

April 20, 2018

Cummins Inc: (CMI)
George Brockmann

Sector: Industrials
Industry: Diversified Industrials/Engine and Turbine Manufacturing
Current Price: \$170.5
Target Price: \$188.41

Company Description:

Cummins Inc designs, manufactures, distributes, and services diesel and natural gas engines, engine-related components, and electric power generation systems worldwide for a multitude of industries.

BUY

Current Price: \$170.5
Target Price: \$188.41
Market Cap: 27B
Beta: 0.95
Avg. Volume: 1,719,872
Adj. ROE: 25.03
Ke: 11.51%
Adj. EBITDA Margin: 14.4%
Adj. ROIC: 17.46
WACC: 11.01%



Thesis:

After a year of consistent margin growth, CMI's stock price has decreased dramatically over fears of international macro issues, along with large one time abnormal costs effecting earnings. For the first time in the year CMI is underperforming the industry while still posting positive numbers, leading to conclusion that the company is currently undervalued. Once the repercussions of the macro related sell-off have passed, along with a new quarter without the abnormal charges, CMI's margin and overall company growth over the year will reflect in an increased stock price that outperforms the market.

Catalysts:

Short Term(within the year):

- Recovery from abnormal costs that plagued the 4th quarter of 2017.
- Recovery from macro related sell-off as a result of talk of trade wars with China.
- Possible acquisition of GE's Jenbacher engine company.
- Release of X12 engine, an engine with "best in class power to weight ratio"

Mid Term(1-2 years):

- Increased investment into electric powertrains
- Further company and product segment growth through planned acquisitions to be done with excess of cash in balance sheet

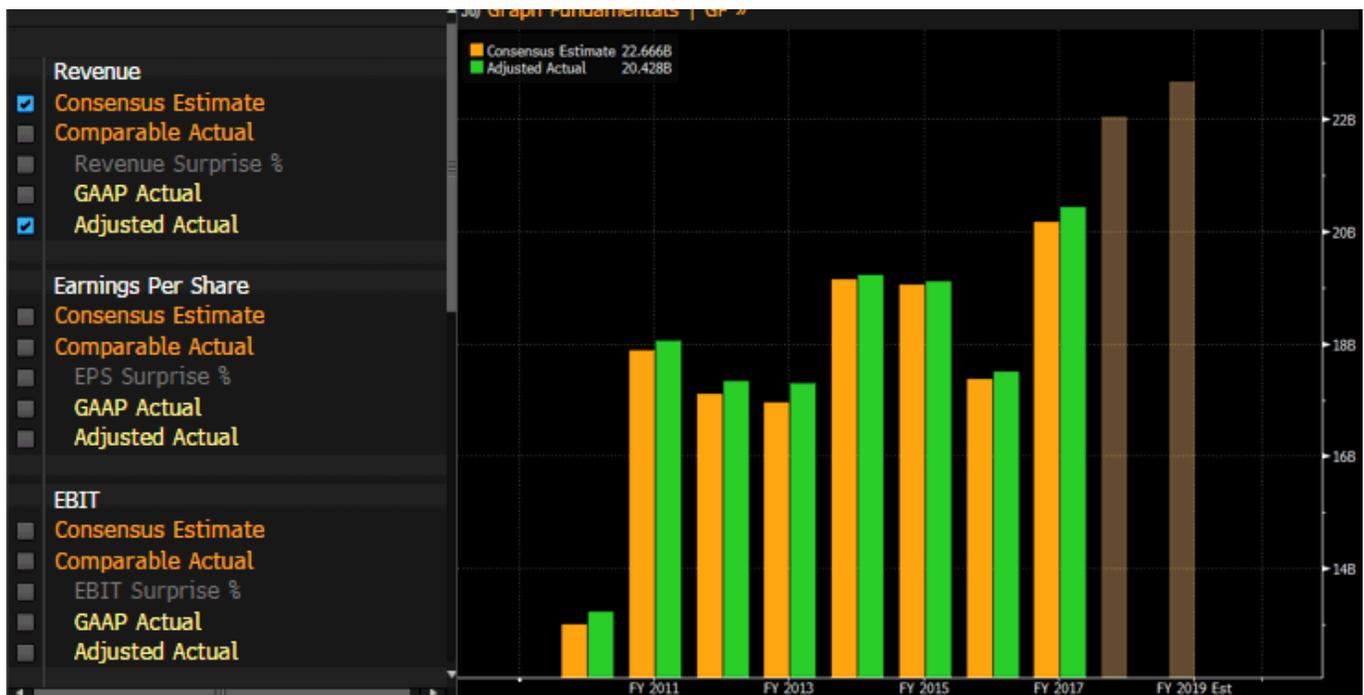
Long Term(3+):

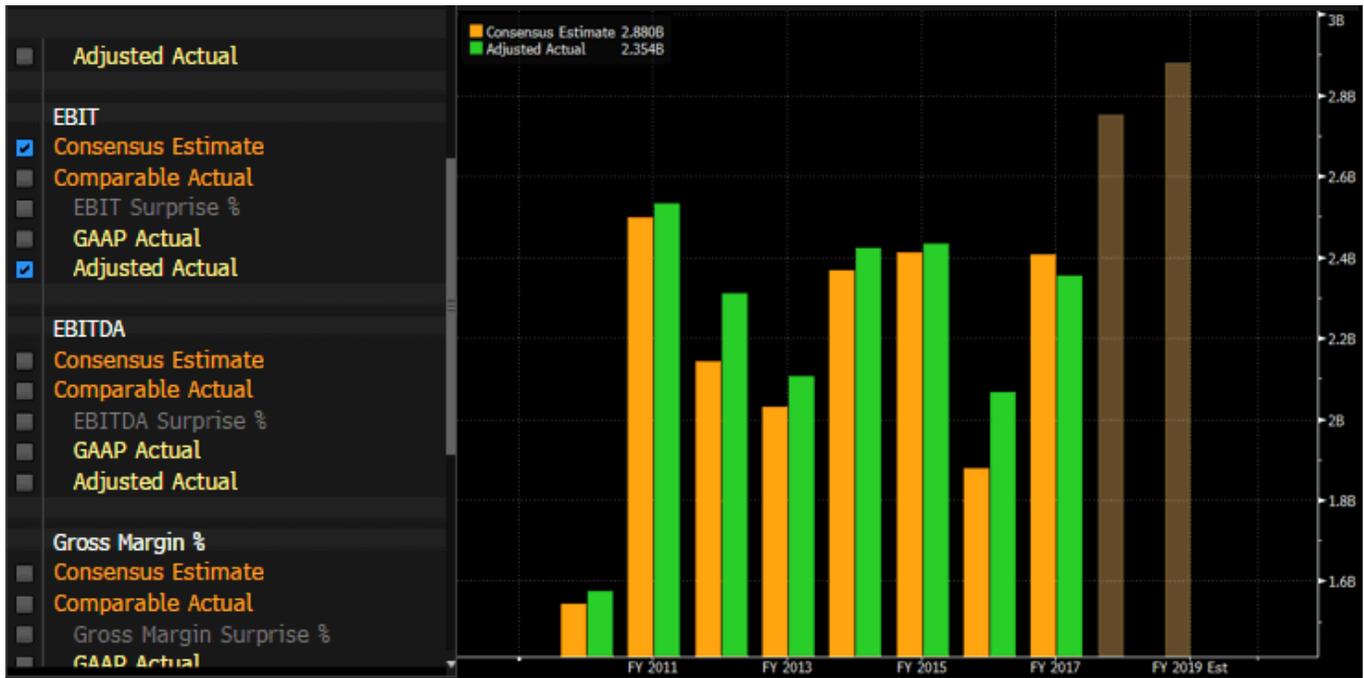
- Planned release of electric powertrain.
- Continued growth of company along with geographic and product line expansion.

Earnings Performance:

CMI ended their fiscal year on 12/31/2017, the year was ended with positive performance in certain sectors, while less than desirable performance in other sectors. Adj. Revenue grew by 16.7% to a company record \$20,428M, this is up from growth of -8.4% in 2016. Adj. Gross Margin decreased to 24.9% from 25.4%, and Adj. EBIT hit \$2,354M however Adj. EBIT Margin decreased to 11.52% from 11.81%. Adj. EBITDA hit \$2940M and the margin decreased from 14.8% to 14.4%. Adj. Net Income hit \$1768.9M from \$1474.6M and Adj. EPS increased from 8.71 to 10.57. CMI increased their short-term debt from \$288M to \$418M and marginally increased their long term debt to \$1588M from \$1568M.

EBIT, Gross Profit, and Net Income Margins are all projected to increase into 2018. The stock price saw a high percentage of growth over 2017 until January 2018 where CMI hit a large amount of abnormal expenses from tax legislation that passed and resulted in great decreases of GAAP reported numbers like net income or EPS, resulting in a large decrease in stock price, even through strong earnings performance. However, when this abnormal expense is factored out through the adjusted numbers, it shows that the company is performing very strongly. However higher costs associated with warranties, acquisitions, and large projects have also negatively affected some of the numbers and margins, these are expected to decrease into the 2018 year. Along with this there is investor sentiment that a possible trade war with China could negatively impact CMI's operations, however as the majority of CMI's products that are sold in China are produced in the borders, a trade war's impact would be negated.





Industry Outlook:

CMI operates in the Industrials segment under the Engine and Turbine Manufacturing Industry. Because of the engine portion of this industry, one of the main drivers for demand is the demand for heavy-duty trucks. This is generally determined by the age and replacement rate of existing fleets of trucks, replacement rates frequently change when new requirements are placed on these trucks that older ones do not have. This was seen in China in 2017 as new regulations were released to increase safety and resulted in new trucks being ordered, positively effecting CMI. This is also effected by positive economic activity as it can lead to increases in road freight activity, which likewise increases demand. Demand is also linked to industrial production and manufacturing, as these industries use the largest engines and use their turbine and power generator equipment, in particular the mining, logging, and long haul freight industries. Anything that affects construction growth also increases demand in this sector, for example strong economic growth or low interest rates.

In 2017 this industry saw higher demand for off-highway units in North America and China, along with higher truck demand as well. Increased demand from mining customers and gas and oil customers led to increases in the power generation section of the industry. There was also increased infrastructure investment and property construction that led to higher sales.

Looking ahead to 2018, it is expected that the industry will benefit from an increase in domestic freight volumes and greater industrial and manufacturing activity will positively affect demand across multiple product segments. This will be driven by US economic expansion along with expected increases in private investment in industrial equipment. This private investment increase will be spurred by a corporate profit that is expected to rebound in 2018, along with rising consumer spending will positively affect private investment in industrials. However there is a possibility of interest rate increases that could negate some of this growth. Another factor that will affect the Industrials segment as a whole is the world price of steel. In 2017 global demand for steel sharply increased and prices did as well, prices are expected to decrease into 2018 as a result of US policies and contraction from previous years price increases.

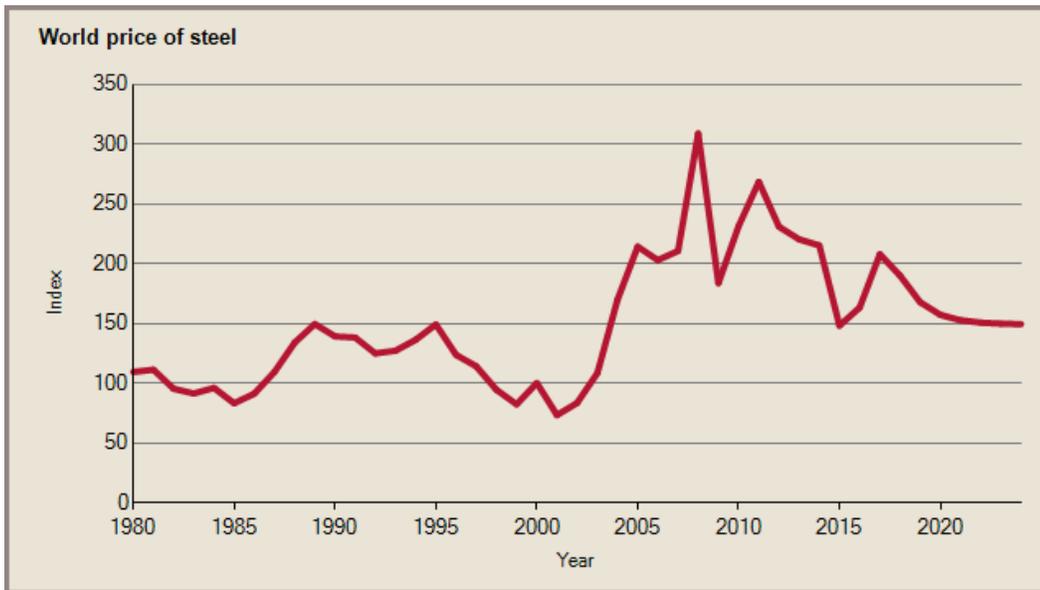
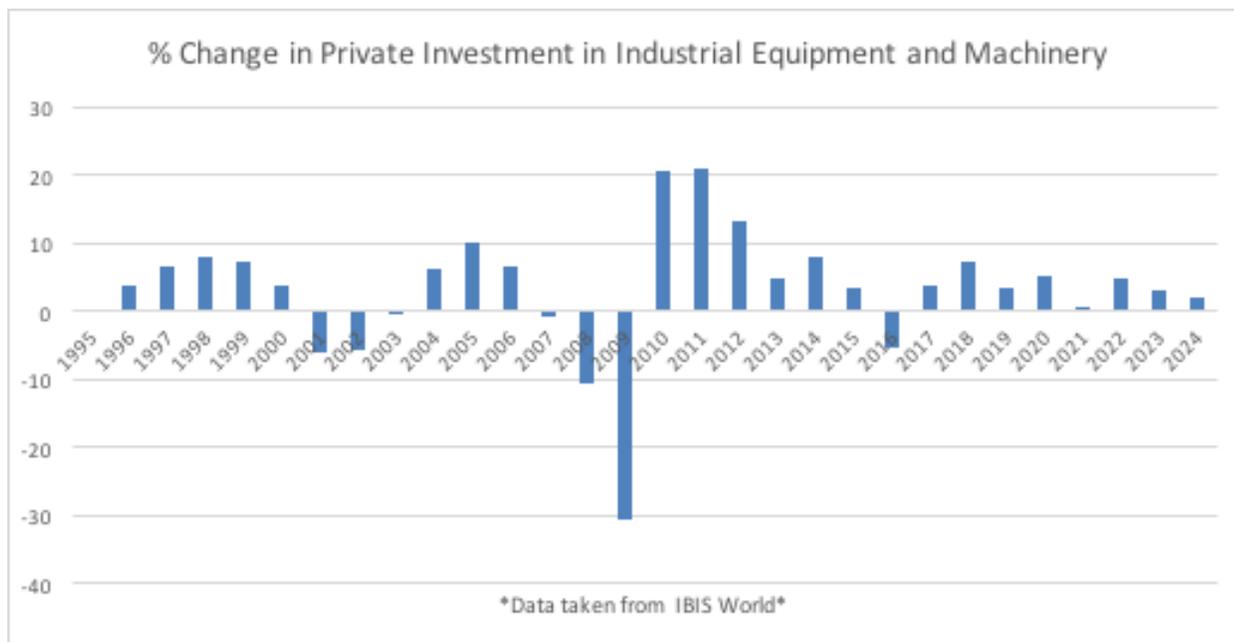


Chart from IBIS World



Mirroring other industries like automotive and the commercial vehicle, the Engine and Turbine Manufacturing Industry is also pushing away from standard engine design and moving towards higher levels of technologies in the engines as fuel emission standards become increasingly stringent. This has also resulted in large amounts of investment in electric engine technologies for this segment.

Recent worries in the industry around a trade war between the United States and China have had a negative impact on companies inside this industry as of recent. However in relation to CMI, if this trade war did occur it would have a negligible effect on their revenue. This is as a result of the fact that the majority of products sold by CMI in China are not shipped there. CMI owns a number of facilities inside the borders of China that produce their products, as well as a number of joint ventures with Chinese companies to produce their products. As a result this possible trade war would not impact CMI majorly.

Business Model:

CMI is a global power leader that designs, manufactures, distributes and services diesel and natural gas engines and engine-related component products, including filtration, aftertreatment, turbochargers, fuel systems, controls systems, air handling systems, transmissions and electric power generation systems. CMI sells their products to original equipment manufacturers (OEMs), distributors and other customers worldwide. They serve their customers through a network of approximately 500 wholly-owned and independent distributor locations and over 7,500 dealer locations in more than 190 countries and territories. CMI has four complementary operating segments: Engine, Distribution, Components and Power Systems. These segments share technology, customers, strategic partners, brand recognition and their distribution network in order to compete more efficiently and effectively in their respective markets. In each of CMI's operating segments, they compete worldwide with a number of other manufacturers and distributors that produce and sell similar products. CMI's products compete primarily on the basis of performance, fuel economy, speed of delivery, quality, customer support and price. CMI also has long-standing relationships with many of the leading manufacturers in the markets they participate in, including PACCAR Inc, Daimler Trucks North America, Navistar International Corporation and Fiat Chrysler Automobiles.

Segment Analysis:

CMI has 4 reportable segments; Engine which makes up 32.6% of revenue, Distribution which is 34.4%, Components creates 21.4% of revenue, and Power Systems which is 11.6% of revenue. CMI is an international company and they sell their products in many different countries around the world. CMI breaks up their geographic areas for revenue into 3 sections; United States which brings in 53.9% of revenue, Other Foreign Countries is 35.6% of revenue, and China which is 10.5% of revenue.

Although it did not bring in the most revenue in 2017, the Engine segment is still the most profitable as it brought in 40.1% of operating income over the year. This segment manufactures and markets a broad range of diesel and natural gas powered engines under the Cummins brand name, as well as certain customer brand names, for the heavy- and medium-duty truck, bus, recreational vehicle (RV), light-duty automotive, construction, mining, marine, rail, oil and gas, defense and agricultural markets. This segment is also split up into 4 sections based on the size of the engine and its use. The Heavy-Duty Truck section manufactures diesel and natural gas engines that range from 310 to 605 horsepower serving global heavy-duty truck customers, and made up 15.1% of revenue in this segment. The Medium-Duty Truck and Bus section manufactures diesel and natural gas engines ranging from 130 to 450 horsepower serving medium-duty truck and bus customers worldwide, applications include pickup and delivery trucks, vocational truck, school bus, transit bus and shuttle bus. Diesel engines are also produced for Class A motor homes in this section, this section produced 42.1% of revenue. The Light-Duty Automotive manufactures 105 to 385 horsepower diesel engines, including engines for the pickup truck market for Fiat Chrysler Automobiles (Fiat Chrysler) and Nissan in North America and it generated 40.5% of revenue in the segment. The final section is the Off-Highway Section which manufactures diesel engines that range from 48 to 715 horsepower to global markets including mining, marine, rail, oil and gas, defense, agriculture and construction equipment and also to the power generation business for standby, mobile and distributed power generation solutions throughout the world and this section produced 2.3% of revenue. After seeing a decrease in sales and revenue from 2015-2016, this segment had a strong year with revenues increasing by 15.3% mostly driven by 20% increase in

sales of medium and heavy unit sales. Over 2017, the Engine segment increased its revenue from \$5774M to \$6661M.

The Distribution segment brought in the most revenue from CMI, but was not the most profitable bringing in 16.1% of operating income. The Distribution segment consists of 28 wholly-owned and 10 joint venture distributors that service and distribute the full range of CMI's products and services to end-users at roughly 450 locations in over 90 distribution territories. CMI's wholly-owned distributors are located in key markets, including North America, Australia, Europe, China, Africa, Russia, Japan, Brazil, Singapore and Central America, while they have joint venture distributors located in key markets, including South America, the Middle East, India, Thailand and Singapore. CMI's distribution network consists of independent, partially-owned and wholly-owned distributors which provide parts and service to their customers. These full-service solutions include maintenance contracts, engineering services and integrated products, where they customize their products to cater to specific needs of end-users. CMI's distributors also serve dealers in their territories by providing new products, technical support, tools, training, parts and product information. This segment is responsible for managing the operations of CMI's distributors as well as their relationships with independent distributors. The Distribution segment serves a diverse customer base with roughly 38 percent of its 2017 and 2016 sales being generated from new engines and power generation equipment, with its remaining sales generated by parts and service revenue. The Distribution segment's revenue increased from \$6157M to \$7029M in 2017.

The Components Segment brought in 21.4% of revenue and 31.5% of operating income, this segment also saw a notable increase in goodwill over 2017 as it tripled as a result of acquisitions. The Components segment supplies products which complement CMI's Engine and Power Systems segments, including aftertreatment systems, turbochargers, transmissions, filtration products and fuel systems for commercial diesel applications. They manufacture filtration systems for on- and off-highway heavy-duty and medium-duty equipment, and are a supplier of filtration products for industrial vehicle applications. In addition, CMI develops aftertreatment systems and turbochargers to help their customers meet increasingly stringent emission standards and fuel systems which have also supplied their Engine segment as well as their joint venture partners. The Emissions Solutions section of this segment involves designing, manufacturing and integrating aftertreatment technology and solutions for their engine markets and making the products more environmentally friendly. The Turbo Technology section of this segment includes the design, manufacturing and marketing of turbochargers for CMI's engine markets. They provide air handling technologies for engines to meet performance requirements and worldwide emission standards. The Filtration section is the design, manufacture and sale of filters, coolant and chemical products. CMI's filtration business offers over 8,300 products for first fit and aftermarket applications including air filters, fuel filters, fuel water separators, lube filters, hydraulic filters, coolants, fuel additives and other filtration systems. CMI produces and sells Fleetguard branded products through this segment as well. In the Electronic and Fuel System section CMI designs and manufactures new, replacement and remanufactured fuel systems primarily for heavy-duty on-highway engines. This segment also develops and supplies electronic control modules, sensors and harnesses for the on-highway, off-highway, and power generation applications. The final section of this segment is the Automated Transmission section, which develops and supplies automated transmissions to the heavy-duty and medium-duty commercial vehicle markets. This section was formed in 2017 from a joint venture with the Eaton Cummins Automated Transmission Technologies and it is consolidated a 50/50 joint venture between Cummins Inc. and Eaton Corporation Plc. In the 2017 year this segment's revenue increased from \$3514M to \$4363M.

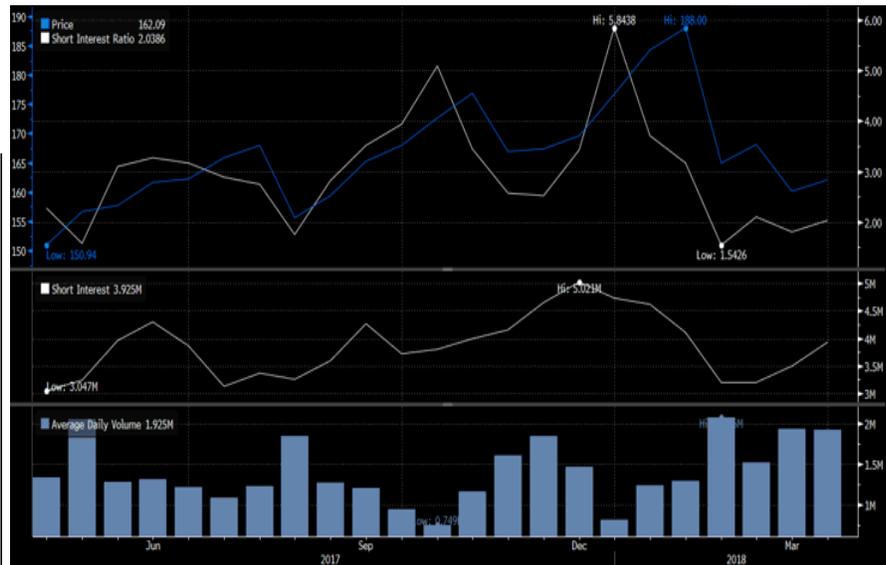
The final reportable segment that CMI has is Power Systems segment. This segment researches emerging technologies and provides integrated power generation products. CMI uses their own research and development capabilities along with business partnerships to develop cost-effective and environmentally sound power solutions. In 2017 this segment made up 11.6% of revenue and 12.3% of operating income. The Power Systems segment is organized around 3 different product lines; power generation, industrials, and generator technologies. The power generation line designs, manufactures, sells and supports back-up and prime power generators ranging from 2 kilowatts to 3.5 megawatts, as well as controls, paralleling systems and transfer switches, for multiple applications. CMI also provides solutions for energy management applications using natural gas or biogas as a fuel. CMI also serves global rental accounts for diesel and gas generator sets. The Industrial line designs, manufactures, sells and supports diesel and natural gas high-horsepower engines up to 5,500 horsepower for a wide variety of equipment in the mining, rail, defense, oil and gas, and commercial marine applications throughout the world. The final line of Generator Technologies designs, manufactures, sells and supports A/C generator and alternator products for internal consumption and for external generator set assemblers. CMI's products in this line are sold under the Stamford, AVK and Markon brands. Over 2017 this segments revenue increased from \$2064M to \$2375M.

In Millions of USD except Per Share	2014 Y		2015 Y		2016 Y		2017 Y	
12 Months Ending	12/31/2014		12/31/2015		12/31/2016		12/31/2017	
Revenue	19,221.0	100.0%	19,110.0	100.0%	17,509.0	100.0%	20,428.0	100.0%
Distribution	5,135.0	26.7%	6,198.0	32.4%	6,157.0	35.2%	7,029.0	34.4%
Engine	7,462.0	38.8%	6,733.0	35.2%	5,774.0	33.0%	6,661.0	32.6%
Components	3,791.0	19.7%	3,745.0	19.6%	3,514.0	20.1%	4,363.0	21.4%
Power Systems	2,833.0	14.7%	2,434.0	12.7%	2,064.0	11.8%	2,375.0	11.6%
Non-segment items	—		—		—		—	
Power Generation	—		—		—		—	
Operating Income	2,498.0	100.0%	2,090.0	100.0%	1,999.0	100.0%	2,446.0	100.0%
Engine	1,031.0	40.2%	636.0	30.1%	686.0	34.6%	959.0	40.1%
Components	684.0	26.6%	727.0	34.5%	641.0	32.3%	754.0	31.5%
Distribution	491.0	19.1%	412.0	19.5%	392.0	19.8%	384.0	16.1%
Power Systems	361.0	14.1%	335.0	15.9%	263.0	13.3%	294.0	12.3%
Non-Segment Items	-69.0		-20.0		17.0		55.0	
Power Generation	—		—		—		—	

Management/Ownership:

CMI is primarily owned by investment advisors with 83.94% of ownership which is an increase of 2.21% since last year. After this is banks with 2.79% of ownership which is a decrease of 0.74% in the past year. Hedge Fund Managers own 2.78% and their positions have decreased by 1.52% in the past year. The majority holder is State Street Corporation with 7.25% of ownership, followed by BlackRock at 7.08%, and Vanguard Group with 6.81%. CMI has 97.24% of their shares freely floated. When CMI's stock price was at their 52 week high in January, short interest was also at the highest of the year at 5.843. Since the stock price decreased rapidly to what it is currently, short interest hit its yearly low of 1.542 and is now hovering around 2.

Top Ownership Type (%)			
54) Ownership Type	04/16/17	Curr	Change
41) Investment Advisor	81.73	83.94	+2.21
42) Bank	3.53	2.79	-0.74
43) Hedge Fund Manager	4.30	2.78	-1.52
44) Pension Fund	2.98	2.61	-0.37
45) Corporation	1.65	2.53	+0.88
46) Insurance Company	1.58	1.73	+0.15
47) Sovereign Wealth Fund	1.42	1.55	+0.13
48) Government	1.80	1.21	-0.59
49) Brokerage	0.41	0.37	-0.04



Chairman and CEO Thomas Linebarger was appointed in 2012, and when he began his tenure the price of CMI was around \$90. Although the price has seen large fluctuations over the years due to macro effects, it is currently around the highest it has ever been. Linebarger graduated from Stanford with a MBA and was hired by CMI shortly after. He was named VP/CFO in 2001, President/COO in 2008, and Chairman/CEO in 2012. His compensation has grown 12.44% over the past 6 years, and the stock price has increased 4.83% over the past 6 years.

Management	Position	Total Compensations Growth	Stock Price Growth During Tenure
Linebarger, N.	Chairman & CEO	12.44% per annum over 6y	4.83% per annum over 6y
Freeland, Richard	President, COO & Director	3.33% per annum over 6y	4.83% per annum over 6y
Ward, Patrick	VP & CFO	2.22% per annum over 6y	4.83% per annum over 6y
Rose, Marya	VP & Chief Administrative Officer	20.31% per annum over 2y	45.53% per annum over 2y
Satterthwaite, Livingston	VP & President of Distribution Business	-6.05% per annum over 5y	5.88% per annum over 5y
Clulow, Christopher	Principal Accounting Officer, VP & Corp		

Capital Allocation Comparison:

CMI has a Total Debt to Total Asset Ratio of 11.10%, which is much lower than the competitor average of 38.27%. CMI currently has 5 bonds out, the average maturity is the year 2048 as all the bonds are long term, and the average coupon of these bonds is 5.61%, the bonds total \$1,473M. CMI has a WACC of 11.01% which is above the competitor average of 8.44%, CMI also has a ROIC of 17.84% which is much higher than the competitor median of 8.38%. Other notable numbers include a Adj. Return on Common Equity of 25.03% for CMI and the competitor average is 16.67%.

Name	Ticker	Mkt Cap	EBITDA Mrgn Adj:Y	OPM:Y	NI Mrgn Adj:Y	ROIC:Y	ROA Adj:Y	Rtrn on CE Adj:Y	Debt/Assets:Y
Median		57.15B	12.19%	8.33%	7.42%	8.38%	4.24%	16.67%	38.27%
100) CUMMINS INC	CMI US	28.20B	14.38%	11.52%	8.66%	17.84%	10.69%	25.03%	11.10%
101) NAVISTAR INTERNATIONAL	NAV US	3.95B	7.78%	5.18%	0.76%	985.67	--	--	82.44%
102) GENERAL ELECTRIC CO	GE US	118.62	13.07%	8.81%	8.88%	5.95%	2.88%	14.64%	35.61%
103) CATERPILLAR INC	CAT US	93.20B	19.44%	13.12%	9.07%	8.79%	5.44%	30.73%	45.32%
104) DAIMLER AG-REGISTERE	DAI GR	86.09B	11.30%	7.85%	6.19%	6.08%	4.08%	16.67%	40.93%
105) HINO MOTORS LTD	7205 J	7.32B	7.26%	4.23%	2.91%	7.97%	4.24%	10.96%	16.37%

(Accounting Adjustments: Adjusted for Abnormal Items When Applicable)

[10 Analyze List](#)

Profitability Comparison:

CMI has seen revenues fluctuate in the past number of years, even experiencing declines at points, however in the past year their revenue hit an all-time high, coupled with this CMI has also seen consistent margin growth. The margin growth comes as a result of the quality of their product and expansion of product segments through internal product innovations as well as a number of acquisitions over the past few years. The fluctuations in revenue come because of the cyclicity of the industry CMI is in and this fluctuation is shared amongst their competitors. However, CMI's 5 year CAGR of revenue of 3.34% is still well above the competitor median of -.09%.

In Millions of USD	2014 Y	2015 Y	2016 Y	2017 Y	Current/LTM	2018 Y Est	2019 Y Est
12 Months Ending	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2017	12/31/2018	12/31/2019
Market Capitalization	26,109.2	15,340.1	22,892.2	29,180.9	28,200.1		
- Cash & Equivalents	2,394.0	1,811.0	1,380.0	1,567.0	1,567.0		
+ Preferred & Other	344.0	344.0	299.0	905.0	905.0		
+ Total Debt	1,686.0	1,639.0	1,856.0	2,006.0	2,006.0		
Enterprise Value	25,745.2	15,512.1	23,667.2	30,524.9	29,544.1		
Revenue, Adj	19,221.0	19,110.0	17,509.0	20,428.0	20,428.0	22,070.0	22,676.4
Growth %, YoY	11.1	-0.6	-8.4	16.7	16.7	8.0	2.7
Gross Profit, Adj	4,861.0	4,947.0	4,452.0	5,090.0	5,090.0	5,845.9	6,051.9
Margin %	25.3	25.9	25.4	24.9	24.9	26.5	26.7
EBITDA, Adj	2,878.0	2,947.0	2,597.0	2,937.0	2,940.0	3,486.6	3,603.7
Margin %	15.0	15.4	14.8	14.4	14.4	15.8	15.9
Net Income, Adj	1,608.8	1,654.5	1,474.6	1,768.9	1,770.8	2,090.1	2,173.6
Margin %	8.4	8.7	8.4	8.7	8.7	9.5	9.6
EPS, Adj	8.79	9.27	8.71	10.57	10.58	12.73	13.47
Growth %, YoY	11.2	5.5	-6.1	21.4	24.9	20.4	5.9
Cash from Operations	2,266.0	2,065.0	1,939.0	2,277.0	2,277.0		
Capital Expenditures	-743.0	-744.0	-531.0	-506.0	-506.0	-718.3	-706.9
Free Cash Flow	1,523.0	1,321.0	1,408.0	1,771.0	1,771.0	1,648.7	1,847.1

Gross and profit margin are both ahead of the competitor median with CMI's being 24.92% and 8.66% compared to 19.39% and 7.42%. Asset and Inventory Turnover are both slightly above the competitor median of 0.95 and 5.25. The cash conversion cycle of CMI is 73.01 which is much lower than the competitor

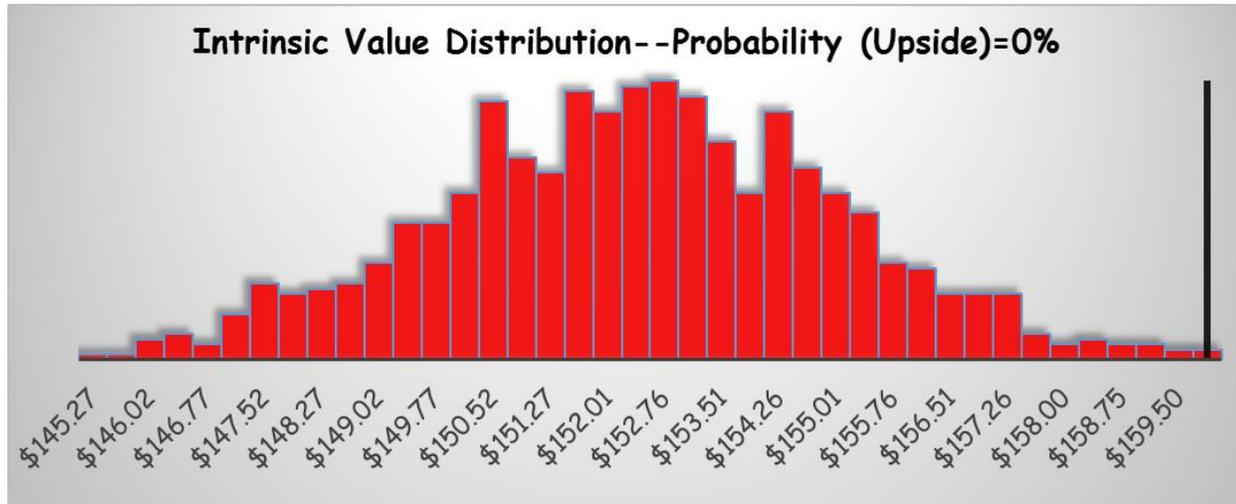
average of 102.56. These numbers imply that CMI is using their working capital efficiently and this is backed up by the margin growth they have seen.

Name	Ticker	Mkt Cap	GM:Y	PM:Y	Ast TO:Y	Inv turnover:Y	A/P Turnover:Y	Cash Conversion Cycle:Y	Rev Gr Adj 5Y CAGR:Y
Median		56.78B	19.39%	7.42%	0.95	5.17	6.55	102.56	-0.09%
100) CUMMINS INC	CMI US	27.93B	24.92%	8.66%	1.23	5.25	7.14	73.01	3.34%
101) CATERPILLAR INC	CAT US	92.29B	30.28%	9.07%	0.60	3.40	5.96	166.91	-7.15%
102) DAIMLER AG-REGISTERED SHA	DAI GR	85.63B	20.89%	6.19%	0.66	5.09	10.84	148.64	7.53%
103) NAVISTAR INTERNATIONAL CO	NAV US	3.85B	17.89%	0.76%	1.45	7.81	5.78	62.11	-7.56%
104) HINO MOTORS LTD	7205 JP	7.37B	16.19%	2.91%	1.46	7.14	5.48	48.67	5.07%
105) GENERAL ELECTRIC CO	GE US	126.14B	9.54%	8.88%	0.32	4.92	7.34	132.10	-3.52%

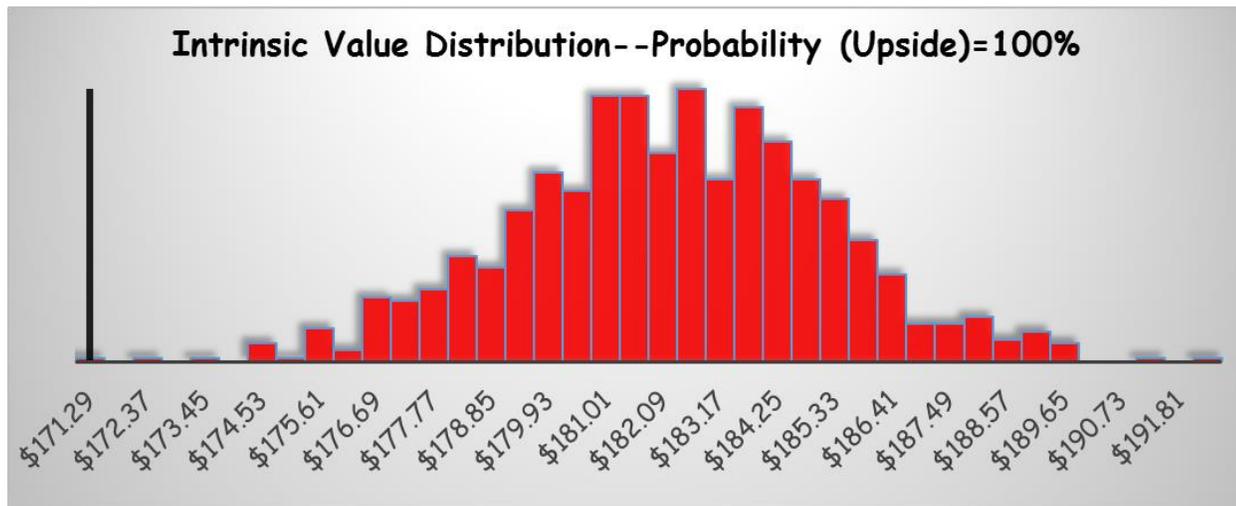
Sensitivity Analysis:

CMI's stock price value is very sensitive to the level revenue and expenses. The base, bear, and bull case valuation are evaluated using a Monte Carlo simulation with different assumptions. Under the bear case there is a 0% intrinsic value probability upside. This creates an intrinsic value of \$152.15, a 1 year target price of \$165.2, and would result in a return of -3%. This is due to making the assumption that operating expenses and costs of revenue increase, resulting in CMI's EBITDA margin not only missing next year's estimates, but decreasing to 14% from the current year's 14.4%. This decrease is reflected in the projections until the continuing period as this delays the anticipated growth of the margin in the years after, and it does not reach the level it would have if CMI met expectations, this decrease was also reflected in the continuing period EBITDA margin as it was lowered to the historical average. Based on historical financial performance, it is highly unlikely that CMI's EBITDA margin would shrink at this rate. Although their margin has fluctuated in the past, based on the current state of the industry and CMI's recent financial success this scenario is unlikely to occur. The bull case involves the assumptions that operating expenses and costs of revenue decrease, resulting in a intrinsic value probability upside of 100%, and giving an intrinsic value of \$182.07, a 1 year target price of \$198.29, creating a return of 16.6%. This comes as a result of CMI beating their EBITDA targets by 5%, this increase is reflected in the projections as the margins reach higher levels than they would have otherwise, the increase over what is expected is also reflected in the EBITDA margin for the continuing period. While this case is optimistic, the assumptions made are not extraordinary and it is very possible that they could be reached if the industry for 2018 is more positive than expected. The most likely case however is the base case, which has an intrinsic value probability upside of 78.56%. This is as a result of the assumptions that EBITDA margin for the next two years hits their targets of 15.8% and 15.9% respectively, this is also reflected in the continuing period EBITDA margin which is equivalent to their estimate of 15.8%, this number is 1.85% higher than the historical average. This case gives CMI a intrinsic value of \$173.14, a 1 year target price of \$188.41, and a target return of 10.5%. Based on their financial performance this scenario is the most likely based on the positive numbers CMI has been reporting and the positive estimates about the direction the industry is set to head in 2018. Once macro worries have subsided along with abnormal expenses being absent from the most recent quarter, it is highly likely that CMI will reach the levels included in this case.

Bear Case



Bull Case



Summary:

In conclusion, CMI is a buy at their current price. This is due to the fact that the company is still posting positive numbers in light of a very tough quarter in regards to expensive abnormal costs and one that was heavy with macro worries. CMI stock price has dropped substantially as of recent as a result of these variables, even though their financials point towards a company that is doing well. This is also backed up by the fact that CMI is outperforming their competitors who are also feeling the sting of macro effects. Along with this, CMI has made recent acquisitions to branch into the electric power segment of this industry, and strong cash positions place them in a good spot for further acquisitions over the coming year. Based on analysis, the upside of CMI is much greater than the downside as upside probabilities are a much more likely occurrence. CMI's 1 year target price is \$188.41 with a return based on current stock price of 10.5%, which is reasonable based on their financials performance. CMI appears to be in strong position to re-approach their 52 week high.

Cummins Inc. (CMI)

CENTER FOR GLOBAL FINANCIAL STUDIES

NEUTRAL

Analysis by **George Brockmann**
4/20/2018

Current Price: **\$170.83**
Dividend Yield: **2.6%**

Intrinsic Value: **\$172.81**
Target Price: **\$188.12**

Target 1 year Return: **12.7%**
Probability of Price Increase: **78.56%**



Description	
Cummins Inc. designs, manufactures, distributes, and services diesel and natural gas engines, and engine-related component products worldwide.	
General Information	
Sector	Industrials
Industry	Machinery
Last Guidance	February 12, 2018
Next earnings date	NM
Market Assumptions	
Estimated Equity Risk Premium	5.61%
Effective Tax rate	27%

Market Data	
Market Capitalization	\$28,114.64
Daily volume (ml)	1.69
Shares outstanding (mil)	164.58
Diluted shares outstanding (mil)	167.27
% shares held by institutions	109%
% shares held by investments Managers	72%
% shares held by hedge funds	3%
% shares held by insiders	0.29%
Short interest	2.38%
Days to cover short interest	2.29
52 week high	\$194.18
52-week low	\$143.83
Volatility	22.89%

Past Earning Surprises		
Quarter ending	Revenue	EBITDA
12/31/2016	3.10%	-7.68%
4/2/2017	10.53%	0.22%
7/2/2017	5.82%	-16.44%
10/1/2017	9.98%	-8.87%
12/31/2017	5.53%	-13.27%
Mean	6.99%	-9.21%
Standard error	1.0%	4.4%

Market and Credit Scores	
Recommendation (STARS) Value--5	4.4%
Recommendation (STARS) Description--Strong Buy	
Quality Ranking Value--B+	
Quality Ranking Description--Average	
Short Score--0	
Market Signal Probability of Default % (Non-Ratings)	-0.314%
CreditModel Score (Non-Ratings)--a+	

Industry and Segment Information	
LTM Revenues by Geographic Segments	LTM Revenues by Business Segments
United States--54%	Engine--44%
China--10%	Distribution--35%
Other International Countries--36%	Components--29%
--	Power Systems--20%
--	Intersegment Eliminations--27%

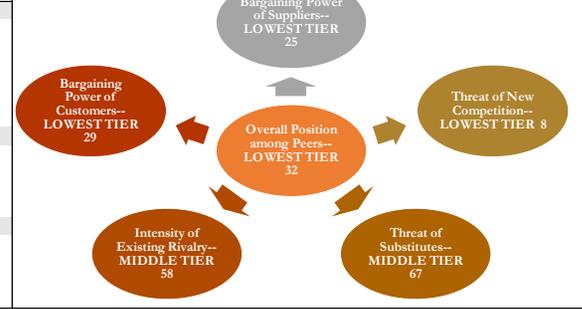
Management	
Position	Person
Chairman & CEO	Linebarger, N.
President, COO & Director	Freeland, Richard
VP & CFO	Ward, Patrick
VP & Chief Administrative Officer	Rose, Marya
VP & President of Distribution Business	Satterthwaite, Livingston
Principal Accounting Officer, VP & Corporate Co	Clulow, Christopher

Total Compensations Growth		Stock Price Growth During Tenure	
12.44% per annum over 6y	Chairman & CEO	4.83% per annum over 6y	Chairman & CEO
3.33% per annum over 6y	President, COO & Director	4.83% per annum over 6y	President, COO & Director
2.22% per annum over 6y	VP & CFO	4.83% per annum over 6y	VP & CFO
20.31% per annum over 2y	VP & Chief Administrative Officer	45.53% per annum over 2y	VP & Chief Administrative Officer
-6.05% per annum over 5y	VP & President of Distribution Business	5.88% per annum over 5y	VP & President of Distribution Business

Peers	
PACCAR Inc	Hinopak Motors Limited
Caterpillar Inc.	Oshkosh Corporation
Navistar International Corporation	MAN SE
General Electric Company	Komatsu Ltd.
Daimler AG	Allison Transmission Holdings, Inc.

Profitability		CMI (LTM)		CMI Historical		Peers' Median (LTM)	
Return on Capital (GAAP)	11.9%	11.28%	9.90%	16.28%	10.97%		
Operating Margin	9%	8.31%	1.19	1.48	14.6%		
Revenue/Capital (GAAP)	1.39	13.4%	7.1%	6.4%	2.27		
ROE (GAAP)	13.5%	1.88	16.7%	23.3%	10.7%		
Net margin	6.1%	12.6%	20.4%	10.7%	51.5%		
Revenue/Book Value (GAAP)	2.22	62.7%	59.2%	14.5%	3.7%		

Invested Funds		CMI (LTM)		CMI Historical		Peers' Median (LTM)	
Cash/Capital	12.6%	0.22	0.18	0.68	4.6%	8.2%	
NWC/Capital	16.4%	4.6%	11%	11%	12%		
Operating Assets/Capital	59.2%	11%	12%				
Goodwill/Capital	3.7%						



Forecast Assumptions		Explicit Period (6 years)		Continuing Period	
Revenue Growth CAGR	3%	3%	2%		
Average Operating Margin	20%	16%	10%		
Average Net Margin	13%	10%	9%		
Growth in Capital CAGR	9%	2%	2%		
Growth in Claims CAGR	1%	2%	2%		
Average Return on Capital	10%	5%	5%		
Average Return on Equity	12%	11%	12%		
Average Cost of Capital	11%	12%	12%		
Average Cost of Equity	12%				

