

Allison Transmission (ALSN)

\$31.76 (As of 03/25/20)

Price Target (6-12 Months): **\$34.00**

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: B

Growth: B

Momentum: C

Summary

Allison Transmission adjusted earnings surpassed the Zacks Consensus Estimate in the fourth quarter of 2019 but declined year over year. The firm's strategic acquisitions including the buyout of Walker Die and C&R Tool bode well. The firm is increasing the pace of development of products that cater to electrification and fuel cell markets for commercial vehicles. Investor-friendly moves are buoying shareholders' confidence. However, the company anticipates year-over year decline in net income and adjusted FCF in 2020. Declining demand for hydraulic fracturing applications in the North America Off-Highway end market is likely to affect the firm's margins. Allison has also been bearing the brunt of rising R&D costs and the trend is likely to continue. That said, investors are recommended to wait for a better entry point.

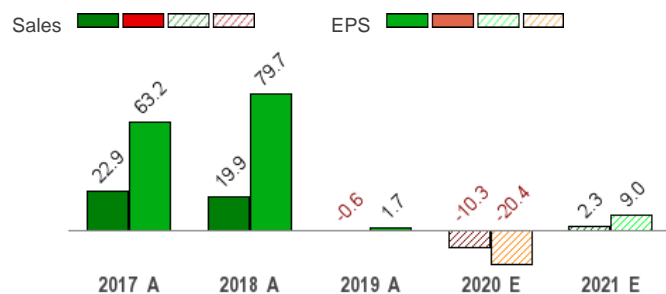
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$50.46 - \$26.15
20 Day Average Volume (sh)	1,869,141
Market Cap	\$3.7 B
YTD Price Change	-34.3%
Beta	1.35
Dividend / Div Yld	\$0.68 / 2.1%
Industry	Automotive - Original Equipment
Zacks Industry Rank	Bottom 9% (229 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	18.1%
Last Sales Surprise	3.8%
EPS F1 Est- 4 week change	-2.4%
Expected Report Date	04/28/2020
Earnings ESP	1.6%
P/E TTM	6.5
P/E F1	8.2
PEG F1	0.8
P/S TTM	1.4

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	626 E	674 E	641 E	612 E	2,477 E
2020	617 E	648 E	604 E	563 E	2,421 E
2019	675 A	737 A	669 A	617 A	2,698 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.16 E	\$1.22 E	\$1.13 E	\$0.98 E	\$4.22 E
2020	\$0.99 E	\$1.08 E	\$1.00 E	\$0.83 E	\$3.87 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 03/25/2020. The reports text is as of 03/26/2020.

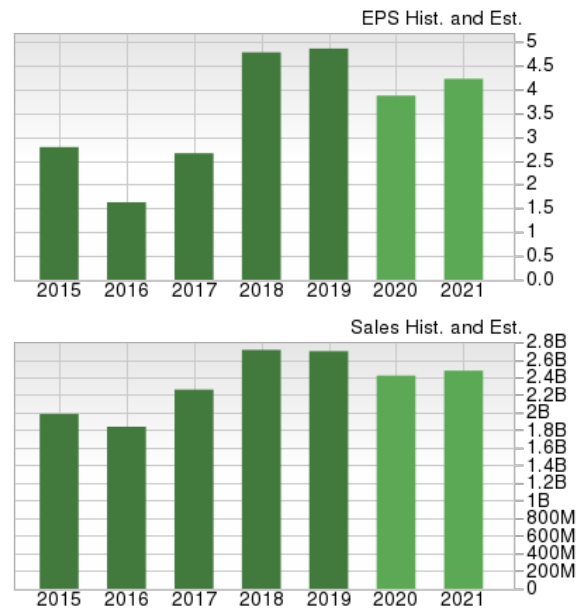
Overview

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. 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.
- ▲ While higher tracked vehicle demand in 2020 is expected to drive net sales in the Defense end market, aluminum dye casting component volume associated with the Walker dye casting acquisition is likely to favourably impact the top-line of Service Parts, Support Equipment & Other end market. The Defense, and Service Parts, Support Equipment & Other end markets are anticipated to increase by 13% and 4% year over year, respectively in 2020.
- ▲ Allison has been making efforts to trim costs through operational efficiency. Moreover, improved operating efficiency is expected to not only reduce SG&A expenses but also enable the company to invest in acquisitions, and product and technology development strategies, in addition to rewarding its shareholders. The firm's ROE of 83.12% is higher than the industry's 22.74%, indicating the management's efficiency in rewarding the shareholders.
- ▲ The firm's recent acquisitions including the buyout of Walker Die and C&R Tool bode well for future growth. Of late, Allison has increased the pace of development of products that cater to electrification and fuel cell markets for commercial vehicles. In this regard, the firm announced acquisitions of Vantage Power and AxleTech's electric vehicle systems division in 2019.

Higher tracked vehicle demand, and aluminum dye casting component volume associated with the Walker dye casting acquisition to favourably impact the company's top-line growth, going forward.

Reasons To Sell:

- ▼ The firm expects 2020 net sales to lie in the range of \$2.37-\$2.47 billion, down from the prior year's guidance of \$2.65-\$2.7 billion. It also anticipates year-over year decline in net income and adjusted FCF in 2020. Net income is projected at \$425-\$475 million, compared to \$555-\$575 million in 2019, and adjusted FCF is expected between \$430-\$480 million in 2020, down from \$570-\$610 million in the last year.
- ▼ 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 going forward, lower demand in the energy sector is anticipated to unfavorably impact the top-line growth in the Outside North America Off-Highway end market.
- ▼ Allison has been bearing the brunt of increasing research and development costs. It expects the costs to soar in the upcoming quarters, in turn denting margins. The company incurred engineering R&D expenses of \$154 million in 2019, compared to \$131 million in 2018. The company's high leverage is also a cause of concern. Its debt-to-capital ratio stands at 76.33%, which restricts the firm's financial flexibility.
- ▼ All automakers are drifting toward the global shift to electric vehicles. Allison is also developing hybrid and electrification products for commercial customers. However, weak product line, increased product initiatives spending, uncertainties about timing and scope of product development are a few concerns for the company, which makes it vulnerable to compete with other transmission producers.

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.

Last Earnings Report

Allison's Q4 Earnings Surpass Estimates, Decline Y/Y

Allison Transmission's fourth-quarter 2019 earnings came in at 85 cents per share, beating the Zacks Consensus Estimate of 72 cents. It delivered better-than-expected results on the back of higher-than-anticipated revenues from the North America On-Highway, Defense, and Service Parts, Support Equipment & Other end markets. The reported figure, however, comes in lower than the year-ago quarter's \$1.14.

Net income in the fourth quarter came in at \$107 million compared with the \$147 million recorded in the year-ago quarter. This downside primarily resulted from lower gross profit and elevated product-initiatives spending.

In the reported quarter, net sales declined 5% year over year to \$617 million due to lower demand in the Service Parts, Support Equipment & Other and Global Off-Highway end markets. The figure, however, outpaced the Zacks Consensus Estimate of \$597 million. Gross profit decreased 12% year over year to \$298 million. Gross margin was 48.3% compared with the prior-year quarter's 52.2%. This downside primarily stemmed from lower net sales and unfavorable mix, partially offset by price increases on certain products and favorable material costs.

CHART

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 increased 9% year over year to \$330 million on stellar demand for rugged duty series, highway series and electric-hybrid propulsion models. This was led by the continued execution of growth initiatives and market-share gains. The reported figure also beat the Zacks Consensus Estimate of \$304 million.

Net sales in the North America Off-Highway end market tanked 94% year over year to \$1 million. In addition, the sales figure missed the Zacks Consensus Estimate of \$6.37 million. Softer demand from hydraulic fracturing applications resulted in this decline.

Net sales in the Defense end market went climbed 17% to \$42 million, owing to higher tracked vehicle demand. The figure also surpassed the Zacks Consensus Estimate of \$35.33 million.

The Outside North America On-Highway end market net sales slid 4% to \$91 million, thanks to bleak demand in Europe and Asia, partially offset by higher demand in South America. It also missed the Zacks Consensus Estimate of \$98 million.

Net sales in the Outside North America Off-Highway end market plummeted 62% to \$18 million in the final quarter of 2019 due to lower demand in the mining, energy and construction sectors. Moreover, the reported tally missed the Zacks Consensus Estimate of \$37.68 million.

Net sales in the Service Parts, Support Equipment & Other end market fell 9% to \$135 million, due to lackluster demand for North America Off-Highway service parts. However, it exceeded the Zacks Consensus Estimate of \$123 million.

Financial Position

Allison had cash and cash equivalents of \$192 million as of Dec 31, 2019 compared with \$231 million as of Dec 31, 2018. Long-term debt was \$2,512 million as of Dec 31, 2019, compared with the \$2,523 million recorded on Dec 31, 2018. The debt-to-capital ratio stands at 76.33%.

In the December-end quarter, the company's net cash provided by operating activities was \$202 million compared with the year-ago quarter's \$232 million. Adjusted free cash flow (FCF) in the reported quarter was \$121 million compared with the prior-year quarter's \$184 million.

2020 Outlook

For full-year 2020, Allison expects net sales of \$2,375-\$2,475 million. It anticipates net income of \$425-\$475 million and adjusted EBITDA is projected at \$855-\$915 million.

Net cash provided by operating activities is projected at \$600-\$640 million for the year, while adjusted FCF is expected in the range of \$430 million to \$480 million.

Quarter Ending **12/2019**

Report Date	Feb 19, 2020
Sales Surprise	3.76%
EPS Surprise	18.06%
Quarterly EPS	0.85
Annual EPS (TTM)	4.86

Valuation

Allison's shares are down 34.3% year to date and 29.7% over the trailing 12-month period. Stocks in the Automotive - Replacement Parts industry and the Zacks Auto sector are down 31.4% and 22.8%, respectively. Over the past year, the Zacks sub-industry and sector are down 24.1% and 13.8%, respectively.

The S&P 500 index is down 23.8% in the year-to-date period and 13.4% in the past year.

The stock is currently trading at 8.03X forward 12-month earnings, which compares to 9.84X for the Zacks sub-industry, 8.81X for the Zacks sector and 14.72X 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 10.99X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$34 price target reflects 8.61X 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	8.03	9.84	8.81	14.72
	5-Year High	29.37	13.46	11.75	19.34
	5-Year Low	6.8	8.52	8.23	14.72
	5-Year Median	10.99	11.59	9.88	17.42
EV/EBITDA TTM	Current	5.78	4.7	8.61	9.07
	5-Year High	12.3	8.62	11.34	12.88
	5-Year Low	5.23	4.35	6.97	8.27
	5-Year Median	8.39	6.57	9.3	10.78
P/S F12M	Current	0.04	0.11	0.5	2.65
	5-Year High	0.14	0.25	0.76	3.43
	5-Year Low	0.04	0.11	0.5	2.54
	5-Year Median	0.09	0.18	0.62	3

As of 03/25/2020

Industry Analysis Zacks Industry Rank: Bottom 9% (229 out of 253)



Top Peers

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

Industry Comparison Industry: Automotive - Original Equipment				Industry Peers		
	ALSN Neutral	X Industry	S&P 500	CAT Neutral	TWIN Neutral	VLVLY Neutral
VGM Score	B	-	-	B	D	A
Market Cap	3.74 B	487.97 M	17.53 B	57.58 B	115.29 M	23.11 B
# of Analysts	8	2	13	10	2	2
Dividend Yield	2.14%	0.00%	2.47%	3.94%	0.00%	7.56%
Value Score	B	-	-	B	C	A
Cash/Price	0.06	0.22	0.07	0.16	0.13	0.34
EV/EBITDA	5.64	3.78	10.68	6.54	5.49	3.74
PEG Ratio	0.85	0.93	1.64	1.24	NA	NA
Price/Book (P/B)	4.85	0.83	2.32	3.94	0.68	1.54
Price/Cash Flow (P/CF)	4.92	3.01	9.40	6.50	4.64	3.87
P/E (F1)	8.47	8.50	14.14	11.96	NA	9.02
Price/Sales (P/S)	1.39	0.28	1.82	1.07	0.43	0.51
Earnings Yield	12.19%	11.09%	7.02%	8.36%	-6.86%	11.09%
Debt/Equity	3.22	0.51	0.70	1.80	0.38	0.72
Cash Flow (\$/share)	6.45	3.19	7.01	16.10	1.85	2.94
Growth Score	B	-	-	C	F	D
Hist. EPS Growth (3-5 yrs)	22.02%	7.17%	10.85%	27.28%	7.61%	38.53%
Proj. EPS Growth (F1/F0)	-20.34%	-8.62%	3.53%	-20.90%	-170.48%	-32.62%
Curr. Cash Flow Growth	-4.87%	-4.22%	5.93%	-6.65%	8.81%	7.58%
Hist. Cash Flow Growth (3-5 yrs)	2.51%	3.83%	8.55%	4.31%	11.18%	NA
Current Ratio	1.65	1.60	1.23	1.47	2.58	1.37
Debt/Capital	76.28%	38.59%	42.57%	64.24%	27.52%	41.77%
Net Margin	22.39%	2.50%	11.64%	11.32%	-2.77%	8.32%
Return on Equity	81.36%	14.04%	16.74%	41.85%	-1.80%	26.11%
Sales/Assets	0.61	1.30	0.54	0.68	0.78	0.83
Proj. Sales Growth (F1/F0)	-10.27%	-2.64%	2.51%	-9.87%	-15.81%	-9.82%
Momentum Score	C	-	-	C	B	A
Daily Price Chg	9.40%	0.83%	2.41%	3.29%	0.70%	7.27%
1 Week Price Chg	-11.94%	-20.37%	-16.96%	-4.15%	14.90%	-27.93%
4 Week Price Chg	-24.16%	-29.97%	-23.98%	-18.39%	-0.46%	-29.54%
12 Week Price Chg	-34.27%	-37.55%	-27.80%	-29.12%	-21.96%	-31.58%
52 Week Price Chg	-29.67%	-36.30%	-18.55%	-20.22%	-49.08%	-24.79%
20 Day Average Volume	1,869,141	248,030	4,285,848	7,341,061	52,956	111,977
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-2.40%	-10.04%	-1.83%	-6.37%	0.00%	1.61%
(F1) EPS Est 12 week change	-7.96%	-14.41%	-2.90%	-18.33%	22.06%	-1.82%
(Q1) EPS Est Mthly Chg	-1.68%	-10.43%	-1.37%	-3.65%	0.00%	0.00%

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	B
Growth Score	B
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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