

Cummins India

Estimate change 
TP change 
Rating change 

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Bloomberg	KKC IN
Equity Shares (m)	277
M.Cap.(INRb)/(USDb)	121 / 1.6
52-Week Range (INR)	653 / 282
1, 6, 12 Rel. Per (%)	8/-13/-30
12M Avg Val (INR M)	514

Financials & Valuations (INR b)

Y/E Mar	2020	2021E	2022E
Sales	51.6	44.4	54.9
EBITDA	5.9	4.6	7.0
PAT	6.4	4.3	6.2
EBITDA (%)	11.4	10.5	12.7
EPS (INR)	23.3	15.7	22.3
EPS Gr. (%)	(10.8)	(32.5)	41.9
BV/Sh. (INR)	150.6	157.8	164.0

Ratios

Net D/E	0.0	(0.0)	(0.0)
RoE (%)	15.4	9.9	13.6
RoCE (%)	14.0	9.1	12.4
Payout (%)	90.3	56.8	72.0

Valuations

P/E (x)	18.8	27.8	19.6
P/BV (x)	2.9	2.8	2.7
EV/EBITDA (x)	20.7	25.7	17.3
Div Yield (%)	3.8	1.7	2.9
FCF Yield (%)	3.0	1.7	0.4

Shareholding pattern (%)

As On	Jun-20	Mar-20	Jun-19
Promoter	51.0	51.0	51.0
DII	28.9	30.4	27.9
FII	8.6	7.5	9.1
Others	11.6	11.2	12.1

FII Includes depository receipts

CMP: INR437

TP: INR330 (-24%)

Sell

Operating performance disappoints; Outlook weak

Export opportunity unlikely to pan out before FY23

- Cummins (KKC) reported weakest top line performance (-63%YoY) in our coverage universe as the company could operate for just one month in 1QFY21. Note that top line included INR1.9b (or 38% of 1QFY21 revenue) of deferred revenue from last quarter.
- Gross margin surprise was largely on account of favorable sales mix with higher contribution from the distribution business. This is likely to reverse as revenue should normalize hereon. Cost cutting benefits (from employee cost and other expenses) were lower than our expectations (v/s other companies in our coverage universe). We fear that cost cutting measures would not be able to make up for the weak revenue outlook.
- CPCB4+ led export opportunity remains a key positive for KKC. However, with the likely deferment of implementation by 9-12 months implies that any benefits from this opportunity would accrue only from FY23. We largely maintain our FY21/22E estimates and our TP of INR330. Maintain **Sell**.

Poor operating performance despite favorable sales mix

- Revenue declined 63% YoY to INR5.0b and was 33% below our expectation. EBITDA at INR29m barely achieved break-even (v/s est. INR382m). **Adj. PAT declined 80% to INR277m and was 45% below our expectation.**
- Domestic sales declined 64% YoY to INR3.6b – Power-gen (down 76%), Industrials (down 68%) and Distribution (down 47%). Exports too plunged 61% YoY to INR1.3b.
- Favorable sales mix as contribution from the higher-margin Distribution business stood at 38% (v/s 27% in FY20). This led to improvement in gross margin to 41% (v/s 34% in 1QFY20). Despite the gross margin surprise, EBITDA margin failed to cheer sentiment as cost cutting benefits from employee cost and other expenses could not offset the poor top line growth.

Key management call highlights

- Power gen – hospitals, data centers, and critical power application projects are recovering faster. However, critical end markets of commercial and residential real estate and hospitality remain weak.
- Distribution should rebound faster than other segments as refurbishment of existing equipment would be a top priority for most customers.
- CPCB4+ norms are likely to be deferred by nine months (v/s earlier timeline of Jul'21). This may open up potential exports to the developed markets of the US and China. However, it is difficult to quantify the opportunity currently. Thus, any export gains may accrue only in FY23, in our view.

Valuation and view

- We largely maintain our FY21/FY22E estimates and our TP of INR330 (15x Mar'22E EPS). Other income (largely driven by dividend and rental income), constituted 43% of PBT in FY20 and supported the company's overall RoE. Adj. for the same, RoE declined to 8.9% in FY20 from reported 15.4%, indicating pain in the core business. Maintain **Sell**.

Quarterly Performance

(INR M)

	FY20				FY21E				FY20	FY21E	MOSL	Var.
Y/E March	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q			1QE	(%)
Sales	13,430	13,084	14,534	10,528	4,982	11,776	14,534	13,073	51,577	44,365	7,387	-32.6%
Change (%)	1.1	-12.0	-3.3	-21.5	-62.9	-10.0	0.0	24.2	-8.9	-14.0	-45.0	
EBITDA	1,514	1,525	2,158	667	29	1,341	1,848	1,430	5,863	4,647	382	-92.4%
Change (%)	-29.5	-39.2	-4.8	-61.2	-98.1	-12.1	-14.4	114.5	-20.2	-40.0	-74.8	
As of % Sales	11.3	11.7	14.8	6.3	0.6	11.4	12.7	10.9	11.4	10.5	5.2	
Depreciation	291	293	296	308	303	310	320	323	1,187	1,256	310	
Interest	52	55	47	49	43	50	50	57	203	200	50	
Other Income	769	926	723	898	666	650	650	655	3,315	2,621	650	
PBT	1,940	2,102	2,538	1,208	349	1,631	2,128	1,706	7,789	5,813	672	-48.1%
Tax	525	269	551	-5	72	411	536	444	1,341	1,463	169	
Effective Tax Rate (%)	27.1	12.8	21.7	(0.4)	20.7	25.2	25.2	26.0	17.2	25.2	25.2	
Adjusted PAT	1,415	1,833	1,988	1,213	277	1,220	1,591	1,262	6,448	4,350	503	-44.9%
Change (%)	(22.7)	(13.4)	6.2	(13.9)	(80.4)	(33.5)	(19.9)	4.1	(10.8)	(32.5)	(64.5)	
Extra-ordinary Income (net)	-	-	(125)	(30)	249	-	-	-	(155)	249	-	
Reported PAT	1,415	1,833	1,862	1,183	526	1,220	1,591	1,262	6,293	4,599	503	4.6%
Change (%)	(22.7)	(13.4)	(0.5)	(16.0)	(62.9)	(33.5)	(14.5)	6.7	(12.9)	(26.9)	(64.5)	

Exhibit 1: Domestic revenue declined 64% YoY in 1QFY21

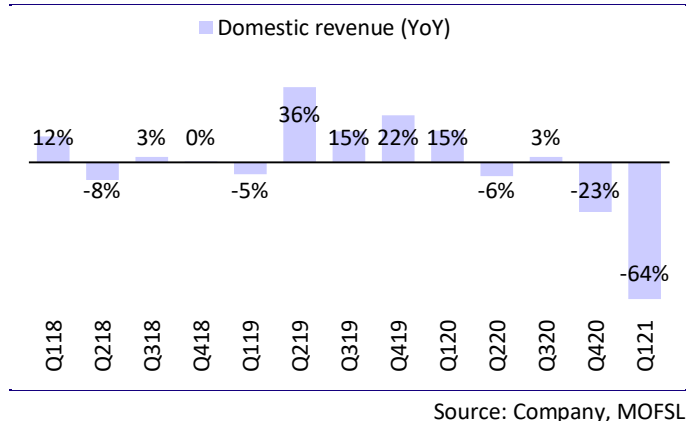


Exhibit 2: Exports declined 61% YoY in 1QFY21

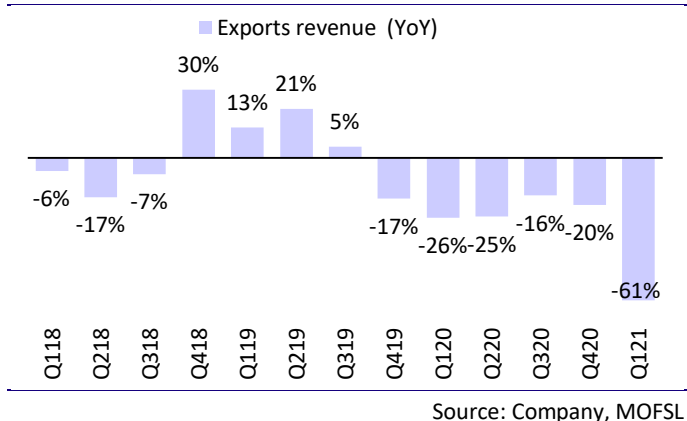


Exhibit 3: Overall revenue declined 63% in 1QFY21

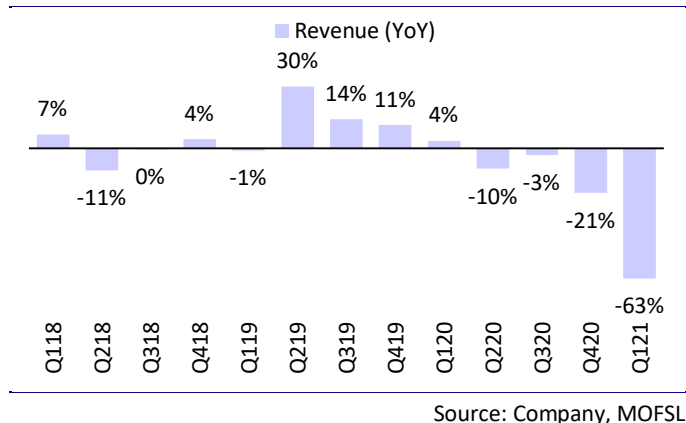
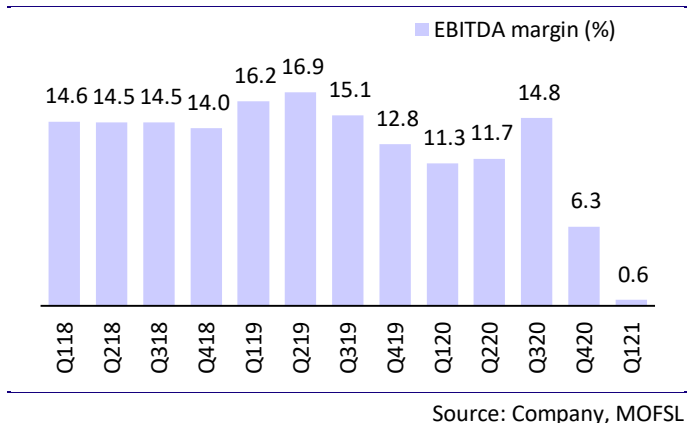
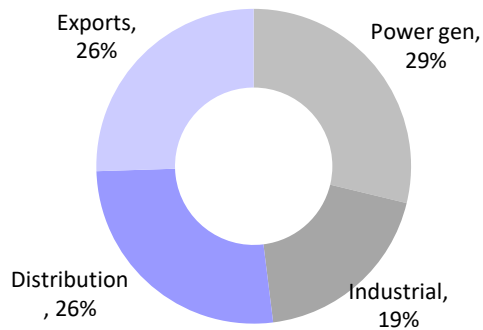


Exhibit 4: EBITDA margin plunged due to lower absorption of fixed cost



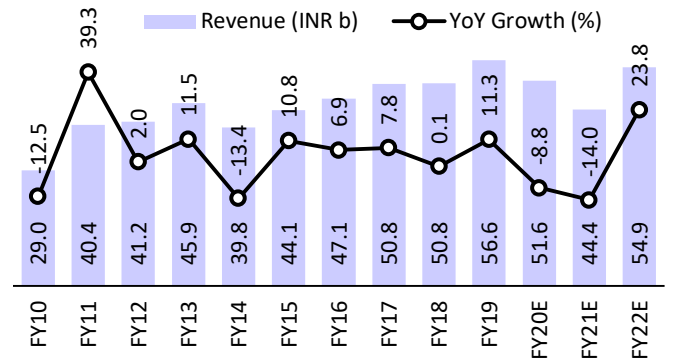
Story in charts

Exhibit 5: FY20 revenue break-up



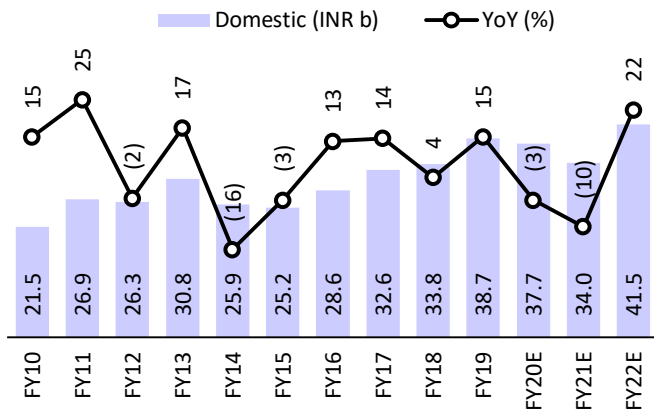
Source: Company, MOFSL

Exhibit 6: Overall revenue expected at 3.2% CAGR over FY20-22E



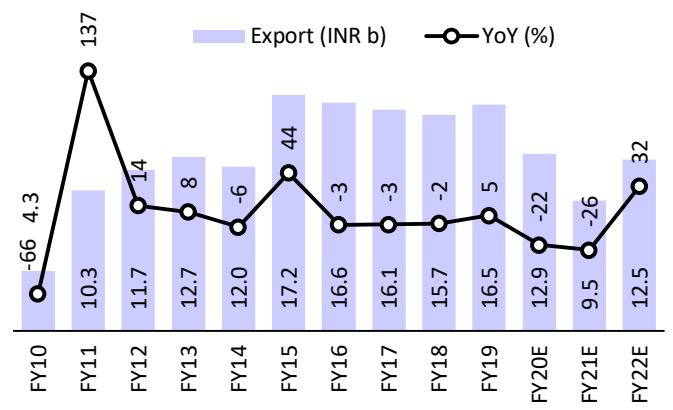
Source: Company, MOFSL

Exhibit 7: Domestic segment expected to post ~5% CAGR over FY20-22E



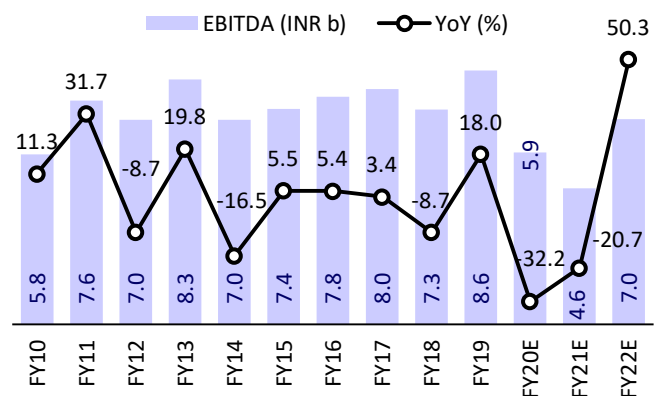
Source: Company, MOFSL

Exhibit 8: Exports should remain flat over FY20-22E



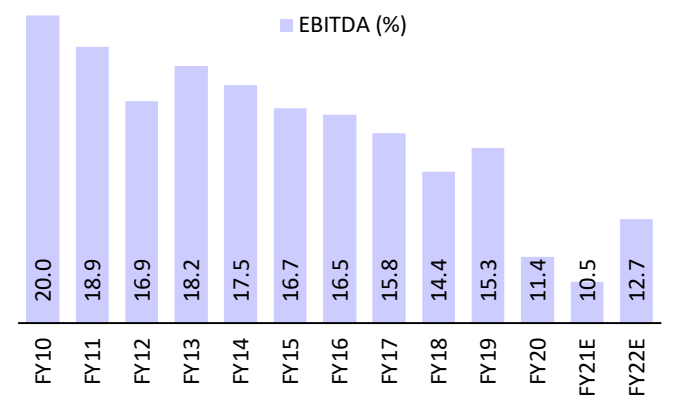
Source: Company, MOFSL

Exhibit 9: EBITDA expected at 9.2% CAGR over FY20-22E...



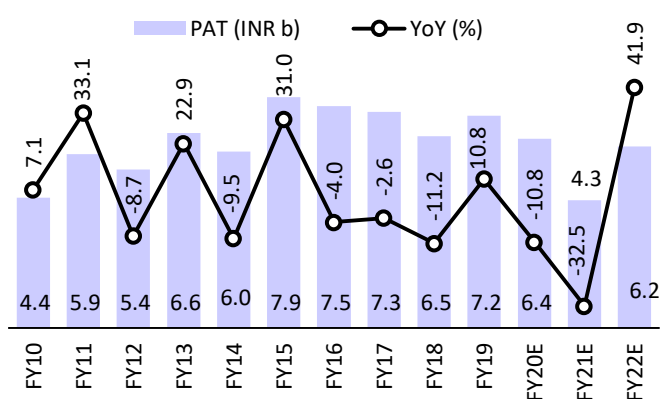
Source: Company, MOFSL

Exhibit 10: ...as EBITDA margins are likely to expand owing to cost-cutting measures



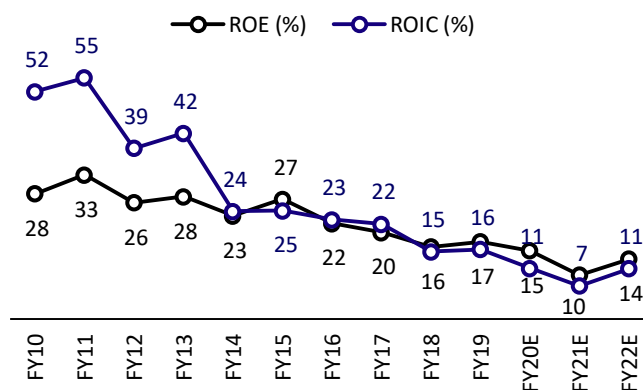
Source: Company, MOFSL

Exhibit 11: PAT growth should remain flat over FY20-22E



Source: Company, MOFSL

Exhibit 12: RoE/RoIC have gradually declined over FY10-20



Source: Company, MOFSL

Highlights from management commentary

- Power gen sales plunged 76% YoY to INR960m, Industrial sales declined 68% YoY to INR800m and Distribution sales dropped 47% YoY to INR1.8b.
- Note that the company operated for just one month during 1QFY21.
- **Demand revival:** Demand in rental, healthcare and data center is recovering. Commercial realty, hospitality, residential realty and manufacturing are also reviving gradually (lower than other segments). Hospitality is in pretty bad shape and would take more time to recover. Current capacity utilization stands at 65-70% (v/s pre-COVID level).
- **Margins:** Higher gross margin was on account of the favorable sales mix – higher proportion of distribution, better mix between HHP and LHP. **Should revert to normal as revenue normalizes.** The company remains focussed on reducing material cost and keeping other costs under control to inch back to its historical margin range.
- **Emission norms update:** As of now, there has been no notification on CPCB4+, but expect the implementation to get postponed (likely by three quarters). The new emission norms do open up export opportunity for KKC in developed markets. Globally, KKC has manufacturing bases in the US, China and India. If KKC India betters its cost and delivery, opportunities could come up for the company.
- Rental income from captive continues at earlier rate. There has been no renegotiation as of now.
- **There was some element of backlog, which could not have been shipped during the Mar'20 quarter (~INR1.9b).**
- The government is focussed on infra development. Spending has been good in the first quarter. Also, the construction end market has not slowed down.

Valuation and view

- We largely maintain our FY21/FY22E estimates and our TP of INR330 (15x Mar'22E EPS). Other income (largely driven by dividend and rental income), constituted 43% of PBT in FY20 and supported the company's overall RoE. Adj. for the same, RoE declined to 8.9% in FY20 from reported 15.4%, indicating pain in the core business. Maintain **Sell**.

Financials and valuations

Income Statement						(INR m)
Y/E March	2018	2019	2020	2021E	2022E	2023E
Total Revenues	50,825	56,590	51,577	44,365	54,908	60,009
Change (%)	0.1	11.3	-8.9	-14.0	23.8	9.3
Raw Materials	32,581	36,135	33,679	28,616	35,965	39,306
Staff Cost	4,979	5,458	5,602	5,113	5,369	5,637
Other Expenses	5,940	6,356	6,434	5,989	6,589	7,201
EBITDA	7,325	8,641	5,863	4,647	6,986	7,865
% of Total Revenues	14.4	15.3	11.4	10.5	12.7	13.1
Depreciation	938	1,103	1,187	1,256	1,354	1,472
Other Income	2,285	2,928	3,315	2,621	2,819	3,037
Interest	148	162	203	200	200	200
PBT	8,523	10,304	7,789	5,813	8,251	9,230
Tax	2,000	3,078	1,341	1,463	2,077	2,323
Rate (%)	23.5	29.9	17.2	25.2	25.2	25.2
Adjusted PAT	6,524	7,226	6,448	4,350	6,174	6,907
Extra-ordinary Income	561	0	-155	249	0	0
Reported PAT	7,085	7,226	6,293	4,599	6,174	6,907
Change (%)	-3.6	2.0	-12.9	-26.9	34.3	11.9

Balance Sheet						(INR m)
Y/E March	2018	2019	2020	2021E	2022E	2023E
Share Capital	554	554	554	554	554	554
Reserves	39,306	40,750	41,195	43,184	44,913	46,847
Net Worth	39,861	41,305	41,750	43,738	45,467	47,401
Loans	2,515	3,092	4,854	4,854	4,854	4,854
Deferred Tax Liability	299	988	800	800	800	800
Capital Employed	42,675	45,384	47,404	49,392	51,121	53,055
Gross Fixed Assets	28,665	29,676	32,837	32,955	35,955	38,955
Less: Depreciation	8,445	9,548	10,499	9,873	11,227	12,698
Net Fixed Assets	20,193	20,128	22,338	23,082	24,728	26,256
Capital WIP	380	1,585	800	800	800	800
Investments	5,487	2,853	8,240	8,240	8,240	8,240
Curr. Assets	29,253	33,970	28,163	27,710	30,274	31,880
Inventory	5,375	6,254	5,729	4,928	6,099	6,666
Debtors	13,263	12,727	11,316	10,696	12,035	13,153
Cash & Bank Balance	4,709	7,379	4,538	6,426	5,136	4,406
Loans & Advances	1,287	0	0	0	0	0
Other Assets	4,621	7,610	6,579	5,659	7,004	7,655
Current Liab. & Prov.	12,637	13,152	12,137	10,440	12,921	14,121
Current Liabilities	11,114	11,450	9,650	8,300	10,273	11,227
Provisions	1,523	1,702	2,487	2,139	2,648	2,894
Net Current Assets	16,616	20,818	16,026	17,270	17,353	17,759
Application of Funds	42,675	45,384	47,404	49,392	51,121	53,055

Financials and valuations

Ratios

Y/E March	2018	2019	2020	2021E	2022E	2023E
Basic (INR)						
Adj EPS	23.5	26.1	23.3	15.7	22.3	24.9
Cash EPS	28.9	30.0	27.0	21.1	27.2	30.2
Book Value	143.8	149.0	150.6	157.8	164.0	171.0
DPS	14.0	16.4	16.4	7.5	12.8	14.4
Payout (incl. Div. Tax.)	65.5	78.6	90.3	56.8	72.0	72.0
Valuation (x)						
P/E	18.5	16.7	18.7	27.8	19.6	17.5
Cash P/E	15.0	14.5	16.1	20.7	16.1	14.5
EV/EBITDA	16.2	13.5	20.6	25.7	17.3	15.5
EV/Sales	2.3	2.1	2.3	2.7	2.2	2.0
Price/Book Value	3.0	2.9	2.9	2.8	2.7	2.6
Dividend Yield (%)	3.2	3.8	3.8	1.7	2.9	3.3
Profitability Ratios (%)						
RoE	16.4	17.5	15.4	9.9	13.6	14.6
RoCE	15.6	16.2	14.0	9.1	12.4	13.3
RoIC	15.7	15.0	11.2	7.3	11.2	11.8
Turnover Ratios						
Debtors (Days)	95	82	80	88	80	80
Inventory (Days)	39	40	41	41	41	41
Creditors. (Days)	54	53	49	49	49	49
Asset Turnover (x)	1.2	1.2	1.1	0.9	1.1	1.1
Leverage Ratio						
Net Debt/Equity (x)	-0.1	-0.1	0.0	0.0	0.0	0.0

Cash Flow Statement

(INR m)

Y/E March	2018	2019	2020	2021E	2022E	2023E
PBT before EO Items	9,084	10,304	7,634	5,813	8,251	9,230
Depreciation	938	1,103	1,187	1,256	1,354	1,472
Interest & other	-2,136	-1,205	-1,366	-2,172	-2,619	-2,837
Direct Taxes Paid	-2,000	-2,361	-1,609	-1,463	-2,077	-2,323
(Inc)/Dec in WC	49	-2,341	144	644	-1,374	-1,135
CF from Operations	5,935	5,500	5,990	4,077	3,536	4,407
(Inc)/Dec in FA	-1,709	-2,734	-2,366	-2,000	-3,000	-3,000
Free Cash Flow	4,226	2,766	3,624	2,077	536	1,407
Investment & Others	3,872	5,103	-2,392	2,621	2,819	3,037
CF from Investments	2,163	2,369	-4,758	621	-181	37
(Inc)/Dec in Debt	8	576	1,762	0	0	0
Interest Paid	-148	-121	-154	-200	-200	-200
Dividend Paid	-4,639	-5,681	-5,681	-2,610	-4,445	-4,973
CF from Fin. Activity	-4,779	-5,226	-4,073	-2,810	-4,645	-5,173
Inc/Dec of Cash	3,319	2,643	-2,841	1,888	-1,291	-729
Add: Beginning Balance	1,291	4,709	7,379	4,538	6,426	5,136
Closing Balance	4,709	7,379	4,538	6,426	5,136	4,406

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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