Cummins Inc. (CMI)

Updated November 10th, 2023 by Nathan Parsh

Key Metrics

Current Price:	$218	**5 Year CAGR Estimate:**	14.1%	**Market Cap:**	$31 B
Fair Value Price:	$258	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date:**	11/22/23
% Fair Value:	84%	**5 Year Valuation Multiple Estimate:**	3.4%	**Dividend Payment Date:**	12/07/23
Dividend Yield:	3.1%	**5 Year Price Target**	$379	**Years Of Dividend Growth:**	18
Dividend Risk Score:	A	**Retirement Suitability Score:**	B	**Rating:**	Buy

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, Distribution, Components, Power Systems, and Accelera. 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 ~$32 billion in annual revenues.

On July 11th, 2023, Cummins raised its quarterly dividend 7% to $1.68, extending the company's dividend growth streak to 18 consecutive years.

On November 2nd, 2023, Cummins reported third quarter results for the period ending September 30th, 2023. Revenue increased 15% to $8.43 billion, which topped expectations by $250 million. Adjusted earnings-per-share of $4.73 compared to $3.21 in the prior year and was $0.04 above estimates.

For the quarter, North America sales were higher by 16% while international grew 13%. As with prior periods, growth was due to the addition of Meritor as well as continued strong demand across key global markets. Revenue for Components increased 20% to $3.2 billion, primarily due to the addition of Meritor, but global demand was high throughout the business. The Engine segment improved 5% to $2.9 billion as North American truck demand remained elevated. Price increases also aided results. Distribution grew 13% to $2.5 billion as North America and international markets were both higher by a double-digit percentage. Power Systems grew 7% to $1.4 billion as power generation and price increases more than offset weaker industrial revenue. Accelera, formerly named New Power, was up 106% to $103 million due to ongoing demand for battery electric systems.

The company reaffirmed its prior guidance for the year as well. Cummins continues to expect revenue growth of 18% to 21% for the year, up from 15% to 20% previously. The company is projected to earn $19.85 in 2023, compared to $19.95, $19.47, and $19.72 previously.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	$7.91	$9.14	$8.92	$8.23	$10.63	$13.15	$14.48	$12.01	$14.61	$15.67	***$19.85***	***$29.17***
DPS	$2.25	$2.81	$3.51	$4.00	$4.21	$4.44	$4.90	$5.28	$5.60	$6.04	***$6.72***	***$9.87***
Shares[1]	187	182	175	168	166	163	152	149	144	142	***143***	***140***

Looking at the 2013 to 2022 period, Cummins grew earnings-per-share by an average compound rate of 7.9%. The growth rate has accelerated somewhat to 8.4% over the last five year. Considering the long- and medium-term growth rates, we reaffirm our earnings-per-share growth rate of 8% through 2028. 2020 was a difficult one for the company, but Cummins saw a rebound in 2021 and 2022. That rebound is expected to continue into the current 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.

[1] In millions of shares.

Disclosure: This analyst has a long position in the security discussed in this research report.

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.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	15.3	15.8	14.0	14.1	15.0	11.4	11.0	16.0	14.9	15.5	***11.0***	***13.0***
Avg. Yld.	1.9%	1.9%	2.8%	3.5%	2.6%	2.9%	3.0%	2.9%	2.6%	2.5%	***3.1%***	***2.6%***

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 cyclicality in earnings. Shares of Cummins have decreased $19, or 8%, since our August 5th, 2023 report. Using the current share price and expected earnings-per-share for the year, Cummins trades with a price-to-earnings ratio of 11.0. If shares were to trade at our target multiple by 2028, then valuation would be a 3.4% tailwind to total returns over this period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

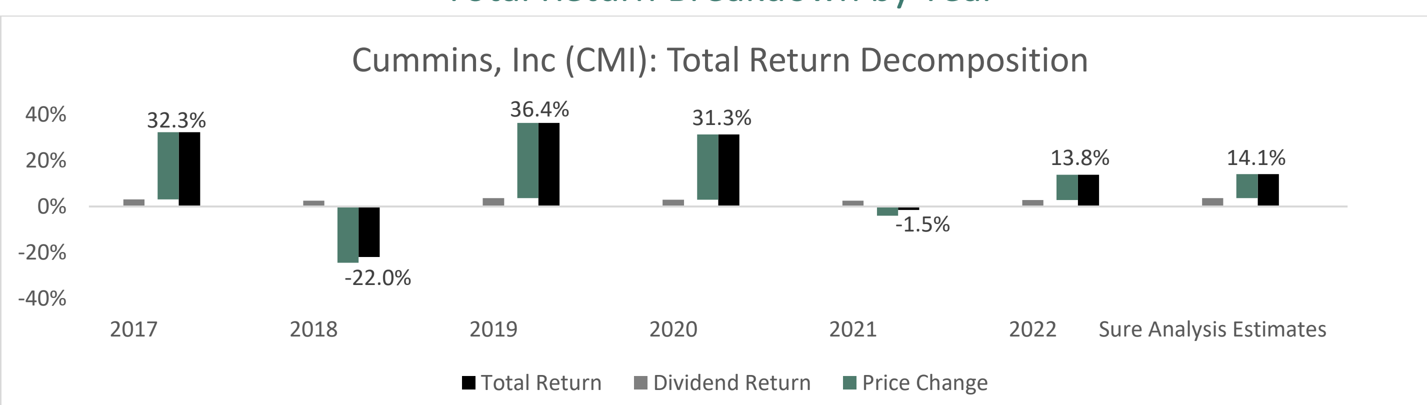
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	28%	31%	39%	49%	40%	34%	33%	44%	38%	39%	***34%***	***34%***

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 14.1% annually through 2028, up from our prior estimate of 12.3%. Our projected return consists of an 8% earnings growth rate, a starting yield of 3.1%, and a small contribution from multiple expansion. Cummins continues to see strong results in all its businesses and the company expects a record year on a number of fronts, including revenue and earnings-per-share. We have lowered our 2028 price target $2 to $379 due to earnings estimates for the year, but Cummins continues to earn a buy recommendation due to projected returns.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	17301	19221	19110	17509	20428	23771	23571	19811	24021	28074
Gross Profit	4,280	4,861	4,947	4,458	5,100	5,737	5,980	4,894	5,695	6,719
Gross Margin	24.7%	25.3%	25.9%	25.5%	25.0%	24.1%	25.4%	24.7%	23.7%	23.9%
SG&A Exp.	1,817	2,095	2,092	2,099	2,429	2,437	2,454	2,125	2,374	2,687
D&A Exp.	407	455	514	530	583	611	672	673	662	784
Operating Profit	1,756	2,018	2,118	1,733	1,977	2,392	2,513	1,847	2,200	2,580
Op. Margin	10.1%	10.5%	11.1%	9.9%	9.7%	10.1%	10.7%	9.3%	9.2%	9.2%
Net Profit	1,483	1,651	1,399	1,394	999	2,141	2,260	1,789	2,131	2,151
Net Margin	8.6%	8.6%	7.3%	8.0%	4.9%	9.0%	9.6%	9.0%	8.9%	7.7%
Free Cash Flow	1,349	1,468	1,266	1,345	1,690	1,594	2,406	2,147	1,470	1,046
Income Tax	531	698	555	474	1,371	566	566	527	587	636

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	14728	15764	15134	15011	18075	19062	19737	22624	23710	30299
Cash & Equivalents	2,699	2,301	1,711	1,120	1,369	1,303	1,129	3,401	2,592	2,101
Accounts Receivable	2,649	2,946	2,820	3,025	3,618	3,866	3,387	3,440	3,990	5,202
Inventories	2,381	2,866	2,707	2,675	3,166	3,759	3,486	3,425	4,355	5,603
Goodwill & Int. Ass.	818	822	810	812	2,055	2,035	2,289	2,256	2,187	5,030
Total Liabilities	6,858	7,671	7,384	7,837	9,911	10,803	11,272	13,635	14,309	20,074
Accounts Payable	1,557	1,881	1,706	1,854	2,579	2,822	2,534	2,820	3,021	4,252
Long-Term Debt	1,740	1,686	1,639	1,856	2,006	2,476	2,367	4,164	4,159	7,855
Shareholder's Equity	7,510	7,749	7,406	6,875	7,259	7,348	7,507	8,062	8,474	8,975
LTD/E Ratio	0.23	0.22	0.22	0.27	0.28	0.34	0.32	0.52	0.49	0.88

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	10.9%	10.8%	9.1%	9.2%	6.0%	11.5%	11.6%	8.4%	9.2%	8.0%
Return on Equity	21.0%	21.6%	18.5%	19.5%	14.1%	29.3%	30.4%	23.0%	25.8%	24.7%
ROIC	17.1%	17.0%	14.6%	15.1%	10.4%	20.5%	21.0%	14.9%	16.0%	13.6%
Shares Out.	187	182	175	168	166	163	152	149	144	142
Revenue/Share	92.31	104.99	107.11	103.40	122.10	146.01	151.00	132.96	164.64	197.29
FCF/Share	7.20	8.02	7.10	7.94	10.10	9.79	15.41	14.41	10.08	7.35

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