

# Stock Pitch: Cummins Inc. (CMI)

**Target Price: \$293 (33% Upside)**

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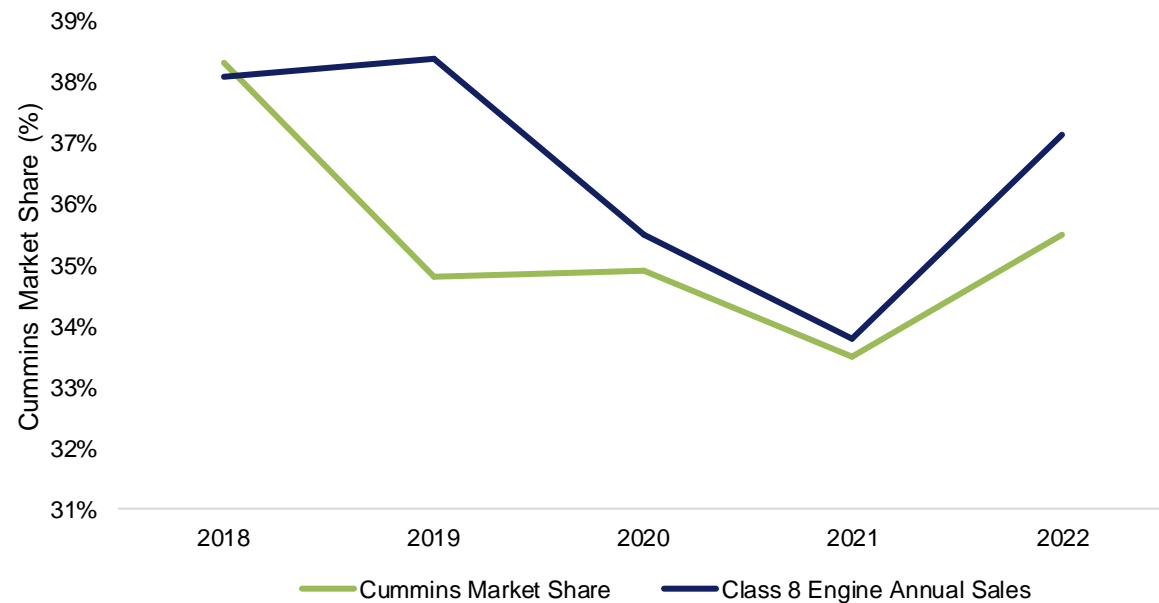
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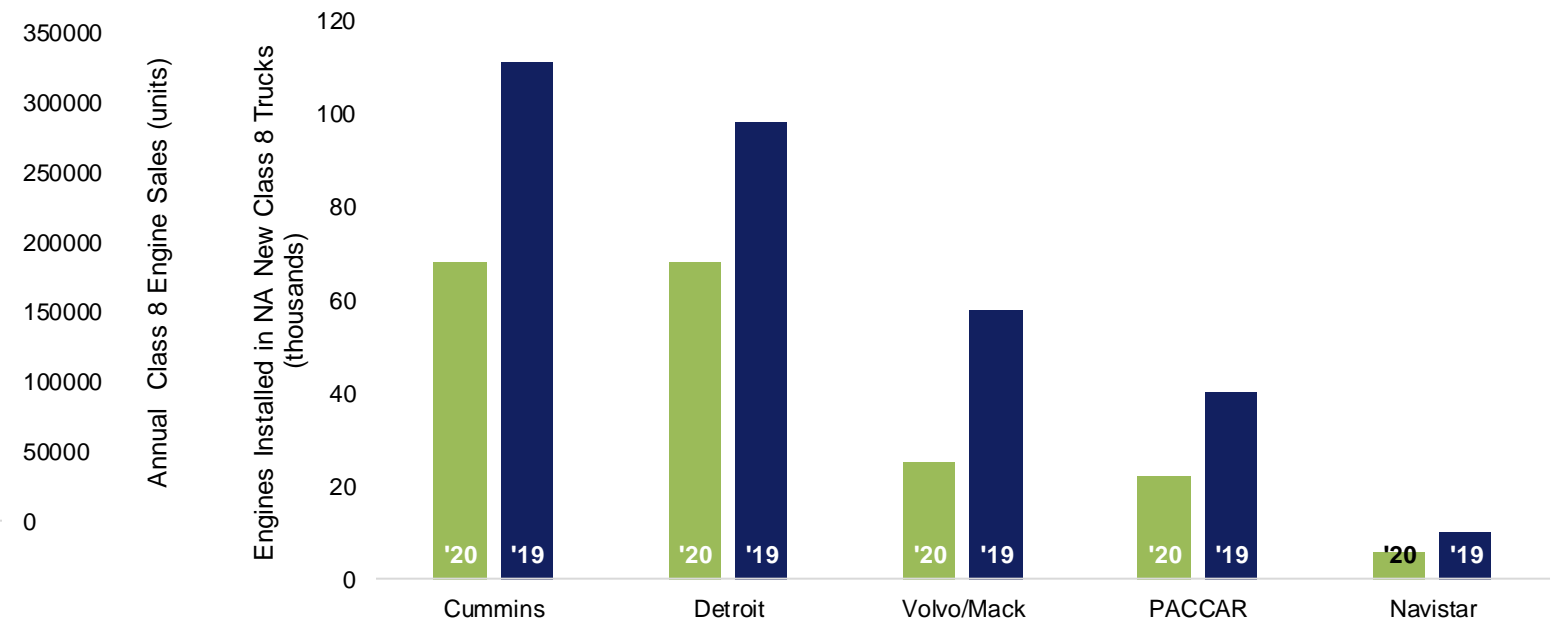
Cummins has exposure to many end markets in the mobility, power, and industrials sector

<b>Automotive Powertrain</b> <b>\$752.3B</b> Market size in 2022 <b>9.6%</b> CAGR through 2030 <b>Engines</b>	<b>Industrial Filtration</b> <b>\$32.88B</b> Market size in 2022 <b>6.89%</b> CAGR through 2031 <b>Components</b>	<b>Industrial Engines</b> <b>\$48.12B</b> Market size in 2021 <b>6.13%</b> CAGR through 2030 <b>Power Systems</b>	<b>EV Powertrain</b> <b>\$7.99B</b> Market size in 2018 <b>28.5%</b> CAGR through 2026 <b>New Power</b>	<b>Green Hydrogen</b> <b>\$2.14B</b> Market size in 2021 <b>51.6%</b> CAGR through 2031 <b>New Power</b>
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**Cummins Market Share Holding Steady**

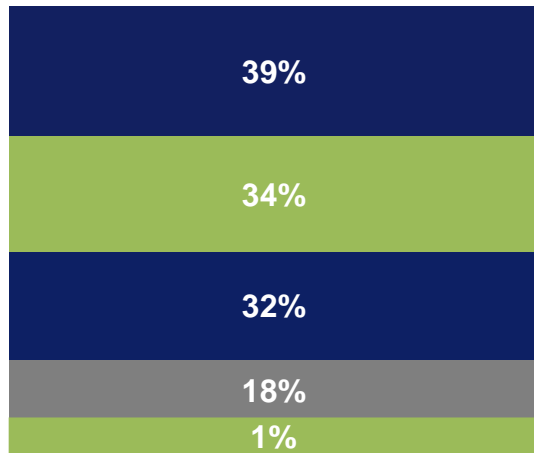


**Cummins Dominating Market Share**

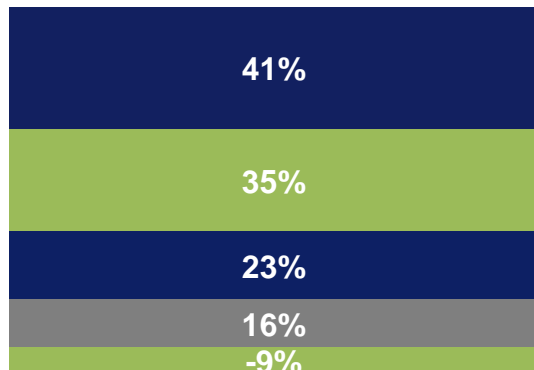


Diverse range with deep domain expertise

## Segmentation by Revenue

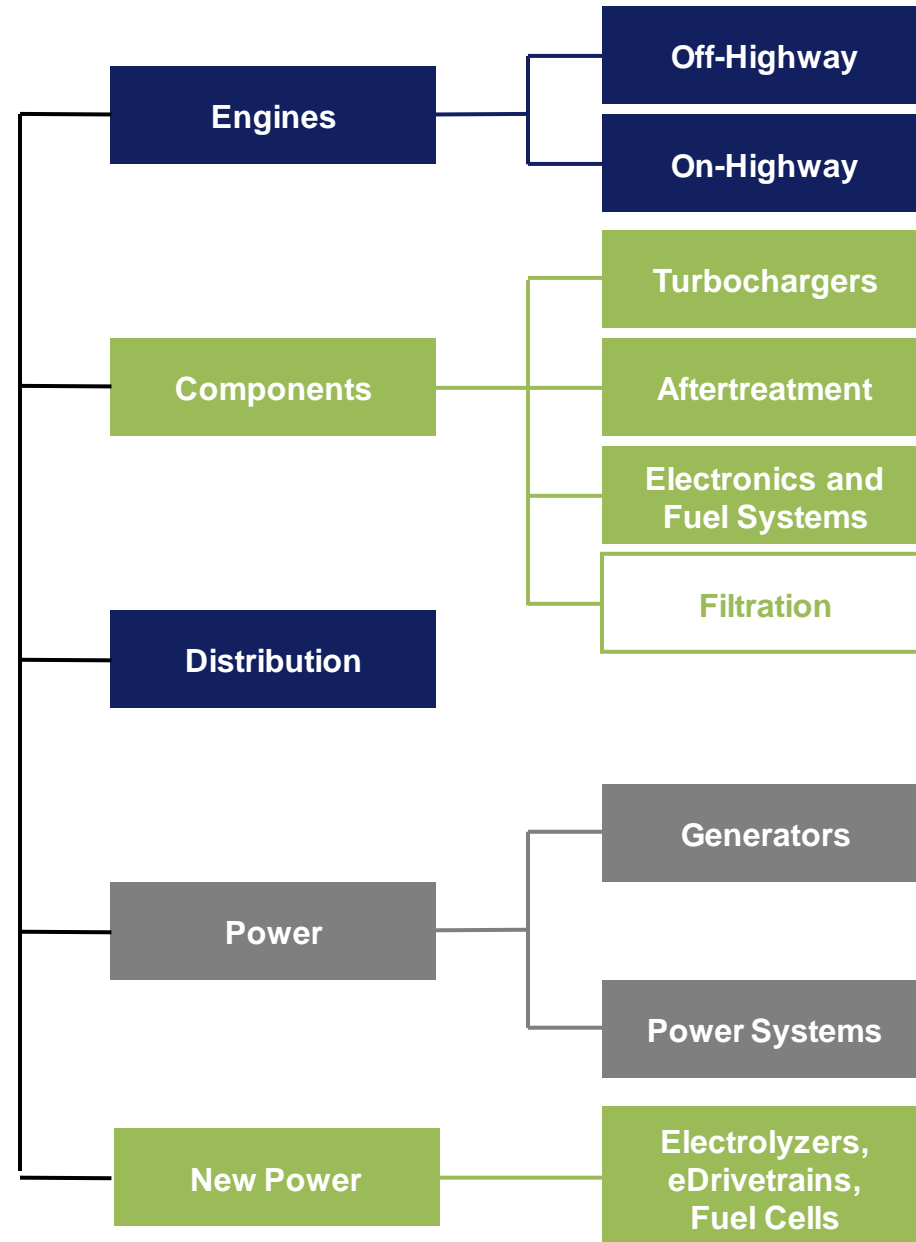


## Segmentation by EBITDA



- Engine
- Components
- Distribution
- Power Systems
- New Power

- Engine
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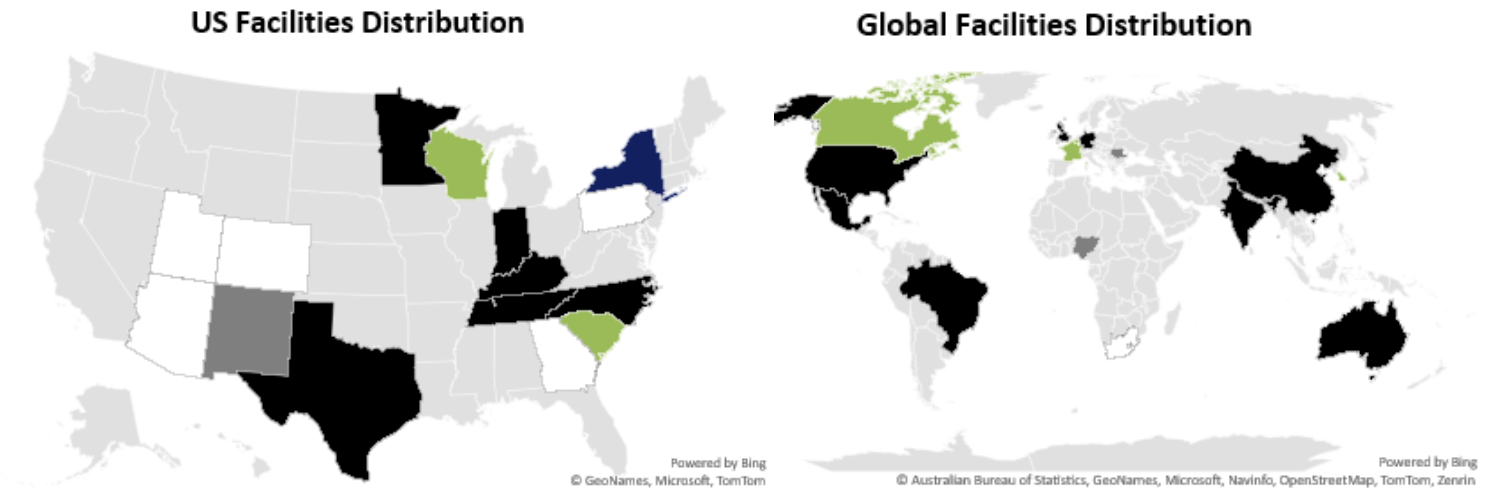
### Financial Metrics

- Market capitalization: \$31.65B
- Revenue: \$28.1B
- EBITDA: \$3.8B (13.5% margin)
- Net Income: \$2.2B
- Diluted EPS: \$15.12
- Current Price: \$220.33 (as of 4/8/2023)
- Median Analyst Target Price: \$258.41, Upside 17.3%

### Key Events

- Apr 2023: President Biden visits Minnesota factory. Reshoring manufacturing including electrolyzers
- Mar 2023: S-1 Filed for Atmus Technologies—filtration business
- Mar 2023: Rebranding of New Power segment to Accelera
- Dec 2022: Electrolyzer backlog tripled YoY to \$300m
- Nov 2022: Meritor acquisition of Siemen’s Commercial Vehicle unit
- Aug 2022: Cummins acquisition of Meritor
- Jan 2022: Introduction of Destination Zero business strategy

### Plants and Factories



### Joint Ventures

Equity Income in millions	2022		2021		2020	
<b>Manufacturing entities</b>						
Dongfeng Cummins engine Company	\$ 45	20%	\$ 82	19%	\$ 63	17%
Beijing Foton Cummins Engine Co.	37	17%	112	19%	113	30%
Chongqing Cummins Engine Company	32	14%	39	19%	35	9%
Tata Cummins	27	12%	18	19%	19	5%
All other manufactureres	28	12%	131	19%	115	30%
<b>Distribution entities</b>				19%		
Komatsu Cummins Chile	44	20%	32	19%	31	8%
All other distributors	11	5%	10	19%	2	1%
Cummins share of net income	\$ 224	100%	\$ 424	152%	\$ 378	100%

### Engines



Brands

Customers

Customer-Competitors

### Components



### New Power



Brands

### Power Systems



Customers





<b>Threat of New Entrants</b>	Low
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- CAPEX requirements for entering powertrain and industrial manufacturing are high, especially due to stringent emissions regulations
- Even if there are new entrants in the transport equipment manufacturing industry, they are likely to become Cummins' customer or partner through a JV

<b>Bargaining Power of Buyers</b>	Medium
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- Global customer base and distribution network ranging from OEMs to distributors and dealers prevent overdependence on any single group of buyers
- Strong relationships built with top four customers (comprising 36% of sales) that outsource their manufacturing to Cummins

<b>Bargaining Power of Suppliers</b>	Low
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- Diversified product portfolio from engines and generators to components and new power technology mitigates supply risks in a single market
- Vertical integration gives Cummins control of their supply chain and manufacturing network

<b>Threat of Substitute Products</b>	Low
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- ICEs, for the near future, remain irreplaceable for various applications, especially long-haul trucking. Regardless, Cummins is ahead of the curve with transitioning to new platforms
- Strong recurring revenue from aftermarket products, especially those linked to mileage e.g. filtration products

<b>Rivalry Among Existing Competitors</b>	Medium
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- Cummins' global footprint exposes them to a lot of competition, but their international JVs strategy has allowed for successful penetration of fragmented markets e.g. China
- Many major competitors are loyal customers with strong relationships. For example, PACCAR, their largest competitor, has been with them for 78 years due to superior quality



## Cummins has a growing opportunity set with a disciplined management team

### **Growth potential in fuel-agnostic ICEs and electric powertrains**

- Management team has efficiently allocated capital towards fairly-priced acquisitions, such as Meritor and Siemen's Commercial Vehicle business, that add onto their full suite of product offerings
- Versatile fuel agnostic engines allow for flexibility under increasingly stringent emissions regulations and provide cost synergies to customers

### **Unique ability to indirectly capture market share through loyal customer-competitor base**

- Long-term relationships and established partnerships with competitors unlocks recurring revenue with high switching costs for customers
- Cummins is the go-to engine manufacturer in China, the largest truck market in the world, supported by their joint ventures with local Chinese firms

### **Head start in electrolyzer & fuel cell technologies through acquisition of Hydrogenics in 2019**

- Far-sighted business development paired with strong order backlog and extensive manufacturing capacity
- Joint effort on Hydrogenics with Air Liquide and growing flagship projects (e.g. 90MW Varennes Carbon Recycling plant backed by Suncor and Shell)
- Potential to eventually spin-off New Power business at considerably high multiple

### **"Once-in-a-generation" management talent coupled with strong policy support**

- Jennifer Rumsey (CEO) has spent two decades at Cummins in numerous roles, starting as an engineer. She now leads the company with a strong passion for building high performance teams and serving customers. Under her leadership, we believe the company will continue to compound value for shareholders
- Proven manufacturing success will continue to grow under the tailwinds of IRA, as President Biden's recent visit to the Fridley Power Systems facility endorses Cummins' leadership and ability to reshore manufacturing to strengthen supply chains

### **Atmus Technologies (filtration products) spin-off to increase total return to CMI shareholders**

- While Cummins will still own 80+% of the new publicly traded entity, Atmus is expected to raise north of \$300m in equity and is likely to trade at a higher multiple
- Eventual share exchange between Cummins and Atmus will reduce outstanding share count, increasing existing shareholders' ownership percentage



# Event Path

Spring 2023 |  
Annual General Meeting

Milestones to be on track with projections and carry out value

1. Receive EPA approval for its fuel cell and hydrogen platform for commercial trucks and roll out fuel-agnostic platform in 2026, a year before stringent EPA emissions regulations take effect

2. Successful integration of Meritor into components business meeting lower 2023 target range of 10.3% EBITDA margin and \$4.5 billion revenue contribution plus successful IPO of Atmus Technologies by end of 2023

3. New Power segment to reach positive EBITDA by 2027 and grow revenue at 40% compound annual growth rate to hit \$1B (RNEF) revenue target in 2026 and \$4B (RNEF) revenue target in 2031

4. Continue to capture at least 33% of Class 8 engine sales through 2025 and maintain robust relationships with key customers to maintain current indirect market share

5. ROIC to remain above 15% target and debt taken on Meritor and Atmus to be steadily paid off to reduce leverage ratio by end of 2024 to historical levels (~2.7x Assets/Equity)

### Revenue Growth

- Management expectations of New Power segment to hit \$6bn seems overly aggressive; if other electrolyzer manufacturers improve their technology and cost curves quicker than Cummins, the revenue growth case would be much weaker
- Global economic slowdown due to increasing interest rates and fear of systemic risk might cause poor GDP numbers for 2023 and 2024, leading to less demand in legacy engines business

### Margins

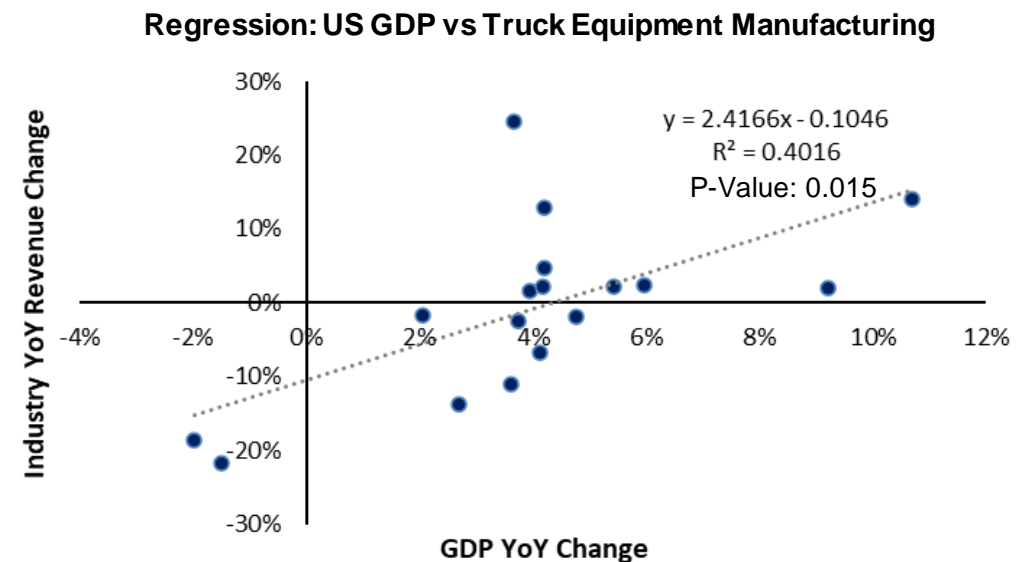
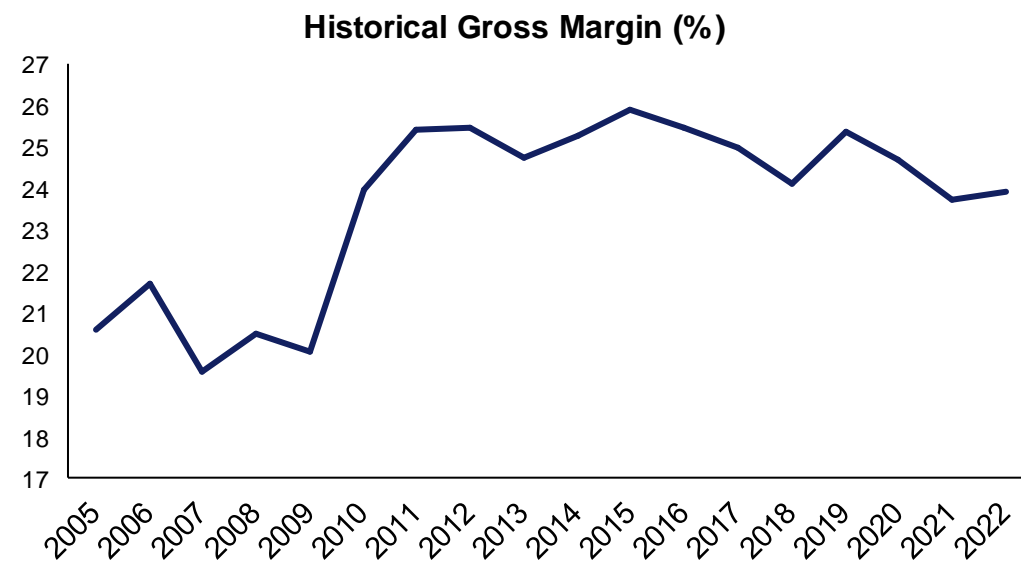
- Supply chain issues and growth efforts in New Power business have led to declining overall margins over the last five years
- New Power business has a long way to go before breaking even on EBITDA basis in 2027

### ROIC

- Aggressive capital deployment in domestic manufacturing expansion and inorganic New Power opportunities may lead to capital destruction

### WACC

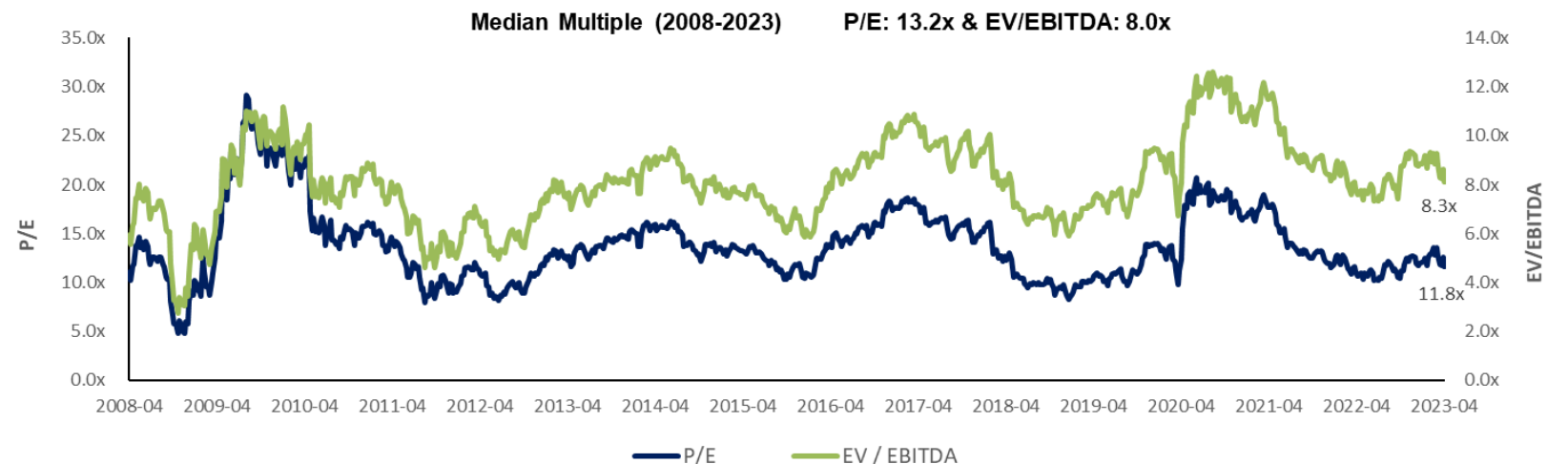
- Recall risk could spook investors as seen by recent recall covering 340k Dodge Ram pickups targeting 2021-2023 models due to overheating concerns on intake heater-grid relays



Comps Tables - FactSet RBICS Sub-Sector - Transportation Equipment Manufacturing (Market Cap Larger than \$10bn)

Company Name	Enterprise Value	EBITDA Margin (%)	ROIC (%)	PEG			Price to			Sales 5 Year Growth	Capital Expenditures 5 Yr Growth	23'-25' Sales Growth	23'-25' EBITDA Growth	Total Return 5 Year (%)	Total Return 10 Year (%)	
				Ratio (x)	P/E (x)	P/BV (x)	FCF Actual (x)	EV/ EBITDA (x)	EV/ Sales (x)							EBITDA 5 Yr Growth
Cummins	38,181.2	12.4%	16.4%	1.06x	14.58x	3.47x	29.97x	11.01x	1.36x	37.9	37.4	56.0	4.01%	10.38%	56.48%	144.53%
PACCAR	40,999.0	15.5%	16.9%	3.32x	17.86x	4.07x	32.86x	9.15x	1.42x	30.5	48.1	-24.7	-0.42%	-6.22%	78.90%	184.05%
Wabtec	21,218.7	18.4%	4.4%	1.61x	27.83x	1.73x	19.81x	13.76x	2.54x	120.4	115.4	66.5	3.58%	5.60%	23.42%	129.52%
Daimler Truck Holding	41,160.6	9.4%	8.8%	1.33x	9.24x	1.21x	-	8.22x	0.77x	-	-	-	2.67%	8.40%	-	-
Volvo B	50,234.2	14.9%	12.0%	2.11x	11.56x	2.39x	29.58x	7.18x	1.07x	29.5	19.4	13.4	-1.47%	-2.02%	41.14%	91.58%
Knorr-Bremse	12,058.5	14.4%	11.9%	2.58x	20.48x	3.84x	30.88x	11.16x	1.60x	0.1	6.8	76.8	4.43%	9.41%	-	-
CRRC H	29,938.5	8.5%	7.2%	-	9.82x	0.76x	6.50x	10.75x	0.91x	0.1	7.3	-14.4	4.11%	9.33%	-15.08%	-6.70%
Weichai Power H	19,642.4	-	4.5%	0.41x	19.26x	1.37x	29.49x	-	0.77x	-	23.0	133.5	7.84%	-	45.13%	76.02%
China Shipbuilding Ind A	8,009.4	-	-1.1%	-	-	1.09x	-	-	1.30x	-	-4.4	6.1	-	-	-34.69%	-22.71%
Zhuzhou CRRC	11,418.6	16.8%	7.5%	-	19.43x	1.49x	35.50x	25.57x	4.29x	5.1	19.8	120.6	10.24%	11.17%	-4.89%	37.66%
China CSSC A	12,478.6	-	2.2%	-	78.76x	2.28x	-	-	1.37x	-	283.7	2,980.1	7.26%	-	5.58%	-7.92%
Ford Otomotiv Sanayi	12,442.4	11.3%	55.5%	3.59x	9.77x	9.58x	15.82x	10.63x	1.20x	109.3	49.0	163.0	23.86%	19.62%	126.48%	186.39%
<b>Average</b>		<b>13.5%</b>	<b>12.2%</b>	<b>2.00x</b>	<b>21.69x</b>	<b>2.77x</b>	<b>25.60x</b>	<b>11.94x</b>	<b>1.55x</b>	<b>41.6</b>	<b>55.1</b>	<b>325.2</b>	<b>6.01%</b>	<b>7.30%</b>	<b>32.25%</b>	<b>81.24%</b>
<b>Median</b>		<b>14.4%</b>	<b>8.2%</b>	<b>1.86x</b>	<b>17.86x</b>	<b>2.00x</b>	<b>29.58x</b>	<b>10.75x</b>	<b>1.33x</b>	<b>30.0</b>	<b>23.0</b>	<b>66.5</b>	<b>4.11%</b>	<b>9.33%</b>	<b>32.28%</b>	<b>83.80%</b>

- ROIC and historical (5-year) EBITDA and Sales growth are well above the median which is validated by the top quartile total return over last decade
- Analysts projected that EBITDA growth over the next two years is slightly above industry median and noticeably above its closest peer, PACCAR
- As the leading diesel engine manufacturer, why is Cummins trading under the median P/E for its generic comp set?
- Undervalued on historical basis





# Comparable Companies

## Sum of the Parts Valuation

- Distribution is a tough segment to value, but it is capital light (low operating leverage) and has had low volatility in earnings which is why it deserves the highest multiple. Distribution set had a median EV/EBITDA multiple of 15x, so we adjusted it down to 12x
- Most analysts value Cummins on a P/E basis, but we believe that fails to capture the growth tilt in their New Power business
- We utilize extremely conservative revenue growth and EBITDA margin figures to calculate the implied value of each segment

\$ in millions

Sum Of The Parts Valuation												
	Revenue'22	EBITDA'22	Margin'22	Revenue Growth	Revenue'23	EBITDA'23	Margin'23	Revenue Multiple	EBITDA Multiple	Implied Value		
<b>Engines</b>	\$ 10,945	\$ 1,541	14.08%	0.00%	\$ 10,945	\$ 1,510	13.8%		7.50x	\$ 11,328		
<b>Components</b>	\$ 9,736	\$ 1,346	13.82%	28.00%	\$ 12,462	\$ 1,720	13.8%		9.80x	\$ 16,854		
<b>Distribution</b>	\$ 8,929	\$ 888	9.95%	2.00%	\$ 9,108	\$ 938	10.3%		12.00x	\$ 11,257		
<b>Power Systems</b>	\$ 5,033	\$ 596	11.84%	5.00%	\$ 5,285	\$ 634	12.0%		11.00x	\$ 6,976		
<b>New Power</b>	\$ 198	\$ (340)	-171.72%	76.77%	\$ 350	\$ (390)	-111.4%	6.39x		\$ 2,237		
<b>Engines</b>										Total Implied Enterprise Value	\$ 48,651	
<b>Components</b>										Net Debt	\$ 5,782	
<b>Power Systems</b>										Non-Controlling Interests	\$ 1,250	
<b>New Power</b>										Investments in Unconsolidates Subs	\$ 1,759	
<b>Distribution</b>										Implied Equity Value	\$ 43,378	
Weichai Power H	Donaldson	Caterpillar	Proterra	Advance Auto Parts							Current Equity Value	\$ 31,149
TRATON	Parker-Hannifin	Generac	Ballard Power Systems	O'Reilly Automotive							<b>Upside</b>	<b>39.26%</b>
DEUTZ	BorgWarner	Mitsubishi Heavy	NEL	AutoZone								
PACCAR	DENSO	NIDEC	Plug Power	Genuine Parts								
Volvo B	Allison Transmiss		BYD A	CarParts.com								
CNH Industrial			ITM Power	Uni-Select								
Isuzu Motors				PARTS ID A								
Ford Motor				Icahn Enterprises								



# Intrinsic Valuation

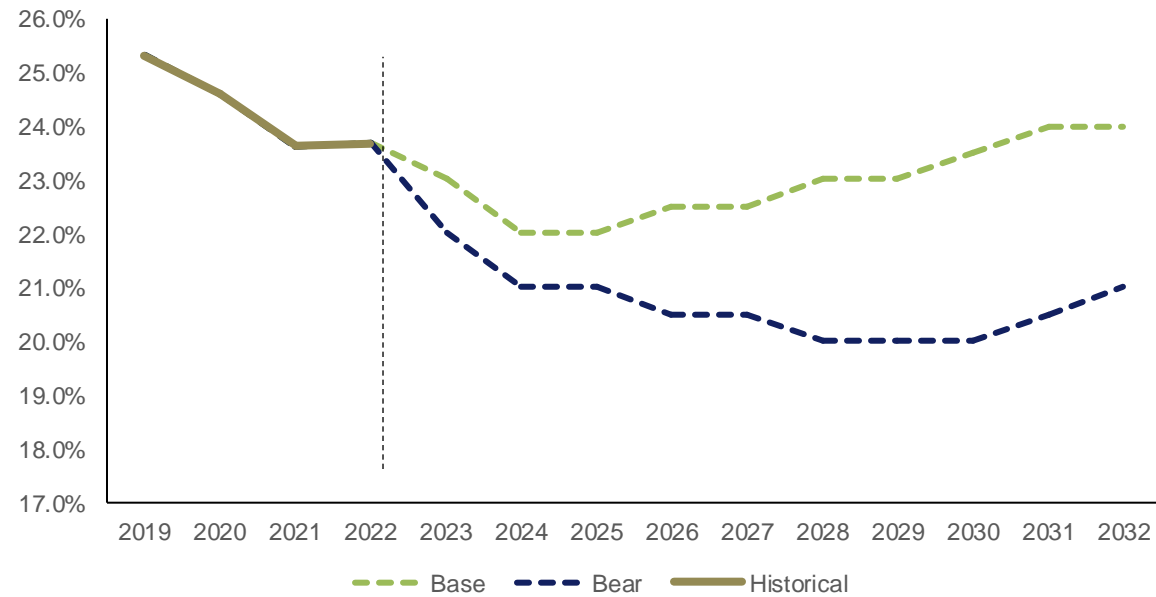
## DCF projections and template walkthrough

3. Projection Assumptions																
3.1. Revenue		Scenario		3	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032		
<b>CAGR Analysis</b>		<b>1) Total Base</b>			11.6%	2.4%	4.6%	4.5%	4.5%	4.5%	4.0%	4.0%	4.0%	3.5%		
		<b>2) Total Bear</b>		<b>Sales Growth</b>	5%	-1%	2%	3%	3%	3%	3%	3%	3%	3%		
		<b>3) Segment Base</b>		<i>Distribution</i>	2%	2%	2%	2%	2%	2%	2%	2%	2%	2%		
				<i>Engine</i>	1%	1%	1%	1%	1%	1%	1%	1%	1%	1%		
				<i>Components</i>	28%	5%	4%	3%	3%	3%	3%	3%	3%	3%		
				<i>Power Systems</i>	5%	4%	3%	3%	3%	3%	3%	3%	3%	3%		
				<i>New Power</i>	82%	70%	60%	50%	40%	30%	30%	25%	25%	20%		
<b>Total Sales</b>		4.2%	3.3%													
		<b>4) Segment Bear</b>		<i>Distribution</i>	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%		
				<i>Engine</i>	-1%	0%	0%	0%	0%	0%	0%	0%	0%	0%		
				<i>Components</i>	20%	3%	3%	3%	3%	3%	3%	3%	3%	3%		
				<i>Power Systems</i>	2%	2%	2%	2%	2%	2%	2%	2%	2%	2%		
				<i>New Power</i>	60%	40%	30%	25%	20%	20%	15%	15%	10%	10%		
<b>3.2. Expenses</b>																
<b>As % of Revenues, IS</b>		Average	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
1) Gross Margin Base		24.3%	25.3%	24.6%	23.6%	23.7%	23.0%	22.0%	22.0%	22.5%	22.5%	23.0%	23.0%	23.5%	24.0%	24.0%
2) Gross Margin Bear		24.3%	25.3%	24.6%	23.6%	23.7%	22.0%	21%	21%	21%	21%	20%	20%	20%	21%	21%
D&A		2.9%	2.8%	3.4%	2.8%	2.8%	2.8%	2.8%	2.8%	2.8%	2.8%	2.7%	2.7%	2.7%	2.7%	2.7%
SGA		10.1%	10.4%	10.7%	9.9%	9.6%	9.5%	9.5%	9.5%	9.5%	9.5%	9.0%	9.0%	9.0%	9.0%	9.0%
Research and Development		4.5%	4.2%	4.6%	4.5%	4.6%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%
1) Satutory TR		21.0%	21%	21%	21%	21%	21%	21.0%	21.0%	21.0%	21.0%	21.0%	21.0%	21.0%	21.0%	21.0%
2) Effective TR		21.4%	19.0%	22.5%	21.3%	22.6%	22.6%	22.6%	22.6%	22.6%	22.6%	22.6%	22.6%	22.6%	22.6%	22.6%
<b>As % of Revenues, CF</b>																
Change in WC		0.42%	-1.43%	-2.44%	2.28%	3.28%	0.00%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%	0.20%
CAPEX		3.0%	3.0%	2.7%	3.1%	3.3%	5.5%	5.5%	5.5%	4.5%	4.0%	4.0%	3.0%	3.0%	3.0%	3.0%
CAPEX % Should be > D&A%			✓	✗	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓

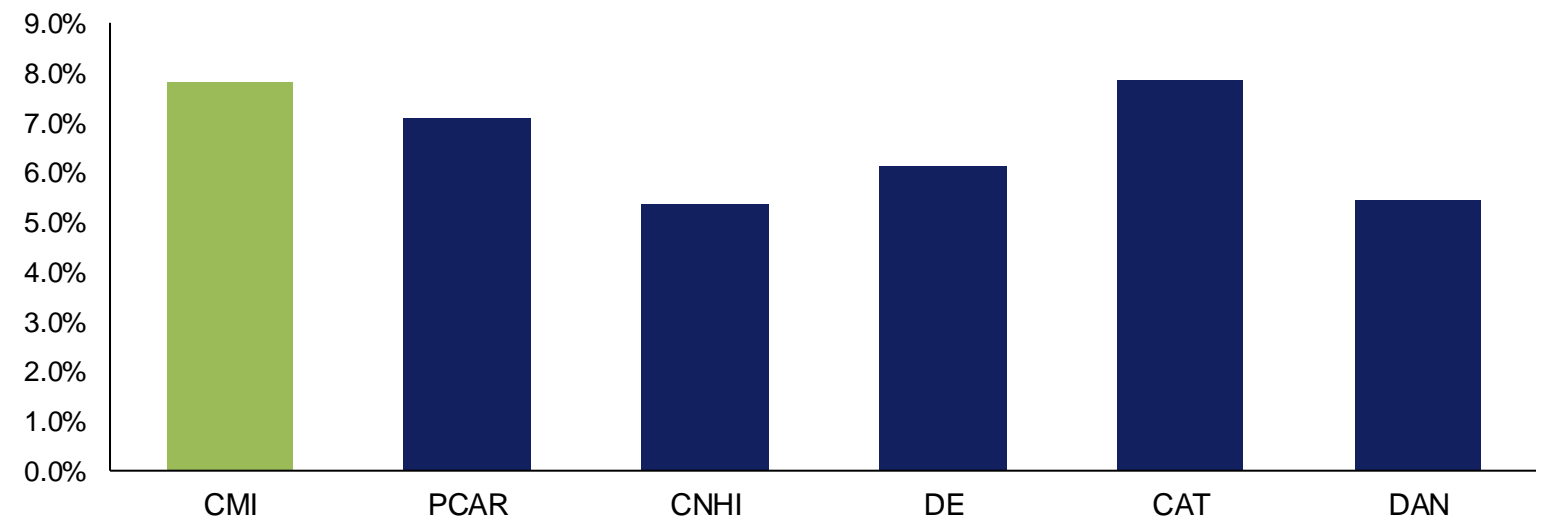
Revenue Projection Analysis			Base Case
	Historical (5Y)	Projected (10Y)	Sales Growth
Distribution	2.7%	2.0%	1.2x
Engine	1.2%	1.0%	1.1x
Components	10.1%	5.6%	1.7x
Power Systems	3.0%	3.3%	1.4x
New Power	132.7%	41.8%	32.9x
			0
Total Sales	4.2%	3.3%	1.3x

Revenue Projection Analysis			Bear Case
	Historical (5Y)	Projected (10Y)	Sales Growth
Distribution	2.7%	0.2%	1.0x
Engine	1.2%	0.1%	1.0x
Components	10.1%	5.3%	1.7x
Power Systems	3.0%	2.3%	1.3x
New Power	132.7%	25.3%	9.5x
			0
Total Sales	4.2%	1.1%	1.1x

Margin Scenarios



WACC



Base Case				
Terminal Growth Rate	Sensitivity Analysis			
	Terminal Rate	Terminal Val	As % of EV	
Implied Enterprise Value	51,810			
(+) Cash	2,573.00	1.5%	\$ 29,174.54	63%
(-) Debt	4,866	2.0%	\$ 31,844.71	65%
Implied Equity Value	49,517	2.5%	\$ 35,018.46	68%
Shares outstanding	141.4	3.0%	\$ 38,853.10	70%
Implied Share Price	<b>\$350.25</b>	3.5%	\$ 43,579.04	72%
Implied Upside/Downside	<b>59%</b>	4.0%	\$ 49,547.90	75%

Sensitivity Table		Current Price: \$220.33			
		Terminal Growth Rate			
		2.5%	3.0%	3.5%	4%
WACC	8.0%	\$ 335.94	\$ 360.66	\$ 390.86	\$ 428.62
	9.0%	\$ 277.08	\$ 293.16	\$ 312.16	\$ 334.96
	10.0%	\$ 234.19	\$ 245.22	\$ 257.94	\$ 272.78
	11.0%	\$ 201.61	\$ 209.47	\$ 218.38	\$ 228.57

Bear Case				
Terminal Growth Rate	Sensitivity Analysis			
	Terminal Rate	Terminal Val	As % of EV	
Implied Enterprise Value	33,496			
(+) Cash	2,573.00	1.5%	\$ 18,113.95	61%
(-) Debt	4,866	2.0%	\$ 19,771.81	63%
Implied Equity Value	31,203	2.5%	\$ 21,742.33	65%
Shares outstanding	141.4	3.0%	\$ 24,123.19	67%
Implied Share Price	<b>\$220.71</b>	3.5%	\$ 27,057.44	70%
Implied Upside/Downside	<b>0%</b>	4.0%	\$ 30,763.40	72%

Sensitivity Table		Current Price: \$220.33			
		Terminal Growth Rate			
		2.5%	3.0%	3.5%	4%
WACC	8.0%	\$ 211.79	\$ 227.13	\$ 245.89	\$ 269.33
	9.0%	\$ 175.08	\$ 185.06	\$ 196.85	\$ 211.01
	10.0%	\$ 148.28	\$ 155.13	\$ 163.02	\$ 172.24
	11.0%	\$ 127.89	\$ 132.77	\$ 138.31	\$ 144.63



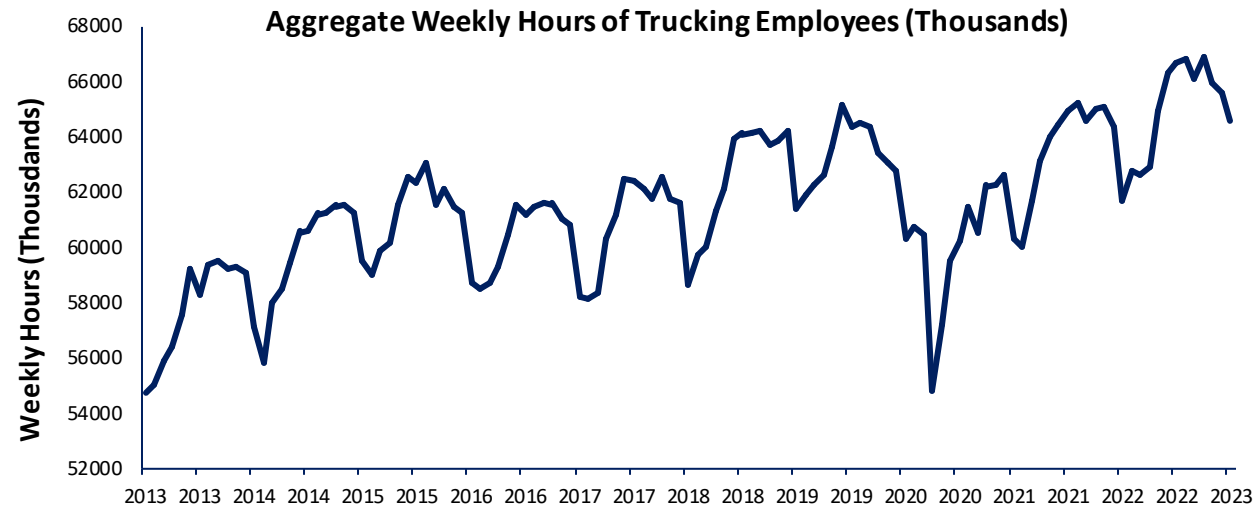


# Scenario Analysis

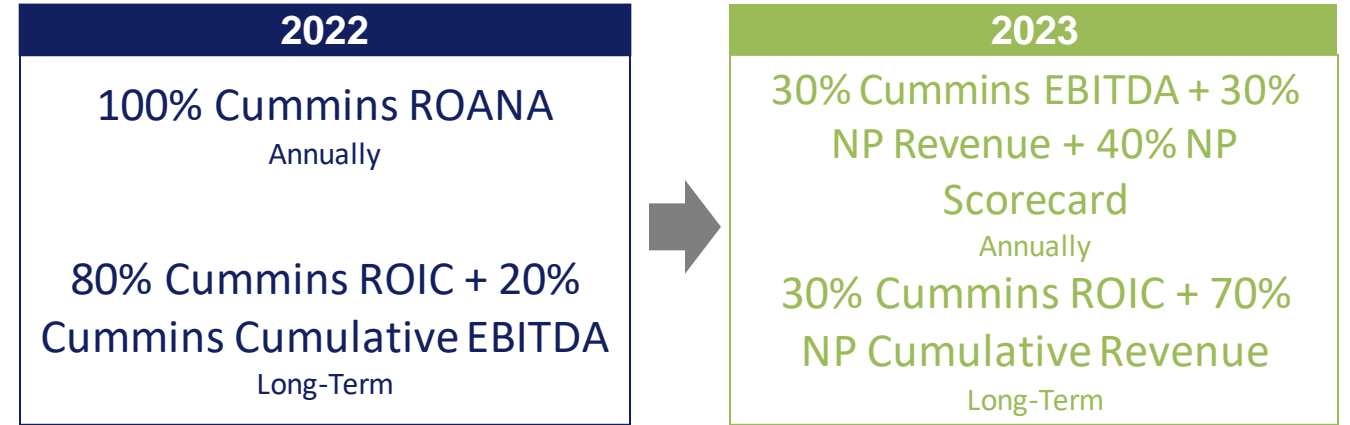
Summing up our valuations

Cummins Valuation Summary	Value	Upside/Downside	Weight
<b>DCF</b>			
Base Case	\$350.25	59.0%	35.0%
Bear Case	\$220.71	0.2%	25.0%
<b>Multiples Valuation</b>			
Peers (SOTP)	\$306.83	39.3%	20.0%
Peers (Generic)	\$269.49	22.3%	20.0%
<b>Analyst Targets</b>			
Mean	\$259.64	17.8%	0.0%
Median	\$264.00	19.8%	0.0%
<b>Target Price</b>	<b>\$293.03</b>	<b>33.0%</b> ✓	<b>1</b>

## More Trucking Demand To Come

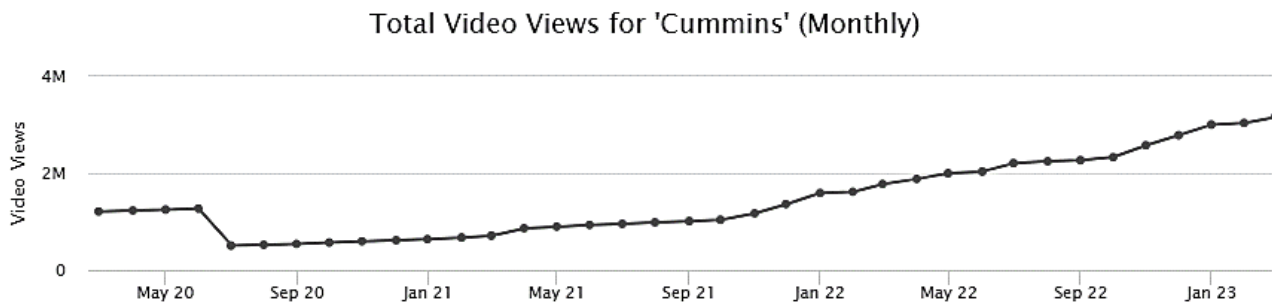


## Astutely Aligned Management Compensation



## Strong Online Endorsement

- ChatGPT endorses Cummins as #1 in diesel engines for trucks
- Positive sentiment for Cummins grows on Facebook, Twitter, and YouTube



## Stellar Workplace Reviews

Company	Overall	Recommendation	CEO Approval	Business Outlook
Cummins	4.2	85%	89%	78%
Caterpillar	4.0	79%	85%	74%
PACCAR	3.6	67%	79%	70%
CNH Industrials	3.9	79%	85%	73%
Weichai	3.1	30%	71%	66%
Deere	4.1	84%	84%	79%