



Cummins Inc. (CMI)

Updated February 5th, 2022 by Nathan Parsh

Key Metrics

Current Price:	\$229	5 Year CAGR Estimate:	10.2%	Market Cap:	\$33 billion
Fair Value Price:	\$230	5 Year Growth Estimate:	8.0%	Ex-Dividend Date:	2/18/2022
% Fair Value:	99%	5 Year Valuation Multiple Estimate:	0.1%	Dividend Payment Date:	3/4/2022
Dividend Yield:	2.5%	5 Year Price Target	\$338	Years Of Dividend Growth:	16
Dividend Risk Score:	B	Retirement Suitability Score:	B	Last Dividend Increase:	7.4%

Overview & Current Events

Cummins, headquartered in Indiana and founded in 1919, designs, manufactures, distributes and services engines for heavy, medium and light-duty trucks. The company's products include diesel and natural gas engines, as well as hybrid and electric platforms. Cummins operates in four segments: Engines (35% of annual revenues), Distribution (26%), Components (24%) and Power Systems (15%). The company also has a small New Power segment, which focuses on electric vehicles. Roughly 60% of its business is done in the U.S. and Canada. The company employs about 60,000 people and serves customers in about 190 countries. Cummins generates ~\$26 billion in annual revenues.

Cummins announced fourth quarter and full year 2022 results on 2/3/2022. For the quarter, revenue grew 1.2% to \$5.9 billion, beating estimates by \$90 million. Net income of \$394 million, or \$2.73 per share, compared unfavorably to net income of \$501 million, or \$3.36 per share, in the prior year, and fell \$0.41 short of expectations. For the year, revenue grew 21% to \$24 billion. Net income of \$2.1 billion, or \$14.61 per share, compared favorably to net income of \$1.8 billion, or \$12.01 per share, in 2020.

For the quarter, revenues for North America declined 4%, but were offset by a 6% improvement in international markets. The Engine segment was up 4% to \$2.4 billion, led by a 5% increase in on-highway revenue. Distribution improved 3% to \$2.1 billion. North America was down 1%, but international grew 10% due to strength in Russia. Revenue for Components was down by 6% to \$1.7 billion due to a 1% drop in North America and a 12% decrease in China. Power Systems grew 10% to \$1.1 billion, as industrial revenue grew 37% on high demand from mining markets. New Power's sales were flat at \$34 million.

Leadership provided an outlook for 2022 as well. The company expects revenue to be up 6% versus 2021. Analysts expect Cummins to earn \$17.72 per share for the year, which would be a 21% increase from the prior year.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	\$8.69	\$7.91	\$9.14	\$8.92	\$8.23	\$10.63	\$13.15	\$14.48	\$12.01	\$14.61	\$17.72	\$26.04
DPS	\$1.80	\$2.25	\$2.81	\$3.51	\$4.00	\$4.21	\$4.44	\$4.90	\$5.28	\$5.60	\$5.80	\$7.40
Shares¹	190	187	182	175	168	166	163	152	149	144	144	142

Looking at the 2012 to 2021 period, Cummins grew earnings-per-share by an average compound rate of 5.9%. The growth rate has accelerated to nearly 11% over the last five year. Taking into account the long- and medium-term growth rates, we reaffirm our earnings-per-share growth rate of 8% through 2027. 2020 was a difficult one for the company, but Cummins saw a rebound in 2021. That rebound is expected to continue into the new year as well. We believe the company will see a higher than usual growth rate as the global economy recovers from the pandemic. Cummins has also benefited from an increase in worldwide emission regulations and fuel efficiency standards. When paired with the company's reliable and superior quality engines, this has afforded the company growth opportunities. This trend is likely to continue, but we believe there is a tipping point whereby the increase in standards starts to be addressed via alternative technologies, such as batteries. In turn, this could slow Cummins' growth profile as the

¹ In millions of shares

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company would either need to invest heavily in new technologies or risk falling behind. Cummins last increased its dividend 7.4% to \$1.45 for the 9/2/2021 payment.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	11.9	15.3	15.8	14.0	14.1	15.0	11.4	11.0	16.0	14.9	12.9	13.0
Avg. Yld.	1.7%	1.9%	1.9%	2.8%	3.5%	2.6%	2.9%	3.0%	2.9%	2.6%	2.5%	2.2%

Over the past decade, shares of Cummins have traded with an average price-to-earnings ratio of slightly more than 13. We believe this is a reasonable multiple considering the company's growth prospects paired with a fair amount of cyclical in earnings. Shares of Cummins have decreased \$13, or 5.4%, since our 11/2/2021 update. Using the current share price and expected earnings-per-share for the year, Cummins trades with a price-to-earnings ratio of 12.9. If shares were to trade at our target multiple by 2027, then valuation would be a 0.1% tailwind to total returns over this time period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

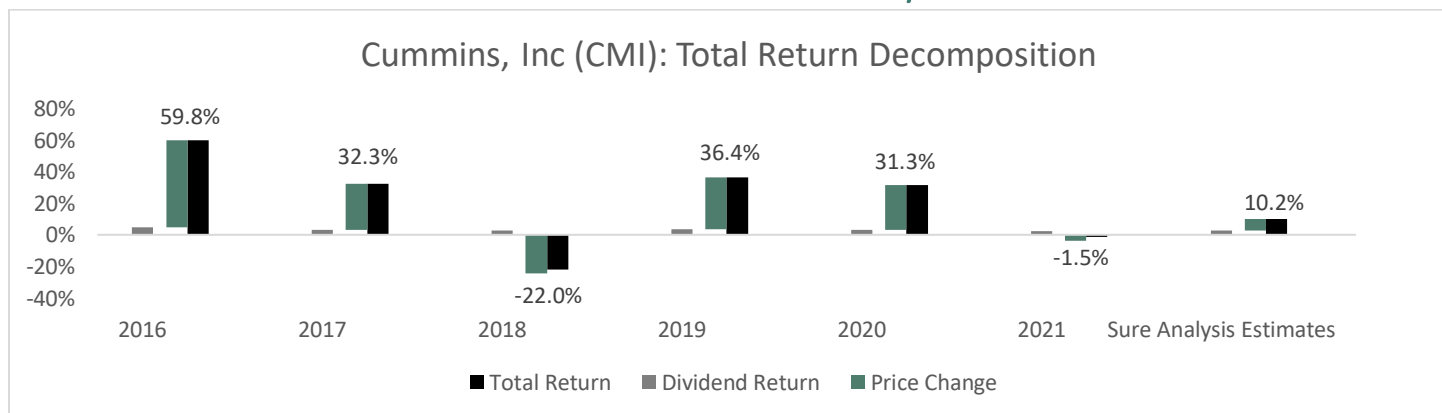
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	21%	28%	31%	39%	49%	40%	34%	33%	44%	38%	33%	28%

During the last recession Cummins posted earnings-per-share of \$4.08, \$2.47, \$5.17 and \$9.07 during the 2008 through 2011 stretch. Meanwhile, the dividend kept increasing during this time. We view this a microcosm of the business at large. That is, in lesser economic times earnings are likely to falter, but the company has the ability to recover quickly, and the dividend payout ratio is low enough to keep the payment steady. Cummins maintains a competitive advantage in its strong brand name, stemming from reliability and superior quality. In turn, the company maintains a large share of the heavy-duty engine market. Two main risks stick out: a high reliance on a few customers, namely PACCAR, Daimler, Chrysler and Navistar, which could turn to manufacturing in-house, and the potential for new technologies to disrupt or require increased investment.

Final Thoughts & Recommendation

Cummins is now projected to return a total of 10.2% annually through 2027, down from our prior estimate of 6.9%. Our projected return consists of 8% earnings growth rate, a starting yield of 2.5%, and a small contribution from multiple expansion. The company saw growth in most of its businesses during the fourth quarter and earnings-per-share were up sharply for the year. We have increased our 2027 price target \$34 to \$338 to reflect EPS estimates for the year, and now rate shares of Cummins as a buy due to projected returns.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	17334	17301	19221	19110	17509	20428	23771	23571	19811	24021
Gross Profit	4,416	4,280	4,861	4,947	4,458	5,100	5,737	5,980	4,894	5,695
Gross Margin	25.5%	24.7%	25.3%	25.9%	25.5%	25.0%	24.1%	25.4%	24.7%	23.7%
SG&A Exp.	1,808	1,817	2,095	2,092	2,099	2,429	2,437	2,454	2,125	2,374
D&A Exp.	361	407	455	514	530	583	611	672	673	
Operating Profit	1,887	1,756	2,018	2,118	1,733	1,977	2,392	2,513	1,847	2,200
Op. Margin	10.9%	10.1%	10.5%	11.1%	9.9%	9.7%	10.1%	10.7%	9.3%	9.2%
Net Profit	1,645	1,483	1,651	1,399	1,394	999	2,141	2,260	1,789	2,131
Net Margin	9.5%	8.6%	8.6%	7.3%	8.0%	4.9%	9.0%	9.6%	9.0%	8.9%
Free Cash Flow	755	1,349	1,468	1,266	1,345	1,690	1,594	2,406	2,147	1,470
Income Tax	533	531	698	555	474	1,371	566	566	527	587

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	12548	14728	15764	15134	15011	18075	19062	19737	22624	23710
Cash & Equivalents	1,369	2,699	2,301	1,711	1,120	1,369	1,303	1,129	3,401	2,592
Accounts Receivable	2,475	2,649	2,946	2,820	3,025	3,618	3,866	3,387	3,440	3,990
Inventories	2,221	2,381	2,866	2,707	2,675	3,166	3,759	3,486	3,425	4,355
Goodwill & Int. Ass.	814	818	822	810	812	2,055	2,035	2,289	2,256	2,187
Total Liabilities	5,574	6,858	7,671	7,384	7,837	9,911	10,803	11,272	13,635	14,309
Accounts Payable	1,339	1,557	1,881	1,706	1,854	2,579	2,822	2,534	2,820	3,021
Long-Term Debt	775	1,740	1,686	1,639	1,856	2,006	2,476	2,367	4,164	4,159
Shareholder's Equity	6,603	7,510	7,749	7,406	6,875	7,259	7,348	7,507	8,062	8,474
LTD/E Ratio	0.12	0.23	0.22	0.22	0.27	0.28	0.34	0.32	0.52	0.49

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	13.6%	10.9%	10.8%	9.1%	9.2%	6.0%	11.5%	11.6%	8.4%	9.2%
Return on Equity	27.2%	21.0%	21.6%	18.5%	19.5%	14.1%	29.3%	30.4%	23.0%	25.8%
ROIC	22.9%	17.1%	17.0%	14.6%	15.1%	10.4%	20.5%	21.0%	14.9%	16.0%
Shares Out.	190	187	182	175	168	166	163	152	149	144
Revenue/Share	91.39	92.31	104.99	107.11	103.40	122.10	146.01	151.00	132.96	164.64
FCF/Share	3.98	7.20	8.02	7.10	7.94	10.10	9.79	15.41	14.41	10.08

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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