

Cummins India

 BSE SENSEX
 37,327

 S&P CNX
 11,032

CMP: INR603
TP: INR695 (+15%)
BUY

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Bloomberg	KKC IN
Equity Shares (m)	277
M.Cap.(INRb)/(USDb)	167 / 2.4
52-Week Range (INR)	885 / 587
1, 6, 12 Rel. Per (%)	-16/-22/-10
12M Avg Val (INR M)	424
Free float (%)	49.0

Financials & Valuations(INR b)

Y/E Mar	2019	2020E	2021E
Net Sales	56.6	60.4	68.6
EBITDA	8.6	8.1	9.7
PAT	7.2	6.9	8.0
EPS (INR)	26.1	24.8	28.9
Gr. (%)	10.8	-4.9	16.4
BV/Sh (INR)	149.0	159.0	170.7
RoE (%)	17.8	16.1	17.5
RoCE (%)	16.9	15.3	16.6
P/E (x)	23.1	24.3	20.9
P/BV (x)	4.0	3.8	3.5

Estimate change



TP change



Rating change

Miss on all fronts; hurt by weakness in higher-margin exports biz

- Op. performance below expectations:** KKC missed our expectations on all fronts. Revenue growth was tepid at 1% YoY (our estimate: 10%) in 1QFY20 due to a decline in exports (-26% YoY). De-growth in the higher-margin export business dragged the overall margin to its lowest level in a decade at 11.3%. Thus, EBITDA declined 30% YoY to INR1.5b (35% miss). Adj. PAT was down 23% YoY to INR1.4b (25% miss).
- The root cause – weak demand trends in overseas markets:** The decline in exports is attributable to weak demand in the key markets of Africa, the Middle East and Asia. LHP exports declined 39% YoY to INR1.3b, while HHP exports were down 10% YoY to INR1.7b. Domestic business grew robustly by 16% YoY to INR9.9b, led by strong growth in Power Generation (+9% YoY) and Industrial (+39% YoY) segments. Distribution & Services segment delivered moderate growth of 8% YoY to INR3.5b. However, **management has lowered its domestic revenue growth guidance to 8-10% from 12-15% earlier** owing to the ongoing economic slowdown. This implies residual growth of 6-9% in the remaining nine months of FY20.
- Margins – no relief in sight given weak exports outlook:** Operating margin shrank 490bp YoY to 11.3% in 1QFY20 on account of a weak revenue mix (25% exports revenue v/s 34% in 1QFY19). Also, INR movement adversely impacted the margin by 100bp. With global markets expected to remain soft and low visibility in the key markets of Africa and South America, **management expects exports to decline 12-15% in FY20 (v/s guidance of flat-to-negative growth at the start of the year)**. To factor in the potential adverse revenue mix in FY20, we have scaled down our margin estimates by 170bp for FY20 (13.4% v/s 15.2% earlier).
- Lowering earnings estimate and TP; maintaining Buy on cheap valuations:** We cut our earnings estimate by 13%/11% for FY20/21 to factor in (a) the pressure on margins, given intense competition in the domestic business and (b) the weak exports outlook. We scale down our TP to INR695 as we assign a target multiple of 24x FY21E EPS. At CMP, the stock trades at FY20/21E P/E of 24x/21x. We maintain **Buy** given cheap valuations.

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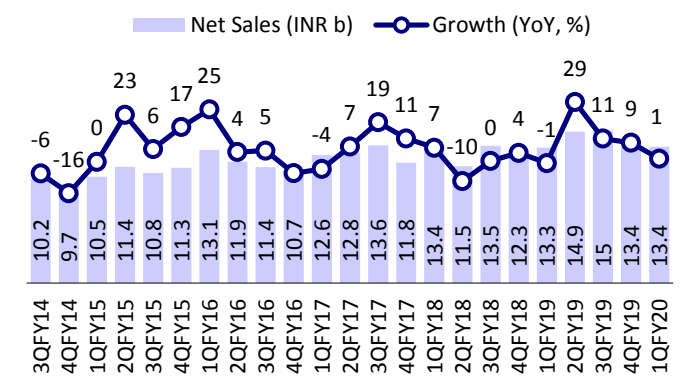
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KKC: Quarterly Performance (Standalone)

(INR Million)

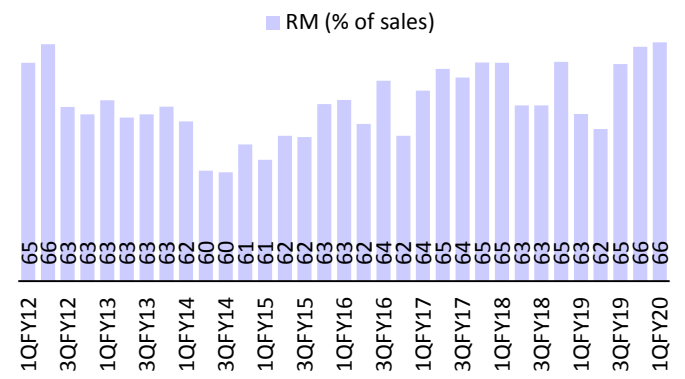
Y/E March	FY19				FY20E				FY19	FY20E	Vs Est. 1QE	Var. (%)
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE				
Sales	13,280	14,869	15,038	13,404	13,430	15,636	16,373	14,950	56,590	60,387	14,620	-8.1%
Change (%)	-1.0	28.9	11.0	8.7	1.1	5.2	8.9	11.5	11.3	6.7	10.1	
EBITDA	2,147	2,509	2,267	1,718	1,514	2,142	2,292	1,998	8,641	8,116	2,325	-34.9%
Change (%)	9.9	49.8	15.3	-0.7	-29.5	-14.6	1.1	16.3	24.0	10.4	8.3	
As of % Sales	16.2	16.9	15.1	12.8	11.3	13.7	14.0	13.4	15.3	13.4	15.9	
Depreciation	271	274	279	280	291	295	295	298	1,103	1,179	292	
Interest	36	40	41	45	52	40	42	28	162	162	38	
Other Income	696	785	755	692	769	790	770	717	2,928	3,046	714	
PBT	2,536	2,980	2,702	2,085	1,940	2,597	2,725	2,388	10,304	9,820	2,709	-28.4%
Tax	706	865	831	676	525	779	818	824	3,078	2,946	813	
Effective Tax Rate (%)	27.8	29.0	30.8	32.4	27.1	30.0	30.0	34.5	29.9	30.0	30.0	
Adjusted PAT	1,830	2,116	1,871	1,409	1,415	1,818	1,908	1,564	7,226	6,874	1,896	-25.4%
Change (%)	10.2	38.4	8.7	(12.6)	(22.7)	(14.1)	2.0	11.0	10.8	(4.9)	3.6	
Extra-ordinary Income (net)	-	-	-	-	-	-	-	-	-	-	-	
Reported PAT	1,830	2,116	1,871	1,409	1,415	1,818	1,908	1,564	7,226	6,874	1,896	-25.4%
Change (%)	(17.6)	38.4	8.7	(12.6)	(22.7)	(14.1)	2.0	11.0	2.0	(4.9)	3.6	

Exhibit 1: Revenue growth muted at 1% YoY impacted by weak performance in exports segment



Source: Company, MOFSL

Exhibit 2: RM costs up 330bp YoY given adverse revenue mix



Source: Company, MOFSL

Domestic business growth offset by weak export performance

- Domestic business grew by a robust 16% YoY to INR9.9b, supported by strong growth in the power generation (+9% YoY) and industrial (+39% YoY) segments. Demand from infrastructure segments supported domestic growth.
- Distribution & service segment delivered moderate growth of 8% YoY to INR3.4b.

Exhibit 3: Quarterly Cost structure analysis

INR M	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
Raw Materials	7,707	8,435	7,282	8,546	8,031	8,330	9,217	9,771	8,817	8,862
Staff Costs	1,069	1,226	1,257	1,317	1,180	1,265	1,468	1,379	1,346	1,376
Other Expenses	1,368	1,506	1,326	1,717	1,391	1,538	1,676	1,620	1,523	1,679
Total	10,144	11,455	9,864	11,580	10,602	11,133	12,360	12,770	11,686	11,916
% of Revenues										
Raw Materials	65.1	65.1	63.1	63.1	65.1	62.7	62.0	65.0	65.8	66.0
Staff Costs	9.0	9.1	10.9	9.7	9.6	9.5	9.9	9.2	10.0	10.2
Other Expenses	11.5	11.2	11.5	12.7	11.3	11.6	11.3	10.8	11.4	12.5
% YoY										
Raw Materials	14.0	8.6	-12.1	-2.0	4.0	-4.5	-1.1	14.3	6.6	6.4
Staff Costs	6.3	17.9	13.5	19.6	10.4	3.2	-1.0	4.7	14.1	8.8
Other Expenses	6.0	3.5	-9.0	17.4	1.6	2.0	-0.2	-6.0	9.5	9.2

Source: Company, MOFSL

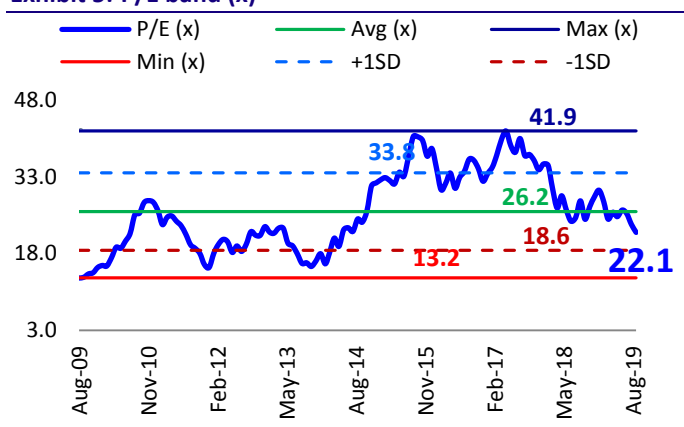
Valuation and view

- We cut our earnings estimate by 13%/11% for FY20/21 to factor in (a) the pressure on margins, given intense competition in the domestic business and (b) the weak exports outlook. We scale down our TP to INR695 as we assign a target multiple of 24x FY21E EPS. At CMP, the stock trades at FY20/21E P/E of 24x/21x. We maintain **Buy** given cheap valuations.

Exhibit 4: Change in estimates

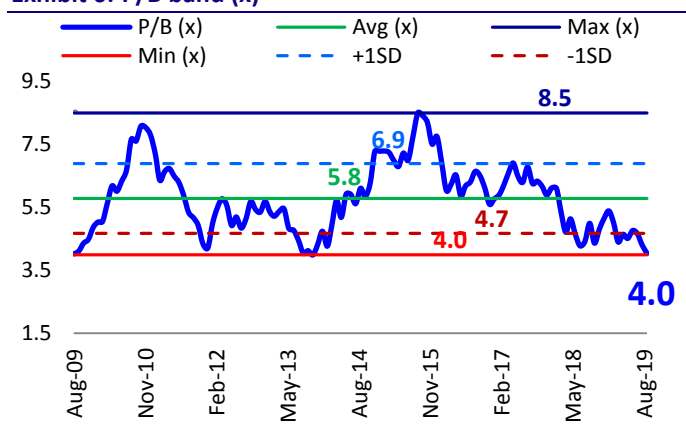
Earnings Change INR m	Old		New		Change	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Revenue	63,362	71,044	60,387	68,613	-5%	-3%
EBITDA	9,607	11,188	8,116	9,721	-16%	-13%
EBITDA margin	15.2%	15.7%	13.4%	14.2%	-1.7%	-1.6%
Reported PAT	7,918	9,032	6,874	8,005	-13%	-11%
Adj. PAT	7,918	9,032	6,874	8,005	-13%	-11%

Exhibit 5: P/E band (x)



Source: Company, MOFSL

Exhibit 6: P/B band (x)



Source: Company, MOFSL

Financials and valuations

Income Statement				(INR Million)	
Y/E March	2017	2018	2019	2020E	2021E
Total Revenues	50,773	50,825	56,590	60,387	68,613
Change (%)	7.8	0.1	11.3	6.7	13.6
Raw Materials	32,745	32,581	36,135	39,252	44,599
Staff Cost	4,334	4,979	5,458	5,989	6,560
Other Expenses	5,677	5,940	6,356	7,030	7,734
EBITDA	8,018	7,325	8,641	8,116	9,721
% of Total Revenues	15.8	14.4	15.3	13.4	14.2
Depreciation	848	938	1,103	1,179	1,293
Other Income	2,080	2,285	2,928	3,046	3,169
Interest	168	148	162	162	162
PBT	9,082	8,523	10,304	9,820	11,435
Tax	1,736	2,000	3,078	2,946	3,431
Rate (%)	19.1	23.5	29.9	30.0	30.0
Adjusted PAT	7,346	6,524	7,226	6,874	8,005
Extra-ordinary Income (net)	0	561	0	0	0
Reported PAT	7,346	7,085	7,226	6,874	8,005
Change (%)	-2.6	-3.6	2.0	-4.9	16.4

Balance Sheet				(INR Million)	
Y/E March	2017	2018	2019	2020E	2021E
Share Capital	554	554	554	554	554
Reserves	36,867	39,306	40,750	43,525	46,757
Net Worth	37,422	39,861	41,305	44,080	47,311
Loans	2,508	2,515	3,092	3,092	3,092
Deferred Tax Liability	24	299	988	988	988
Capital Employed	39,953	42,675	45,384	48,159	51,391
Gross Fixed Assets	22,705	28,665	29,676	32,676	35,676
Less: Depreciation	7,703	8,445	9,548	10,727	12,020
Net Fixed Assets	15,001	20,193	20,128	21,949	23,656
Capital WIP	4,631	380	1,585	1,585	1,585
Investments	7,074	5,487	2,853	2,853	2,853
Curr. Assets	23,702	29,253	33,970	35,435	38,855
Inventory	5,621	5,375	6,254	6,496	7,398
Debtors	9,557	13,263	12,727	13,221	15,055
Cash & Bank Balance	1,291	4,709	7,379	7,812	7,399
Loans & Advances	1,287	1,287	0	0	0
Other Assets	5,948	4,621	7,610	7,906	9,003
Current Liab. & Prov.	10,455	12,637	13,152	13,663	15,558
Current Liabilities	9,036	11,114	11,450	11,895	13,545
Provisions	1,419	1,523	1,702	1,768	2,013
Net Current Assets	13,247	16,616	20,818	21,772	23,296
Application of Funds	39,953	42,675	45,384	48,159	51,391

Financials and valuations

Ratios

Y/E March	2017	2018	2019	2020E	2021E
Basic (INR)					
Adj EPS	26.5	23.5	26.1	24.8	28.9
Cash EPS	29.6	26.9	30.0	29.1	33.5
Book Value	135.0	143.8	149.0	159.0	170.7
DPS	14.0	15.0	13.0	12.3	14.3
Payout (incl. Div. Tax.)	52.8	58.7	49.7	49.7	49.7
Valuation (x)					
P/E	22.8	25.6	23.1	24.3	20.9
Cash P/E	20.4	22.4	20.1	20.8	18.0
EV/EBITDA	21.0	22.5	18.8	20.0	16.8
EV/Sales	3.4	3.3	2.9	2.8	2.4
Price/Book Value	4.5	4.2	4.0	3.8	3.5
Dividend Yield (%)	2.3	2.5	2.1	2.0	2.4
Profitability Ratios (%)					
RoE	21.2	18.3	17.8	16.1	17.5
RoCE	20.0	16.1	16.9	15.3	16.6
RoIC	22.1	16.6	16.1	14.0	15.6
Turnover Ratios					
Debtors (Days)	69	95	82	82	82
Inventory (Days)	40	39	40	40	40
Creditors. (Days)	44	54	53	53	53
Asset Turnover (x)	1.3	1.2	1.2	1.3	1.3
Leverage Ratio					
Debt/Equity (x)	0.1	0.1	0.1	0.1	0.1

Cash Flow Statement

Y/E March	2017	2018E	2019E	2020E	2020E
(INR Million)					
PBT before EO Items	9,082	9,084	10,304	9,820	11,435
Depreciation	848	938	1,103	1,179	1,293
Interest	-9	-35	162	162	162
Direct Taxes Paid	-1,867	-1,823	-3,078	-2,946	-3,431
(Inc)/Dec in WC	371	(370)	(1,694)	(684)	(2,099)
CF from Operations	8,426	7,795	6,797	7,531	7,360
EO Income	-983	-1,464	662	0	0
CF from Oper. Incl. EO Items	7,443	6,331	7,459	7,531	7,360
(Inc)/Dec in FA	(2,315)	(905)	(2,217)	(3,000)	(3,000)
Free Cash Flow	5,128	5,426	5,242	4,531	4,360
Investment & Others	(2,538)	2,763	2,634	0	0
CF from Investments	-4,853	1,858	417	-3,000	-3,000
(Inc)/Dec in Networth	0	0	(1,473)	0	0
(Inc)/Dec in Debt	0	0	0	0	0
Interest Paid	-90	-100	0	0	0
Dividend Paid	-4,663	-4,639	-4,309	-4,099	-4,773
Others	2,508	8	576	0	0
CF from Fin. Activity	(2,245)	(4,731)	(5,206)	(4,099)	(4,773)
Inc/Dec of Cash	344	3,458	2,671	432	(413)
Add: Beginning Balance	897	1,239	4,709	7,379	7,812
Closing Balance	1,241	4,696	7,379	7,812	7,399

Corporate profile

Company description

Cummins India is a 51 % subsidiary of Cummins Inc. USA. Cummins India is the country's leading manufacturer of diesel and natural gas engines for power generation, industrial and automotive markets. Cummins in India is a group of eight legal entities (including Cummins India) across 200 locations in the country with a combined turnover of USD1.5b in 2013 and employing close to 9,000 individuals.

Exhibit 1: Sensex rebased

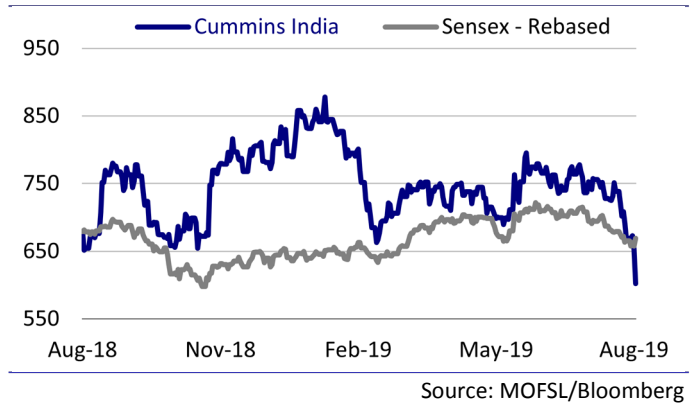


Exhibit 2: Shareholding pattern (%)

	Jun-19	Mar-19	Jun-18
Promoter	51.0	51.0	51.0
DII	27.9	27.2	23.1
FII	9.1	9.1	13.2
Others	12.1	12.7	12.7

Note: FII Includes depository receipts Source: Capitaline

Exhibit 3: Top holders

Holder Name	% Holding
Life Insurance Corporation Of India	4.5
Axis Mutual Fund Trustee Limited A/C Axis Mutual Fund A/C Axis Long Term Equity Fund	4.2
Sbi Blue Chip Fund	4.0
Reliance Capital Trustee Co Ltd.A/C Reliance Large Cap Fund	2.3
Franklin Templeton Mutual Fund A/C Franklin India Equity Fund	1.7

Source: Capitaline

Exhibit 4: Top management

Name	Designation
Mark A Levett	Chairman
Sandeep Sinha	Managing Director
Antonio Leitao	Director
Norbert Nusterer	Director
Suzanne Wells	Director

Source: Capitaline

Exhibit 5: Directors

Name	Name
Anjuly Chib Duggal*	Rajeev Bakshi*
Nasser Munjee*	Venu Srinivasan*
P S Dasgupta*	J M Barrowman
Prakash M Telang*	Donald G Jackson

*Independent

Exhibit 6: Auditors

Name	Type
Ajay Joshi and Associates	Cost Auditor
K R Chandratre	Secretarial Audit
S R B C & Co LLP	Statutory

Source: Capitaline

Exhibit 7: MOFSL forecast v/s consensus

EPS (INR)	MOFSL forecast	Consensus forecast	Variation (%)
FY20	24.8	28.5	-13.0
FY21	28.9	32.5	-11.0

Source: Bloomberg

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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