

Allison Transmission (ALSN)

\$40.22 (As of 06/04/20)

Price Target (6-12 Months): **\$42.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 10/14/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: A

Growth: C

Momentum: C

Summary

Allison is the leading manufacturer of fully-automatic transmissions for medium and heavy-duty commercial vehicles. The firm's strategic buyouts of Walker Die, C&R Tool & Engineering, Vantage Power and AxleTech's EV systems division are anticipated to boost long-term prospects. Allison's diverse revenue sources, especially the defense end market, provide a hedge against economic cycles and disruptions. The firm's investor-friendly moves are commendable. However, low business confidence amid the coronavirus crisis is likely to hurt the firm's near-term sales and earnings. Plummeting truck orders, and contracting demand in the construction, mining and energy sector is likely to weigh on the company. Allison's stretched balance sheet and high operating costs also play spoilsport.

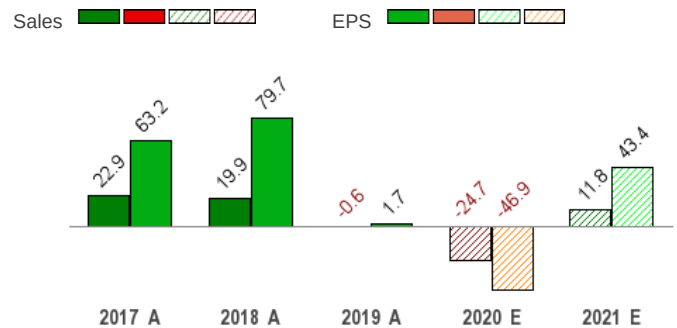
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$49.73 - \$26.15
20 Day Average Volume (sh)	809,719
Market Cap	\$4.6 B
YTD Price Change	-16.8%
Beta	1.32
Dividend / Div Yld	\$0.68 / 1.7%
Industry	Automotive - Original Equipment
Zacks Industry Rank	Bottom 47% (133 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	27.7%
Last Sales Surprise	6.7%
EPS F1 Est- 4 week change	-7.0%
Expected Report Date	07/29/2020
Earnings ESP	28.3%
P/E TTM	8.5
P/E F1	15.6
PEG F1	1.6
P/S TTM	1.7

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	587 E	604 E	591 E	562 E	2,271 E
2020	637 A	450 E	471 E	497 E	2,031 E
2019	675 A	737 A	669 A	617 A	2,698 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.02 E	\$1.06 E	\$1.09 E	\$0.96 E	\$3.70 E
2020	\$1.20 A	\$0.36 E	\$0.51 E	\$0.54 E	\$2.58 E
2019	\$1.32 A	\$1.46 A	\$1.23 A	\$0.85 A	\$4.86 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 06/04/2020. The reports text is as of 06/05/2020.

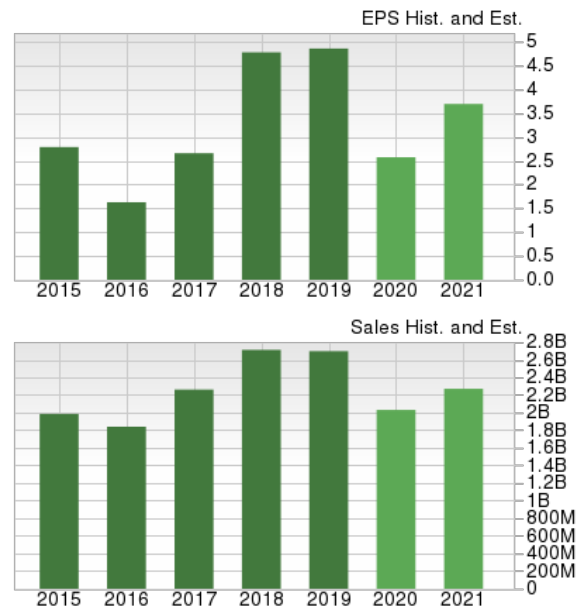
Overview

Headquartered in Indianapolis, IN, Allison Transmission Holdings, Inc. is a designer and manufacturer of fully-automatic transmissions for medium and heavy-duty commercial, and heavy-tactical U.S. defense vehicles. The company's transmissions are used for a wide variety of applications that include on-highway trucks, buses, motorhomes, off-highway vehicles and equipment, and defense vehicles. The company also offers electric hybrid propulsion systems. In 2018, Allison globally sold roughly 60% of all fully-automatic transmissions for medium and heavy-duty on-highway commercial vehicle applications.

The company has segregated revenues by end markets. In North America, it serves On-Highway (contributed 54.6% in 2019), Off-Highway (1.1%) end markets. Likewise, Outside North America, it serves On-Highway (contributed 14.4% in 2019) and Off-Highway (4.1%) end markets. Beside on and off-highway, it also serves Defense (5.6%), and Service Parts, Support Equipment and Other (20.2%) end markets.

Allison is one of the largest transmission manufacturers for on-highway, medium and heavy-duty commercial vehicle market. Within the on-highway market, it serves fully-automatic transmissions in North America, majorly catering to Class 8, followed by Class 6-7 trucks, school buses, transits/shuttle, motorhomes and others. Outside North America, Africa (collectively, "EMEA") is the company's largest market.

In the off-highway market, the company offers products used in vehicles and equipment that serve energy, mining and construction applications in North America and Outside the region. Further, Outside North America, EMEA's mining and construction are the largest markets.



Reasons To Buy:

- ▲ Allison is the largest manufacturer of fully-automatic transmissions for medium and heavy-duty commercial vehicles. It holds the leading position in several niche markets and faces limited competition. Notably, the company holds approximately 60% of the total market share on a global basis. It has a strong and diversified presence in North America. In addition, the company is focusing on increasing its footprint in emerging and under-served markets.
- ▲ Allison's strategic buyouts are expected to bolster its long-term growth. Acquisitions of Walker Die and C&R Tool & Engineering have enhanced the quality of its on-highway transmissions. Allison has also increased the pace of development of products that cater to electrification and fuel-cell markets for commercial vehicles. Buyout of Vantage Power and AxleTech's electric vehicle systems division has accelerated Allison's electrification strategy, expanding its system and integration level capabilities in alternative propulsion.
- ▲ Allison's diverse revenue sources provide a hedge against economic cycles and disruptions. Notably, the defense end market is acting as a partial offset to a sluggish global demand environment. Recently, Allison clinched a two-year approximately \$162 million contract to supply the U.S. Army with the X1100 cross-drive transmission. The firm is actively working with defense end-market partners to develop new cross-drive transmissions for tracked defense applications. Collaborative efforts with Caterpillar Defense on powertrain development also bode well for its long-term prospects.
- ▲ The company's plans to slash the capex by 35% year over year in a coronavirus-led uncertain economic environment will offer some respite. While many companies have suspended dividends and stock buybacks in a bid to conserve cash, Allison intends to preserve shareholders value. To investors' delight, the firm hiked its payout by two cents in first-quarter 2020 and bought back \$180 million of shares during the period. Notably, the firm's ROE of 79% is considerably higher than the industry's 21.5%, indicating management's efficiency in rewarding shareholders.

Allison's strategic buyouts of Walker Die, C&R Tool & Engineering, Vantage Power and AxleTech's EV systems division are expected to boost long-term prospects.

Reasons To Sell:

- ▼ The coronavirus pandemic has crippled the auto industry, and resulted in sales and production decline, thereby hurting Allison, a manufacturer of fully-automatic transmissions. The pandemic has affected Allison's customers worldwide, leading to temporary plant closures, change in processes and cut in production levels. Allison withdrew the 2020 guidance in response to disruptions to the company's supply chain due to the pandemic-led crisis. Low business confidence amid the pandemic is likely to hurt the firm's near-term sales and earnings.
- ▼ Given the gloomy scenario, truck orders are plummeting, with heavy-duty truck orders down 51% in April and medium-duty orders down 69%. Weakness in Off-Highway end market due to contracting demand for hydraulic fracturing applications is likely to adversely impact the company's bottom line in 2020. While lower demand in Europe and Asia is expected to hurt net sales in the Outside North America On-Highway end market, lower demand in construction and mining sector is anticipated to hurt top-line growth in the Outside North America Off-Highway end market.
- ▼ The company's stretched balance sheet also plays a spoilsport. As of Mar 31, 2020, long-term debt stood at \$2,512 million, \$114 million in cash and cash equivalents, depicting financial weakness. Its total debt-to-capital ratio stands at 0.78, higher than its industry's 0.45. A high total debt-to-capital ratio restricts the firm's financial flexibility.
- ▼ Contracting margins are likely to be a lingering issue. Allison has been bearing the brunt of inflating research and development costs. Such costs are expected to soar in the upcoming quarters, in turn denting margins. The company's cash flow from operating activities is declining since past several quarters. Weak revenue and income amid coronavirus woes are likely to strain cash flows in the near term.

Coronavirus woes and high debt levels are major headwinds for the transmission manufacturer.

Last Earnings Report

Allison's Q1 Earnings & Sales Fall Y/Y in Q1

Allison Transmission reported first-quarter 2020 earnings of \$1.20 per share, beating the Zacks Consensus Estimate of 94 cents. The reported figure, however, was lower than the year-ago quarter's \$1.32 per share. Net income in the first quarter was \$139 million compared with \$167 million recorded in the year-ago quarter. The downside primarily resulted from lower gross profit and elevated product-initiative spending.

In the reported quarter, net sales declined 6% year over year to \$637 million due to lower demand in the North America On-Highway and Outside North America On-Highway end markets. The figure, however, outpaced the Zacks Consensus Estimate of \$597 million. Gross profit decreased 9% year over year to \$326 million. Gross margin was 51.2% compared with the prior-year quarter's 53.2%. The downside primarily stemmed from lower net sales and unfavorable mix, partially offset by favorable material costs.

Quarter Ending **03/2020**

Report Date	May 04, 2020
Sales Surprise	6.70%
EPS Surprise	27.66%
Quarterly EPS	1.20
Annual EPS (TTM)	4.74

Quarter in Detail

Allison segregates its revenues by the end markets served, which are as follows:

Net sales in the North America On-Highway end market decreased 7% year over year to \$352 million due to lower demand for rugged duty series models. The reported figure, however, beat the Zacks Consensus Estimate of \$317 million.

Net sales in the North America Off-Highway end market tanked 43% year over year to \$8 million. Fluctuations in the demand for hydraulic fracturing applications resulted in the decline. However, the sales figure surpassed the Zacks Consensus Estimate of \$3.45 million.

Net sales in the Defense end market climbed 25% to \$40 million, owing to higher tracked vehicle demand. The figure also surpassed the Zacks Consensus Estimate of \$39 million.

The Outside North America On-Highway end market's net sales slid 23% to \$72 million, thanks to the bleak demand in Europe and Asia. The metric also missed the Zacks Consensus Estimate of \$84 million.

Net sales in the Outside North America Off-Highway end market was flat at \$27 million with the same period in 2019, driven by higher demand in the energy sector, offset by lower demand in the mining and construction sectors. However, the reported figure beat the Zacks Consensus Estimate of \$18.26 million.

Net sales in the Service Parts, Support Equipment & Other end market rose 5% to \$138 million, driven by aluminum die casting component volume associated with the Walker Die Casting acquisition. It also surpassed the Zacks Consensus Estimate of \$130 million.

Financial Position

Allison had cash and cash equivalents of \$114 million as of Mar 31, 2020, compared with \$192 million as of Dec 31, 2019. As of Mar 31, 2020, long-term debt stood at \$2,512 million, unchanged from Dec 31, 2019. The long-term debt-to-capital ratio stands at 78.4%.

In the March-end quarter, the company's net cash provided by operating activities was \$148 million compared with the year-ago quarter's \$194 million. Adjusted free cash flow in the reported quarter was \$127 million compared with the prior-year quarter's \$175 million.

During the quarter under review, the company bought back \$180 million shares and increased the quarterly dividend payment to 17 cents per share.

2020 Outlook

Allison scrapped the previously issued 2020 guidance as it expects that the coronavirus pandemic's impacts to strain its operations in the days to come. For 2020, the company lowered the capital expenditure target by approximately 35% from that reported in 2019.

Valuation

Allison's shares are down 16.8% year to date and down 8.4% over the trailing 12-month period. Stocks in the Automotive - Replacement Parts industry and the Zacks Auto sector are down 9.9% and up 1.2% respectively, on a year-to-date basis. Over the past year, the Zacks sub-industry and sector are down 0.2% and up 17.1%, respectively.

The S&P 500 index is down 3.2% in the year-to-date period and up 9.9% in the past year.

The stock is currently trading at 13.17X forward 12-month earnings, which compares to 27.18X for the Zacks sub-industry, 24.64X for the Zacks sector and 22.55X for the S&P 500 index.

Over the past five years, the stock has traded as high as 29.37X and as low as 6.8X, with a 5-year median of 10.91X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$42 price target reflects 13.77X forward 12-month earnings per share.

The table below shows summary valuation data for ALSN:

Valuation Multiples - ALSN					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	13.17	27.18	24.64	22.55
	5-Year High	29.37	27.18	24.64	22.55
	5-Year Low	6.8	8.36	8.2	15.23
	5-Year Median	10.91	11.41	9.87	17.49
EV/EBITDA TTM	Current	6.78	5.58	10.95	11.56
	5-Year High	12.3	8.44	11.3	12.86
	5-Year Low	5.23	3.96	6.94	8.26
	5-Year Median	8.08	6.33	9.25	10.81
P/S F12M	Current	2.13	0.69	0.76	3.51
	5-Year High	3.36	0.78	0.76	3.51
	5-Year Low	1.3	0.44	0.49	2.53
	5-Year Median	2.4	0.61	0.61	3.02

As of 06/04/2020

Industry Analysis Zacks Industry Rank: Bottom 47% (133 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Cummins Inc. (CMI)	Neutral	3
Dana Incorporated (DAN)	Neutral	3
Eaton Corporation, PLC (ETN)	Neutral	3
Magna International Inc. (MGA)	Neutral	5
Twin Disc, Incorporated (TWIN)	Neutral	4
BorgWarner Inc. (BWA)	Underperform	4
Caterpillar Inc. (CAT)	Underperform	5
AB Volvo (VLVLY)	Underperform	5

Industry Comparison Industry: Automotive - Original Equipment				Industry Peers		
	ALSN	X Industry	S&P 500	CAT	TWIN	VLVLY
Zacks Recommendation (Long Term)	Neutral	-	-	Underperform	Neutral	Underperform
Zacks Rank (Short Term)	3	-	-	5	4	5
VGM Score	B	-	-	B	A	B
Market Cap	4.55 B	873.46 M	22.58 B	69.80 B	72.66 M	32.57 B
# of Analysts	8	3	14	10	1	3
Dividend Yield	1.69%	0.00%	1.87%	3.19%	0.00%	2.46%
Value Score	A	-	-	C	C	A
Cash/Price	0.03	0.20	0.06	0.11	0.11	0.23
EV/EBITDA	6.47	5.03	12.93	7.53	3.94	5.03
PEG Ratio	1.58	3.55	3.06	2.17	NA	NA
Price/Book (P/B)	6.57	1.30	3.09	4.90	0.50	2.17
Price/Cash Flow (P/CF)	6.23	4.43	12.17	8.01	2.92	5.45
P/E (F1)	15.83	30.10	22.17	26.10	NA	19.46
Price/Sales (P/S)	1.71	0.36	2.41	1.37	0.28	0.75
Earnings Yield	6.41%	1.87%	4.27%	3.83%	-65.68%	5.12%
Debt/Equity	3.62	0.34	0.76	1.71	0.38	0.72
Cash Flow (\$/share)	6.45	3.73	7.01	16.10	1.85	2.94
Growth Score	C	-	-	B	A	C
Hist. EPS Growth (3-5 yrs)	23.40%	6.96%	10.87%	30.62%	22.93%	33.64%
Proj. EPS Growth (F1/F0)	-47.02%	-60.08%	-10.79%	-55.33%	-528.92%	-55.97%
Curr. Cash Flow Growth	-4.87%	-5.27%	5.48%	-6.65%	8.81%	7.58%
Hist. Cash Flow Growth (3-5 yrs)	2.51%	3.82%	8.55%	4.31%	11.18%	NA
Current Ratio	1.56	1.56	1.29	1.42	2.53	1.37
Debt/Capital	78.38%	41.92%	44.75%	63.12%	27.35%	41.77%
Net Margin	21.65%	1.92%	10.59%	10.41%	-14.33%	7.20%
Return on Equity	78.97%	11.52%	16.26%	37.15%	-6.68%	21.80%
Sales/Assets	0.60	1.25	0.55	0.65	0.78	0.79
Proj. Sales Growth (F1/F0)	-24.74%	-15.11%	-2.61%	-24.07%	-24.55%	-22.31%
Momentum Score	C	-	-	D	A	C
Daily Price Chg	3.00%	0.00%	-0.08%	1.47%	3.04%	0.69%
1 Week Price Chg	5.63%	4.84%	4.60%	6.81%	1.10%	8.14%
4 Week Price Chg	11.38%	18.42%	12.07%	20.20%	-13.83%	29.93%
12 Week Price Chg	23.91%	32.81%	25.17%	39.78%	-23.77%	34.40%
52 Week Price Chg	-8.40%	-5.89%	0.34%	4.51%	-62.83%	11.56%
20 Day Average Volume	809,719	189,833	2,537,324	3,794,481	64,934	136,107
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-6.96%	-1.67%	-0.08%	-1.00%	0.00%	0.00%
(F1) EPS Est 12 week change	-35.08%	-67.62%	-16.19%	-47.03%	-496.23%	-34.66%
(Q1) EPS Est Mthly Chg	-24.85%	-7.69%	0.00%	0.00%	0.00%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	A
Growth Score	C
Momentum Score	C
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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