

Cummins Inc. (CMI)

\$164.77 (As of 01/27/20)

Price Target (6-12 Months): **\$175.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 12/30/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: B

Growth: B

Momentum: F

Summary

Cummins has been focusing on introducing innovative products and making acquisitions to generate high returns. It has entered into a number of buyout deals in the last couple of years. Notably, the Hydrogenic buyout is likely to boost its ability to innovate hydrogen fuel-cell technologies across commercial markets. Cummins' strong balance sheet with low leverage also provides enough financial flexibility to tap on to growth opportunities. However, lower production of heavy-duty trucks in North America will hurt the bottom line of Cummins going forward. Weak domestic markets as well as reduced demand in off-highway markets are expected to remain concerns in the coming periods amid economic slowdown. Worryingly, the company is battling with elevated expenses, owing to rising R&D expenses for product development and high material costs.

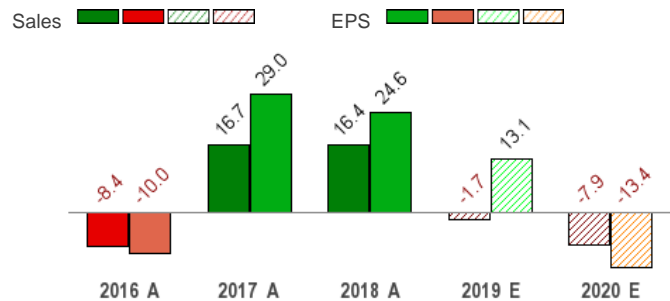
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$186.73 - \$141.14
20 Day Average Volume (sh)	1,026,619
Market Cap	\$25.2 B
YTD Price Change	-7.9%
Beta	1.14
Dividend / Div Yld	\$5.24 / 3.2%
Industry	Automotive - Internal Combustion Engines
Zacks Industry Rank	Top 42% (108 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-0.3%
Last Sales Surprise	-1.2%
EPS F1 Est- 4 week change	-1.1%
Expected Report Date	02/04/2020
Earnings ESP	-2.3%
P/E TTM	10.4
P/E F1	12.7
PEG F1	1.6
P/S TTM	1.1

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	5,290 E	5,569 E	5,462 E	5,316 E	21,512 E
2019	6,004 A	6,221 A	5,768 A	5,378 E	23,361 E
2018	5,570 A	6,132 A	5,943 A	6,126 A	23,771 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$3.35 E	\$3.41 E	\$3.43 E	\$2.63 E	\$12.96 E
2019	\$4.20 A	\$4.27 A	\$3.83 A	\$2.44 E	\$14.96 E
2018	\$3.30 A	\$4.14 A	\$4.05 A	\$3.48 A	\$13.23 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 01/27/2020. The reports text is as of 01/28/2020.

Overview

Cummins Inc. is a leading global designer, manufacturer and distributor of diesel and natural gas engines and powertrain-related component products. Powertrain components include fuel systems, turbochargers, transmissions, batteries and electrified power systems, among others. Headquartered in Columbus, IN, the company offers products to original equipment manufacturers (OEMs), distributors and dealers through a network of roughly 600 company-owned and independent distributor facilities over 7,600 dealer locations in more than 190 countries and territories.

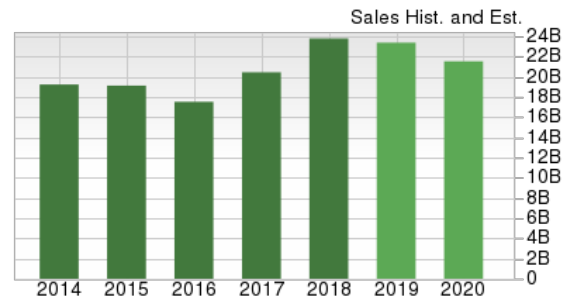
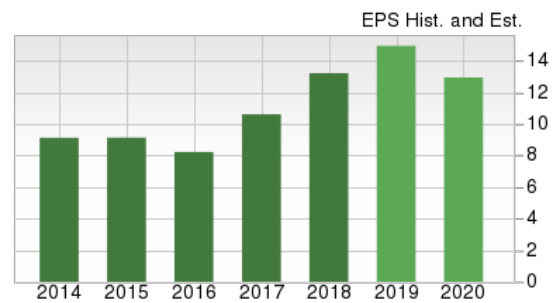
Cummins has the following four operating segments:

The **Engine** segment (35% of consolidated net sales in 2018) produces diesel and natural gas-based engines for on-highway and industrial markets. The engines are used in heavy and medium-duty trucks, buses, recreational vehicles, and various industrial applications such as construction, mining, agriculture, marine, oil and gas, rail, and defense.

The **Power Generation** segment (15%) sells power generators, diesel and natural gas high-horsepower engines, and AC generator or alternator products for internal consumption and external generator set assemblers. The unit is organized in Power Generation, Industrial and Generator Technologies product lines.

The **Components** segment (24%) has five businesses namely, Emission solutions, Turbo technologies, Filtration, Electronics and fuel systems, and Automated transmissions. The systems offered by this unit support the Engine and Power Systems segments of Cummins. The segment offers filtration systems for industrial vehicle applications and develops turbochargers, fuel systems and electronics that comply with strict emission and fuel standards.

The **Distribution** segment (26%) includes 28 wholly and partially-owned distributorships and 10 joint ventures that offer a varied range of products and services, including Parts, Engines, Power generation and Service. The segment has a diverse customer base, with a global presence. In 2018, the segment's new engines and power generation equipment sales to diverse customers were approximately 40%.



Reasons To Buy:

- ▲ Cummins focuses on introducing innovative products and strategies such as partnerships in order to record high returns. Besides widening the product portfolio, it collaborated with Hyundai Construction and Isuzu Motors in October 2018. The collaboration with Hyundai is to develop an electric powered mini excavator while the one with Isuzu Motors will discover opportunity in the powertrain area. Further, the company partnered with Russia's KAMAZ to supply electrified power solutions for KAMAZ's new line of battery-powered vehicles.
- ▲ Cummins is poised to gain from acquisitions. In sync with its aim to be a leader in electrified power, the company has acquired Hydrogenic Corp. The buyout will likely boost Cummins' ability to innovate hydrogen fuel-cell technologies across commercial markets. The company also announced the acquisition of Efficient Drivetrains, Inc., in July 2018. Earlier in January 2018, the company announced its buyout of the automotive battery business of United Kingdom's Johnson Matthey.
- ▲ Cummins is focused on enhancing the shareholder value by pursuing aggressive share repurchases and increasing dividend payouts. For 2019, the company aimed at returning 75% of full-year operating cash flow to shareholders in forms of dividends and share repurchases. In July 2019, the company increased quarterly dividend by 15% from \$1.14 per share to \$1.31 per share.

Acquisitions, along with partnerships and product offerings, will aid Cummins. The company also remains committed to boost shareholders' value.

Reasons To Sell:

- ▼ With Cummins being the largest independent engine manufacturer in the world, contracting demand for heavy trucks — which is the firm's most significant end market — is likely to mar the company's prospects, going forward. Lower production of heavy-duty trucks in North America, as well as declines in shipments to construction markets will hurt the bottom line of Cummins.
- ▼ Apart from the domestic markets, lower truck production in India, Brazil, China and Europe as well as reduced demand in off-highway markets is expected to remain weak in the coming period amid economic slowdown concerns. Lower demand in global construction markets and soft light duty truck demand in China amid trade tussle and weak economy will dent its revenues in the Chinese markets.
- ▼ The company is battling with elevated expenses, owing to rising R&D expenses for product development and high material costs. Further, expenses are expected to increase in the coming quarters for launching on-highway products that comply with emission regulation. Additionally, tariff-related commodity costs and fluctuating foreign currencies will likely hamper Cummins' margins.

Declining demand for heavy trucks — which is Cummins' chief end market — is likely to mar its prospects in both domestic and international regions, going forward.

Last Earnings Report

Cummins Delivers Dismal Q3 Results, Trims View

Cummins reported earnings of \$3.83 per share in third-quarter 2019, missing the Zacks Consensus Estimate of \$3.84. Lower-than-expected profits from the Engine segment led to the underperformance. Earnings before interest & tax for the segment were \$341 million, missing the Zacks Consensus Estimate of \$403 million.

In the reported quarter, net income attributable to the company was \$622 million compared with net income of \$692 million in the prior-year quarter.

Its revenues declined 3% year over year to \$5.76 billion in the reported quarter. Moreover, revenues missed the Zacks Consensus Estimate of \$5.83 billion.

Earnings before interest, taxes, depreciation and amortization (EBITDA) declined to \$958 million (16.6% of sales) from \$983 million (16.5% of sales) recorded in the prior-year quarter.

Segmental Performance

Sales for the Engine segment declined 11% year over year at \$2.4 billion. The segment's EBITDA declined to \$341 million (14.1% of sales) from \$405 million (14.9% of sales) a year ago.

Sales for the Distribution segment grew 4% to \$2 billion. The segment's EBITDA rose to \$186 million (9.3% of sales) from \$155 million (8% of sales) a year ago.

Sales for the Components segment declined 6% to \$1.7 billion. The segment's EBITDA was \$286 million (17.3% of sales) compared with the year-ago quarter figure of \$288 million (16.4% of sales).

Sales for the Power Generation segment improved 2% to \$1.1 billion. The segment's EBITDA declined to \$158 million (14% of sales) in third-quarter 2019 from \$163 million (14.7% of sales) in the year-ago quarter.

Sales for the Electrified Power segment were \$9 million. The segment witnessed EBITDA loss of \$36 million.

Financial Position

Cummins' cash and cash equivalents were \$1.6 billion as of Sep 29, 2019, up from \$1.3 billion as of Dec 31, 2018. Long-term debt totaled \$1.62 billion as of Sep 29, 2019, compared with \$1.60 as of Dec 31, 2018.

Outlook

For 2019, Cummins now projects revenue decline of 2%. Initially, it expected revenues to remain at the same level as 2018. The company revised projection downward on lower truck production in North America, India, Brazil and Europe, and a decline in demand in off-highway markets, including North America construction and global mining. EBITDA is now expected to be 15.9-16.3% (compared with previously mentioned 16.25-16.75%) on lower volume and the Hydrogenics acquisition. Further, the company anticipates returning 75% of operating cash flow to shareholders in forms of dividends and share repurchases.

Quarter Ending **09/2019**

Report Date	Oct 29, 2019
Sales Surprise	-1.21%
EPS Surprise	-0.26%
Quarterly EPS	3.83
Annual EPS (TTM)	15.78

Valuation

Cummins' shares are up 16.1% over the trailing 12-month period. Stocks in the Zacks Automotive – Internal Combustion Engines industry and the Zacks Automotive sector are up 19.2% and 13.5%, over the past year, respectively.

The S&P 500 index is up 26.8% in the past year.

The stock is currently trading at 12.58X forward 12-month earnings, which compares to 12.92X for the Zacks sub-industry, 10.92X for the Zacks sector and 18.94X for the S&P 500 index.

Over the past five years, the stock has traded as high as 18.94X and as low as 8.06X, with a 5-year median of 12.96X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$175 price target reflects 13.36X forward 12-month earnings.

The table below shows summary valuation data for CMI:

Valuation Multiples - CMI					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	12.58	12.92	10.92	18.94
	5-Year High	18.94	18.3	11.75	19.34
	5-Year Low	8.06	8.58	8.23	15.18
	5-Year Median	12.96	12.86	9.93	17.45
EV/EBITDA TTM	Current	7.07	7.07	8.74	12.25
	5-Year High	11.26	11.26	11.33	12.86
	5-Year Low	4.76	4.76	7.05	8.48
	5-Year Median	7.48	7.48	9.27	10.68
P/S F12M	Current	1.17	1.2	0.67	3.52
	5-Year High	1.53	1.49	0.76	3.52
	5-Year Low	0.81	0.85	0.5	2.54
	5-Year Median	1.15	1.18	0.62	3

As of 01/27/2020

Industry Analysis Zacks Industry Rank: Top 42% (108 out of 255)



Top Peers

BorgWarner Inc. (BWA)	Neutral
Caterpillar Inc. (CAT)	Neutral
Deere & Company (DE)	Neutral
Navistar International Corporation (NAV)	Neutral
PACCAR Inc. (PCAR)	Neutral
Tenneco Inc. (TEN)	Neutral
Daimler AG (DDAIF)	Underperform
AB Volvo (VLVLY)	Underperform

Industry Comparison Industry: Automotive - Internal Combustion Engines				Industry Peers		
	CMI Neutral	X Industry	S&P 500	BWA Neutral	CAT Neutral	DDAIF Underperform
VGM Score	B	-	-	A	C	A
Market Cap	25.24 B	7.17 B	23.86 B	7.92 B	75.01 B	50.15 B
# of Analysts	6	8	13	9	9	3
Dividend Yield	3.18%	0.91%	1.81%	1.77%	3.04%	0.00%
Value Score	B	-	-	A	B	A
Cash/Price	0.07	0.07	0.04	0.11	0.10	0.62
EV/EBITDA	7.19	1.35	13.94	5.14	7.91	6.18
PEG Ratio	1.60	1.96	2.00	1.21	1.47	2.38
Price/Book (P/B)	2.88	2.17	3.25	1.73	5.00	0.72
Price/Cash Flow (P/CF)	9.57	7.72	13.46	5.83	8.23	3.06
P/E (F1)	12.86	12.41	18.67	9.40	12.86	7.79
Price/Sales (P/S)	1.05	1.05	2.62	0.78	1.36	0.26
Earnings Yield	7.86%	8.07%	5.35%	10.64%	7.78%	12.84%
Debt/Equity	0.18	0.18	0.72	0.36	1.71	1.58
Cash Flow (\$/share)	17.22	1.20	6.92	6.58	16.49	15.32
Growth Score	B	-	-	B	D	A
Hist. EPS Growth (3-5 yrs)	14.89%	14.89%	10.68%	9.55%	23.01%	0.39%
Proj. EPS Growth (F1/F0)	-13.42%	-13.64%	7.51%	3.76%	-2.50%	39.78%
Curr. Cash Flow Growth	17.21%	16.45%	13.40%	11.56%	35.57%	-10.36%
Hist. Cash Flow Growth (3-5 yrs)	8.77%	15.50%	8.78%	7.21%	6.65%	1.70%
Current Ratio	1.52	1.19	1.22	1.58	1.44	1.22
Debt/Capital	15.61%	24.31%	42.92%	26.56%	63.05%	61.31%
Net Margin	10.53%	10.53%	11.39%	7.43%	10.99%	2.40%
Return on Equity	28.52%	28.52%	17.19%	19.43%	42.51%	11.23%
Sales/Assets	1.21	1.21	0.54	1.00	0.70	0.58
Proj. Sales Growth (F1/F0)	-8.25%	-0.99%	4.09%	1.66%	-4.45%	0.34%
Momentum Score	F	-	-	F	D	F
Daily Price Chg	-2.59%	-3.42%	-1.40%	-2.24%	-3.31%	-2.74%
1 Week Price Chg	-2.68%	-2.38%	-1.09%	-5.51%	-5.01%	-7.04%
4 Week Price Chg	-8.03%	-4.68%	-0.25%	-11.61%	-7.99%	-13.76%
12 Week Price Chg	-8.04%	0.74%	3.64%	-15.32%	-7.62%	-20.00%
52 Week Price Chg	15.37%	13.93%	18.08%	-5.47%	9.13%	-21.57%
20 Day Average Volume	1,026,619	18,203	1,615,215	1,093,849	2,521,839	43,856
(F1) EPS Est 1 week change	-0.58%	-0.29%	0.00%	-0.54%	-0.57%	-5.89%
(F1) EPS Est 4 week change	-1.11%	-0.55%	0.00%	-1.45%	-1.45%	-6.96%
(F1) EPS Est 12 week change	-6.62%	2.88%	-0.17%	-0.05%	-4.29%	-18.98%
(Q1) EPS Est Mthly Chg	-0.81%	-0.81%	0.00%	-2.94%	-0.23%	NA

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	B
Growth Score	B
Momentum Score	F
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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