

Cummins Inc. (CMI)

\$198.88 (As of 07/29/20)

Price Target (6-12 Months): **\$209.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 07/29/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:A

Value: B

Growth: B

Momentum: B

Summary

Technology leadership, impressive product portfolio, strong geographic diversification and broad global distribution network will boost Cummins' long term prospects. The firm's efforts and investments to ramp up its capabilities in fuel cell and hydrogen production technology bode well. Acquisition of Hydrogenic Corp will boost Cummins' ability to innovate hydrogen fuel-cell technologies across commercial markets. Healthy balance sheet and safe dividend history are other positives. However, Industry truck production is expected to decline 20% year over year in 2020 amid coronavirus, which will adversely impact Cummins' results. Further, high product and technology-related expenses, unfavorable forex translations and continuous losses from New Power segment raise concerns. Thus, the stock warrants a cautious stance.

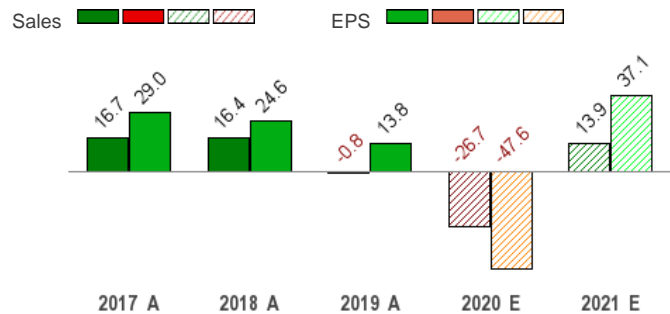
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$204.98 - \$101.03
20 Day Average Volume (sh)	1,073,563
Market Cap	\$29.3 B
YTD Price Change	11.1%
Beta	1.14
Dividend / Div Yld	\$5.24 / 2.6%
Industry	Automotive - Internal Combustion Engines
Zacks Industry Rank	Top 11% (28 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	129.4%
Last Sales Surprise	7.9%
EPS F1 Est- 4 week change	-0.6%
Expected Report Date	11/03/2020
Earnings ESP	5.1%
P/E TTM	17.3
P/E F1	25.2
PEG F1	3.1
P/S TTM	1.5

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	4,742 E	5,265 E	5,413 E	5,461 E	19,692 E
2020	5,011 A	3,852 A	3,830 E	4,458 E	17,285 E
2019	6,004 A	6,221 A	5,768 A	5,578 A	23,571 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.63 E	\$2.71 E	\$3.08 E	\$2.28 E	\$10.82 E
2020	\$3.18 A	\$1.95 A	\$1.51 E	\$1.51 E	\$7.89 E
2019	\$4.20 A	\$4.27 A	\$3.83 A	\$2.56 A	\$15.05 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 07/29/2020. The reports text is as of 07/30/2020.

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 five operating segments:

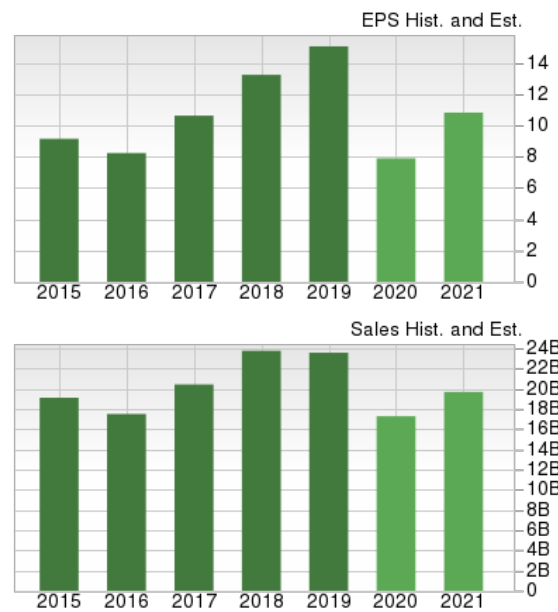
The **Engine** segment (34% of consolidated net sales in 2019) produces diesel and natural gas-based engines for on-highway and industrial markets. The engines are used in heavy and medium-duty trucks, buses, recreational vehicles, and various industrial applications such as construction, mining, agriculture, marine, oil and gas, rail, and defense.

The **Power Generation** segment (15.9%) 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 (23%) 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 **Distribution** segment (27%) 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.

The **New Power** segment (0.1%) designs, manufactures, sells and supports electrified power systems ranging from fully electric to hybrid. It currently offers the Cummins PowerDrive series of fully electric and hybrid powertrain systems targeting various applications in the Class 4-8 commercial vehicle markets and are developing the Cummins Battery Electric System and the Cummins Hybrid Power Plug-In System for the urban bus market.



Reasons To Buy:

- ▲ Cummins' position as a global power leader with dominant market share bode well. The firm's commitment to moving toward a decarbonized future is commendable. Technology leadership, impressive product portfolio, strong geographic diversification and broad global distribution network will boost its long term prospects. The firm focuses on introducing innovative products and enters into various collaborations in order to record high returns. Further, adoption or increased enforcement of new emissions standards is also a tailwind. Increased demand for more fuel efficient and emissions compliant engines provide abundant opportunities to the firm.
- ▲ Cummins' efforts and investments to ramp up its capabilities in fuel cell and hydrogen production technology bode well for long term prospects. Acquisition of Hydrogenic Corp will boost Cummins' ability to innovate hydrogen fuel-cell technologies across commercial markets. Investment in Loop Energy and partnership with NPROXX will expand Cummins' fuel cell and hydrogen-processing technology capabilities.
- ▲ Cummins' strong balance sheet with low leverage and high liquidity is another tailwind. The company has a total debt-to-capital ratio of 0.17, lower than the Auto sector's 0.66. Low leverage increases the financial flexibility of the firm to tap onto growth opportunities. Moreover, the company has a times interest earned ratio of 23.71, higher than the sector's 5.40. Investment grade credit ratings of A+ and A2 from Standard & Poor's and Moody's, respectively, boost optimism.
- ▲ Cummins' safe and reliable dividend history keep the shareholders happy. The company has been paying dividends for over 70 years. At a time, when many firms belonging to the auto space have suspended dividends amid coronavirus-led uncertainty, Cummins has maintained its payout, thus preserving shareholders' value. Notably, the company's ROE of 21.04% compares favorably with the sector's 8.67%, underscoring the management's efficiency to reward shareholders. Further, cost-containment efforts including pay cuts, discretion spending reduction and employee retrenchment are likely to offer respite to margins amid coronavirus-led low sales. Capex for 2020 is also estimated to be 25% lower than the previous year.

Cummins' efforts and investments to ramp up its capabilities in fuel cell and hydrogen production technology bode well for long term prospects.

Reasons To Sell:

- ▼ The coronavirus pandemic has crippled the auto industry, and has to decline in sales and production, hurting the manufacturer and distributor of diesel and natural gas engines, and powertrain-related component products. Such has been the wrath of coronavirus that Cummins recorded lowest quarterly sales in the second quarter of 2020. Further, the company witnessed the biggest year-over-year decline in revenues ever. While the firm expects third-quarter sales to improve sequentially, coronavirus-led uncertainty still looms large. On account of this, Cummins refrained from providing any forecast for full-year 2020.
- ▼ Orders are likely to remain weak in 2020 with continued sluggish freight activity. Industry truck production is expected to decline 20% year over year in 2020, which will adversely impact Cummins' results. Also, weak demand in China in the upcoming quarter would play a spoilsport. Notably, Cummins witnessed record levels of demand in China, with the country being the only bright spot for the firm in the second-quarter. However, demand for trucks and construction equipment in China is expected to decline in the third quarter, which will weigh on the earnings and revenues of the firm.
- ▼ The company's New Power segment is suffering from continuous losses amid high product and technology-related expenses. The trend is likely to continue, hurting the margins and cash flow of the company. As it is, cash flow from operating expenses declined 70.7% year over year during the first six months of 2020. Markedly, the engine maker reported negative cash flow of \$22 million during the recent quarter.
- ▼ Expenses are expected to increase in the coming quarters due to the launch of on-highway products that comply with emission regulation. Additionally, tariff-related commodity costs and fluctuating foreign currencies will likely hamper Cummins' margins. Unfavorable forex translations negatively impacted the revenues by 2% and 1% in the second and first quarters of 2020, respectively.

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 Q2 Earnings Beat Estimates, Down Y/Y

Cummins reported second-quarter 2020 earnings of \$1.95 per share, which surpassed the Zacks Consensus Estimate of \$0.85. Higher-than-expected contribution from Distribution, Engine and Power Systems segments led to the outperformance. EBITDA from the said segments came in at \$160 million, \$150 million and \$91 million, which topped the consensus mark of \$101 million, \$85 million and \$76 million, respectively.

The bottom line, however, declined from second-quarter 2019 earnings of \$4.27 a share amid coronavirus woes. Cummins' revenues also declined 38% year over year to \$3,852 million. However, revenues beat the Zacks Consensus Estimate of \$3,569 million.

Quarter Ending **06/2020**

Report Date	Jul 28, 2020
Sales Surprise	7.94%
EPS Surprise	129.41%
Quarterly EPS	1.95
Annual EPS (TTM)	11.52

Key Takeaways

Sales for the Engine segment declined 47.3% year over year to \$1,423 million. The segment's EBITDA declined to \$150 million (accounting for 10.5% of sales) from \$416 million (15.4% of sales) a year ago. Decline in global demand in truck and construction markets resulted in lower on- and off-highway revenues than the prior-year quarter. Sales slid in all regions served, apart from China.

Sales for the Distribution segment totaled \$1,605 million, down 20.8% year over year. Revenues from North America declined 25% and international sales were down 12% from the year-ago quarter. The segment's EBITDA fell to \$160 million (10% of sales) from \$172 million (8.5% of sales) a year ago amid lower demand and unfavorable forex translations.

Sales for the Components segment declined 37.7% from the prior-year quarter to \$1,150 million. The segment's EBITDA was \$141 million (12.3% of sales) compared with the year-ago figure of \$297 million (16.1% of sales). Sales in North America and international markets declined 55% and 9% year over year, respectively. Weak demand in Brazil, Europe and India weighed on international sales. Nonetheless, sales surged 63% year over year in China on the back of record level of truck production.

Sales for the Power Systems segment declined 35.4% from the year-ago quarter to \$777 million. The segment's second-quarter 2020 EBITDA declined to \$91 million (11.7% of sales) from \$173 million (14.4% of sales) in the year-ago period. Power generation and industrial revenues fell 37% and 33%, respectively, from a year ago. Lower demand in mining and oil/gas markets weighed on the segment's sales.

Sales for the New Power segment were \$10 million. The segment recorded EBITDA of negative \$38 million amid high product and technology-related expenses.

Cummins' cash and cash equivalents were \$1,751 million as of Jun 28, 2020, up from \$1,129 million on Dec 31, 2019. Long-term debt totaled \$1,639 million, up from \$1,576 million on Dec 31, 2019.

While the firm expects third-quarter sales to improve sequentially, coronavirus-led uncertainty still looms large. On account of this, Cummins refrained from providing any forecast for full-year 2020.

Valuation

Cummins' shares are up 11.1% in the year-to-date period and 21.3% over the trailing 12-month period. Stocks in the Zacks Automotive – Internal Combustion Engines industry and the Zacks Automotive sector are down 21.3% and up 32.2%, in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are up 11.1% and 18.6%, respectively.

The S&P 500 index is up 0.1% and 8.5% in the year-to-date period and over the past year, respectively.

The stock is currently trading at 21.31X forward 12-month earnings, which compares to 20.92X for the Zacks sub-industry, 27.05X for the Zacks sector and 22.44X for the S&P 500 index.

Over the past five years, the stock has traded as high as 21.31X and as low as 8.06X, with a 5-year median of 13.1X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$209 price target reflects 22.4X 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	21.31	20.92	27.05	22.44
	5-Year High	21.31	20.92	27.05	22.44
	5-Year Low	8.06	8.58	8.2	15.25
	5-Year Median	13.1	12.73	9.9	17.52
EV/EBITDA TTM	Current	9.23	8.95	11.57	11.95
	5-Year High	11.28	11.28	11.79	12.85
	5-Year Low	4.63	4.63	6.94	8.25
	5-Year Median	7.3	7.3	9.32	10.88
P/S F12M	Current	1.58	1.57	0.87	3.54
	5-Year High	1.58	1.57	0.87	3.54
	5-Year Low	0.74	0.85	0.49	2.53
	5-Year Median	1.13	1.14	0.61	3.02

As of 07/29/2020

Industry Analysis Zacks Industry Rank: Top 11% (28 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Penske Automotive Group, Inc. (PAG)	Outperform	3
Allison Transmission Holdings, Inc. (ALSN)	Neutral	3
American AxleManufacturing Holdings, Inc. (AXL)	Neutral	3
Daimler AG (DDAIF)	Neutral	3
Meritor, Inc. (MTOR)	Neutral	4
Mazda Motor Corporation (MZDAY)	Neutral	2
Navistar International Corporation (NAV)	Neutral	3
PACCAR Inc. (PCAR)	Neutral	3

Industry Comparison

Industry: Automotive - Internal Combustion Engines

Industry Peers

	CMI	X Industry	S&P 500	AXL	MZDAY	PCAR
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	2	3
VGM Score	A	-	-	C	B	A
Market Cap	29.34 B	8.87 B	22.69 B	905.82 M	3.82 B	29.73 B
# of Analysts	4	7	14	4	2	8
Dividend Yield	2.64%	0.68%	1.8%	0.00%	4.15%	1.49%
Value Score	B	-	-	F	A	A
Cash/Price	0.07	0.05	0.07	0.81	1.31	0.14
EV/EBITDA	8.01	5.20	13.11	16.88	1.56	7.51
PEG Ratio	3.07	2.70	3.05	NA	NA	2.34
Price/Book (P/B)	3.61	3.23	3.15	2.31	0.33	3.04
Price/Cash Flow (P/CF)	10.08	10.08	12.28	1.25	2.64	8.58
P/E (F1)	24.60	19.37	22.27	NA	NA	26.47
Price/Sales (P/S)	1.45	0.81	2.46	0.15	0.12	1.44
Earnings Yield	3.97%	5.69%	4.25%	-18.48%	-21.05%	3.78%
Debt/Equity	0.20	0.12	0.75	8.95	0.37	0.74
Cash Flow (\$/share)	19.73	1.67	6.94	6.39	1.15	10.02
Growth Score	B	-	-	A	D	B
Hist. EPS Growth (3-5 yrs)	16.19%	16.19%	10.85%	-9.73%	NA	11.45%
Proj. EPS Growth (F1/F0)	-47.56%	-27.39%	-7.70%	-191.51%	-402.38%	-52.71%
Curr. Cash Flow Growth	9.29%	-26.94%	5.31%	-19.99%	-26.16%	6.65%
Hist. Cash Flow Growth (3-5 yrs)	7.28%	9.82%	8.55%	13.70%	NA	11.72%
Current Ratio	1.42	1.07	1.31	1.68	1.43	1.32
Debt/Capital	16.78%	16.78%	44.23%	89.95%	27.03%	42.85%
Net Margin	8.46%	5.18%	10.45%	-16.69%	1.68%	7.95%
Return on Equity	21.04%	39.92%	14.99%	15.33%	5.16%	16.85%
Sales/Assets	1.00	1.39	0.53	0.89	1.23	0.75
Proj. Sales Growth (F1/F0)	-26.67%	0.00%	-1.97%	-30.42%	-22.22%	-35.43%
Momentum Score	B	-	-	D	A	A
Daily Price Chg	1.98%	1.88%	1.52%	1.91%	-4.56%	0.63%
1 Week Price Chg	2.80%	0.63%	0.37%	4.46%	-3.06%	7.94%
4 Week Price Chg	16.34%	18.02%	5.44%	10.79%	2.36%	15.81%
12 Week Price Chg	29.44%	-3.81%	15.38%	95.37%	16.28%	25.90%
52 Week Price Chg	21.27%	0.63%	-1.61%	-33.64%	-36.31%	22.60%
20 Day Average Volume	1,073,563	66,882	1,846,377	1,254,902	41,955	1,971,561
(F1) EPS Est 1 week change	1.28%	0.64%	0.00%	0.00%	0.00%	1.91%
(F1) EPS Est 4 week change	-0.61%	2.08%	0.27%	1.98%	9.29%	12.95%
(F1) EPS Est 12 week change	3.54%	1.21%	-0.85%	9.27%	27.84%	8.43%
(Q1) EPS Est Mthly Chg	1.34%	1.34%	0.13%	59.52%	10.35%	48.91%

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	B
VGM Score	A

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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