummins'') of proxies to be voted at the Annual Meeting of Shareholders to be held on Tuesday, April 1, 1997, and at any adjournment thereof (the ''Annual Meeting''). This proxy statement, together with the enclosed proxy, is first being mailed to the shareholders of the Company on or about March 1, 1997.

Holders of the Company's Common Stock of record at the close of business on February 14, 1997 are entitled to vote at the Annual Meeting. On that date there were issued and outstanding 41,907,422 shares of Common Stock, each of which is entitled to one vote.

Each share of Common Stock represented by a properly executed proxy will be voted at the Annual Meeting in accordance with the instructions indicated on that proxy, unless such proxy has been previously revoked. If no instructions are indicated on a signed proxy, the shares represented by such proxy will be voted as recommended by the Board of Directors.

A shareholder may revoke the proxy at any time before it is voted by delivering to the Secretary of the Company written notice of such revocation. This notice must include the number of shares for which the proxy had been given and the name of the shareholder of such shares as it appears on the stock certificate(s) evidencing ownership of such shares. In addition, any shareholder who has executed a proxy but is present at the Annual Meeting will be entitled to cast its vote in person instead of by proxy, thereby cancelling the previously executed proxy.

PRINCIPAL SECURITY OWNERSHIP

The following table identifies those shareholders known to the Company to be the beneficial owners of more than five percent of the Common Stock of the Company and shows as to each such shareholder as of February 14, 1997 (i) the number of shares beneficially owned by such shareholder(s) and the nature of such beneficial ownership and (ii) the percentage of the entire class of Common Stock so beneficially owned:

	Amount and Nature of Beneficial Ownership	Percent of Class
FMR Corporation 82 Devonshire Street Boston, MA 02109	5,959,786(1)	14.22%
Miller Anderson & Sherrerd, LLP One Tower Bridge West Conshohocken, PA 19428	5,751,687(2)	13.72%
Cummins Engine Company, Inc. Employee Benefits Trust c/o The Vanguard Fiduciary Trust Company Post Office Box 2900 Valley Forge, PA 19482	3,750,000	8.95%
The Capital Group Companies, Inc. 333 South Hope Street Los Angeles, CA 90071	2,500,260(3)	5.97%
Cummins Engine Company, Inc. and Affiliates Employee Stock Ownership Trust c/o The Vanguard Fiduciary Trust Company Post Office Box 2900 Valley Forge, PA 19482	2,222,080	5.30%

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(1) The source of this information is a Schedule 13G dated February 14, 1997 disclosing beneficial ownership by FMR. FMR states in its 13G that it has sole investment power for all of the shares, sole voting power for 117,776 shares and no shared investment or voting power.

(2) The source of this information is a Schedule 13G dated February 14, 1997 disclosing beneficial ownership by MAS, and information known to the Company regarding a purchase transaction that occurred on January 8, 1997. MAS states in its 13G that it has shared investment power for 3,851,687 shares, shared voting power for 3,255,287 shares and no sole voting or investment power.

(3) The source of this information is a Schedule 13G dated February 25, 1997 disclosing beneficial ownership by certain operating subsidiaries of the Capital Group Companies, Inc. These entities were reported to possess, in the aggregate, sole voting power for 260 shares, sole investment power for all of the shares and no shared voting or investment power.

ELECTION OF DIRECTORS

(Item 1)

It is intended that votes will be cast pursuant to the accompanying proxy for the election of the twelve nominees listed below, all of whom are presently directors of the Company. All directors will serve for the ensuing year and until their respective successors are elected and qualified. A shareholder may withhold authority from such shareholder's proxy to vote for the election of any or all of the nominees listed below.

The Board of Directors has no reason to believe that any of the nominees will be unable to serve if elected. If, for any reason, one or more of such persons should be unable to serve, it is intended that votes will be cast for a substitute nominee or nominees designated by the Board of Directors unless the Board of Directors decides to reduce the number of directors.

The names of the nominees for directors, together with certain information regarding them, are set forth below. Biographical sketches of these nominees, which include their business experience during the past five years and directorships of other corporations, are provided on pages 21 through 26 of this proxy statement.

Name and Occupation	Age	First Year Elected a Director(1)	Amount and Nature of Beneficial Ownership as of February 28, 1997(2)	Percent of Class
Harold Brown Counselor, Center for Strategic & International Studies; Partner, Warburg, Pincus & Co., venture banking firm	69	1985	946(3)	*
Robert J. Darnall Chairman, President and Chief Executive Officer, Inland Steel Industries, Inc., steel manufacturing and materials distribution	58	1989	1,562	*
Walter Y. Elisha Chairman and Chief Executive Officer, Springs Industries, Inc., manufacturer of home furnishings, industrial and specialty fabrics	64	1991	1,562	*
Hanna H. Gray President Emeritus and Professor of History, University of Chicago	66	1977	746	*
James A. Henderson Chairman of the Board and Chief Executive Officer of Cummins	62	1974	172,768(4)	*
William I. Miller Chairman, Irwin Financial Corporation, financial services company	40	1989	37,324(5)	*
Donald S. Perkins Retired Chairman, Jewel Companies, Inc., diversified retailing	69	1974	4,562	*
William D. Ruckelshaus Principal, Madrona Investment Group, L.L.C.	64	1974	1,562	*
Henry B. Schacht Chairman and Chief Executive Officer, Lucent Technologies, Inc., communication industry products	62	1969	118,086(6)	*

Name and Occupation	Age	First Year Elected a Director(1)	Amount and Nature of Beneficial Ownership as of February 28, 1997(2)	Percent of Class
Theodore M. Solso President and Chief Operating Officer of Cummins	49	1994	91,233(7)	*
Franklin A. Thomas Consultant, TFF Study Group	62	1973	1,253	*
J. Lawrence Wilson Chairman and Chief Executive Officer, Rohm and Haas Company, chemicals and plastics manufacturing	61	1990	2,554	*

*Less than 1%.

(1) Except for Mr. Ruckelshaus, each Director has served continuously since the year indicated. Mr. Ruckelshaus served on the Board of Directors from 1974 until 1983 when he returned to Federal Government service and was reelected to the Board of Directors in 1985.

(2) Except as indicated, the voting and investment powers of the shares listed are held solely by the reported owner.

(3) These shares are held by a trust, of which Dr. Brown is a co-trustee, settlor and beneficiary.

(4) Includes 56,200 shares which Mr. Henderson has the right to acquire within the next 60 days through the exercise of stock options. Also included are 400 shares held by Mr. Henderson's wife who has sole voting and investment powers thereof.

(5) Includes 15,003 shares held by Mr. Miller for the benefit of his children.

(6) Includes 66,900 shares which Mr. Schacht has the right to acquire within the next 60 days through the exercise of stock options granted to him prior to his retirement as an employee of the Company.

(7) Includes 29,000 shares which Mr. Solso has the right to acquire within the next 60 days through the exercise of stock options. Also included are 15,919 shares held by a family trust and 14,604 shares held by a family limited partnership of which Mr. Solso is a general partner.

Directors will be elected by a plurality of the votes cast. Votes cast for a nominee and, if no contrary instructions are indicated on a signed proxy, the shares represented by such proxy will be voted for a nominee. Abstentions, broker non-votes and instructions on a signed proxy withholding a vote will result in a nominee receiving fewer votes. However, the number of votes otherwise cast for the nominee will not be affected by such actions.

The Board of Directors and Its Committees

The Board of Directors held six meetings during 1996. All of the directors attended 75% or more meetings of the Board and Committees on which they served.

The Board of Directors has established eight standing committees. The functions performed by certain of these committees and the members of the Board of Directors currently serving on these committees are as follows:

Audit Committee. The members of the Audit Committee are D. S. Perkins (Chairman), H. H. Gray and W. D. Ruckelshaus. The Committee reviews the accounting and auditing principles and procedures of the Company. The Audit Committee reviews the scope, timing, and fees for the annual audit and the results of audit examinations performed by the internal auditors and independent public accountants, including their recommendations to improve the system of accounting and internal controls. The Audit Committee met four times during 1996.

Compensation Committee. The members of the Compensation Committee are H. H. Gray (Chairman), H. Brown, D. S. Perkins, W. D. Ruckelshaus and F. A. Thomas. The Compensation Committee administers and determines eligibility for and makes awards under the Company's stock option and other stock incentive plans. The Committee also reviews and evaluates the Company's executive compensation standards and practices, including salaries, bonus distributions, deferred compensation practices and participation in stock purchase plans. The Compensation Committee met four times during 1996.

Nominating and Organization Committee. The members of the Nominating and Organization Committee are F. A. Thomas (Chairman), H. Brown, R. J. Darnall, W. Y. Elisha, H. H. Gray, W. I. Miller, D. S. Perkins, W. D. Ruckelshaus, H. B. Schacht and J. L. Wilson. The Nominating and Organization Committee reviews and makes recommendations to the Board with respect to membership, size, composition, procedures and organization of the Board of Directors. The Committee also evaluates the Chief Executive Officer's performance and monitors meeting attendance of Board members. This Committee will consider shareholders' recommendations of nominees for election to the Board of Directors. Shareholder recommendations, including biographical information as to the proposed candidate and a statement from the shareholder as to the qualifications and willingness of such person to serve on the Company's Board of Directors, must be submitted in writing to the Secretary of the Company in accordance with the procedures established in the Company's By-Laws. The Nominating and Organization Committee replaced the former Nominating Committee and met three times during 1996.

Executive Committee. The members of the Executive Committee are J. A. Henderson (Chairman), W. I. Miller and T. M. Solso. The Executive Committee is authorized to exercise the powers of the Board of Directors in the management and direction of the business and affairs of the Company during the intervals between meetings of the Board of Directors. The Executive Committee met one time during 1996.

Other Committees. In addition to the Committees described above, the Board of Directors has established the following committees: Business Development and Finance Committee (J. L. Wilson, Chairman, W. Y. Elisha and H. B. Schacht); Employee Development and Benefits Committee (R. J. Darnall, Chairman, W. I. Miller and F. A. Thomas); Proxy Committee (H. B. Schacht, Chairman, and F. A. Thomas); and Technology Committee (H. Brown, Chairman, and T. M. Solso).

Each director who is not an officer of the Company receives an annual fee of $45,000, $27,000 of which is paid in cash and $18,000 of which is paid in the form of restricted stock. Each non-officer director also receives $1,000 for each special meeting of the Board of Directors attended. Committee chairmen (other than the Executive or Proxy Committee) receive an additional annual fee of $9,000. Non-chair members of the Audit, Business Development and Finance, Executive, Compensation, Employee Development and Benefits, Nominating and Organization and Technology Committees receive an additional $6,000 fee for each such Committee membership. Committee members also receive $1,000 for attending a Committee meeting (other than a meeting of the Executive Committee) that is not held in connection with a regular or special meeting of the Board of Directors.

As part of the Company's overall support of charitable and educational institutions and as an aid in attracting and retaining qualified directors, the Company has established the Cummins Engine Company Charitable Bequest Program in which all directors participate. Upon the death of a director, the Company will donate ten equal annual installments of $100,000 to one or more qualifying institutions designated by such director, subject to certain vesting requirements based upon years of service as a director. The Company has purchased life insurance policies on each director, the proceeds of which fund donations under the program. Directors will not receive any financial benefit from the program since all charitable deductions accrue solely to the Company.

Nominee Harold Brown has a consulting arrangement with the Company pursuant to which he provides consulting services in connection with the Company's research and development activities and related technology issues. During 1996, the Company paid Dr. Brown $50,000 for these services. In addition, the Company has established a Science and Technology Advisory Council on which Dr. Brown serves as Chairman. The Council advises senior management and the Board of Directors on the direction and implication of developments in science, technology and environmental issues that may have applicability to the Company's current and future business goals and objectives. For his services on the Council, Dr. Brown is paid an annual retainer of $17,000, including $7,000 for serving as Chairman, and an additional fee of $3,000 for each day of meetings attended during the year.

The Company has a deferred compensation plan for non-employee directors, pursuant to which such directors may elect to defer receipt of all or any portion of their compensation while they serve as a director of the Company. Upon ceasing to be a director, the deferred compensation, plus accrued interest, is paid to the director or the director's beneficiary in a lump sum or in annual installments, not to exceed ten, as specified by the director. Upon a change of control of the Company (as defined in the plan), such deferred compensation and interest is paid in cash to the director in one lump sum.

During 1996, the Company maintained a retirement plan for non-employee directors who had no vested rights under any other pension plan sponsored by the Company and who had served as a director for 5 or more years. Under the plan, annual payments equal to the amount of fees (excluding Committee fees) paid or payable for the final year of service were to be made to a former director each year for the lesser of 20 years or the number of years served as a director. Upon a change of control of the Company (as defined in the plan), the actuarial present value of accrued but unpaid benefits was to be distributed to the director in one lump sum.

In early 1997, the Board of Directors determined to eliminate any future service accruals under the retirement plan and to provide to each non-employee director, in lieu thereof, an increase in the amount of the annual retainer fee payable in restricted Common Stock from $6,000 to $18,000 based on the trailing 30 trading day average of closing prices of the Common Stock on the date of the Company's Annual Meeting each year. Directors with vested retirement plan benefits on the date future accruals were eliminated will be given an option to have their accrued benefits frozen and retained in the plan for future payment, or to convert the present value (using the same actuarial assumptions as are applicable to the payment of pension benefits to the Company's employees) of their accrued benefits into phantom units of Common Stock based on a trailing trading day average of closing prices of Common Stock on the date of conversion. The stock units, including additional stock units credited thereon as dividend equivalents, will be evidenced by bookkeeping entries. Recipients will have no voting or investment power with respect to the stock units. The value of each director's stock units will be payable only in cash on or after the director's ceasing to be a member of the Board or upon a change of control of the Company.

EXECUTIVE COMPENSATION

Compensation Committee Report

The Compensation Committee Report is organized as follows:

- Role of the Compensation Committee
- Objectives and Principles
- Compensation Program Elements
- Compensation of the Chief Executive Officer

Role of Compensation Committee

The Compensation Committee is made up of five members of the Board of Directors of the Company, who are not current or former employees of the corporation. The Committee has oversight responsibility for the Company's executive compensation programs. The Committee sets the general compensation philosophy of the Company. It reviews the elements of the compensation program, the specifics of each element, the goals and measurements used in the program, and the results of the compensation program compared to the philosophy to determine if the compensation program is performing as expected.

In addition, the Committee reviews the individual levels and awards for each of the five most highly paid officers and takes appropriate action. In its review, the Committee has direct access to advice from professional executive compensation consultants. The Committee also reviews its actions with the full Board of Directors.

Objectives and Principles of Executive Compensation

Cummins' executive compensation is designed to attract, motivate, and retain the personnel required to achieve the Company's performance goals in the competitive global business environment. The program is designed to reflect the individual's contribution and the performance of the Company. The program attempts to strike an appropriate balance between short-term and long-term performance.

The Company is committed to the concept of pay for sustained financial performance. We evaluate performance over several periods of time. While the specific elements of executive compensation vary from time to time, the Compensation Committee focuses on this central principle of pay for performance in reviewing the compensation program, any proposed changes, and the specific awards.

The Committee follows several principles, in addition to pay for performance, in designing and implementing compensation programs for its officers.

- Programs should provide competitive compensation opportunity, the concept of opportunity is important in our program. We believe the executive should have the opportunity to do well if the Company does well, but that total compensation should vary in relation to the Company's performance.

- An individual's compensation should be at the median of the range when compared to the compensation of individuals in U.S. industrial companies with sales volumes similar to Cummins, when Cummins' financial performance is at the median of those companies.
- There should be a balance between short-term and long-term elements of compensation.
- The more senior a person's position, the more the compensation should be ''at risk'', i.e., dependent on the performance of the Company.
- Stock should be an important part of the program in order to link the management's compensation with shareholders' expectations; the greater the level of responsibility of the person, the more the compensation should be stock-based.
- The system should be as simple and as easily understood as possible.
- Payouts should not accumulate, causing large one-time payments.

In addition to these principles, we have the following observations:

- No single program accomplishes these aims consistently; a mix of programs is best
- There is no single best comparator of performance with other companies; a mix of comparators should be used.
- In this complex area, relative simplicity seems the best that can be achieved.
- There is no perfect program; change should be expected from time to time as the outcome of the Committee's periodic reviews.

Section 162(m) of the Internal Revenue Code (''Section 162(m)'') limits the corporate tax deduction to one million dollars for compensation paid annually to any one of the named executive officers in the proxy, unless the compensation meets certain requirements. The Committee adopted changes to the compensation program, approved by shareholders in 1995, that qualify payments under the Senior Executive Bonus Plan and Senior Executive Three Year Performance Plan for tax deductibility under Section 162(m). These changes were designed to maximize tax deductibility, while retaining the ability to attract, retain and motivate executives to achieve our business objectives. Payments under these plans were certified by the Compensation Committee for each payment period in 1996.

As indicated below, the Base Salary of the named executive officers is set at the median of the range of the salaries of individuals with similar positions in companies of similar size to Cummins. The Committee intends to continue this policy notwithstanding the enactment of Section 162(m).

Compensation Program Elements

The Company's executive compensation program consists of four elements: Base Salary, Short-Term Bonus, Medium-Term compensation, and Long-Term compensation. Each is designed to accomplish a somewhat different objective. In total, they are designed to fulfill the Company's basic goals of linking pay to financial performance and paying competitively. All officers participate in each element of the program.

We use survey data provided by our compensation consultants to determine competitive levels of pay. These surveys include over 300 U.S. industrial corporations (including the eleven companies that comprise the ''Peer Group'' companies used in the Shareholder Return Performance Presentation on page 12 of this Proxy Statement). Each element of pay described below is intended to provide compensation for each position at the median of the amounts companies of similar size in the survey would pay the same position.

1. Base Salary

Base Salary is reviewed annually. It is the only fixed portion of the executive's compensation. Base Salary is normally set at the median of the range of the salaries of individuals with similar positions in companies of similar size to Cummins.

2. Short-Term Bonus

This element is designed to link executive pay to the short-term performance of the Company. The payout is made quarterly, with the Payout Factor calculated on a formula established by the Committee and reviewed annually. Each person is assigned a participation rate that is a percent of salary. The quarterly bonus is then determined as follows.

(Short-Term Bonus) equals (Annual Base Salary) times (participation percentage assigned to each job) times (Payout Factor) times (¼).

Participation rates are based on the same survey data as base salaries and are set at the median of the range for like positions in similarly sized companies.

The Payout Factor for the quarterly bonus is set to yield a 1.0 Payout Factor for Company financial performance that is at the median of U.S. industrial companies measured over recent history. In 1996, return on equity was the measure used to compare performance. Return on equity levels are converted to equivalent return on sales levels for use in the Payout Factor formula. In determining the return on sales level equivalent to the market median return on equity to establish the 1.0 Payout Factor point for the Short-Term Bonus Plan for 1996, we used a full corporate tax rate, not taking credit for tax loss carryforwards.

When the Company's performance is less than the median, the quarterly bonus pays less than 1.0—and does not pay at all if the Company is not profitable. When the Company's performance exceeds the median, the quarterly Payout Factor is greater than 1.0 and compensation is greater than the median of those companies included in our surveys.

The Company organized into Business Units in the second half of 1996. Beginning in 1997, one-half of the bonus for senior managers of the Company's Business Units will be determined by the return on net assets of the Company's Business Units, and one-half will continue to be based on the Company's performance, as described above. The Committee believes this formula will provide appropriate balance, compensating for performance measured at the Business Unit level as well for the total Company. Basing a significant portion of the bonus on total Company results rewards Business Units for working in an integrated way, maximizing our total financial performance; adding the Business Unit measure emphasizes business results each key manager affects most directly.

In order to comply with the requirements of Section 162 (m), designated officers (the Chief Executive Officer and the Chief Operating Officer in 1996) were compensated under a modified version of the Short-Term Bonus Plan, called the Senior Executive Bonus Plan. The Senior Executive Bonus Plan differs from the Short-Term Bonus Plan in which many employees at all levels of the Company, including all officers, participate, only in that the Compensation Committee has no discretion to increase the payouts once it establishes the performance measures each year.

3. Medium-Term: Three Year Performance Plan

The Three Year Performance Plan measures Cummins' performance versus the Peer Group companies over a rolling three-year cycle. For each three-year Award Cycle, a Target Award is granted to each participant, expressed as a dollar amount.

The Committee establishes performance guidelines to determine the portion of the granted amount to be paid for each three-year Award Cycle. A new Award Cycle begins each year, hence payout opportunity is annual. The first payout under this program was in 1995. The performance measure for Award Cycles ending before 1999 is return on equity. The Committee establishes a scale of multiples of the Target Award to be paid for various levels of Company performance over each Award Cycle. The plan pays the full granted amount if Cummins' performance (based on the applicable performance measure) is equal to the median of the Peer Group companies over the three-year cycle. A portion or multiple of the granted amount is paid if three-year performance is less or greater than the median of these companies, based on a scale established by the Committee. The maximum that can be paid is two times the Target Award for performance that is twice the median of the Peer Companies.

As with the Short-Term Bonus Plan, to comply with the requirements of Section 162(m), designated officers (the Chief Executive Officer and Chief Operating Officer in 1996) were compensated under a modified version of the Three Year Performance Plan, called the Senior Executive Three Year Performance Plan. The plans are identical except that the Committee's discretion to adjust payments upward is eliminated in the Senior Executive Three Year Performance Plan.

4. Long-Term: The 1992 Cummins Stock Incentive Plan

Annually in December 1992 through 1995, and in July, 1996, restricted stock and stock options were granted to officers under the 1992 Cummins Stock Incentive Plan. Restrictions on the restricted stock will lapse on one-third of each grant annually, beginning two years and one month from the date of each grant. The stock options expire ten years from grant, but cannot be exercised for the first two years.

Grant amounts under the Medium-Term and Long-Term plan elements are set to provide total compensation opportunity at the median of that provided by similarly-sized U.S. industrial companies in our survey base, when combined with Base Salary and Short-Term Bonus. The Committee reviews the proportion of total compensation that is dependent on Company performance in determining the allocation of the compensation opportunity among each of the Medium-Term and Long-Term plan elements for each position. More senior positions have a larger proportion of total compensation opportunity dependent on Company performance than do less senior positions.

Compensation of the Chief Executive Officer

Approximately one-third of the CEO's annualized total compensation opportunity is fixed Base Salary. Two-thirds of the total is based on Company performance, assuming median Company financial performance. When the Company's performance is better than the median, the variable compensation elements pay more and comprise a larger portion of the total. When the Company's performance is less than median, the variable elements pay less and comprise a smaller proportion of the total.

The Base Salary and Short-Term Bonus participation rate of the CEO are set at the median of our survey companies specifically as described under the Base Salary and Short-Term Bonus sections appearing earlier in this report.

In 1994 and 1995, the Company exceeded market median financial performance and the Short-Term Bonus payouts reflected this performance. However, Company performance in 1996 lagged the market median, and this is reflected in lower bonus payouts for the CEO in 1996. While the Company's Profit Before Tax was 27% less, the CEO's Short-Term Bonus was 48.7% less, from $646,500 in 1995 to $333,675 in 1996.

In July, 1996 the CEO received grants of restricted stock and stock options under the Long-Term 1992 Stock Incentive Plan, as well as a Target Award (payable in 2000) under the Medium-Term Three Year Performance Plan. This was the fifth set of grants under these Plans. The Committee intends to continue making grants annually.

In determining grant amounts for the CEO, as explained earlier, the Committee set the total of the four elements of the executive compensation program—Base Salary, Short-Term Bonus, Medium-Term Plan, and the Long-Term Plan—to provide annualized compensation opportunity to the CEO equal to the median of the range of total compensation opportunity provided for CEOs by the survey companies described earlier in this report.

The CEO, on a yearly basis, discusses in detail his priorities and objectives with the Nominating and Organization Committee (the members and responsibilities of the Nominating and Organization Committee are shown on page 5 of this proxy). The Nominating and Organization Committee formally reviews the CEO's performance against his stated objectives, especially the progress made by the Company in implementing its business strategy and achieving its business objectives, both short-term and long-term. This review considers both quantitative and qualitative performance matters, and is a key factor in setting the CEO's compensation.

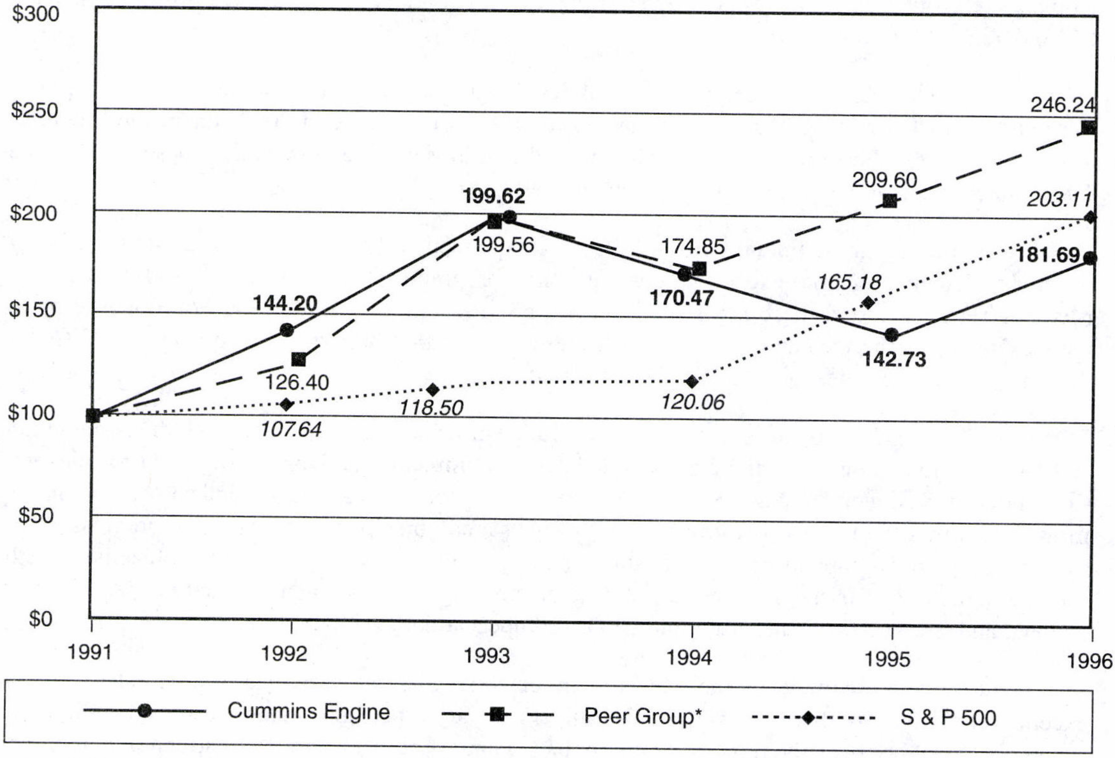
The Committee commends the CEO for the objectives he has very clearly articulated and for excellent progress in their attainment. During 1996, an especially noteworthy and significant accomplishment has been the reorganization of the Company into a business unit structure that places substantial and appropriate focus on the priorities of customer service and shareholder value.

We hope this general discussion and the following tables and graphs help you understand the Company's executive compensation philosophy and program.

HANNA H. GRAY, CHAIRMAN
HAROLD BROWN
DONALD S. PERKINS
WILLIAM D. RUCKELSHAUS
FRANKLIN A. THOMAS

Shareholder Return Performance Presentation

The following graph compares the cumulative total shareholder return on the Common Stock of the Company for the last five fiscal years with the cumulative total return on the S&P 500 Index and an index of peer companies selected by the Company. The comparisons in this table are required by the Securities and Exchange Commission and are not intended to forecast or be indicative of possible future performance of the Company's stock.



*Arvin Industries, Inc., Caterpillar, Inc., Dana Corporation, Deere & Company, Dresser Industries, Inc., Eaton Corporation, Ford Motor Company, General Motors Corporation, Ingersoll-Rand Company, Navistar International Corporation and Paccar, Inc.

Compensation Tables and Other Information

The summary compensation table and accompanying notes and other information on the following pages include individual compensation information for the last three fiscal years on the Company's Chairman and Chief Executive Officer and the four other most highly compensated executive officers during 1996. The dollar value of perquisites and other personal benefits for each of the named executive officers was less than the established reporting threshold and is not included in the table.

SUMMARY COMPENSATION TABLE

Name and Principal Position	Year	Salary	Bonus	(1) Restricted Stock Awards	(2) Stock Options/ SARs (#)	(3) Medium-Term Performance Plans	(4) LTIP Payouts	(5) All Other Compensation
	ANNUAL COMPENSATION			LONG TERM COMPENSATION — Awards		LONG TERM COMPENSATION — Payouts		
J. A. Henderson								
Chairman of the Board	1996	$772,500	$333,675	$575,000	37,500	$375,000	$ 0	$13,524
and Chief Executive	1995	$727,500	$646,500	$418,500	28,100	$382,500	$ 0	$52,700
Officer	1994	$654,000	$767,940	$346,000	22,600	$203,680	$1,081,250	$39,520
T. M. Solso								
President and Chief	1996	$517,500	$204,187	$391,000	22,100	$200,000	$ 0	$47,896
Operating Officer	1995	$480,000	$390,500	$267,375	17,900	$225,000	$ 0	$38,024
	1994	$405,417	$439,381	$177,325	11,500	$ 91,706	$ 378,438	$28,203
F. J. Loughrey								
Executive Vice President	1996	$376,250	$134,750	$211,600	11,900	$ 93,750	$ 0	$15,951
Group President—	1995	$347,292	$259,792	$162,750	10,800	$112,500	$ 0	$20,720
Industrial	1994	$275,000	$222,131	$129,750	8,000	$ 57,704	$ 173,000	$19,230
C. R. Cordaro								
Executive Vice President	1996	$293,750	$101,531	$170,200	9,600	$ 68,750	$ 0	$23,887
Group President—	1995	$270,000	$181,125	$131,750	8,800	$ 82,500	$ 0	$23,552
Automotive	1994	$257,500	$226,294	$ 75,688	4,900	$ 54,438	$ 173,043	$18,246
J. K. Edwards								
Executive Vice President	1996	$293,750	$101,531	$170,200	9,600	$ 68,750	$ 0	$ 1,957
Group President—	1995	$252,500	$168,750	$131,750	8,800	$ 82,500	$ 0	$17,458
Power Generation	1994	$235,000	$206,663	$ 86,500	6,000	$ 37,688	$ 86,414	$18,276

(1) Pursuant to the Company's 1992 Stock Incentive Plan, a total of 93,700 shares of Restricted Stock were granted in 1996, having a total value at date of grant of $3,841,700. Shares are restricted for two years and one month subsequent to grant, then are vested in ⅓ annual increments, if the participant remains an employee of the Company. Dividends will be paid on these shares. As of year-end 1996, the total number of shares of Restricted Stock and the value thereof held by each executive officer was as follows: J. A. Henderson, 37,167 shares, $1,709,682; T. M. Solso, 23,001 shares, $1,058,046; F. J. Loughrey, 13,201 shares, $607,246; J. K. Edwards, 10,500 shares, $483,000; C. R. Cordaro, 10,084 shares, $463,864.

(2) Stock options awarded pursuant to the Company's 1992 Stock Incentive Plan and 1986 Stock Option Plan.

(3) The payout for 1996 represents payout for the 1992 Award Cycle under the Three Year Performance Plan. This was the second payout under the Three Year Performance Plan. The payout is calculated as the individual's Target Award times Payout Factor for the Award Cycle. The Payout Factor was based on the Company's Return on Equity compared to the median ROE of a panel of eleven comparator companies over the Three Year Award Cycle. The payout in 1994 represents payout for the 1989-1993 Award Cycle under the Five Year Performance Plan. This was the final payout under that plan. The payout was calculated as Base Salary times the individual's Participation Percentage times Payout Factor for the Award Cycle. The Payout Factor was based on the Company's Return on Equity compared to the median ROE of a panel of eleven comparator companies over the Five Year Award Cycle.

(4) Represents shares distributed under the Company's Performance Share Plan. The Performance Share Plan was adopted in 1987 under which executive officers and other key employees were awarded Share Rights to be converted into shares of the Company's Common Stock by December 31, 2006, or earlier as financial performance goals established by the Compensation Committee were achieved. The Plan was intended to cover the seven-year period 1988 through 1994. There were no distributions of Share Rights for Plan Year 1988, Plan Year 1989, or Plan Year 1990. The distribution for Plan Year 1991 was made in February 1992; the 1992 distribution was made in February 1993; the 1993 distribution was made in February 1994; the final distribution was made in January 1995.

(5) Amounts reported as "All Other Compensation" for 1996 include, respectively, matching contributions by the Company under the Retirement and Savings Plan and "above market" earnings on previously deferred compensation as follows: J. A. Henderson ($449 and $13,075); T. M. Solso ($2,014 and $45,882); F. J. Loughrey ($1,993 and $13,958); C. R. Cordaro ($1,979 and $21,908); J. K. Edwards ($1,957 and $0).

Security Ownership of Management

Set forth below is information as of February 28, 1997, regarding the beneficial ownership of Common Stock of the Company by the Chief Executive Officer, each of the other named executive officers during 1996 and the directors and executive officers of the Company as a group.

	Amount and Nature of Beneficial Ownership	Percent of Class
James A. Henderson Chairman of the Board and Chief Executive Officer	172,768(1)	*
Theodore M. Solso President and Chief Operating Officer	91,233(2)	*
F. Joseph Loughrey Executive Vice President Group President—Industrial	43,777(3)	*
C. Roberto Cordaro Executive Vice President Group President—Automotive	36,490(4)	*
John K. Edwards Executive Vice President Group President—Power Generation	32,886(5)	*
All directors and executive officers as a group, a total of 21 persons	668,610(6)	1.6%

*Less than 1%

(1) See footnote 4 to the director nominee listing on page 4.

(2) See footnote 7 to the director nominee listing on page 4.

(3) Includes 15,750 shares which Mr. Loughrey has the right to acquire within the next 60 days through the exercise of stock options.

(4) Includes 13,150 shares which Mr. Cordaro has the right to acquire within the next 60 days through the exercise of stock options.

(5) Includes 14,950 shares which Mr. Edwards has the right to acquire within the next 60 days through the exercise of stock options.

(6) Includes 246,450 shares which the officers and directors have the right to acquire within the next 60 days through the exercise of stock options.

The following table discloses, for each of the named executive officers, information regarding individual grants of stock options and stock appreciation rights made during 1996, and their potential realizable values.

Option/SAR Grants in Last Fiscal Year

	Individual Grants				Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation for Option Terms	
Name	(1) Options/SARs Granted (#)	% of Total Options/SARs Granted to Employees in Fiscal Year	Exercise Price ($/share)	Expiration Date	5% ($)	10% ($)
J. A. Henderson	32,500	8.2%	$40.625	7/8/06	$831,797	$2,099,297
	5,000	1.3%	$37.688	9/3/06	$118,716	$ 299,616
T. M. Solso	22,100	5.6%	$40.625	7/8/06	$565,622	$1,427,522
F. J. Loughrey	11,900	3.0%	$40.625	7/8/06	$304,566	$ 768,666
J. K. Edwards	9,600	2.4%	$40.625	7/8/06	$245,700	$ 620,100
C. R. Cordaro	9,600	2.4%	$40.625	7/8/06	$245,700	$ 620,100

Stock option and stock appreciation right exercise activity during 1996, on an aggregated basis for each of the named executives, is contained in the following table. Also disclosed are the number and value of options and appreciation rights, on an aggregated basis, held by each named executive as of December 31, 1996.

Aggregated Option/SAR Exercises in Last Fiscal Year, and FY-End Option/SAR Value

			Number of Unexercised Options/SARs at FY-end (#)		Value of Unexercised In-the-Money Options/SARs at FY-End ($)	
Name	Number of Securities Underlying Options/SARs Exercised	Value Realized ($)	Exercisable	Unexercisable	Exercisable	Unexercisable
J. A. Henderson	0	$0	56,200	60,600	$220,390	$371,225
T. M. Solso	0	$0	29,000	40,000	$117,555	$243,977
F. J. Loughrey	0	$0	15,750	22,700	$ 53,880	$139,503
J. K. Edwards	0	$0	14,950	18,400	$114,010	$113,152
C. R. Cordaro	0	$0	13,150	18,400	$ 43,026	$113,152

Estimated benefits payable to each named executive pursuant to long-term incentive plan rights awarded during 1996 are disclosed in the following table.

Long-Term Incentive Plan Awards in Last Fiscal Year/SAR Value

Name	Number of Shares, Units or other Rights(1)	Period Until Payout	Estimated Future Payouts Under Non-Stock Based Plans		
			Threshold	Target	Maximum
J. A. Henderson	0		$105,000	$420,000	$840,000
T. M. Solso	0		$ 71,250	$285,000	$570,000
F. J. Loughrey	0		$ 38,750	$155,000	$310,000
C. R. Cordaro	0		$ 25,000	$100,000	$200,000
J. K. Edwards	0		$ 25,000	$100,000	$200,000

(1) No shares, units or other rights were awarded in the last fiscal year. The Company has made targeted dollar awards under its Three Year Performance Plan and Senior Executive Three Year Performance Plan, with payouts tied to Company performance over a rolling three-year cycle, as determined by the Compensation Committee of the Board of Directors. The Committee establishes performance measures as guidelines. For the 1996-1998 Award Cycle under the Three Year Performance Plan (payable in 1999), and the 1997-1999 Award Cycle under the Senior Executive Three Year Performance Plan (payable in 2000), the performance guidelines are tied to achieving certain levels of return on equity (ROE) compared to the Peer Group companies. The Target Award will be earned if the Company's ROE is equal to the median ROE of the Peer Group companies. The Threshold Payment will be earned if the Company's ROE is 50% of the Peer Group companies' median ROE. The Maximum Payment is earned if the Company's ROE is 200% of the Peer Group companies' ROE.

Pension Plan Table

The Company maintains retirement pension programs for its employees, including the executive officers named in the Summary Compensation Table on page 13. Elements of the program for the executive officers include the Company's Cash Balance Pension Plan, the Excess Benefit Plan which provides pension benefits in excess of limitations imposed by the Internal Revenue Code, and the Supplemental Life Insurance and Deferred Income Program. The following table sets forth the estimated maximum annual pension benefits payable on a straight life annuity basis under the program to the officers in various compensation and years of service classifications upon retirement at age 65. An officer who is among the Company's two highest paid executive officers at the time of retirement will receive an annual benefit greater than amounts reflected in the table by an amount equal to 10% of the officer's covered compensation.

Average Total Cash Compensation (Base Salary plus Short-Term Bonus)	Estimated Annual Benefit Upon Retirement				
	10 Years	15 Years	20 Years	25 Years	30+ Years
$ 200,000	$ 40,000	$ 60,000	$ 80,000	$ 90,000	$100,000
$ 275,000	$ 55,000	$ 82,500	$110,000	$123,750	$137,500
$ 350,000	$ 70,000	$105,000	$140,000	$157,500	$175,000
$ 425,000	$ 85,000	$127,500	$170,000	$191,250	$212,500
$ 500,000	$100,000	$150,000	$200,000	$225,000	$250,000
$ 575,000	$115,000	$172,500	$230,000	$258,750	$287,500
$ 650,000	$130,000	$195,000	$260,000	$292,500	$325,000
$ 725,000	$145,000	$217,500	$290,000	$326,250	$362,500
$ 800,000	$160,000	$240,000	$320,000	$360,000	$400,000
$ 875,000	$175,000	$262,500	$350,000	$393,750	$437,500
$ 950,000	$190,000	$285,000	$380,000	$427,500	$475,000
$1,025,000	$205,000	$307,500	$410,000	$461,250	$512,500
$1,100,000	$220,000	$330,000	$440,000	$495,000	$550,000
$1,175,000	$235,000	$352,500	$470,000	$528,750	$587,500
$1,250,000	$250,000	$375,000	$500,000	$562,500	$625,000
$1,325,000	$265,000	$397,500	$530,000	$596,250	$662,500
$1,400,000	$280,000	$420,000	$560,000	$630,000	$700,000
$1,475,000	$295,000	$442,500	$590,000	$663,750	$737,500

Compensation for purposes of the pension program is the highest average total cash compensation, including base salary and short-term bonus payments, for any consecutive five-year period prior to retirement. Covered compensation is disclosed under the "Salary" and "Bonus" columns of the Summary Compensation Table. Covered compensation and full years of service as of December 31, 1996 for the Company's Chief Executive Officer and the other named executive officers are as follows: J. A. Henderson, $1,126,433, 32 years; T. M. Solso, $700,973, 25 years; F. J. Loughrey, $463,558, 23 years; C. R. Cordaro, $398,052, 18 years; J. K. Edwards, $368,055, 24 years.

Change of Control Arrangements

In the event of a change of control of the Company, the Company will provide benefits to certain executives including the Chief Executive Officer and other executive officers named in the Summary Compensation Table on page 13. Each of the named executive officers would be entitled to three year's salary plus twelve quarterly bonus payments. The Company will also provide for the full vesting of certain insurance and retirement benefits and the continuation in effect for a three-year severance period of certain other employee benefits. In addition, the Company's retirement plans will allocate any actuarial surplus assets to fund increased pension benefits, stock options previously granted will become fully exercisable, and certain long-term incentive plan awards will be paid in cash. The value of supplemental and excess retirement annuity benefits will also be paid in cash. A change of control for these purposes is defined in each of the various plans and programs providing these benefits.

Compensation Committee Interlocks and Insider Participation

The members of the Company's Compensation Committee are Hanna H. Gray, Harold Brown, Donald S. Perkins, William D. Ruckelshaus and Franklin A. Thomas.

Member Harold Brown has a consulting arrangement with the Company pursuant to which he provides consulting services in connection with the Company's research and development activities and related technology issues. During 1996, the Company paid Dr. Brown $50,000 for these services. In addition, the Company has established a Science and Technology Advisory Council on which Dr. Brown serves as Chairman. The Council advises senior management and the Board of Directors on the direction and implication of developments in science, technology and environmental issues that may have applicability to the Company's current and future business goals and objectives. For his services on the Council, Dr. Brown is paid an annual retainer of $17,000, including $7,000 for serving as Chairman, and an additional fee of $3,000 for each day of meetings attended during the year.

Other Transactions and Agreements With Directors and Officers

As an employee of the Company, nominee James A. Henderson has deferred receipt of certain amounts of his salary and bonus pursuant to the Company's Deferred Compensation Plan. Amounts deferred have been included in the respective Summary Compensation Tables of the Company's proxy statements for the years in which earned. On March 26, 1996 the Company and Mr. Henderson agreed that he would forego receipt of $1,215,119 of his Deferred Compensation Plan account balance and future earnings thereon in exchange for entering into a split-dollar life insurance arrangement with the Company. Under the terms of the Deferred Compensation Plan, Mr. Henderson's unpaid balance would have continued to accrue interest and would have been payable beginning one year following the year of his retirement. Discounted at 7%, the present value cost to the Company of the Deferred Compensation Plan liability, assuming the Plan's expected rate of return on the unpaid balance, would have been $970,706. Under the split-dollar arrangement, the Company will pay premiums of $249,489 per year for ten years to a life insurance trust in connection with an insurance policy or policies on the lives of Mr. Henderson and his wife and will be refunded all of such premiums at the end of the 10th year, resulting in an equal present value cost to the Company of $970,706.

Prior to his retirement from the Company, nominee Henry B. Schacht also deferred receipt of certain amounts of compensation pursuant to the Deferred Compensation Plan, which amounts had been included in the Summary Compensation Tables. As of July 19, 1996, the total amounts deferred including accrued interest thereon payable by the Company to Mr. Schacht was $2,116,723.

On that date, the Company and Mr. Schacht agreed that he would forego receipt of his Deferred Compensation Plan account balance and future earnings thereon in exchange for a split-dollar life insurance arrangement similar to Mr. Henderson's. Mr. Schacht's unpaid balance would have continued to accrue interest and would have been payable in a lump sum in 2004. Discounted at 7%, the present value cost to the Company of the Deferred Compensation liability, under the same assumptions as for Mr. Henderson, would have been $1,767,127. Under the split-dollar arrangement, the Company will pay premiums of $454,184 per year for ten years in connection with an insurance policy or policies on the lives of Mr. Schacht and his wife and will be refunded all of such premiums at the end of the 10th year, resulting in an equal present value cost to the Company of $1,767,127.

Pursuant to the Company's 1986 Stock Option Plan, 1992 Stock Incentive Plan and its Key Employee Stock Investment Plan, certain officers have exercised options and purchased shares of Common Stock of the Company on an installment basis. The interest rate on these loans is the minimum annual rate permitted under the Internal Revenue Code without imputation of income. The following table shows, as to those executive officers and directors of the Company who were indebted to the Company in excess of $60,000 since January 1, 1996, the largest aggregate amount owed for such purchases and loans at any time since January 1, 1996, and the amount owed as of January 31, 1997:

	Largest Amount of Indebtedness	Amount of Indebtedness as of January 31, 1997
M. E. Chesnut	$ 80,750.00	$ 80,750.00
C. R. Cordaro	$220,000.00	$ 0
M. R. Gerstle	$ 70,162.50	$ 13,800.00
J. A. Henderson	$667,933.72	$667,933.72
M. D. Jones	$196,125.00	$ 0
K. M. Patel	$155,500.00	$155,500.00
B. S. Pitts	$ 84,250.00	$ 84,250.00
T. M. Solso	$182,500.00	$182,500.00

The Company has a policy of purchasing from employees of the Company shares of Common Stock of the Company that have been acquired under the Key Employee Stock Investment Plan, 1986 Stock Option Plan and 1992 Stock Incentive Plan. The purchase price for such shares is the closing price quoted on the New York Stock Exchange Composite Tape on the date of purchase. During 1996, three executive officers sold shares to the Company pursuant to this policy.

SELECTION OF INDEPENDENT PUBLIC ACCOUNTANTS

(Item 2)

The Board of Directors has voted to appoint Arthur Andersen LLP as the firm of independent public accountants to audit the accounts of the Company for the year 1997. Arthur Andersen LLP has acted as independent public accountants for the Company since 1952. Although the selection and appointment of independent public accountants is not required to be submitted to a vote of the shareholders, the Board of Directors has decided, as in the past, to ask the Company's shareholders to ratify the appointment. A representative of Arthur Andersen LLP will be present, will have the opportunity to make a statement and will be available to answer appropriate questions at the Annual Meeting of Shareholders.

The proposal to ratify the appointment of Arthur Andersen LLP as the firm of independent public accountants to audit the accounts of the Company for the year 1997 will be adopted if the number of votes cast in favor of ratification exceeds the number of votes cast against ratification. Votes cast against and abstentions on the Item will be counted as votes against the Item. Broker non-votes will not change the number of votes cast for or against the Item. If the shareholders do not ratify the selection of Arthur Andersen LLP, the selection of independent public accountants will be determined by the Audit Committee and the Board of Directors after careful consideration of all information submitted by shareholders.

The Board of Directors recommends that shareholders vote FOR this Proposal.

OTHER BUSINESS

The Board of Directors does not know of any business to be presented for action at the meeting other than that set forth in Items 1 and 2 of the Notice of Annual Meeting of Shareholders. However, if other business properly comes before the Meeting, the persons named in the enclosed proxy will vote the returned proxies as the Board of Directors recommends.

OTHER INFORMATION

1997 Shareholder Proposals

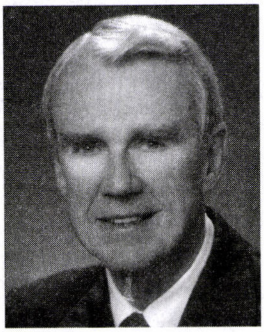
Proposals intended to be presented by shareholders of the Company at the 1998 Annual Meeting of Shareholders must be submitted to and received by the Secretary of the Company for inclusion in the Company's proxy statement and form of proxy for that Meeting not later than November 1, 1997.

Expenses of Solicitation

The cost of this proxy solicitation will be borne by the Company. Morrow & Co., 345 Hudson Street, New York, New York 10013, has been retained to assist in the solicitation of proxies and will receive a fee not to exceed $6,500 plus expenses. Proxies may also be solicited by directors, officers and employees of the Company at no additional cost. Banks, brokerage houses and other institutions, nominees or fiduciaries will be requested to forward the proxy materials to the beneficial owners of the Common Stock and will be reimbursed for their reasonable expenses incurred in forwarding such matters.

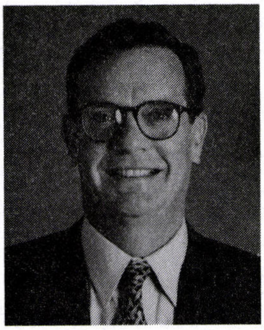
March 1, 1997

NOMINEES FOR BOARD OF DIRECTORS



JAMES A.
HENDERSON

Mr. Henderson was elected Chairman of the Board of the Company in 1995 after serving as Chief Executive Officer since 1994 and its President since 1977. He received a Bachelor of Arts degree from Princeton University in 1956, served in the U.S. Navy and received an M.B.A. from Harvard in 1963. He joined the Company in 1964 as Assistant to the Chairman and in 1965 was elected Vice President—Management Development. After serving as Vice President—Personnel and Vice President—Operations, Mr. Henderson was elected Executive Vice President in 1971. He was also Chief Operating Officer from 1975 to 1994. He serves as a Director of Inland Steel Industries, Inc., American Information Technologies Corporation, Landmark Communications, Inc., Ryerson Tull, Inc. and Rohm and Haas Company. He is also President of the Board of Trustees, The Culver Educational Foundation, a member of the Policy Committee of the Business Roundtable, and a member of The Business Council.



THEODORE M.
SOLSO

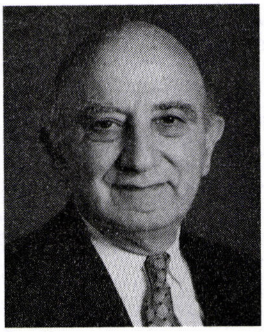
Mr. Solso was elected President and Chief Operating Officer of the Company in 1995 after serving as Executive Vice President—Operations since 1992 and Chief Operating Officer since 1994. From 1988 to 1992 he was Vice President and General Manager—Engine Business after serving in various other executive positions with the Company. Mr. Solso received a B.A. from DePauw University in 1969 and an M.B.A. degree from Harvard University in 1971. He is a Director of Amoco Corporation, Cyprus Amax Minerals Company and Irwin Financial Corporation, and is a member of the boards of Cummins Engine Foundation, Heritage Fund of Bartholomew County and Otter Creek Golf Course in Columbus, Indiana. He is also a member of the Board of Trustees, DePauw University and of the Dean's Advisory Boards of the Schools of Business of Hofstra University and Indiana University.

HAROLD BROWN

Dr. Brown is Counselor at the Center for Strategic and International Studies and a partner in the venture banking firm of Warburg, Pincus & Co. Dr. Brown received an A.B. in 1945, an A.M. in 1946 and a Ph.D. in Physics in 1949, all from Columbia University. From 1947 to 1952, he taught and held research positions at Columbia, the Stevens Institute of Technology and the University of California at Berkeley. He then was associated with Livermore Laboratory at the University of California, becoming Director in 1960. Dr. Brown was Director of Defense Research and Engineering from 1961 until 1965, when he was named Secretary of the Air Force, a position he held until 1969 when he became President of the California Institute of Technology. From January, 1977 until January, 1981, he served as Secretary of Defense. From 1981 until 1984, he was Distinguished Visiting Professor and from 1984 until June, 1992, Chairman of the Foreign Policy Institute at The Johns Hopkins University. Dr. Brown is a member of the National Academy of Sciences, the National Academy of Engineering and a Fellow of the American Physical Society. He is a Director of Alumax, Inc., Evergreen Holdings, Inc., International Business Machines Corporation, Mattel, Inc. and Philip Morris Companies, Inc. He is a Trustee of the California Institute of Technology and the Rand Corporation.

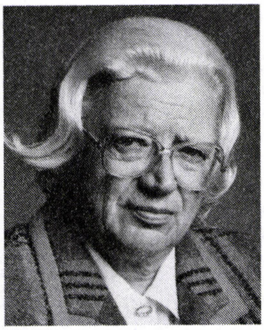
ROBERT J. DARNALL

Mr. Darnall is Chairman, President and Chief Executive Officer of Inland Steel Industries, Inc. Mr. Darnall is a graduate of DePauw University, B.A. in Mathematics in 1960; Columbia University, B.S. in Civil Engineering in 1962; and the University of Chicago, M.B.A. in 1973. He joined the Inland Steel Company, predecessor of Inland Steel Industries, in 1962. Mr. Darnall advanced through a number of positions at the company's Indiana Harbor Works steel plant, becoming General Manager in 1979. He was elected Vice President, Engineering and Corporate Planning, in 1981, and Executive Vice President in 1982, and he was also elected to Inland's Board of Directors in 1983. In 1984, he was elected President of Inland Steel Company and Chief Operating Officer of its Integrated Steel business segment. He became President and Chief Operating Officer of Inland Steel Industries, Inc. in 1986, and was named to his current position in 1992. He serves as a Director of Household International, Inc., Ryerson Tull, Inc. and the Federal Reserve Bank of Chicago, and as a Trustee or Director of DePauw University, The University of Chicago, the Glenwood School for Boys, and Junior Achievement of Chicago.



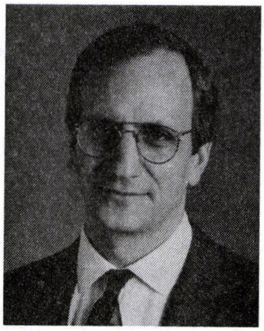
WALTER Y. ELISHA

Mr. Elisha is Chairman and Chief Executive Officer of Springs Industries, Inc. Mr. Elisha is a graduate of Wabash College and the Harvard Business School. He has been a Director of Springs Industries, Inc. since 1980 and served as President and Chief Operating Officer from 1980 to 1981. Mr. Elisha has served as Springs Industries, Inc.'s Chief Executive Officer since 1981 and has been Chairman of its Board since 1983. Mr. Elisha also serves on the Board of Directors for AT&T. Mr. Elisha is an honorary trustee of the Brookings Institution and a trustee of the Committee for Economic Development, a member of The Business Roundtable serving on its Policy Committee, the Business Council, the Council on Competitiveness, and is a member of the President's Advisory Committee for Trade Policy and Negotiations, and is past President of the American Textile Manufacturers Institute. Mr. Elisha is also a Trustee of Wabash College and has served as a member of the Board of Directors of the Associates of the Harvard Business School.



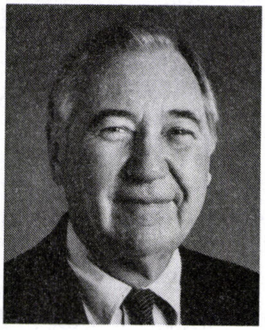
HANNA H. GRAY

Mrs. Gray is President Emeritus and Professor of History, University of Chicago. Mrs. Gray was graduated with a B.A. from Bryn Mawr College in 1950 and a Ph. D. from Harvard in 1957. During 1950–51 she was a Fulbright scholar at Oxford. She was an Instructor at Bryn Mawr in 1953–54 and was on the Harvard faculty from 1955–60. She became an Assistant Professor at the University of Chicago in 1961, was promoted to Associate Professor in 1964 and in 1972 was appointed Dean and Professor of History at Northwestern University. Mrs. Gray was Provost and Professor of History at Yale from 1974 to 1978 and was acting President from 1977–78. She served as President of the University of Chicago from 1978–1993. She became President Emeritus of the University of Chicago in 1993 and is now the Harry Pratt Judson Distinguished Service Professor of History. Mrs. Gray is a Fellow of the American Academy of Arts and Sciences and a Trustee of numerous educational institutions. She is also a Director of J.P. Morgan and Company and Morgan Guaranty Trust Company, Atlantic Richfield Company, and American Information Technologies Corporation.



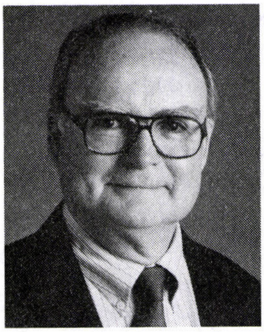
WILLIAM I. MILLER

Mr. Miller is Chairman of Irwin Financial Corporation. Mr. Miller received a B.A. from Yale University in 1978 and an M.B.A. degree from Stanford University in 1981. He was President of Irwin Management Company, a family investment management company, from 1984 to 1990. Since September, 1990, he has been Chairman of Irwin Financial Corporation, a publicly traded diversified financial services company, of which he has been a Director since 1985. Mr. Miller continues to serve as Chairman of the Board and a Director of Irwin Management Company and as Chairman of the Board of Tipton Lakes Company (a real estate development firm). Mr. Miller is a Director of Tennant Company (a manufacturer of industrial cleaning equipment), a Director of the New Perspective Fund, Inc. and a Trustee of the EuroPacific Growth Fund (both are mutual funds). Mr. Miller also is a Trustee of The Taft School, Watertown, CT, and Public Radio International, Minneapolis, MN.



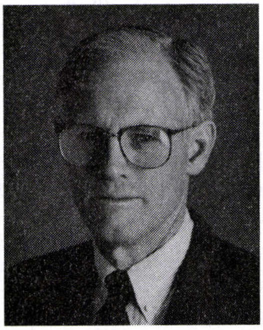
DONALD S. PERKINS

Mr. Perkins is the former Chairman of Jewel Companies, Inc. Mr. Perkins graduated from Yale University and the Harvard Business School. He served in the U.S. Merchant Marines in the mid 1940s and the Air Force in the early 1950s. Starting as a trainee with the then Jewel Tea Company in 1953, he was elected Vice President in 1960, Executive Vice President three years later, President in 1965 and Chairman and Chief Executive Officer in 1970. He retired from Jewel Companies, Inc. in 1983. Mr. Perkins also serves as a Director of the AON Corporation, Current Assets, Illinova and Illinois Power Company, Inland Steel Industries, Inc., LaSalle Street Fund, LaSalle U.S. Realty Income and Growth Fund Inc., Lucent Technologies Inc., The Putnam Funds, Ryerson Tull, Inc., Springs Industries, Inc. and Time Warner Incorporated. He is an Honorary trustee of The Brookings Institution, trustee and Vice Chairman of Northwestern University, trustee of the Hospital Research and Educational Trust, Honorary Chairman of The Illinois Coalition and Protector of the Thyssen-Bornemisza Continuity Trust. He is also a member of The Business Council, the Civic Committee of The Commercial Club of Chicago, a Director of the Golden Apple Foundation, Leadership for Quality Education and a member of the Spencer Stuart Advisory Board.



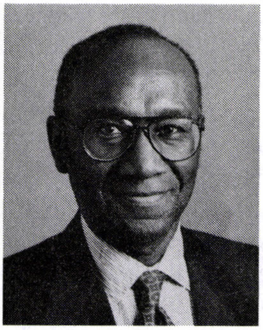
WILLIAM D.
RUCKELSHAUS

Mr. Ruckelshaus is currently a Principal in the Madrona Investment Group, L.L.C. and is Chairman of Browning-Ferris Industries. He was Chairman and Chief Executive Officer of Browning-Ferris Industries until 1996. Mr. Ruckelshaus received a B.A. from Princeton in 1957 and an LL. B. from Harvard in 1960 after serving in the U.S. Army. He was Deputy Attorney General and Chief Counsel in the Indiana Attorney General's Office from 1960–65. He was elected to the Indiana House of Representatives, where he served as Majority Leader in the 1967 session. Mr. Ruckelshaus first served in the Federal Government from January, 1969 to October, 1973, as Assistant Attorney General, as Administrator of the Environmental Protection Agency, Acting Director of the F.B.I. and Deputy Attorney General. He returned as Administrator of the Environmental Protection Agency from 1983 through January, 1985. He practiced law in Washington, D.C., from 1973 until joining Weyerhaeuser in 1976 as Senior Vice President. He was of counsel in the law firm of Perkins Coie, with offices in Seattle, Portland, Anchorage and Washington, D.C. from 1985 to 1988. Mr. Ruckelshaus is a Director of Monsanto, Inc., Nordstrom, Inc., Weyerhaeuser Company, and Gargoyles, Inc.



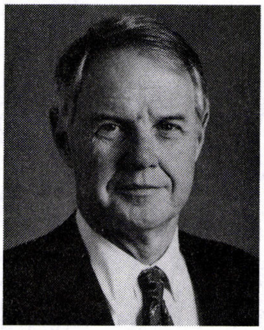
HENRY B.
SCHACHT

Mr. Schacht was named Chairman and Chief Executive Officer of Lucent Technologies, Inc. in 1995. Mr. Schacht served as Chairman of the Board of the Company from 1977 to 1995 and Chief Executive Officer from 1973 to 1994. He was President of the Company from 1969 to 1977. Mr. Schacht joined Cummins as Vice President—Finance in 1964, and served in various executive positions. He earned a B.S. in Industrial Administration from Yale in 1956 and, after serving in the U.S. Navy, an M.B.A. from Harvard in 1962. Mr. Schacht was with Irwin Management Company before joining Cummins. He is a Director of Lucent Technologies, Inc., Aluminum Company of America and The Chase Manhattan Corporation; a Trustee of The Yale Corporation, Committee for Economic Development and The Ford Foundation; and a member of the Council for Foreign Relations, Inc. and The Business Council.



FRANKLIN A. THOMAS

Mr. Thomas is currently a Consultant with the TFF Study Group and served as President of The Ford Foundation until 1996. Mr. Thomas received a B.A. from Columbia University in 1956 and an LL. B. in 1963. From 1956 to 1960, he was a navigator with the U.S. Air Force. Mr. Thomas served as attorney for the Federal Housing Finance Agency (1963–64), Assistant U.S. Attorney for the Southern District of New York (1964) and a Deputy Police Commissioner for New York City (1965–67). Mr. Thomas was President and Chief Executive Officer of the Bedford Stuyvesant Restoration Corporation from 1967 to 1977. He was an attorney and consultant engaged in private practice from 1977 to 1979. He is also a Director of Citicorp/Citibank, N.A., Alcoa, Lucent Technologies, Inc., and PepsiCo. and serves as a Trustee for The Ford Foundation.



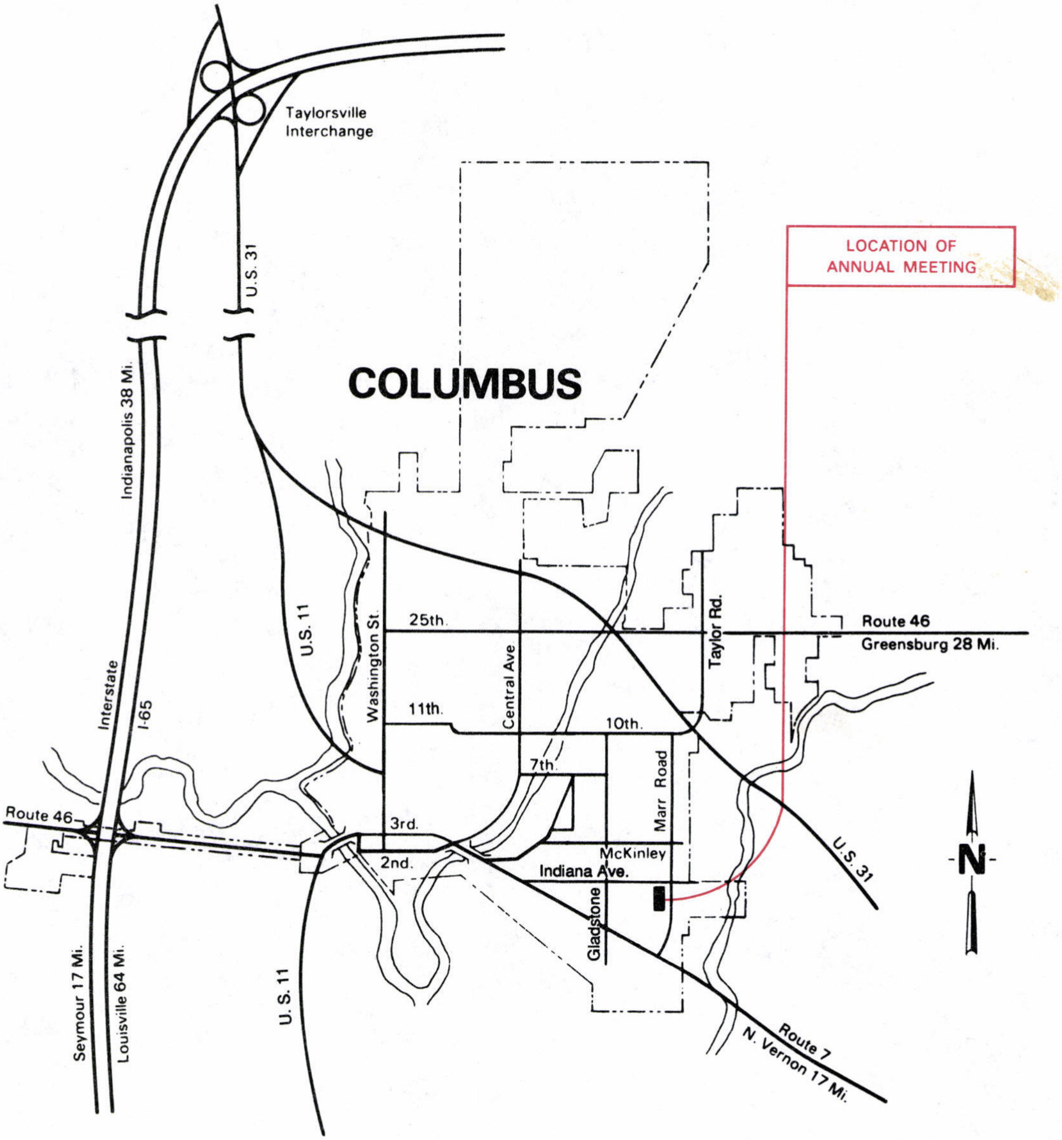
J. LAWRENCE WILSON

Mr. Wilson has been Chairman and Chief Executive Officer of Rohm and Haas Company since 1988. Mr. Wilson received a bachelor's degree in mechanical engineering from Vanderbilt University in 1958 and an M.B.A. from Harvard University in 1963. He served as an officer in the U.S. Navy from 1958 to 1961. Mr. Wilson joined Rohm and Haas Company in 1965 as an operations research analyst. He has since held positions as President of a medical products subsidiary, Director of the European region, Treasurer and Chief Financial Officer, Business Director for the Industrial Chemicals Group, Group Vice President in charge of the company's Administrative and Finance and Vice Chairman. Mr. Wilson has been a Director of Rohm and Haas Company since 1977. Mr. Wilson is a member of the board of Vanderbilt University, and the Vanguard Group of Investment Companies. He serves as Chairman of the Board of the Philadelphia High School Academies, Inc. and is Chairman of The Chemical Manufacturers Association.

CUMMINS ANNUAL SHAREHOLDER MEETING

April 1, 1997—10:30 A.M. (E.S.T.)

COLUMBUS EAST HIGH SCHOOL AUDITORIUM



Contents

Description of the Company's Business

Cummins Engine Company is the leading worldwide designer and manufacturer of diesel engines ranging from 76 to 6,000 horsepower. The company also produces natural gas engines, as well as engine components and subsystems.

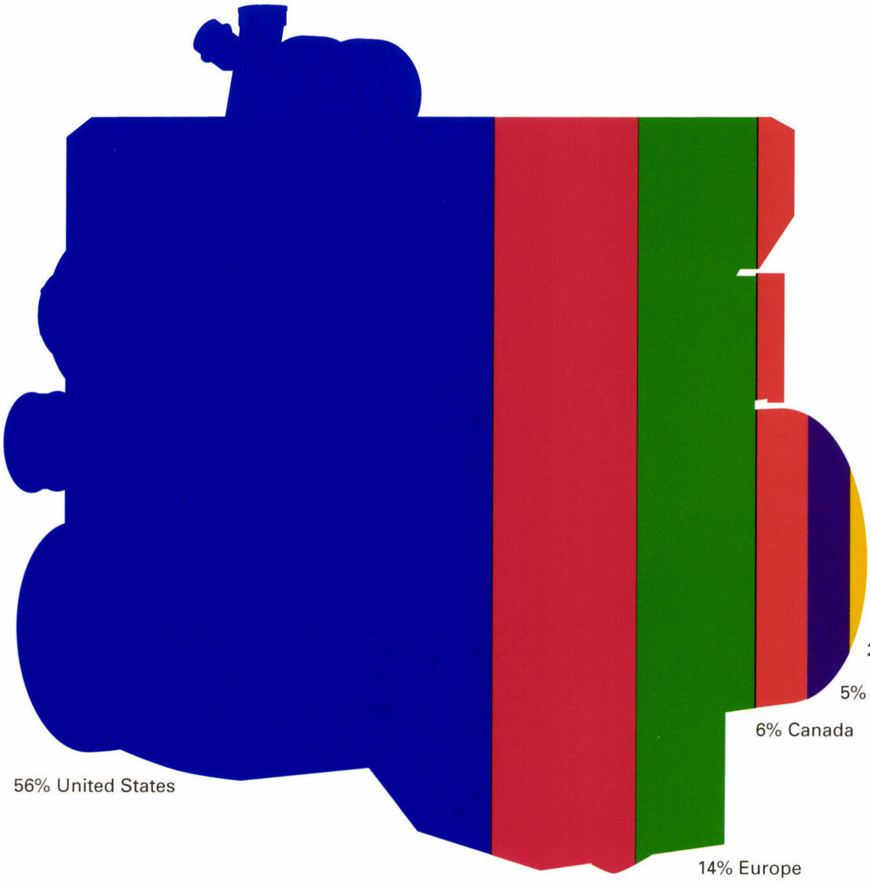
As the world's largest manufacturer of diesel engines above 200 horsepower, Cummins provides power and components for a wide variety of equipment in its key markets: automotive, power generation, industrial and filtration.

Cummins' 1996 sales were $5.3 billion and it employs 23,500 people worldwide.

Corporate Headquarters

Cummins Engine Company, Inc.
Columbus, Indiana 47202-3005

Net Sales by Marketing Territory



Highlights

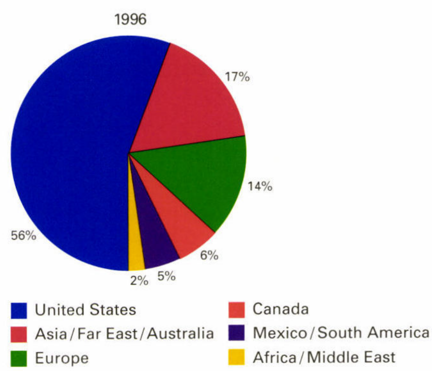
Cummins Engine Company, Inc.

Dollars in millions, except per share amounts	1996	1995
Summary of operations:		
Net sales	$5,257	$5,245
Earnings before taxes and restructuring charges	214	295
Net earnings	160	224
Per common share:		
Net earnings	$ 4.01	$ 5.52
Cash dividends	1.00	1.00
Common shareholders' investment	33.24	29.39
Common shares outstanding (millions)	39.4	40.2
Supplemental data:		
Property, plant and equipment expenditures	$ 304	$ 223
Number of employees	23,500	24,300
Engine shipments:		
Midrange	237,400	222,100
Heavy-duty	85,000	107,300
High-horsepower	9,900	9,500
Total shipments	332,300	338,900

To the Shareholders:

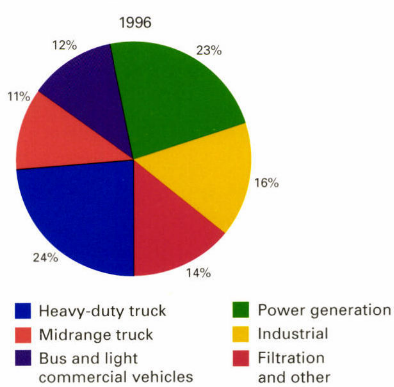
1996 was a year in which our commitment to a broader market and geographical revenue base began to pay off. Cummins reported record revenues of $5.3 billion, despite a 27-percent drop in engine shipments to the North American heavy-duty truck market, reflecting a continuing market slowdown which began in the second half of 1995. The decline in heavy-duty revenues was more than offset by increased shipments to other markets, particularly outside the U.S. In 1996, 44 percent of Cummins' business was in international markets, compared to 42 percent in 1995 and 35 percent a decade ago.

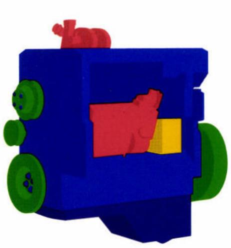
Sales by Marketing Territory



Our revenues reflected an improved balance by market in 1996.

Sales by Market





Financial Results
In spite of the drop in the North American heavy-duty market, Cummins was solidly profitable in 1996. Our operating earnings were $214 million, $81 million lower than 1995 earnings before a restructuring charge of $118 million, for three reasons.

First, in 1996 we moved into a period of heavy investment in our new product development program, described later. Our product development investment is expected to peak in 1997.

Second, as revenues from the North American heavy-duty truck market went down, they were replaced by increased revenues in power generation and industrial markets where margins are not at target levels and, therefore, do not fully offset lost margin in heavy-duty truck sales.

Third, in 1996 we continued to absorb additional costs as a result of restructuring actions announced in the fourth quarter of 1995. Our restructuring has included a reduction in people, exiting several smaller businesses, consolidation of North American parts centers, and the closure of four plants. As staffing is reduced and facilities are closed, we establish retraining and outplacement centers with the objective of placing each of our people affected.

Because we are shutting down these operations in a way which does not pose hardship for our customers, the full impact of the savings is not expected to be realized until late 1997 and 1998. The savings are intended to help improve margins in markets currently below target and to help offset increased costs of new product development in these peak years.

Five years of solid financial performance and attention to our balance sheet have placed us in a strong position, despite increased capital expenditures for new products. We closed 1996 with a debt-to-capital ratio of 24 percent. This conservative level was planned to assure that we would be able to afford capital investments for new products and equity investments in business alliances, regardless of economic conditions we might encounter. These investments are vital to meeting our customers' needs and pursuing new business opportunities that support our long-term target of 10 percent annual growth.

We completed a 2.5-million-share repurchase program during 1996 and acquired an additional 1.3 million shares in January 1997. The number of shares outstanding has been reduced by 3.8 million over a two-and-one-half-year period, and we have announced a program to repurchase an additional 1.7 million shares over the next several years.

Over time, we intend to continue to use our strong balance sheet to benefit our shareholders in four ways: investment in product development and market opportunities to continue our tradition of internally-generated growth, strategic acquisitions, a reduction in shares outstanding and dividends.

New Product Development Program
In 1996, we moved into the most intensive phase of investment in our comprehensive new product development program, which includes the improvement or replacement of each of our current engines and the development of two new fuel systems.

A vital part of these efforts is to build our capability in *Smart Power,* which is the use of electronic controls, software and information technology to enable our end-user customers to manage their businesses more efficiently. The computer on our engines enables us to bring far more value to the customer than just clean, reliable power.

Many of our product-development programs are being carried out with strategic partners. In addition to helping defray expense and capital costs, this approach improves our ability to understand customer needs around the world and to learn from other world-class technical organizations.

Here is a brief summary of our progress:

- The new QUANTUM system of high-horsepower engines for industrial, marine and power generation markets continues to be developed. The QSK 19 engine is already available to our industrial customers and is winning broad market acceptance. The engine utilizes a new fuel system developed jointly with Scania, a leading European integrated truck manufacturer in Sweden. The QST 30, developed with Komatsu, was introduced in 1996. The QSK 45 and QSK 60 will be introduced with increased power in 1998.

- The QUANTUM system features two new engine families as a result of our joint venture with Wartsila Diesel International. The QSZ family became available in limited quantities in 1996 in a diesel version for power generation customers. The QSW family will be introduced in both diesel and natural gas versions in power generation applications in 1997. These new engine families will extend our product range to 4.5 megawatts.

- Beginning in 1997, we will release the first of the next generation of midrange and heavy-duty engines incorporating electronic management and the latest technology in air handling, combustion and materials. These engines will provide automotive, industrial and power generation customers with compact, lightweight packages for medium- and heavy-duty applications from 130 to 600 horsepower and will be known as the *Interact System.*

- Included in the *Interact System* are the next-generation midrange B and C Series diesel engines featuring electronic controls and diagnostics, higher power ratings and improved response. Our partnership with Case Corporation has been vital to the successful development of these products, which we believe are truly world leaders.

- The *Interact System* also will include a new heavy-duty engine, to be announced in mid-1997, which is expected to set new standards for horsepower, weight and performance. It will be available in 1998.

- In 1996, we formed a joint venture with IVECO and New Holland to design and manufacture a new generation of one-litre-per-cylinder diesel engines with power outputs ranging from 50 to 275 horsepower.

We are very excited about the potential for these new products.

Customer Led Quality
We continue to pursue the five Customer Led Quality objectives which drive our business. They are:

First, we are committed to providing our customers with a comparative advantage in each of our markets worldwide, measured in product performance, economic value to the customer and all aspects of customer support.

This is the first and most important objective. Without *comparative advantage,* the other objectives are not possible over a sustained period of time.

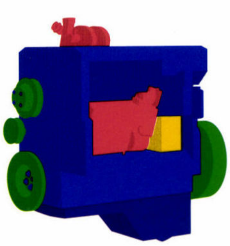
Comparative advantage is a customer term. The customer compares the value received from Cummins with that of other potential suppliers. Our goal is to gain and keep customers for life. For us to do so, customers must be able to count on us to meet all of their product and support needs over the long term. Our new product development program is designed to meet customers' future product needs in an environment of increasingly stringent emission requirements.

Customer support is equally vital. We maintain the most extensive distribution and service system for diesel engines in the world, with 33 distributors operating about 200 parts and service centers in North America and an additional 110 distributors in over 130 countries.

- In 1996, we consolidated North American parts centers in Memphis, Tennessee, the logistics hub for North America, enabling us to offer next-day delivery of parts throughout the United States. In addition to improving support for customers, this program, part of our restructuring, resulted in significant efficiency gains.
- In partnership with our distributors in the United States and United Kingdom, we also have introduced programs designed to provide sophisticated support 24 hours a day, 7 days a week to our customers to minimize their downtime and enable them to meet the needs of their customers.

We believe that improved customer support offers Cummins and its customers sustained *comparative advantage.*

The second objective is to achieve an average of 15-percent return on equity over the economic cycle. This return is required to sustain a comparative advantage in each market in the future and to afford investment in new business.



To focus our efforts on serving customers throughout the world more efficiently and effectively, we have reorganized the company into four worldwide Business Units, each headed by a seasoned Cummins manager with broad experience.

The Automotive Group includes trucks of all sizes, from pickups to heavy-duty, as well as buses and recreational vehicles. It is headed by Roberto Cordaro, who has been with Cummins for 18 years.

The Power Generation Group includes Cummins engines for power generation, Onan and Petbow generator sets and Newage alternators. Over 70 percent of its sales are in international markets. It is headed by Jack Edwards, who has been with Cummins for 24 years.

The Industrial Group serves customers in worldwide construction, agricultural, mining, marine, logging, rail and government markets. It is headed by Joe Loughrey, who has been with Cummins for 23 years.

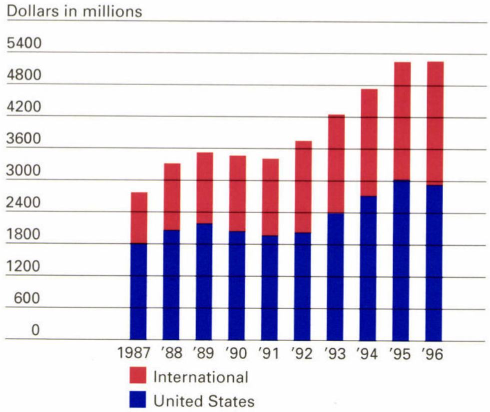
The Filtration Group includes Fleetguard, Inc., and its subsidiaries. Over 50 percent of its business is outside the United States. It is headed by Dave Jones, who has been with Cummins for 26 years.

We firmly believe this business unit structure will enable us to be more responsive to an increasingly diverse customer base, to pursue future growth opportunities, and to improve our financial performance through more clearly defined responsibility and accountability. Operating plans beginning in 1997 are the first formulated by business unit teams. Units will be measured on a comprehensive basis, including return on average net assets, responsiveness to customers and growth.

The third objective is to grow profitably at an average of 10 percent per year to provide a superior total return to our shareholders. This also will permit us to meet the objectives of all of our stakeholders.

For the past 20 years, Cummins has averaged revenue growth of 10 percent annually, ranking in the top 25 percent of industrial companies. Our goal is to continue that growth while improving profitability.

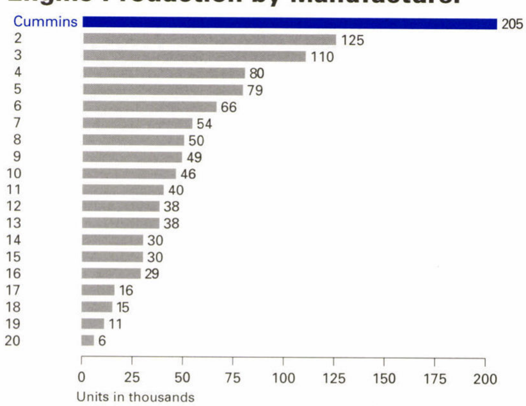
Net Sales



Much of our growth is expected to be outside the United States. Worldwide requirements for power continue to grow rapidly, both in size and variety of application. Diesel technology offers advantages to both developed and developing countries. It can generate electrical power. It provides power for construction equipment to build roads and other elements of the infrastructure and, of course, for transportation.

The expansion of our product line has coincided with the desire of many countries to improve the quality of life and employment opportunities for their citizens. They want to attract foreign investment, which means lowering trade barriers and competing with world leaders. In many cases, this means finding partners.

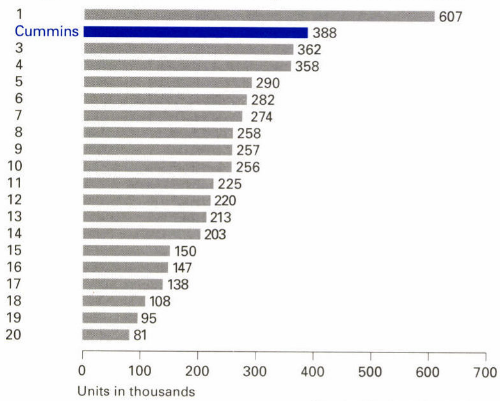
1995 Worldwide 200 HP+ Diesel Engine Production by Manufacturer



Source: Rhein & Associates

Cummins is the worldwide diesel engine technology leader and remains the largest producer of diesel engines above 200 horsepower and the second largest producer of diesel engines above 50 horsepower. We are, therefore, a logical partner for companies around the world. We bring our latest technology to our alliances, and we manufacture and purchase components locally. We select partners who are strong in their local markets; who know their customers, the local culture and business environment; and from whom we can learn.

1995 Worldwide 50 HP+ Diesel Engine Production by Manufacturer



Source: Rhein & Associates

Key business alliances have enabled us to take our current product line and extend our customer base geographically. Agreements reached in 1996 included:

- An expansion of our license agreement with Dongfeng Motors into a joint venture to produce C Series engines. Dongfeng is the largest truck producer in China and has produced B Series engines under license since 1987.
- A license agreement with PT Perkasa Heavyndo of Indonesia, a subsidiary of the Texmaco Group, one of the largest textile and engineering companies in Indonesia. Under the agreement, PT Perkasa will manufacture B Series engines for the Association of Southeast Asian Nations (ASEAN) automotive market.
- Wuxi Newage, a joint venture with Jiangsu Hai Xing Electrical Machinery Group (HXEM), to manufacture alternators in China.

Other key geographically-based alliances continued to make progress in 1996. They include:

- our joint venture with Kirloskar, which has provided power for the Indian market since 1962;

- our joint venture with Tata Engine and Locomotive Co. Ltd. (TELCO), the largest vehicle manufacturer in India, to provide B Series engines for India's truck market;

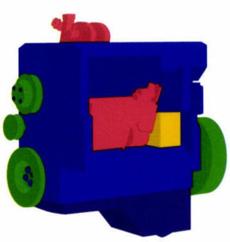
- our joint venture with China National Heavy-duty Truck Corporation for manufacture of the N14, K19, KV, L10 and M11 engines for high-horsepower and heavy-duty applications in China;

- our license agreement in Turkey with BMC Sanayi, which launched a new vehicle family in 1996 powered exclusively by our B and C Series engines.

The fourth objective is to demonstrate a commitment to help improve the communities in which we operate and to be responsible citizens of society.

We have long believed it is in our self interest to be concerned about the society in which we do business. For Cummins, responsible citizenship goes beyond legal requirements to doing what is right. This core belief continues to drive our work on emissions, our standards for conducting business, and our involvement in improving the communities where our people live and work.

Since the early 1970's, Cummins has contributed to the regulation process which sets standards to achieve a clean and healthy environment. We invest heavily in technology to control emissions, and we continue to build on our leadership position in the use of alternative fuels, particularly natural gas. By the end of 1996, Cummins' production of natural gas engines totaled more than 1,600. These engines are in use throughout the United States and Canada and have been introduced in the United Kingdom. In addition, we are seeing increased interest in natural gas engines in other markets worldwide.



One of our core operating principles is integrity. We want our customers, suppliers, partners and our own people in all the countries in which we do business to be able to believe us, trust us and count on us. To help our people understand what is expected of them, we developed a Cummins Code of Business Conduct, pulling together many of the ethics guidelines in place for many years. The code was adopted by the Board of Directors in 1995 and has been produced in eight languages. Training sessions for all our people are now being conducted.

Responsible citizenship also means helping improve local communities. Cummins people worldwide have responded, contributing money, time and energy to help others. A sampling of projects follows:

- In Memphis, Tennessee, Diesel ReCon employees have focused on education through support for an elementary school, a day-care center and the LeMoyne-Owen College. Employees donated to the college's capital campaign and worked to establish a Cummins Center for Faculty and Instructional Development at the college, funded by a donation from the Cummins Engine Foundation. Funding from the foundation also is supporting a multicultural learning partnership between LeMoyne-Owen and the Bartholomew Consolidated School Corp. in Columbus, Indiana.

- In San Luis Potosi, Mexico, building on the successful engagement of employees in the 1995 Special Olympics, a local Cummins Engine Foundation has been established. Projects include support of a school for the blind and work with the community to identify employment opportunities for future graduates.

- In Pune, India, our joint venture Kirloskar Cummins Ltd. (KCL) continues to expand its involvement on a number of fronts. The Cummins College of Engineering for Women has graduated 318 engineers in the last two years. In addition, 1,000 family members of KCL employees are enrolled in a network of 39 Family Circles designed to help them broaden their knowledge base, build skills and become more independent. To stimulate concern for the environment among students at an early age, KCL has conducted environmental workshops for teachers and established 17 nature clubs with over 1,100 student members.

The final Customer Led Quality objective is to attract, train, challenge and fully utilize outstanding and diverse people at all levels in order to achieve our objectives.

We believe the company that will be best prepared for the future is the one whose people feel responsibility to act quickly for the customer.

To achieve this objective we invest in our people so they have the capability and responsibility to anticipate customer requirements and meet them.

We were pleased when Cummins was singled out with a handful of other companies by President Clinton to participate in the President's Conference on Corporate Citizenship last year because of "exemplary efforts with our employees."

The involvement of each of our employees in improvement work for the customer continues to be an important objective.

Outlook

The world can change so rapidly that it is difficult to look ahead more than a few quarters with confidence. As this letter is written, however, economic conditions worldwide appear favorable, led by a U.S. economy which is growing at a modest pace with manageable inflationary pressures. It is the kind of environment in which manufacturing companies can invest in product development programs and improve continuously for their customers.

If this favorable environment is maintained, we expect to continue to invest aggressively to meet the future needs of customers throughout the world while also improving our financial results.

We thank you for your support and hope you will be able to join us at our Annual Shareholders' Meeting on April 1 in Columbus, Indiana.

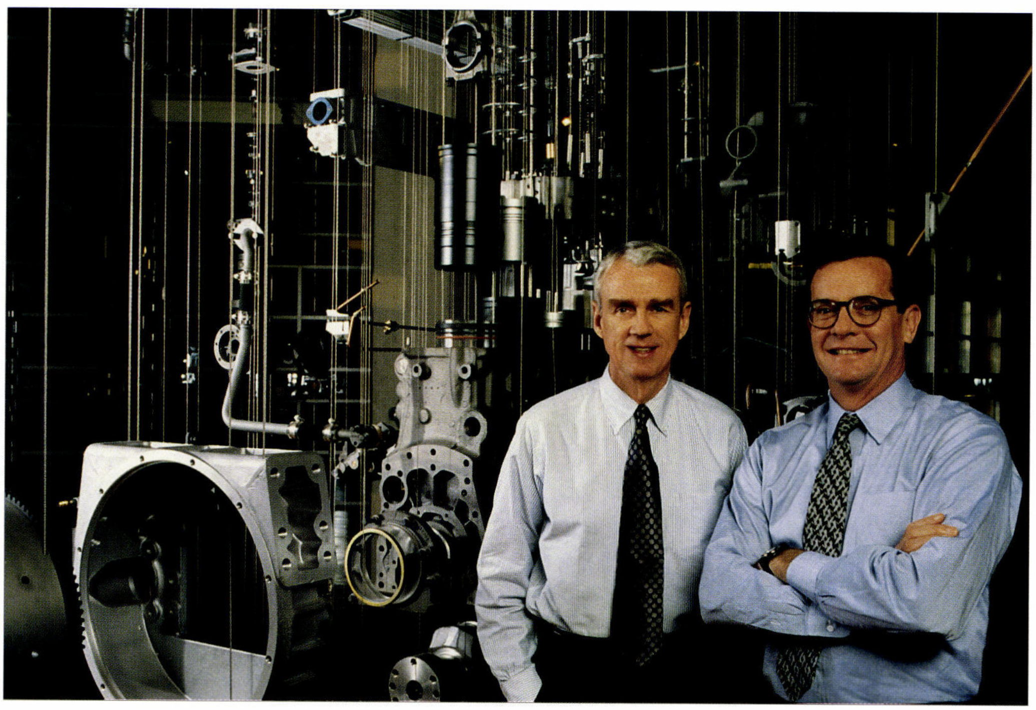
Jim Henderson

James A. Henderson
Chairman and Chief Executive Officer

Tim Solso

Theodore M. Solso
President and Chief Operating Officer

Cummins Engine Company, Inc.
March 1, 1997



Chairman Jim Henderson (left) and President Tim Solso stand in the Cummins headquarters lobby near the "exploded" NT, an engine whose continually evolving technology provides leading performance for Cummins' customers worldwide.

Irwin Miller

Irwin Miller has requested that he not be nominated for re-election to the Cummins Board of Directors at the 1997 annual meeting. Reluctantly, we have agreed to his request. He has served on the Cummins Board since 1935, except for a leave of absence during World War II to serve as an officer in the U.S. Navy aboard the aircraft carrier *U.S.S. Langley.* He led the Board as Chairman for 26 years.

Fortunately, Irwin has assured me that his active interest and involvement in the company and its people will continue as strong as ever. No one else has his depth of experience and understanding about this company. When he arrived as General Manager in 1934, the company had lost money for all of its 15 years. It shipped 301 engines that year, with sales revenues of $600,000 and 60 employees. He brought a strong interest in each person in the company, as well as management ability and a vision of the future to complement the entrepreneurial instincts and inventive skills of Clessie Cummins.

Irwin led the company until 1977, by which time revenues had reached $1.26 billion with profits of $67 million. He has continued to serve it ably as a director through difficult and prosperous times. At a particularly difficult moment in the company's history, long after his retirement as an officer, he reinvested in the company, along with his sister, based on his belief in its long-term prospects.

I had the good fortune to work directly for Irwin when I first came to Cummins. I soon learned he thinks first as a concerned citizen of the world and that gives him a perspective that is different from many businessmen. It is what has led him to be among the first to address the problems of injustice in society and to insist upon the importance of Cummins' being a responsible corporate citizen.

I also learned that while he is personally modest and soft-spoken, and has a warm sense of humor, he is an intense competitor with a burning desire to see Cummins as the very best at meeting every customer's needs and a firm belief that we can and will do so. He is proud of the accomplishments of each of us.

Irwin is the reason many of us came to Cummins. His example of personal and corporate responsibility and integrity, and his insistence on very high standards and doing what is right in all situations, while successfully competing with the world's best, has given us confidence it can be done.

I am pleased to report that his colleagues on the Board of Directors have named him Honorary Chairman and that he will continue to help, encourage and, yes, occasionally prod us in his new role.

– Jim

Jim Henderson

Cummins' Worldwide Business

Cummins reorganized its businesses last year into four market groups—automotive, power generation, industrial and filtration—in an effort to better focus its efforts on serving the customer.

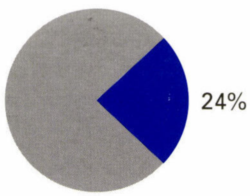
This new organization is enabling Cummins to be more responsive to its customers, accelerate pursuit of growth opportunities and achieve improved cost effectiveness.

The Automotive Group includes heavy-duty and midrange trucks, as well as bus and light commercial vehicles.

Net Sales

Automotive Group

Heavy-duty Truck



	1996	1995
($M)	$1,261	$1,550
(%)	24	30

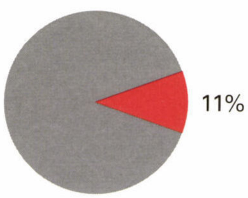
Markets and Products

Cummins' share of the North American heavy-duty truck market has held steady at 35 percent and the company has been the leader in this market for nearly a quarter century. Cummins' share of the heavy-duty truck market is growing outside the United States as well.

Growth will be realized by providing customers complete business solutions through products, information and support tailored to their needs and effective utilization of electronic controls and information management.

Products include a full range of 260- to 525-horsepower diesel engines with the popular L10, the advanced M11 Plus and the performance leader N14 Plus, as well as the natural gas L10.

Midrange Truck



	1996	1995
($M)	$587	$607
(%)	11	11

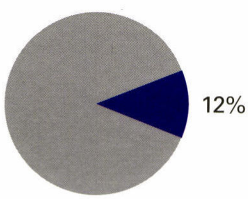
After only four years in the North American midrange diesel truck market, Cummins has a 31-percent share.

Cummins has a strong and growing share of this market in other countries, including Turkey, Mexico, Brazil, India and China.

Cummins is pursuing growth in this market by offering the most reliable, cost-effective power which meets the unique needs of midrange and intercity delivery truck customers.

Products include a full range of 120- to 300-horsepower with the proven B3.9, B5.9 and C8.3 engines.

Bus and Light Commercial Vehicles



	1996	1995
($M)	$599	$532
(%)	12	10

Cummins is the exclusive diesel power in the increasingly popular Dodge Ram pickup truck, which now enjoys a 38-percent share of the U.S. diesel three-quarter-ton and one-ton pickup market. The company also has a growing share of the various bus markets worldwide.

The growth of the pickup truck market and increasing acceptance of natural gas engines for buses are providing opportunities for Cummins.

Products include a full range of 130- to 300-horsepower B and C Series diesel engines as well as natural gas engines ranging from 150 to 300 horsepower.

The Power Generation Group includes Cummins engines, Onan and Petbow generator sets and Newage alternators.

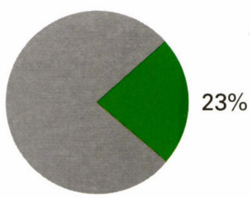
The Industrial Group includes construction, logging, mining, agricultural, marine, rail and government markets.

The Filtration Group, through the Fleetguard subsidiary, provides a broad line of filtration products.

Net Sales

Markets and Products

Power Generation Group



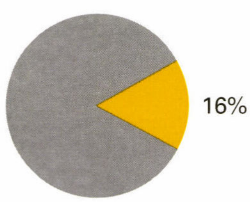
	1996	1995
($M)	$1,213	$1,092
(%)	23	21

Cummins has a growing share of a number of its key markets including recreational vehicles, as well as various overseas markets.

Growth is occurring in a number of areas, particularly in the Far East, which enjoyed an increase of 20 percent in the past year. This growth is the result of Cummins' ability to offer a comprehensive line of power generating equipment and its alliances with global partners, such as Wartsila of Finland and Wuxi of China.

Products include the complete line of equipment from 20 kilowatts to 4.5 megawatts including the QUANTUM range, Onan and Petbow generator sets and switches, and Newage alternators.

Industrial Group



	1996	1995
($M)	$863	$776
(%)	16	15

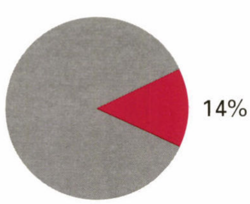
Cummins holds a strong share in a number of industrial markets.

The company enjoys a 14-percent share of the construction equipment market, more than 8 percent of the agricultural market and 9 percent of the worldwide marine market.

Growth is expected through a continued broadening of the product line, providing best-in-class customer support, offering customers the lowest operating cost and pursuing global markets.

Products include the entire engine line from 76 to 6,000 horsepower.

Filtration Group and Other



	1996	1995
($M)	$734	$688
(%)	14	13

Fleetguard has grown rapidly and is a major player in the $12 billion global filtration market. Its share of each of its markets has been increasing and currently is 15 percent of the worldwide heavy-duty engine market.

Continued growth is expected, particularly as Fleetguard continues to expand internationally and move into new filtration markets. Products include filters for heavy-duty engines, hydraulic fluids and air, as well as industrial and specialty filters.

Holset is Cummins' subsidiary which designs and produces turbochargers and other components for all of the company's markets. It continues to expand globally and to develop alliances with strategic partners.

"A strong focus on the customer, introduction of the *Interact System* of technologies, products and services, coupled with close relationships with equipment manufacturers who are leaders in their markets, position the Automotive Group for continued profitable growth."

C. Roberto Cordaro
Executive Vice President,
Group President–Automotive

Automotive Group

The Automotive Group reported another strong year in 1996 as a result of its product leadership in world markets. Cummins continues to make investments which should maintain its leadership position throughout the heavy- and medium-truck power range of 120 to 525 horsepower with its B, C, L, M and N Series products. The upcoming new platforms, termed the *Interact System* of engines, will grow the power coverage and provide dynamic power that is truly interactive with driver, business and environmental needs.

Market share gains are anticipated as major new product lines are launched over the next two years, as existing partnerships in Europe, China and India are developed, and as new alliances are formed.

The company's leadership in the North American heavy-duty market continued for the 24th consecutive year. The market did soften, as expected, down 23 percent from the 1995 record to 176,000 units. Cummins' products are performing better than ever and the focus on customer satisfaction and superior value is paying off as its share held steady at 35 percent.

In the North American distribution channel, Cummins implemented QUICKSERVE, a guaranteed diagnostics and service program to minimize downtime, providing customers with significant comparative advantage.

Shipments of midrange engines to the North American medium-duty diesel truck market remained very strong at 49,200 units. Market share and the overall market size were down from record 1995 levels. Cummins has a 31-percent share after only four years of participation in this market, and remains the diesel engine of choice at Ford, Freightliner and PACCAR.

In Europe, electronic "Euro2" engines were introduced and the M11 became the industry leader in its class for fuel economy. A joint venture was announced in 1996 with IVECO and New Holland to design and manufacture the next generation 4-, 5- and 6-litre engines based on the successful B Series.

In Mexico, the economy began to recover and Cummins' share of the heavy-duty market continued strong at 69 percent. Cummins' position in the Brazilian midrange market was solid with its two partners, Ford and Volkswagen, and the company participated in VW's innovative manufacturing plant as a partner supplier. In Turkey, Cummins' market-leading partner, BMC Sanayi, launched a new vehicle family, the Professional series, powered exclusively by the "Euro1 and 2" B and C Series. Sales were up 65 percent over 1995.

A license agreement was signed late last year with PT Perkasa Heavyndo of Indonesia to produce the B Series, primarily for the ASEAN automotive market. Chinese operations at Dongfeng were expanded from the license of the B Series to include a joint venture for the C Series. Cummins' business remains very strong in China with great potential through the Dongfeng agreements and direct imports. The automotive market in India continues to grow, and Cummins' joint venture with the truck market leader, Tata, is now producing the B Series.

Bus and light commercial vehicle markets continued their growth in 1996. These markets now comprise nearly 24 percent of the Automotive Group's sales. Cummins' first member of the *Interact System*—ISB275—is being introduced initially into the recreational vehicle market. Cummins sold 72,300 engines for the Dodge Ram, which enjoyed increased levels of customer acceptance. Demand for alternate-fueled products for transit bus markets continues. Natural gas comprises one-third of Cummins' transit bus volume. In the U.K. bus market, Cummins' share remains strong due to its successful partnership with Dennis S.V. Cummins continues to develop this market worldwide, particularly in Mexico and Asia. Sales to the school bus market continued strong during 1996.

The low operating cost of the B Series Euro2 engine makes it a popular choice for vehicles across Europe, such as this DAF Leyland urban delivery truck.


SECURICOR
OMEGA
LOGISTICS
SECURICOR
OMEGA
LOGISTICS
45
LEYLAND
DAF
P57 KHJ
B 06
DT 05

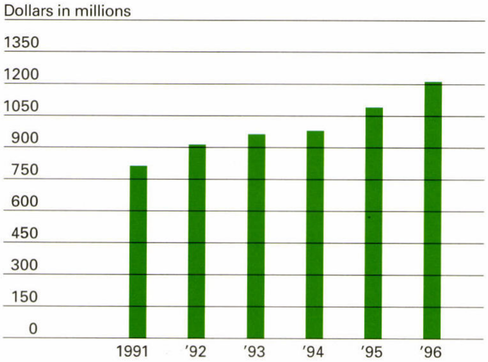
"The opportunity for growth in the Power Generation Group is high and Cummins, with its comprehensive product line and global presence, is positioning itself to capture that potential."

John K. Edwards
Executive Vice President,
Group President–Power Generation and International

Power Generation Group

1996 was an exciting year of progress for Cummins' Power Generation business. Sales of power generation products—Cummins engines, Onan and Petbow generator sets and Newage alternators—grew to $1.2 billion. Sales growth exceeding 20 percent in the Far East more than offset a weaker North American standby generator set market. Cummins is beginning to realize the benefits of its continuing efforts to better serve the rapidly expanding Far East markets.

Power Generation Sales



The creation of Power Generation as a separate business unit was a key strategic initiative. Power Generation began as a distribution channel for Cummins engines, but the goal now is to become the leading global power systems supplier. The restructuring transformed Power Generation from Cummins' second largest market to an autonomous business, intensely focused on providing comparative advantage. The group has divested its ancillary operations and is aligning its core competencies into a unified value-added power supplier.

Together with its partners—Wartsila, Kirloskar and Komatsu—the Power Generation Group will soon offer a comprehensive product line from 20 kilowatts to 4.5 megawatts. Over the next few years, it will introduce new products across this range with increased power density, natural gas capability and state-of-the-art electronic controls. These new products will solidify its reputation for advanced technology, reliability and durability.

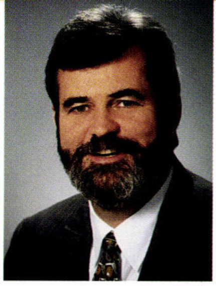
Cummins' joint venture with Wartsila to produce high-horsepower engines is proceeding on schedule. The QSZ family of products was introduced this year with initial deliveries in Europe and Asia. The QSW family will be introduced in 1997. These products will provide clear life-cycle cost advantages to the rapidly expanding prime power markets above 1 megawatt. Over the past decade, the worldwide power generation market has been growing at almost 6 percent annually, but the segment above 1 megawatt has been growing at 25 to 30 percent annually. To maximize this growth potential, an international cross-functional introduction team has been formed to focus on executing a successful worldwide launch and rapidly attaining market share.

The mobile business group of Onan Corp., a Cummins subsidiary, provides generator sets and gasoline engines to a variety of markets. In 1996, the market for recreational vehicle generators was particularly strong and Onan continues to enjoy a high market share. Onan also introduced the new "Quiet Diesel," a variable speed generator set. This product offers reduced noise and less vibration, and exemplifies Onan's commanding leadership in product technology.

Newage, another Cummins subsidiary, is the world's leading manufacturer of alternators in its product range, and its global presence continues to expand. During 1996, plans were initiated to triple manufacturing capacity at its existing joint venture in India, and a new joint venture agreement was completed in China. Production of Newage alternators in China will commence in the first half of 1997.

A bank of eight Cummins/Onan generator sets recently installed at Atlanta's Hartsfield Airport provide its new International Concourse power during periods of high demand and also standby power.

"Cummins' Industrial Group continues to experience significant growth due to its broad product offering, its partnerships with leading global manufacturers and a strong distribution system worldwide."

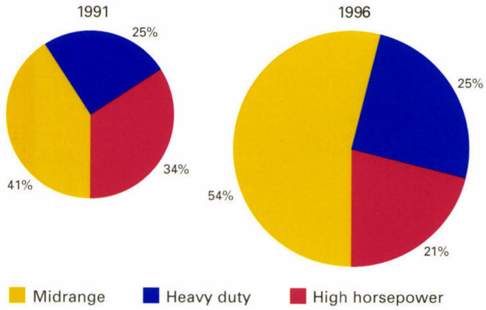


F. Joseph Loughrey
Executive Vice President,
Group President–Industrial

Industrial Group
A strong global economy in 1996, combined with heightened acceptance of Cummins-powered products, generated an 11 percent increase in engine and parts sales and a record year for the Industrial Group.

Sales of 77,800 engines to the construction, agricultural, mining, marine and rail markets exceeded the 1995 record by 9 percent. Continued growth was achieved in North America, the South Pacific, and South and Central America, as well as in construction, agricultural and mining markets.

Industrial Sales by Product



Notable growth also was recorded in Europe with new account acquisitions and in China's emerging construction segment.

During the first full year of U.S. emissions standards for industrial engines, Cummins' comprehensive line-up of engines ranging from 76 to 6,000 horsepower continued to make strong advances. Leading the way were the 26 new midrange engine ratings for these markets as well as new products with electronics for heavy-duty and high-horsepower applications.

The QUANTUM series of engines, initiated with the launch of the QSK19 in 1995, was enhanced in late 1996 with announcement to the global mining market of two new products, the QSK45 and QSK60. The Cummins K2000E 50-litre engine continues to set new standards of performance in world mining markets with competitive operating costs and superior levels of reliability, durability and life-to-overhaul compared to the competition.

As equipment owners demand more sophisticated equipment, electronic systems controls have become a critical factor in maximizing performance and productivity. Cummins' development of electronic engine control technology and information systems offers a unique opportunity to assist equipment manufacturers in the design and development of customized electronic systems and controls. Cummins' close working relationships with partners like Case and Komatsu offer end users a unique combination of talent and technologies to better meet their needs.

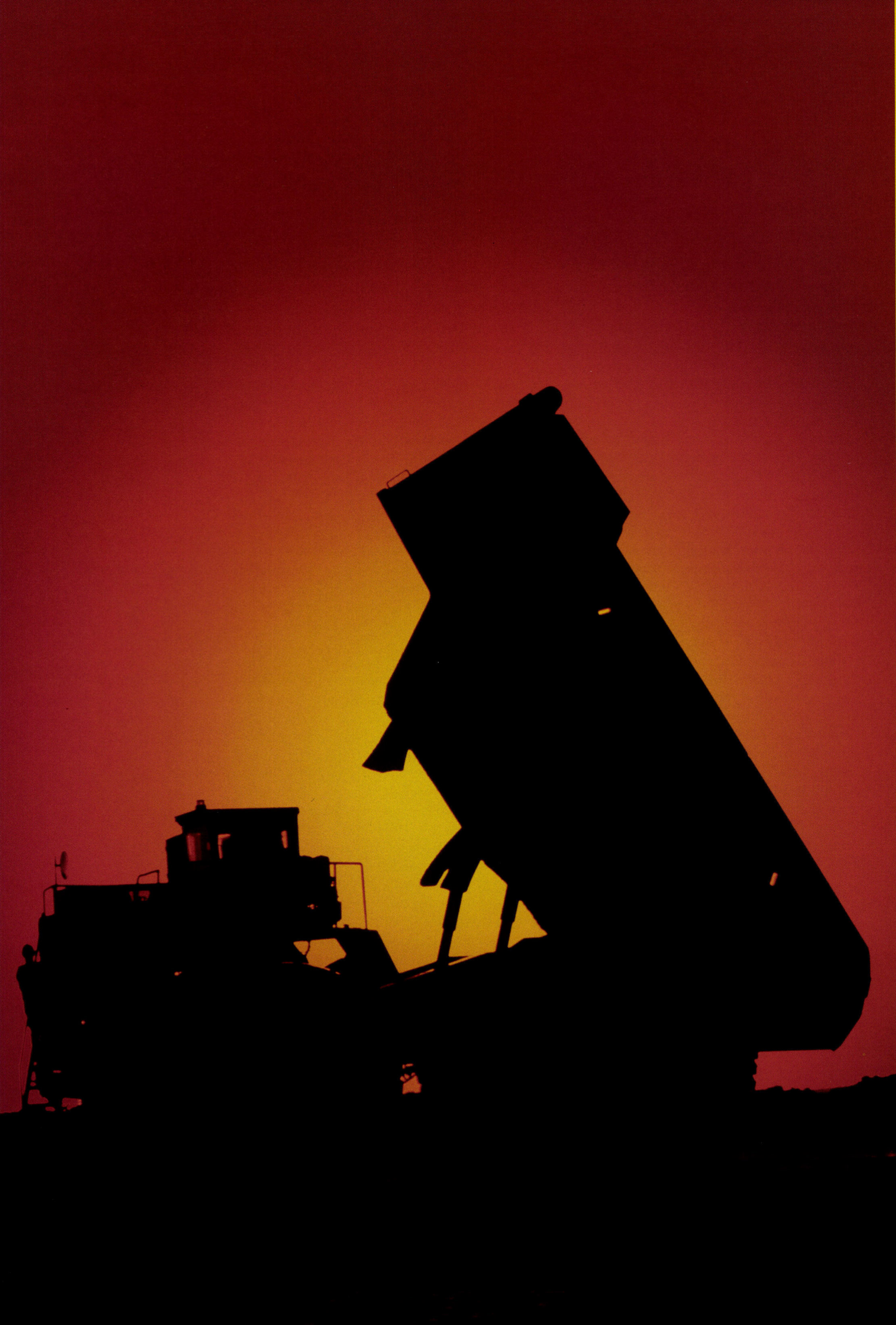
Marine shipments grew approximately 30 percent in 1996 over the 1995 level, and were nearly 70 percent higher than 1993. Sales growth in the recreational market resulted from continued strong customer acceptance of several new models in the Diamond Performance Series.

Cummins Marine continued to be the number one volume supplier of diesel engines to the North American recreational marine market.

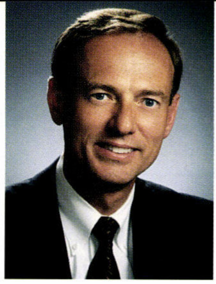
Commercial marine sales grew dramatically as a result of strong worldwide acceptance of the K/KV engine series, which was uprated in 1995, and addition of several new KV models in 1996.

Cummins' joint venture with Wartsila to develop and manufacture the QSW/Z product will greatly expand marine product offerings to 6,000 horsepower, significantly above the 1,800 horsepower available today.

The QUANTUM Series QSK45 and QSK60 engines, announced late last year to the global mining market, will provide reliable power for rear dump trucks and other equipment.



"The Filtration business has grown 15 percent annually for more than two decades, and growth is expected to continue as exciting new services and technically-advanced products are introduced to customers around the world."



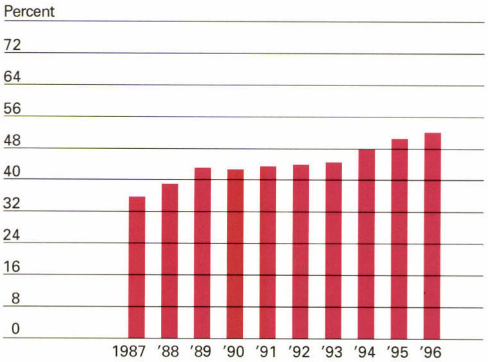
M. David Jones
Vice President–
Filtration Group
and President–
Fleetguard, Inc.

Filtration Group

Cummins' success in filtration has been built on a foundation of working closely with customers—equipment manufacturers, distribution partners, and end users—to provide innovative solutions to their most pressing filtration needs. Engineers apply new filtration technology to develop products that maximize equipment up-time and minimize total cost of operation. Customer support teams continuously look for new ways to provide value-added services. And the company's broad international scope provides the capability to support customers around the world.

Fleetguard, Cummins' filtration company, initially focused on heavy-duty engine filtration for Cummins. However, sales for products made by customers other than Cummins now constitute two-thirds of Fleetguard's total sales. While there are a few larger filtration companies around the world, a significant portion of their sales come from either passenger car or non-vehicle markets. Fleetguard is now the leading heavy-duty engine filtration company in the world.

Fleetguard International Sales as a Percent of Total



Fleetguard once again performed well in 1996. U.S. and international markets were strong despite a slowdown in the European and Brazilian economies. Over 50 percent of 1996 sales were outside the United States.

Fleetguard's international expansion continued on schedule with the opening of a state-of-the-art manufacturing facility in Shanghai, a joint venture with Shenlong Auto Accessories Corporation. It is the largest, most modern filter plant in China today. Fleetguard India continued to grow with the addition of new customers and products. A new distribution center in South Africa performed well in its first year.

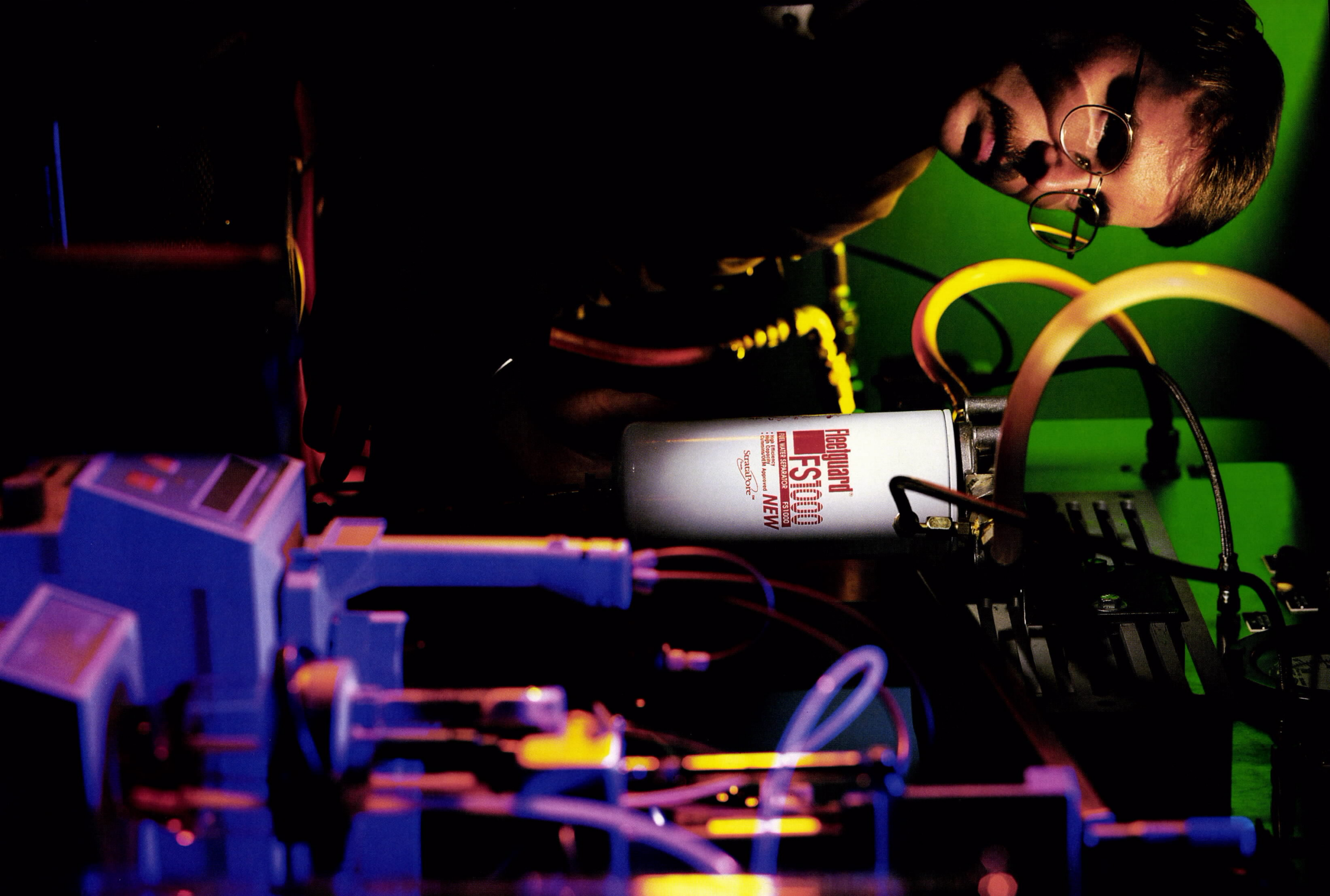
Fleetguard's subsidiary companies—Kuss Corporation (specialty filtration), Separation Technologies (industrial hydraulic filtration) and Lubricon (fluid analysis laboratories) —continued to expand their businesses with aggressive growth strategies in both domestic and international markets.

In 1996, Fleetguard's new StrataPore media won the prestigious American Filtration & Separations Society Award for Innovative New Technology. This new media offers finer and more precise filtration, greater capacity for longer life applications and improved environmental benefits. The new extended service ES System program for antifreeze and diesel coolant products was developed to address the increasing need for longer service intervals and lower maintenance costs.

Multilingual capabilities were added to the Customer Assistance Centers throughout the organization, and Fleetguard introduced its web site with 24-hour electronic coverage and same day rapid response to all customer inquiries returned in the customer's native language.

Commitment to quality has long been an operating principle at Fleetguard, which has received quality certifications from Navistar, Case, John Deere, Ford, DAF and Scania as well as ISO 9000 certification at six facilities around the world and QS 9000 in two U.S. plants.

The StrataPore media, first used to protect electronic fuel systems, has undergone strenuous testing and is now being expanded to all applications where filtration of fine particles and long life are critical.


Fleetguard
FS1000
FUEL WATER SEPARATOR FS1000
NEW
StrataPore

Management's Discussion and Analysis of Results of Operations and Financial Condition

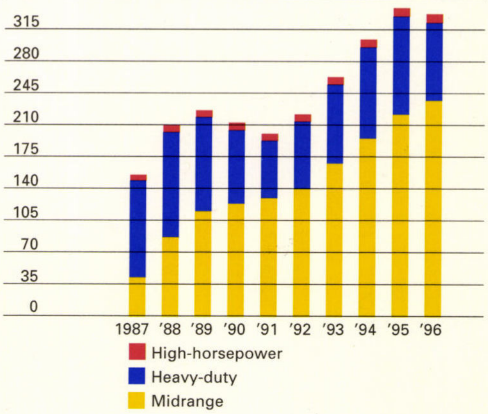
Overview

In 1996, the company had record sales of $5.3 billion, $12 million higher than 1995 and 11 percent higher than 1994. This record performance was achieved despite a 27-percent reduction in engine shipments to the North American heavy-duty truck market as a result of the slowdown in that market.

The company shipped 332,300 engines in 1996, compared to 338,900 in 1995 and 304,300 in 1994 as follows:

Engine shipments	1996	1995	1994
Midrange	237,400	222,100	195,600
Heavy-duty	85,000	107,300	99,900
High-horsepower	9,900	9,500	8,800
Total shipments	332,300	338,900	304,300

Engine Shipments



Net earnings were $160 million, or $4.01 per share, in 1996. Net earnings were $224 million, or $5.52 per share, in 1995 and $253 million, or $6.11 per share, in 1994.

Results of Operations

The percentage relationship between net sales and other elements of the company's *Consolidated Statement of Earnings* for each of the last three years was:

Percent of net sales	1996	1995	1994
Net sales	100.0	100.0	100.0
Cost of goods sold	77.5	75.8	75.0
Gross profit	22.5	24.2	25.0
Selling and administrative expenses	13.8	13.2	13.5
Research and engineering expenses	4.8	5.0	5.0
Net expense (income) of joint ventures and alliances	–	–	(.1)
Interest expense	.3	.2	.4
Other (income) expense, net	(.5)	.2	–
Restructuring charges	–	2.2	–
Earnings before income taxes	4.1	3.4	6.2
Provision (credit) for income taxes	1.1	(.9)	.9
Net earnings	3.0	4.3	5.3

Sales by Market

The company's sales for each of its key markets during the last three years were:

Dollars in millions	1996	1995	1994
Automotive:			
Heavy-duty truck	$1,261	$1,550	$1,483
Midrange truck	587	607	500
Bus and light commercial vehicles	599	532	469
Power generation	1,213	1,092	980
Industrial	863	776	686
Filtration and other	734	688	619
Net sales	$5,257	$5,245	$4,737

Automotive

Sales to the heavy-duty truck market were almost 20 percent lower than in 1995 and 15 percent lower than 1994. The lower level of sales in 1996 was due to a decline in demand for the North American heavy-duty truck market. In 1996, factory retail sales of heavy-duty trucks in North America were 23 percent lower than the previous year's level. This lower market size resulted in the company's lower level of engine shipments in North America. Cummins continued to lead this market, however, with a market share of 35 percent in 1996. The company's market share was 35 percent in 1995 and 34 percent in 1994. In the fourth quarter of 1996, the North American market was stronger, indicating it may be reaching the bottom of the current down cycle.

International engine shipments for heavy-duty trucks were 14 percent lower than in 1995 and 49 percent below 1994. The decline in engine shipments in 1996 was due primarily to lower demand in European markets. However, in the fourth quarter, certain international markets showed signs of improvement, particularly in Mexico.

Sales of engines for the midrange truck market in 1996 were 3 percent lower than 1995 and 17 percent higher than in 1994. Overall, there was a decrease in demand for medium-duty trucks in North America during 1996, which caused a 3-percent decline in the company's engine shipments in North America. Midrange engines for international markets were 7 percent higher than in 1995 and 16 percent higher than 1994, primarily in Brazil and Mexico.

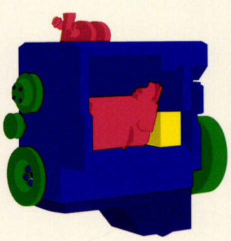
In the bus and light commercial vehicles market, sales were 13 percent higher than 1995 and 28 percent higher than 1994. The increase in 1996 was due to record demand for the company's midrange engines in the Dodge Ram pickup truck, which was 13 percent above 1995.

Power Generation

Sales of power generation represented 23 percent of the company's net sales in 1996. Record sales of $1.2 billion in 1996 were $121 million higher, an 11-percent increase compared to 1995, and $233 million, or 23 percent higher, than 1994. The increase in sales in 1996 was due to a 20-percent increase in international markets reflecting strong demand in China, India and Southeast Asia.

Industrial

Record sales of $863 million to industrial markets were 11 percent higher than 1995 and 26 percent higher than 1994. The increase in sales in 1996 was primarily due to strong demand for construction applications in both North American and international markets. In addition, there was strong demand for the company's engines in marine applications worldwide in 1996, almost 30 percent above 1995 and 55 percent higher than 1994.



Filtration and Other

Sales of $734 million in 1996 for filtration and other products were 7 percent higher than 1995 and 19 percent higher than 1994. The increase in sales during 1996 was due primarily to strong demand in international markets.

Gross Profit

The company's gross profit percentage was 22.5 percent of net sales in 1996, compared to 24.2 percent in 1995 and 25.0 percent in 1994.

The company's gross profit was affected by several factors in 1996, the most significant of which was the decline in heavy-duty engine production that resulted in lower fixed cost absorption. Gross profit also was affected by the softer market for midrange truck engines, higher sales of lower margin power generation products, and costs associated with the restructuring actions and new product introductions. While restructuring activities are proceeding, as reflected by gains on disposals of certain operations in "other income," expenses associated with implementation of certain of these actions adversely affected gross profit. As disclosed in *Note 13* to the *Consolidated Financial Statements,* the company has entered into commodity swap contracts that have the effect of fixing the cost of certain material purchases.

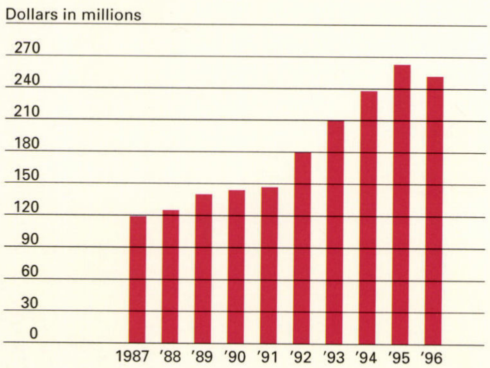
The cost of product coverage programs was 2.7 percent of net sales in 1996, compared to 2.4 percent of net sales in 1995 and 2.3 percent of net sales in 1994.

Operating Expenses

Selling and administrative expenses were $725 million (13.8 percent of net sales) in 1996, compared to $692 million (13.2 percent of net sales) in 1995 and $641 million (13.5 percent of net sales) in 1994. In 1996, expenditures associated with the restructuring actions, marketing programs and new product launches offset the decrease in salaries and wages as a result of headcount reductions.

Research and engineering expenses of $252 million in 1996 were 4.8 percent of net sales, compared to $263 million in 1995 and $238 million in 1994, both of which were 5.0 percent of net sales.

Research and Engineering Expenses



In 1996, the company's share of start-up losses of its joint venture with Wartsila were offset by earnings from Kirloskar Cummins, due to strong demand in its markets.

Other Income and Expense
Interest expense of $18 million was $5 million higher than 1995 due to the higher level of borrowings. In 1996, other income of $24 million was due to interest income and gains on the disposal of certain operations and businesses associated with the restructuring actions.

Restructuring Charges
As disclosed in *Note 2* to the *Consolidated Financial Statements,* results of operations in 1995 included restructuring charges of $118 million ($77 million after taxes) for costs to consolidate operations and reduce the worldwide work force. Approximately 2,300 employees have separated from the company as a result of the actions.

Provision for Income Taxes
The company's income tax provision in 1996 was $54 million, an effective tax rate of 25 percent, reflecting tax breaks on export sales and $6 million for reinstatement of the research tax credit in the second half of 1996. Tax provisions of the Small Business Job Protection Act that was signed into law in August 1996 included reinstatement of this credit for an 11-month period, beginning July 1, 1996.

The company reduced its valuation allowance for tax benefit carryforwards $68 million in 1995 and $32 million in 1994. The tax provision for 1995 also included a credit of $35 million for additional tax benefits related to the amendment of prior years' returns.

Cash Flow and Financial Condition
Key elements of the *Consolidated Statement of Cash Flows* were:

Dollars in millions	1996	1995	1994
Net cash provided by operating activities	$ 193	$ 406	$ 376
Net cash used in investing activities	(259)	(373)	(261)
Net cash (used in) provided by operating and investing activities	(66)	33	115
Net cash provided from (used for) financing activities	110	(121)	(50)
Effect of exchange rate changes on cash	4	1	5
Net change in cash and cash equivalents	$ 48	$ (87)	$ 70

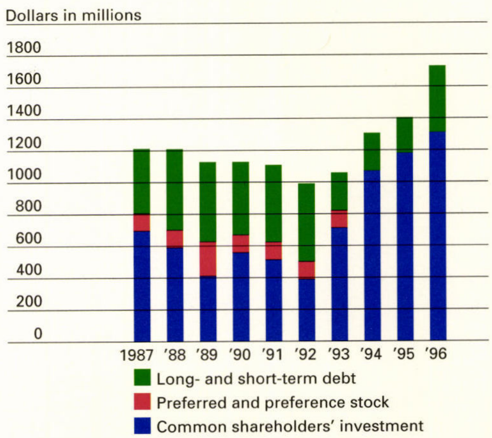
During 1996, net cash used in operating and investing activities was $66 million. The lower level of net cash provided by operating activities was due to net cash requirements for the restructuring activities, including increased inventories at certain locations, and an increase in accounts receivable. In the second quarter of 1996, an agreement for the sale of up to $110 million of accounts receivable was not renewed by the company, which resulted in the increase in receivables. Capital expenditures during 1996 were $304 million, compared to $223 million in 1995 and $238 million in 1994. The increased level of expenditures in 1996 was related to continued investments for new products. The company expects a significant increase in these expenditures in 1997, some of which may be funded externally.

Investments in joint ventures and alliances of $5 million reflected the net effect of repayment of temporary advances to Consolidated Diesel at the end of 1995 and capital contributions of $50 million during 1996, primarily to the company's joint venture with Wartsila. The company expects to continue to make investments in certain of its joint ventures during 1997.

Net cash provided from financing activities was $110 million in 1996. As disclosed in *Note 5* to the *Consolidated Financial Statements,* the company issued commercial paper in 1996 to replace a financing arrangement whereby receivables were previously sold without recourse. A subsidiary of the company also issued notes in 1996, which resulted in net proceeds of $100 million. In February 1997, the company issued $120 million in debentures under its shelf registration statement.

As disclosed in *Note 9* to the *Consolidated Financial Statements,* the company completed a program begun in 1994 to repurchase 2.5 million shares of its common stock. In January 1997, the company repurchased 1.3 million shares of its common stock from Ford Motor Company and was authorized by the Board of Directors to repurchase an additional 1.7 million shares in the open market. In January 1997, the company also announced that it will issue 3.75 million shares of its common stock to an employee benefits trust.

Total Capitalization

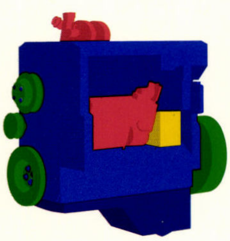


Forward-looking Statements

This Management's Discussion and Analysis of Results of Operations and Financial Condition, and other sections of this annual report, contain forward-looking statements that are based on current expectations, estimates and projections about the industries in which Cummins operates, management's beliefs and assumptions made by management. Words, such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates," variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions ("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. Cummins undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

Future Factors include increasing price and product competition by foreign and domestic competitors, including new entrants; rapid technological developments and changes; the ability to continue to introduce competitive new products on a timely, cost effective basis; the mix of products; the achievement of lower costs and expenses; domestic and foreign governmental and public policy changes, including environmental regulations; protection and validity of patent and other intellectual property rights; reliance on large customers; technological, implementation and cost/financial risks in increasing use of large, multi-year contracts; the cyclical nature of Cummins' business; the outcome of pending and future litigation and governmental proceedings and continued availability of financing, financial instruments and financial resources in the amounts, at the times and on the terms required to support Cummins' future business.

These are representative of the Future Factors that could affect the outcome of the forward-looking statements. In addition, such statements could be affected by general industry and market conditions and growth rates, general domestic and international economic conditions, including interest rate and currency exchange rate fluctuations, and other Future Factors.



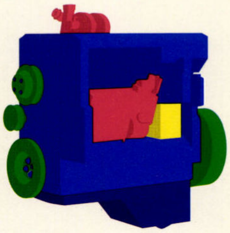
Consolidated Statement of Earnings
Cummins Engine Company, Inc.

Millions, except per share amounts	1996	1995	1994
Net sales	$5,257	$5,245	$4,737
Cost of goods sold	4,072	3,974	3,551
Gross profit	1,185	1,271	1,186
Selling and administrative expenses	725	692	641
Research and engineering expenses	252	263	238
Net expense (income) of joint ventures and alliances	–	2	(4)
Interest expense	18	13	17
Other (income) expense, net	(24)	6	–
Restructuring charges	–	118	–
Earnings before income taxes	214	177	294
Provision (credit) for income taxes	54	(47)	41
Net earnings	$ 160	$ 224	$ 253
Earnings per share	$ 4.01	$ 5.52	$ 6.11

The accompanying notes are an integral part of this statement.

Consolidated Statement of Financial Position
Cummins Engine Company, Inc.

Millions, except per share amounts	December 31, 1996	1995
Assets		
Current assets:		
Cash and cash equivalents	$ 108	$ 60
Receivables	669	597
Inventories	587	513
Other current assets	189	218
	1,553	1,388
Investments and other assets:		
Investments in joint ventures and alliances	207	211
Other assets	119	115
	326	326
Property, plant and equipment:		
Land and buildings	460	436
Machinery, equipment and fixtures	1,931	1,875
Construction in process	270	164
	2,661	2,475
Less accumulated depreciation	1,375	1,327
	1,286	1,148
Intangibles, deferred taxes and deferred charges	204	194
Total assets	$3,369	$3,056
Liabilities and shareholders' investment		
Current liabilities:		
Loans payable	$ 93	$ 60
Current maturities of long-term debt	39	42
Accounts payable	380	376
Accrued salaries and wages	84	85
Accrued product coverage and marketing expenses	126	152
Income taxes payable	16	30
Other accrued expenses	283	308
	1,021	1,053
Long-term debt	283	117
Other liabilities	753	703
Shareholders' investment:		
Common stock, $2.50 par value, 43.9 shares issued	110	110
Additional contributed capital	929	926
Retained earnings	535	406
Common stock in treasury, at cost, 4.5 and 3.7 shares	(169)	(135)
Unearned compensation	(46)	(51)
Cumulative translation adjustments	(47)	(73)
	1,312	1,183
Total liabilities and shareholders' investment	$3,369	$3,056



The accompanying notes are an integral part of this statement.

Consolidated Statement of Cash Flows

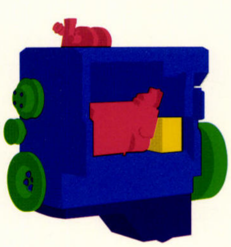
Cummins Engine Company, Inc.

Millions	1996	1995	1994
Cash flows from operating activities:			
Net earnings	$ 160	$ 224	$ 253
Adjustments to reconcile net earnings to net cash from operating activities:			
Depreciation and amortization	149	143	128
Restructuring actions	(42)	114	–
Accounts receivable	(56)	(91)	(37)
Inventories	(62)	3	(46)
Accounts payable and accrued expenses	28	99	69
Deferred income taxes	17	(100)	(7)
Other	(1)	14	16
Total adjustments	33	182	123
Net cash provided by operating activities	193	406	376
Cash flows from investing activities:			
Property, plant and equipment:			
Additions	(304)	(223)	(238)
Disposals	26	6	5
Investments in joint ventures and alliances	(5)	(147)	(9)
Other	24	(9)	(19)
Net cash used in investing activities	(259)	(373)	(261)
Net cash (used in) provided by operating and investing activities	(66)	33	115
Cash flows from financing activities:			
Proceeds from borrowings	200	2	–
Payments on borrowings	(47)	(37)	(34)
Net borrowings under credit agreements	32	19	17
Repurchases of common stock	(34)	(69)	(5)
Dividend payments	(40)	(40)	(26)
Other	(1)	4	(2)
Net cash provided from (used for) financing activities	110	(121)	(50)
Effect of exchange rate changes on cash	4	1	5
Net change in cash and cash equivalents	48	(87)	70
Cash and cash equivalents at beginning of year	60	147	77
Cash and cash equivalents at end of year	$ 108	$ 60	$ 147
Cash payments during the year for:			
Interest	$ 16	$ 13	$ 19
Income taxes	40	59	43

The accompanying notes are an integral part of this statement.

Consolidated Statement of Shareholders' Investment
Cummins Engine Company, Inc.

Millions, except per share amounts	1996	1995	1994
Convertible preference stock, no par value, 1.0 shares authorized:			
Beginning balance (.2 shares)	$ –	$ –	$ 112
Converted to common stock or redeemed (.2 shares)	–	–	(112)
Ending balance	–	–	–
Common stock, $2.50 par value, 150.0 shares authorized:			
Beginning balance (43.9, 43.8 and 40.6 shares)	110	109	101
Conversion of preference stock and debt (2.9 shares)	–	–	7
Other (.1 and .3 shares)	–	1	1
Ending balance (43.9, 43.9 and 43.8 shares)	110	110	109
Additional contributed capital:			
Beginning balance	926	927	823
Conversion of preference stock and debt	–	–	104
Other	3	(1)	–
Ending balance	929	926	927
Retained earnings:			
Beginning balance	406	232	4
Net earnings for the year	160	224	253
Cash dividends declared	(40)	(40)	(26)
Additional minimum liability for pensions	9	(10)	1
Ending balance	535	406	232
Common stock in treasury:			
Beginning balance (3.7, 2.2 and 2.1 shares)	(135)	(72)	(67)
Stock repurchased (.8, 1.6 and .1 shares)	(34)	(69)	(5)
Stock issued (.1 shares)	–	6	–
Ending balance (4.5, 3.7 and 2.2 shares)	(169)	(135)	(72)
Unearned compensation:			
Beginning balance	(51)	(55)	(59)
Shares allocated to participants	5	4	4
Ending balance	(46)	(51)	(55)
Cumulative translation adjustments:			
Beginning balance	(73)	(69)	(93)
Adjustments	26	(4)	24
Ending balance	(47)	(73)	(69)
Shareholders' investment	$1,312	$1,183	$1,072



The accompanying notes are an integral part of this statement.

Note 1. Summary of Significant Accounting Policies:

Principles of Consolidation: The consolidated financial statements include the accounts of Cummins Engine Company, Inc., and its majority-owned subsidiaries. Affiliated companies in which Cummins does not have a controlling interest are accounted for using the equity method.

The statements and notes have been prepared in conformity with generally accepted accounting principles and include some amounts which are estimates based upon currently available information and management's judgment of current conditions and circumstances.

Revenue Recognition: The company recognizes revenues on the sale of its products, net of estimated costs of returns, allowances and sales incentives, when the products are shipped to customers.

Product Coverage Programs: Estimated costs of commitments for product coverage programs are charged to earnings at the time the company sells its products.

Foreign Currency: The company uses the local currency as the functional currency for its manufacturing operations outside the United States, except those in Brazil and Mexico for which it uses the U.S. dollar. At operations which use the local currency as the functional currency, results are translated into U.S. dollars using average exchange rates for the year, while assets and liabilities are translated into U.S. dollars using year-end exchange rates. The resulting translation adjustments are recorded as a separate component of shareholders' investment; gains and losses from foreign currency transactions are included in net earnings. At the Company's operations in Brazil and Mexico, cash and certain other monetary assets and liabilities (such as receivables and payables) and revenues and expenses are translated into U.S. dollars using current exchange rates. Inventories and nonmonetary assets, such as fixed assets, are translated into U.S. dollars using historical exchange rates. The resulting translation adjustments and gains and losses from foreign currency transactions are reflected in net earnings.

Research and Development: Expenditures for research and development of new products, as well as engineering expenditures during early production and ongoing efforts to improve existing products, are charged to earnings as incurred, net of contract reimbursements. Research and development costs approximated $235 million in 1996, $230 million in 1995 and $200 million in 1994.

Cash Equivalents: Cash equivalents are investments that are readily convertible to known amounts of cash and have original maturities of three months or less.

Inventories: The company accounts for approximately 25 percent of its inventories using the last-in, first-out (LIFO) cost method. These LIFO inventories include substantially all of the Company's U.S. heavy-duty and high-horsepower engine and engine parts inventories. All other inventories are valued at the lower of first-in, first-out (FIFO) cost or net realizable value.

Dollars in millions	December 31, 1996	1995
Finished products	$334	$283
Work-in-process and raw materials	319	292
Inventories at FIFO cost	653	575
Excess of FIFO over LIFO	(66)	(62)
Inventories	$587	$513

Property, Plant and Equipment: The company depreciates substantially all engine production equipment using a modified units-of-production method, which is based upon units produced subject to a minimum level. Depreciation of all other equipment is computed using the straight-line method for financial reporting purposes. The estimated service lives to compute depreciation range from 20 to 40 years for buildings and 3 to 20 years for machinery, equipment and fixtures. Where appropriate, the company uses accelerated depreciation methods for tax purposes. Maintenance and repair costs are charged to earnings as incurred.

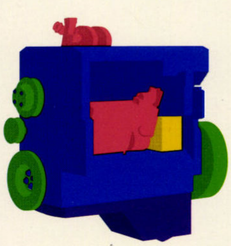
Earnings Per Share: Primary earnings per share are computed by subtracting preference stock dividend requirements from net earnings and dividing that amount by the weighted-average number of common shares outstanding during each year. Fully diluted earnings per share are computed by dividing net earnings by the weighted-average number of shares outstanding, assuming the exercise of stock options and the conversion of debt and preference stock to common stock.

Note 2. Restructuring Charges: Results of operations in 1995 included restructuring charges of $118 million ($77 million after taxes) for costs to reduce the worldwide work force through a series of actions, including voluntary and involuntary separations, retirements and plant consolidations. Facility consolidations included closing or restructuring selected operations in Europe, Brazil and North America. The components of the restructuring charges were:

Dollars in millions	
Work force reductions	$ 82
Asset write downs	32
Other	4
Total	$118

Estimated costs for work force reductions were based on amounts pursuant to benefit programs and contractual provisions or statutory requirements at the affected operations. Approximately $53 million has been charged to the liabilities as of December 31, 1996.

Note 3. Operating Leases: Certain of the company's manufacturing plants, warehouses and offices are leased facilities. The company also leases manufacturing and office equipment. Most of these leases require fixed rental payments, expire over the next ten years and can be renewed or replaced with similar leases. Rental expense under these leases approximated $55 million in each of the last three years. Future minimum payments for leases with original terms of more than one year are $32 million in 1997, $28 million in 1998, $22 million in 1999, $18 million in 2000, $15 million in 2001 and $59 million thereafter.



Note 4. Investments in Joint Ventures and Alliances:

Dollars in millions	December 31, 1996	1995
Cummins Wartsila	$ 59	$ 31
Consolidated Diesel	38	96
Kirloskar Cummins	36	27
Chongqing Cummins	16	15
Tata Cummins	13	13
Behr America	12	12
Cummins Komatsu	9	3
Other	24	14
Carrying value	$207	$211

Summary financial information for these 50-percent or less owned joint ventures and alliances:

Dollars in millions	1996	1995	1994
Net sales	$1,328	$1,091	$914
Earnings	2	6	15
Cummins' share	–	(2)	4

Dollars in millions	December 31, 1996	1995
Current assets	$ 458	$ 330
Noncurrent assets	478	340
Current liabilities	(305)	(231)
Noncurrent liabilities	(248)	(63)
Net assets	$ 383	$ 376
Cummins' share	$ 207	$ 211

In connection with various joint venture agreements, the company is required to purchase engine products in amounts to provide for the recovery of specified costs of the joint venture. Under the agreement with Consolidated Diesel, Cummins' purchases approximated $540 million in 1996 and 1995, with future minimum purchases of $6 million in 1997 and 1998, $9 million in 1999, $10 million in 2000 and 2001 and $85 million thereafter. The company's carrying value of Consolidated Diesel at December 31, 1995 included temporary financing of $50 million that was repaid to Cummins in 1996.

Note 5. Long-Term Debt:

Dollars in millions	December 31, 1996	1995
8.2% notes, due 2003	$108	$ –
Commercial paper	90	–
10.35%–10.65% medium-term notes, through 1998	35	73
Guaranteed notes of ESOP Trust, due 1998	67	68
Other	22	18
Total indebtedness	322	159
Less current maturities	39	42
Long-term debt	$283	$117

Aggregate maturities of long-term debt for the five years subsequent to December 31, 1996 are $39 million, $101 million, $19 million, $18 million and $20 million. At December 31, 1996 and 1995, the weighted-average interest rate on loans payable and current maturities of long-term debt was 7 percent and 8 percent, respectively.

In 1996, a subsidiary of the company issued 8.2 percent notes, which resulted in net proceeds of $100 million.

The company maintains a revolving credit agreement, under which there were no outstanding borrowings at December 31, 1996 or 1995. In 1996, the agreement was amended, increasing the available amount from $300 million to $400 million and extending the term to 2001. The revolving credit agreement supported commercial paper borrowings at December 31, 1996. The commercial paper initially was issued as replacement financing for an arrangement whereby the company sold up to $110 million receivables without recourse. The agreement for the sale of receivables expired in the second quarter of 1996 and was not renewed by the company. The company also maintains other domestic and international credit lines with approximately $90 million available at December 31, 1996.

The company has guaranteed the outstanding borrowings of its ESOP Trust. Cash contributions to the Trust, together with the dividends accumulated on the common stock held by the Trust, are used to pay interest and principal due on the notes. Cash contributions and dividends to the ESOP Trust and the company's compensation expense approximated $10 million in each year. The unearned compensation, which is reflected as a reduction to shareholders' investment, represents the historical cost of the ESOP Trust's shares of common stock that have not yet been allocated to participants.

In February 1997, the company issued $120 million of 6.75 percent debentures that mature in 2027. Holders have a one-time option in 2007 to redeem the debentures. The company also has a recall right after 10 years.

Note 6. Other Liabilities:

Dollars in millions	December 31, 1996	1995
Accrued retirement and post-employment benefits	$530	$533
Accrued product coverage and marketing expenses	112	86
Deferred taxes	28	21
Accrued compensation	28	21
Other	55	42
Other liabilities	$753	$703

Note 7. Income Taxes:

Dollars in millions	1996	1995	1994
Current:			
U.S. Federal and state	$22	$ 30	$29
Foreign	15	23	19
	37	53	48
Deferred:			
U.S. Federal and state	–	(93)	(9)
Foreign	17	(7)	2
	17	(100)	(7)
Tax provision (credit)	$54	$ (47)	$41

The company expects to realize all of its tax assets, including the use of all carryforwards before any expiration. A valuation allowance previously maintained against tax carryforward benefits was released to earnings as a reduction of income tax expense in the amount of $68 million in 1995 and $32 million in 1994. Tax benefits of $35 million also were recorded as a reduction to income tax expense in 1995 for changes in the treatment of foreign tax credits and foreign sales corporation benefits for prior years.

Significant components of the company's net deferred tax assets relate to the following tax effects of differences between financial and tax reporting:

Dollars in millions	December 31, 1996	1995
U.S. accrued employee benefits	$ 247	$ 236
U.S. accrued product coverage and marketing expenses	72	73
Restructuring charges	10	25
U.S. plant and equipment	(125)	(124)
Other net U.S. differences	21	7
Net foreign taxable differences, primarily plant and equipment	(23)	(7)
U.S. Federal carryforward benefits:		
General business tax credits, expiring 2000 to 2010	45	58
Minimum tax credits, no expiration	9	11
Net deferred tax assets	$ 256	$ 279

Balance sheet classification		
Current assets	$131	$164
Noncurrent assets	153	136
Noncurrent liabilities	(28)	(21)
Net deferred tax assets	$256	$279

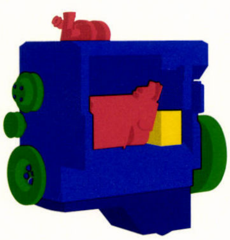
Earnings before income taxes and differences between the effective tax rate and U.S. Federal income tax rates were:

Dollars in millions	1996	1995	1994
Earnings before income taxes:			
U.S.	$134	$135	$181
International	80	42	113
	$214	$177	$294
Tax at 35 percent U.S. statutory rate	$ 75	$ 62	$103
Adjustment to beginning-of-year valuation allowance	–	(68)	(32)
Change in treatment of foreign tax credit and foreign sales corporation benefits of prior years	–	(35)	–
Research tax credits	(6)	(6)	(9)
Current-year foreign sales corporation benefits	(11)	(5)	–
Differences in rates and taxability of foreign subsidiaries	–	–	(18)
All other, net	(4)	5	(3)
Tax provision (credit)	$ 54	$ (47)	$ 41

Note 8. Retirement Plans: The company has various contributory and noncontributory pension plans covering substantially all employees. Benefits for salaried plans generally are based upon annual compensation, and benefits under the hourly plans generally are based upon various monthly amounts for each year of service. The company has a non-qualified excess benefit plan that provides certain employees with defined retirement benefits in excess of qualified plan limits imposed by U.S. tax law. In addition, the company has a plan that provides officers and other key employees with term life insurance during active employment and supplemental retirement benefits.

Dollars in millions	December 31, 1996	1995
Benefit obligation:		
Vested	$(1,286)	$(1,139)
Accumulated	$(1,410)	$(1,332)
Projected	$(1,491)	$(1,467)
Plan assets	1,555	1,367
Funded status	64	(100)
Unrecognized:		
Experience gain	(114)	(26)
Prior service cost	70	106
Transition asset	(21)	(29)
Additional liability	(35)	(63)
Accrued liability	$ (36)	$ (112)

The projected benefit obligation for underfunded plans was $694 million at December 31, 1996 and $688 million at December 31, 1995, of which $109 million and $168 million, respectively, was recorded as a liability. The projected benefit obligation for the company's principal plans was determined using a weighted-average discount rate of 7.75 percent in 1996 and 7 percent in 1995. The long-term rate of return on assets was assumed to be 9.25 percent in 1996 and 10 percent in 1995. The assumed long-term rate of compensation increase for salaried plans approximated expected inflation in both 1996 and 1995.



Note 8. (continued)
It is the company's policy to make contributions to plans sufficient to meet the funding requirements of applicable laws and regulations, plus such additional amounts as deemed to be appropriate. Plan assets consisted principally of equity securities and corporate and fixed-income Government obligations. Cummins common stock represented 6 percent of plan assets at December 31, 1996.

Dollars in millions	1996	1995	1994
Service cost	$ 45	$ 40	$ 42
Interest cost	104	99	89
Asset return:			
Actual	(155)	(214)	(26)
Deferred	39	110	(79)
Transition asset amortization	(9)	(9)	(9)
Other	16	14	12
Pension cost	$ 40	$ 40	$ 29

While the company provides certain health care and life insurance benefits to eligible retirees and their dependents, it reserves the right to change benefits covered under these plans. The plans are contributory, with retirees' contributions adjusted annually, and contain other cost-sharing features, such as deductibles, coinsurance and spousal contributions. The general policy is to fund benefits as claims and premiums are incurred.

Dollars in millions	1996	1995	1994
Service cost	$ 9	$ 8	$10
Interest cost	36	38	33
Other	10	7	10
Total health care costs	$55	$53	$53

Dollars in millions	December 31, 1996	1995
Obligation for:		
Retirees	$273	$238
Employees eligible to retire	145	125
Others	127	163
Unrecognized:		
Prior service cost	4	(10)
Experience loss	(38)	(40)
Accrued liability	$511	$476

The weighted-average discount rate used to determine the accumulated benefit obligation was 7.75 percent in 1996 and 7 percent in 1995. The weighted-average trend rate for medical benefits was 8.9 percent, grading down to an ultimate rate of 5.5 percent by 2006. The health care cost trend rate assumption could have a significant effect on the determination of the obligation. For example, increasing the rate by one percent would increase the accumulated benefit obligation by $31 million and net cost by $3 million.

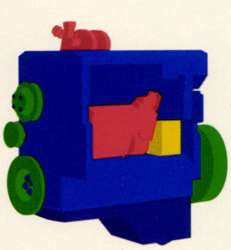
Note 9. Common Stock Repurchases:
In 1994, the Board of Directors authorized repurchase by the company of up to 2.5 million shares of its common stock. During 1996, the company completed this program with the repurchase of .8 million shares of stock on the open market at an aggregate purchase price of $34 million, or average price of $41.35 per share. The company repurchased 1.6 million shares at an aggregate purchase price of $69 million, or average price of $43.57 per share, in 1995 and .1 million shares at an aggregate purchase price of $5 million, or average price of $42.47 per share, in 1994. All of the acquired shares are held as common stock in treasury.

In January 1997, the company announced that it will issue 3.75 million shares of its common stock to an employee benefits trust to fund obligations of employee benefit and compensation plans, principally retirement savings plans. Shares of the common stock held by this trust will not be used in the calculation of the company's earnings per share until distributed from the trust and allocated to a benefit plan. The company also announced in January 1997 repurchase of 1.3 million shares of its common stock from Ford Motor Company and that the Board of Directors has authorized the repurchase of an additional 1.7 million shares in the open market.

Note 10. Segments of the Business: The company operates in a single industry segment—designing, manufacturing and marketing diesel engines and related products. The company's key markets for engines are automotive (heavy-duty trucks, midrange trucks, bus and light commercial vehicles), power generation and industrial. Manufacturing, marketing and technical operations are maintained in major areas of the world. Summary financial information is listed below for each geographic area. Earnings for each area may not be a meaningful representation of each area's contribution to consolidated operating results because of significant sales of products between and among the company's various domestic and international operations.

Dollars in millions	U.S.	Europe	All Other	Corporate Items	Combined
1996					
Net sales:					
To customers in the area	$2,904	$ 770	$619	$ –	$4,293
To customers outside the area	581	363	20	–	964
Intergeographic transfers	415	180	129	(724)	–
Total	$3,900	$1,313	$768	$(724)	$5,257
Earnings before income taxes	$ 111	$ 75	$ 22	$ 6	$ 214
Identifiable assets	$2,069	$ 624	$517	$ 159	$3,369
1995					
Net sales:					
To customers in the area	$3,010	$ 772	$524	$ –	$4,306
To customers outside the area	587	342	10	–	939
Intergeographic transfers	367	186	126	(679)	–
Total	$3,964	$1,300	$660	$(679)	$5,245
Earnings (loss) before income taxes	$ 178	$ 113	$ 24	$(138)	$ 177
Identifiable assets	$1,853	$ 598	$483	$ 122	$3,056
1994					
Net sales:					
To customers in the area	$2,708	$ 657	$538	$ –	$3,903
To customers outside the area	594	234	6	–	834
Intergeographic transfers	410	159	114	(683)	–
Total	$3,712	$1,050	$658	$(683)	$4,737
Earnings (loss) before income taxes	$ 177	$ 87	$ 44	$ (14)	$ 294
Identifiable assets	$1,618	$ 499	$412	$ 177	$2,706

Total sales for each geographic area are classified by manufacturing source and include sales to customers within and outside the area and intergeographic transfers. Transfer prices for sales between the company's various operating units generally are at arm's length, based upon business conditions, distribution costs and other costs which are expected to be incurred in producing and marketing products. Corporate items include interest and other income and expense. Identifiable assets are those resources associated with the operations in each area. Corporate assets are principally cash and investments.



The company generally sells its products on open account under credit terms customary to the region of distribution. The company performs ongoing credit evaluations of its customers and generally does not require collateral to secure its customers' receivables.

Net sales by marketing territory:

Dollars in millions	1996	1995	1994
United States	$2,925	$3,018	$2,712
Asia, Far East and Australia	868	723	626
Europe	759	783	671
Canada	313	384	330
Mexico and South America	260	233	318
Africa and Middle East	132	104	80
Net sales	$5,257	$5,245	$4,737

Note 11. Shareholders' Rights Plan: The company has a Shareholders' Rights Plan which it first adopted in 1986. The Rights Plan provides that each share of the company's common stock has associated with it a stock purchase right. The Rights Plan becomes operative when a person or entity acquires 15 percent of the company's common stock or commences a tender offer to purchase 20 percent or more of the company's common stock without the approval of the Board of Directors. In the event a person or entity acquires 15 percent of the company's common stock, each right, except for the acquiring person's rights, can be exercised to purchase $400 worth of common stock for $200.

In addition, for a period of 10 days after such acquisition, the Board of Directors can exchange such right for a new right which permits the holders to purchase one share of the company's common stock for $1 per share. If a person or entity commences a tender offer to purchase 20 percent or more of the company's common stock, unless the Board of Directors redeems the rights within 10 days of the event, each right can be exercised to purchase one share for $200.

The plan also allows holders of the rights to purchase shares of the acquiring person's stock at a discount if the company is acquired or 50 percent of the assets or earnings power of the company is transferred to an acquiring person.

Note 12. Employee Stock Plans: Under the company's stock incentive and option plans, officers and other eligible employees may be awarded stock options, stock appreciation rights and restricted stock. Under the provisions of the stock incentive plan, up to one percent of the company's outstanding shares of common stock at the end of the preceding year is available for issuance under the plan each year. At December 31, 1996, there were 174,741 shares of common stock available for grant and 792,075 options exercisable under the plans.

Options	Number of Shares	Weighted-average Exercise Price
Dec. 31, 1993	525,070	$32.54
Granted	349,927	43.05
Exercised	(10,200)	27.44
Dec. 31, 1994	864,797	37.49
Granted	360,625	39.98
Exercised	(22,520)	30.83
Cancelled	(19,627)	41.03
Dec. 31, 1995	1,183,275	38.45
Granted	394,150	40.13
Exercised	(47,475)	32.43
Cancelled	(19,800)	41.00
Dec. 31, 1996	1,510,150	38.88

Options outstanding at December 31, 1996 have exercise prices between $15.94 and $53.25 and a weighted-average remaining life of 5 years. The weighted-average fair value of options granted was $11.36 per share in 1996 and $10.41 per share in 1995. The fair value of each option was estimated on the date of grant using a risk-free interest rate of 6.7 percent in 1996 and 5.7 percent in 1995, current annual dividends, expected lives of 10 years and expected volatility of 27 percent. If the company had used a fair-value method of accounting for awards subsequent to January 1, 1995, net earnings would have been reduced less than $2 million in 1996.

Note 13. Guarantees, Commitments and other Contingencies: Accounts receivable that have been sold with recourse amounted to $25 million at December 31, 1996. Commitments under outstanding letters of credit, guarantees and contingencies approximated $185 million. Based on borrowing rates currently available to the company for bank loans with similar terms and average maturities, the fair value of total indebtedness of $322 million at December 31, 1996 was approximately $335 million. The carrying values of all other receivables and liabilities approximated fair values at December 31, 1996.

The company enters into forward exchange contracts to hedge the effects of fluctuating currency rates on certain assets and liabilities, such as accounts receivable and payable, that are denominated in other than the functional currencies of entities. The contracts typically provide for the exchange of different currencies at specified future dates and rates. The gain or loss due to the difference between the forward exchange rates of the contracts and current rates offsets in whole or in part the loss or gain on the assets or liabilities being hedged. The company had $214 million of contracts outstanding at December 31, 1996, which mature in 1997 and are denominated in a variety of foreign currencies where the company does business.

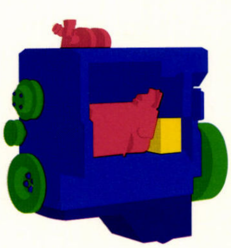
Commodity swap contracts at December 31, 1996 amounted to $35 million and have the effect of fixing the company's cost of certain future material purchases. These contracts mature through 1998. Gains or losses on the contracts are reflected in earnings concurrently with the hedged items.

Cummins and its subsidiaries are defendants in a number of pending legal actions, including actions related to use and performance of the company's products. The company carries product liability insurance covering significant claims for damages involving personal injury and property damage. In the event the company is determined to be liable for damages in connection with such actions and proceedings, the unreserved and uninsured portion of such liability is not expected to be material. The company also has been identified as a potentially responsible party at several waste disposal sites under U.S. and related state environmental statutes and regulations. The company denies liability with respect to many of these legal actions and environmental proceedings and vigorously is defending such actions or proceedings. The company has established reserves which it believes are adequate for its expected future liability in such actions and proceedings where the nature and extent of such liability can be estimated reasonably based upon presently available information.

Note 14. Quarterly Financial Data (unaudited):

Dollars in millions, except per share amounts	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Full Year
1996					
Net sales	$1,316	$1,316	$1,264	$1,361	$5,257
Gross profit	316	300	270	299	1,185
Net earnings	49	44	26	41	160
Earnings per share	$ 1.21	$ 1.10	$ .67	$ 1.03	$ 4.01
1995					
Net sales	$1,334	$1,361	$1,219	$1,331	$5,245
Gross profit	343	340	277	311	1,271
Net earnings	67	69	46	42	224
Earnings per share	$ 1.63	$ 1.69	$ 1.14	$ 1.05	$ 5.52

Included in net earnings in the fourth quarter of 1995 was a restructuring charge of $116 million ($76 million after taxes). There also was a tax credit of $68 million. Net earnings for 1995 included restructuring charges of $118 million ($77 million after taxes).



Management's Responsibility for Financial Statements

Management is responsible for the preparation of the company's consolidated financial statements and all related information appearing in this report. The statements and notes have been prepared in conformity with generally accepted accounting principles and include some amounts which are estimates based upon currently available information and management's judgment of current conditions and circumstances. The company engaged Arthur Andersen LLP, independent public accountants, to examine the consolidated financial statements. Their report appears on this page.

To provide reasonable assurance that assets are safeguarded against loss from unauthorized use or disposition and that accounting records are reliable for preparing financial statements, management maintains a system of accounting and controls, including an internal audit program. The system of accounting and controls is improved and modified in response to changes in business conditions and operations and recommendations made by the independent public accountants and the internal auditors.

The Board of Directors has an Audit Committee whose members are not employees of the company. The committee met four times in 1996 with management, internal auditors and representatives of the company's independent public accountants to review the company's program of internal controls, audit plans and results, and the recommendations of the internal and external auditors and management's responses to those recommendations.

Report of Independent Public Accountants

To the Shareholders and Board of Directors of Cummins Engine Company, Inc.:

We have audited the accompanying consolidated statement of financial position of Cummins Engine Company, Inc., (an Indiana corporation) and subsidiaries as of December 31, 1996 and 1995, and the related consolidated statements of earnings, cash flows and shareholders' investment for each of the three years in the period ended December 31, 1996. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Cummins Engine Company, Inc., and subsidiaries as of December 31, 1996 and 1995, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1996, in conformity with generally accepted accounting principles.

Arthur Andersen LLP

Chicago, Illinois,
January 27, 1997.

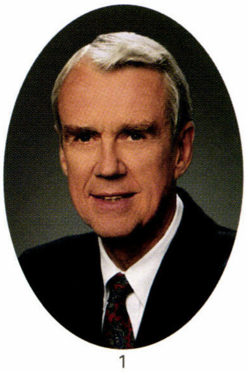
Summary of Consolidated Financial Information

Cummins Engine Company, Inc.

Dollars in millions, except per share amounts	1996	1995	1994	1993	1992
Results of operations:					
Net sales	$5,257	$5,245	$4,737	$4,248	$3,749
Cost of goods sold	4,072	3,974	3,551	3,211	2,907
Gross profit	1,185	1,271	1,186	1,037	842
Selling, administrative, research and engineering expenses	977	955	879	789	712
Interest expense	18	13	17	36	41
Other, net	(24)	8	(4)	7	13
Restructuring charges	–	118	–	–	–
Earnings before income taxes	214	177	294	205	76
Provision (credit) for income taxes	54	(47)	41	22	9
Earnings before extraordinary items and cumulative effect of accounting changes	160	224	253	183	67
Extraordinary items	–	–	–	(6)	(6)
Cumulative effect of accounting changes	–	–	–	–	(251)
Net earnings (loss)	160	224	253	177	(190)
Preference stock dividends	–	–	–	8	8
Earnings (loss) available for common shares	$ 160	$ 224	$ 253	$ 169	$ (198)
Per common share:					
Earnings before extraordinary items and cumulative effect of accounting changes:					
Primary	$ 4.01	$ 5.52	$ 6.11	$ 4.95	$ 1.77
Fully diluted	4.01	5.52	6.11	4.77	1.77
Net earnings (loss):					
Primary	4.01	5.52	6.11	4.79	(6.01)
Fully diluted	4.01	5.52	6.11	4.63	(6.01)
Cash dividends	1.00	1.00	.625	.20	.10
Common shareholders' investment	33.24	29.39	25.79	18.40	11.21
Average number of common shares (millions):					
Primary	39.8	40.7	41.4	35.3	32.9
Fully diluted	39.8	40.7	41.4	38.3	32.9
Operating percentages:					
Gross profit	22.5%	24.2%	25.0%	24.4%	22.5%
Return on net sales	3.0	4.3	5.3	4.2	(5.0)
Financial data:					
Working capital	$ 532	$ 335	$ 458	$ 371	$ 271
Property, plant and equipment, net	1,286	1,148	1,090	958	929
Total assets	3,369	3,056	2,706	2,390	2,230
Long-term debt	283	117	155	190	412
Shareholders' investment	1,312	1,183	1,072	821	501
Supplemental data:					
Property, plant and equipment expenditures	$ 304	$ 223	$ 238	$ 174	$ 139
Depreciation and amortization	149	143	128	125	123
Common shareholders of record	4,800	5,000	4,800	4,400	4,800
Number of employees	23,500	24,300	25,600	23,600	23,400

The extraordinary charges in 1993 and 1992 related to the early extinguishment of debt.

Effective January 1, 1992, the company adopted changes in accounting for retirees' health care, income taxes and postemployment benefits per SFAS Nos. 106, 109 and 112.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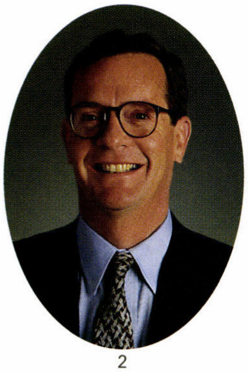
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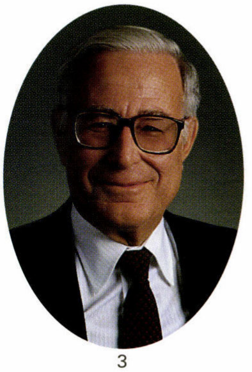
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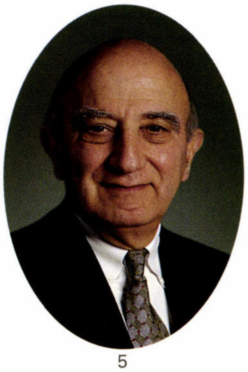
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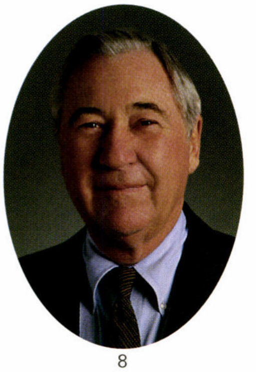
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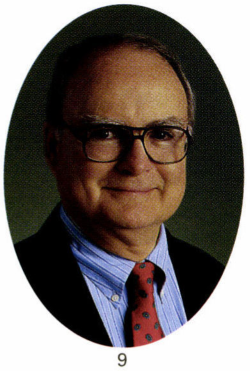
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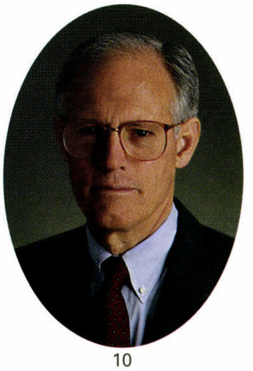
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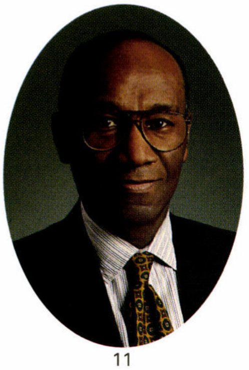
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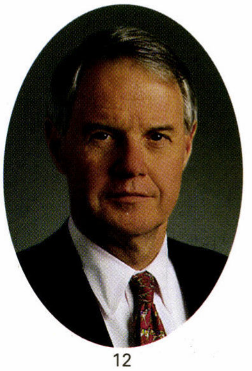
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Directors and Committees

Directors

1	James A. Henderson	Chairman and Chief Executive Officer of Cummins
2	Theodore M. Solso	President and Chief Operating Officer of Cummins
3	Harold Brown	Counselor, Center for Strategic & International Studies; Partner, Warburg, Pincus & Co., venture banking firm
4	Robert J. Darnall	Chairman, President and Chief Executive Officer, Inland Steel Industries, Inc., steel manufacturing and materials distribution
5	Walter Y. Elisha	Chairman and Chief Executive Officer, Springs Industries, Inc., manufacturer of home furnishings, industrial and specialty fabrics
6	Hanna H. Gray	President Emeritus and Professor of History, University of Chicago
7	William I. Miller	Chairman, Irwin Financial Corporation, financial services company
8	Donald S. Perkins	Retired Chairman, Jewel Companies, Inc., diversified retailing
9	William D. Ruckelshaus	Principal, Madrona Investment Group, L.L.C.
10	Henry B. Schacht	Chairman and Chief Executive Officer, Lucent Technologies, Inc., communication industry products
11	Franklin A. Thomas	Consultant, TFF Study Group, non-profit initiative to assist the development process in South Africa
12	J. Lawrence Wilson	Chairman and Chief Executive Officer, Rohm and Haas Company, chemicals and plastics manufacturing
	J. Irwin Miller	Honorary Chairman

Committees of the Board

Audit Committee: Chairman Donald Perkins, Hanna Gray and William Ruckelshaus
Business Development and Finance Committee: Chairman Lawrence Wilson, Walter Elisha and Henry Schacht
Compensation Committee: Chairman Hanna Gray, Harold Brown, Donald Perkins, William Ruckelshaus and Franklin Thomas
Employee Development and Benefits Committee: Chairman Robert Darnall, William Miller and Franklin Thomas
Executive Committee: Chairman James Henderson, William Miller and Theodore Solso
Nominating and Organization Committee: Chairman Franklin Thomas, Harold Brown, Robert Darnall, Walter Elisha, Hanna Gray, William Miller, Donald Perkins, William Ruckelshaus, Henry Schacht and Lawrence Wilson
Proxy Committee: Chairman Henry Schacht and Franklin Thomas
Technology Committee: Chairman Harold Brown and Theodore Solso

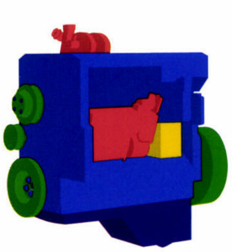
Officers

Corporate Management

James A. Henderson	Chairman and Chief Executive Officer
Theodore M. Solso	President and Chief Operating Officer

Corporate Support

Kiran M. Patel	Vice President and Chief Financial Officer
Mark E. Chesnut	Vice President–Public Policy
Wayne H. Draeger	Vice President–Financial Administration
George Fauerbach	Vice President–Business Development
Mark R. Gerstle	Vice President–Law and Corporate Affairs, and Secretary
John McLachlan	Vice President–Corporate Controller (retirement April 1, 1997)
Rick J. Mills	Vice President–Corporate Controller
Brenda S. Pitts	Vice President–Human Resources
John A. Swaim	Vice President–Quality
Donald W. Trapp	Vice President–Treasurer



Officers and Executives

Automotive Group

C. Roberto Cordaro	Executive Vice President, Group President–Automotive
Martha F. Brooks	Vice President–Worldwide Marketing for Medium-Duty and Heavy-Duty Trucks
Charles J. Bumb	Vice President–National Accounts
Keith E. Chambers	Vice President–Heavy-Duty Engine Program
Dale F. Good	Vice President–North American Sales and Service
Jeffrey D. Jones	Vice President–Automotive Fleet Sales and Service
James D. Kelly	Vice President–Worldwide Operations, Automotive Business
Peter V. McDowell	Vice President–European Automotive Business
John H. Stang	Vice President–Automotive Engineering
Christine M. Vujovich	Vice President–Worldwide Marketing for Bus and Light Commercial Automotive, and Environmental Management

Power Generation Group

John K. Edwards	Executive Vice President, Group President–Power Generation
Samuel D. Hires	Vice President–High-Horsepower Engineering
Jerome E. Johnson	General Manager–Power Generation Americas
Michael F. Mitchell	Vice President–Power Generation Operations
Kenneth G. Sanford	Vice President–Power Generation, Asia Pacific
Steven L. Zeller	Vice President and Managing Director–Newage International Ltd.

Industrial Group

F. Joseph Loughrey	Executive Vice President, Group President–Industrial
Iain M. Barrowman	President–Cummins Wartsila Engine Company
Frank J. McDonald	Vice President–Worldwide Midrange Operations
Bryan W. Swank	Vice President–Advanced Midrange Engine Program
Bharat S. Vedak	Vice President–Industrial Business Marketing
William H. Wolpert	General Manager–Worldwide Marine Business

Filtration Group

M. David Jones	Vice President–Filtration Group and President, Fleetguard, Inc.

North America

Gottfried Muench	Vice President–Distribution, Customer Support and Aftermarket
Richard M. Gold	General Manager–Aftermarket Business
Robert J. Weimer	Vice President–Customer Support

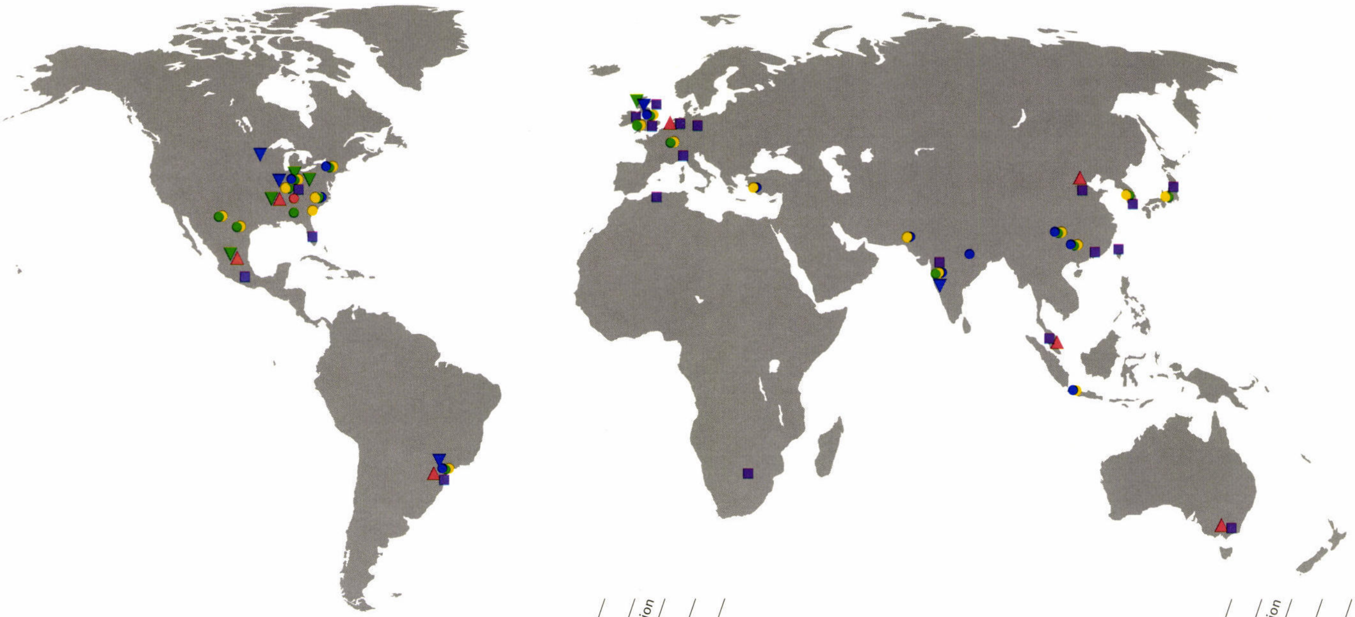
International

Mark A. Levett	Vice President–International
Steven M. Chapman	Vice President–China and Southeast Asia
J. Thompson Dewing	Vice President and Managing Director–Central Area Business Organization
Lucas L. Godinez	General Manager–Latin America
Michael Green	Managing Director–South Pacific
Jong S. Kim	Managing Director–Korea
Steven P. Knaebel	Vice President–Mexico
Ronald L. Moore	Area Business Manager–India
Tony Satterthwaite	Area Director–Southeast Asia
Hiroyuki Tajima	Managing Director–Cummins North Asia

Technology and Operations Support

Russell J. Bunio	Vice President–Worldwide Manufacturing Support and Chief Procurement Officer
Patrick F. Flynn	Vice President–Research
Wynne W. Gulden, Jr.	Vice President–Information Processes and Technology
H. Karl Kuehner	Vice President–Fuel Systems
Michael J. Percy	Vice President–Cummins Technical Center Operations (retirement April 1, 1997)
Richard B. Stoner, Jr.	Group Vice President–Technology Businesses
Richard M. Sturgeon	Vice President–Information Technology
James E. Sweetnam	Vice President and Group Managing Director–Holset Engineering Company, Ltd.
Ronald H. Temple	Vice President–Electronics
John C. Wall	Vice President–Research and Development

Cummins' Worldwide Locations



Engine Manufacturing

Operations	Production	Automotive	Power Generation	Industrial	Filtration
BMC Sanayi ve Ticaret A.S.** *Izmir, Turkey*	B3.9 / 5.9 C8.3	●		●	
Chongqing Cummins Engine Company Ltd.* *Chongqing, China*	NT K19 / 38 / 50 L10 / M11	●	●	●	
Columbus Engine Plant *Columbus, Indiana*	N14 / NT	●	●	●	
Columbus Midrange Engine Plant *Columbus, Indiana*	B5.9	●			
Consolidated Diesel Company* *Rocky Mount, North Carolina*	B3.9 / 5.9 C8.3	●	●	●	
Cummins Brasil Ltda. *Sao Paulo, Brazil*	B3.9 / 5.9 / C8.3 NT / N14	●	●	●	
Cummins Industrial Center *Seymour, Indiana*	K19 V903 QSK19		●	●	
Cummins Komatsu Engine Co.* *Seymour, Indiana*	QST30		●	●	
Cummins Marine Division *Charleston, South Carolina*	Marine product development and upfit			●	
Cummins Natural Gas Engines, Inc. *Fort Worth, Texas* *Clovis, New Mexico*	G-NT G-K19 G-V28		●	●	
Cummins Wartsila Engine Co.* *Mulhouse, France*	QSZ		●	●	
Cummins Wartsila Engine Co.* *Daventry, England*	QSW		●	●	
Darlington Engine Plant *Darlington, England*	B3.9 / 5.9 C8.3	●	●	●	
Daventry Engine Plant *Daventry, England*	K38 K50		●	●	
Dongfeng Cummins Engine Co. Ltd.* *Xiangfan, Hubei, China*	C8.3	●	●	●	
Dongfeng Motor Corporation** *Xiangfan, Hubei, China*	B3.9 / 5.9	●			

Operations	Production	Automotive	Power Generation	Industrial	Filtration
Engine Systems Ltd.* *Bin Qasim, Pakistan*	B5.9 C8.3	●		●	
Fleetguard, Inc. *Nashville, Tennessee*	Specialty filtration and lubricant analysis				●
Jamestown Engine Plant *Jamestown, New York*	L10 / M11 G-L10	●	●	●	
Kirloskar Cummins Limited* *Pune, India*	C8.3 / NT / N14 V28 / K's G-NT / N14 / G-K's	●	●	●	
Komatsu Cummins Engine Company, Ltd.* *Oyama, Japan*	B3.9 B5.9		●	●	
Onan Corporation *Fridley, Minnesota* *Huntsville, Alabama*	Generator sets, electronic controls, & gasoline engines		●		
PT Perkasa Heavyndo** *Jakarta, Indonesia*	B3.9 B5.9	●		●	
SsangYong Heavy Industries Co., Ltd.** *Seoul, South Korea*	NT / N14 K19 V903		●	●	
Tata Cummins Ltd.* *Jamshedpur, India*	B3.9 B5.9	●			

Cummins Technical Centers *Columbus, Indiana* *Fridley, Minnesota* *Darlington, England* *Pune, India* *Sao Paulo, Brazil*	Research, technology, and engine and other product development
Components Atlas Inc. *Fostoria, Ohio*	Crankshafts and camshafts
Cummins S.A. *San Luis Potosi, Mexico*	Engine components and remanufactured engines
Diesel ReCon Company *Memphis, Tennessee*	Remanufactured engines and components
Fuel Systems Division *Columbus, Indiana*	Fuel system design and manufacture
Holset Engineering Company *Huddersfield, England*	Turbochargers

■ International Offices
▲ Parts Distribution Centers
▼ Technical Centers
▼ Components
* Joint Venture
** Licensee

Shareholder Information

Annual Meeting:
Shareholders are invited to attend the company's Annual Meeting on April 1, 1997, at 10:30 a.m. (Eastern Standard Time) in Columbus, Indiana. The meeting will be held in the Robbins Auditorium of Columbus East High School.

Form 10-K Annual Report:
The company's 1996 filing with the Securities and Exchange Commission on Form 10-K contains the consolidated financial statements, notes and other related financial information. If you wish a copy of the Form 10-K, please write to:

Deb Miller (Mail Code 60915)
Director–Investor Relations
Cummins Engine Company, Inc.
Box 3005
Columbus, IN 47202-3005

Stock Transfer Agent, Registrar and Dividend Disbursing Agent:
The First Chicago Trust Company of New York is the company's common stock transfer agent and registrar. The bank maintains the company's shareholder records and is responsible for disbursing dividend checks. Changes of address and questions should be addressed as follows:

General Shareholder Correspondence
First Chicago Trust Company of New York
P. O. Box 2500
Jersey City, NJ 07303-2500

Questions concerning transfers of stock ownership should be directed to the above address at P. O. Box 2506. Cummins' Shareholder Representatives at the bank may be called at (201) 324-0498. They are available on the Internet at http://www.fctc.com and for the hearing impaired at TDD @ (201) 222-4955.

Dividend Distribution:
Common stock dividends are payable quarterly, upon authorization of the Board of Directors, on or about the fifteenth of March, June, September and December.

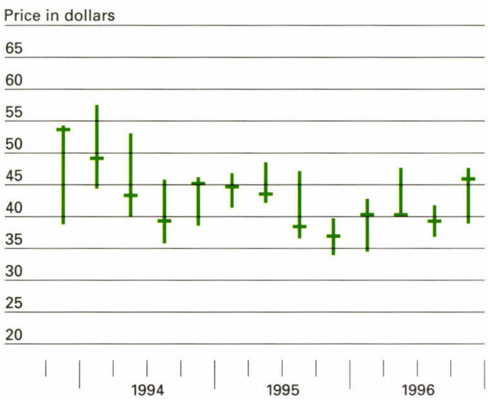
Dividend Reinvestment:
As an added service to shareholders, Cummins has established a Dividend Reinvestment Plan, administered by First Chicago Trust Company of New York. This plan gives common stock shareholders of record the option of having their cash dividends and optional cash payments applied to the purchase of additional shares. Commission and other expenses of the plan are paid by Cummins, so that participants' funds are used solely for the purchase of additional shares.

Shareholders wishing information about this plan may call (800) 446-2617 or write to:

First Chicago Trust Company of New York
P. O. Box 2598
Jersey City, NJ 07303-2598

Exchange Listings:
The common stock of Cummins Engine Company, Inc., was listed on the New York Stock Exchange in 1964 and the Pacific Stock Exchange in 1988. The stock is listed under the symbol CUM.

Cummins' Common Stock Price



Shareholder Inquiries:
Shareholders desiring general information about the company may write to Deb Miller, Director–Investor Relations, at the above address, or call (812) 377-3121. Quarterly results and other financial information are available on Cummins' home page on the Internet (http://www.cummins.com) or may be requested through debmiller@cob.cummins.com.

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