

07 August 2023

India | Equity research | Q1FY24 result review

Cummins India

Capital Goods

Pre-buying and domestic business led strong performance

Cummins India reported revenue / EBITDA / PAT growth of 31% / 59% / 51% YoY at INR 22.1bn / 3.4bn / 3.2bn respectively. Powergen segment (+76% YoY) benefited from domestic and pre-buying demand. The Central Pollution Control Board (CPCB) has changed the deadline for CPCB II genset sales to Jun'24. ([Link to Memorandum: Link](#)). Exports were flat because of weakness in the key markets. EBITDA margin was at 15.4% while guidance of 100bps YoY expansion still holds. Distribution business gained strong foothold, which we believe will likely continue on the back of specialised servicing & maintenance requirements post launch of the new norms. Maintain **HOLD** with a revised target price of **INR 1,707** (earlier: INR 1,736).

Powergen – Finally moving up the technology ladder

Cummins' powergen segment finally moved up the technology ladder with the introduction of CPCB IV+ gensets on 1st Jul'23 (for up to 800kVA). Pre-buying led to 76% YoY growth in the segment's quarterly revenue. However, the Central Pollution Control Board (CPCB) issued a memorandum allowing the sale of CPCB II gensets until 30th Jun'24. We believe implementation of CPCB 4+ will be gradual.

Exports growth was flat

Exports worth INR 5bn during Q1FY24 were flat YoY and QoQ. This was primarily due to weakness in Latin America, APAC, Europe and Africa. Within product categories, both LHP and HHP witnessed flat growth. Management plans to increase their market share in these regions with more aggressive strategies amidst slowdown.

Distribution business gained strong foothold

Distribution business revenue grew 28% YoY to INR 5.3bn. The quarterly run-rate has improved from INR 3bn in FY21 to >INR 5bn. We expect this to continue with increasing electrical content post implementation of CPCB IV+.

Maintain HOLD with a revised target price of INR 1,707

While the domestic market continues to be robust, slowdown in exports remains a key monitorable in the short term. Factoring-in higher employee costs and weak EBITDA margin, we tweak our estimates for FY24E/FY25E.

Financial summary

Y/E Mar-31 (INR mn)	FY22A	FY23A	FY24E	FY25E
Net Revenue	60,256	76,123	88,622	1,03,445
EBITDA	8,851	12,426	13,855	16,755
EBITDA Margin (%)	14.7	16.3	15.6	16.2
Net Profit	9,667	12,098	13,613	16,453
EPS (Rs)	34.9	43.6	49.1	59.4
EPS % Chg YoY	22.1	51.7	12.0	22.2
P/E (x)	66.0	43.5	38.9	31.8
EV/EBITDA (x)	53.3	37.5	33.3	27.1
RoCE (%)	15.8	21.1	21.3	22.9
RoE (%)	18.0	24.0	23.7	24.8

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Market Data

Market Cap (INR)	498bn
Market Cap (USD)	6,021mn
Bloomberg Code	KKC IN
Reuters Code	CUMM.BO
52-week Range (INR)	1,981 / 1,104
Free Float (%)	49.0
ADTV-3M (mn) (USD)	15.1

Price Performance (%)	3m	6m	12m
Absolute	12.5	26.0	54.7
Relative to Sensex	7.2	9.0	14.2

ESG Disclosure	2021	2022	Change
ESG score	46.0	56.1	10.1
Environment	24.9	39.9	14.9
Social	34.3	43.4	9.1
Governance	78.6	84.9	6.3

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: Bloomberg, I-sec research

Earnings Revisions (%)	FY24E	FY25E
Revenue	0.5	(0.1)
EBITDA	(5.8)	(6.9)
EPS	(3.7)	(3.2)

Previous Reports

28-05-2023: [Q4FY23 results review](#)

09-02-2023: [Q3FY23 results review](#)

Concall highlights

Financial performance update

- Domestic powergen sales for the quarter came in at INR 8.7bn (up 76% YoY).
- Distribution sales were at INR 5.3bn (up 28% YoY).
- Industrial domestic business sales stood at INR 2.4bn (flat YoY).
- LFP exports were at INR 2bn (flat YoY).
- Segmental breakup of revenues:
 - Low horsepower: INR 1bn
 - Mid-range horsepower: INR 2.7bn
 - Heavy-duty segment: INR 1.1bn
 - High horsepower: INR 3.9bn

Guidance

Cummins guided for double-digit revenue growth for FY24.

CPCB IV+ Implementation

- Company has successfully launched CPCB IV+ compliant gensets.
- Government has announced at the last minute that CPCB gensets can be produced and sold till the 30th Jun'24.
- Cummins has a full orderbook of gensets for deliveries up to Jun'24. It is not concerned about the product or orderbook, but with figuring out the right mix of both CPCB II and CPCB IV+ product lines and supply chains.
- Price of new CPCB IV+ gensets can increase by 20-50% depending on various factors such as volumes, specifications, etc.
- Localisation of CPCB IV engines is >80% and Cummins will eventually increase it to 90%. The last 10% is very difficult to localise because some of the electronic components are not made in India.
- 15-25% of FY24 revenue is expected come from CPCBIV+ genset sales.

Markets/customers who might directly move to CPCB IV+

CPCB IV+ gensets are being adopted in Delhi NCR Region as CPCB II gensets were not allowed to run for several months of the year unless they install retrofit kits which are very expensive.

Exports

- CPCB IV+ gensets are the lowest-emission gensets in the world, which opens up other geographies for Cummins. Company is reconfiguring some of its products for other markets as the Indian configuration cannot directly be used in other countries. For instance, India and North America operate on 50 Hertz and 60 Hertz electrical cycles respectively, hence the engines in the two territories operate at different RPMs.
- Cummins is witnessing significant slowdown in Europe. Asia-Pacific, Latin America and North America regions too have slowed down and Africa markets remain flat.
- Company is contemplating whether to launch new products to try gaining market share in a declining market by leveraging the lower cost base in India.

Margins

- Company continues to maintain its target of 100bps YoY improvement in margins.
- Margins have reduced QoQ because of increase in wage increments and some one-time expenses such as warranty.

Market outlook

Short term: Pre-buying in the past has led to good quarterly growth. Hence the management expects demand to slow down in the short term.

Long term: Company expects the market to grow at ~2x GDP growth because, as the market becomes more dependent on power, sensitivity of power cuts and unreliable grid power increases.

Distribution business

- Cummins is offering longer and better maintenance packages with its products because, with time, the products have become complicated with increase in electronic components. With comprehensive packages over the longer-term, the customer remains with Cummins and purchases genuine parts from Cummins.
- In India, penetration of Cummins in distribution is lower compared to that of Cummins companies in other parts of the world.

Exhibit 1: Q1FY24 result highlights

INR mn	Q1FY24	Q1FY23	YoY(%)	Q4FY23	QoQ(%)	FY23	FY22	YoY(%)
Net Sales	22,087	16,867	31.0	19,260	14.7	77,444	61,404	26.1
EBITDA	3,406	2,138	59.3	3,216	5.9	11,202	8,851	26.6
Margin	15.4	12.7	274bps	16.7	-128bps	14.5	14.4	5bps
Depreciation	358	337	6.4	372	(3.8)	1,405	1,340	4.8
Finance Cost	77	19	295.9	66	17.3	158	115	37.2
Other Income	1,175	1,001	17.4	1,306	(10.1)	4,200	2,875	46.1
Extraordinary income	-	(143)		14		(129)	1,324	
PBT	4,146	2,641	57.0	4,098	1.2	13,710	10,271	33.5
Tax	989	653	51.6	930	6.3	2,956	2,728	8.4
tax rate	23.9	24.7	-86bps	22.7	115bps	21.6	26.6	-500bps
Reported PAT	3,157	1,988	58.8	3,167	(0.3)	10,754	7,879	36.5
Adjusted PAT	3,157	2,095	50.7	3,157	(0.0)	10,851	6,886	57.6
Margin(%)	14.3	12.4	187bps	16.4	-210bps	14.0	11.2	280bps
EPS	11.4	7.6		11.4		39.1	24.8	57.6

Source: Company data, I-Sec research

Exhibit 2: Quarterly segmental trend

INR mn	Q1FY24	Q1FY23	YoY(%)	Q4FY23	QoQ(%)	FY23	FY22	YoY(%)
Revenues								
PowerGen	8,730	4,960	76.0	6,720	29.9	25,550	19,690	29.8
Distribution	5,340	4,160	28.4	4,830	10.6	18,720	14,840	26.1
Industrial	2,360	2,370	(0.4)	2,170	8.8	10,460	8,990	16.4
Domestic	16,770	11,720	43.1	13,960	20.1	55,600	43,520	27.8
Exports	4,980	4,850	2.7	4,930	1.0	20,500	16,100	27.3
Total	21,750	16,570	31.3	18,890	15.1	76,100	60,300	26.2

Source: Company data, I-Sec research

Outlook and Valuation

We expect a slight slowdown in the short term due to the high growth as a result of strong pre-buying trend induced by CPCB IV+ norms. Factoring-in higher employee costs and weak EBITDA margins, we tweak our estimates for FY24E/FY25E. We have broadly maintained our revenue estimates while cutting EBITDA estimates for FY24E and FY25E by 5% each, and cut PAT for FY24E and FY25E by 3% and 2% respectively.

We continue to assign a core earnings valuation multiple of 30x FY25E and add back the cash and discount the lease rentals @6% for 5 years. This leads to a target price of **INR 1,707** (previously: INR 1,736). Maintain **HOLD**.

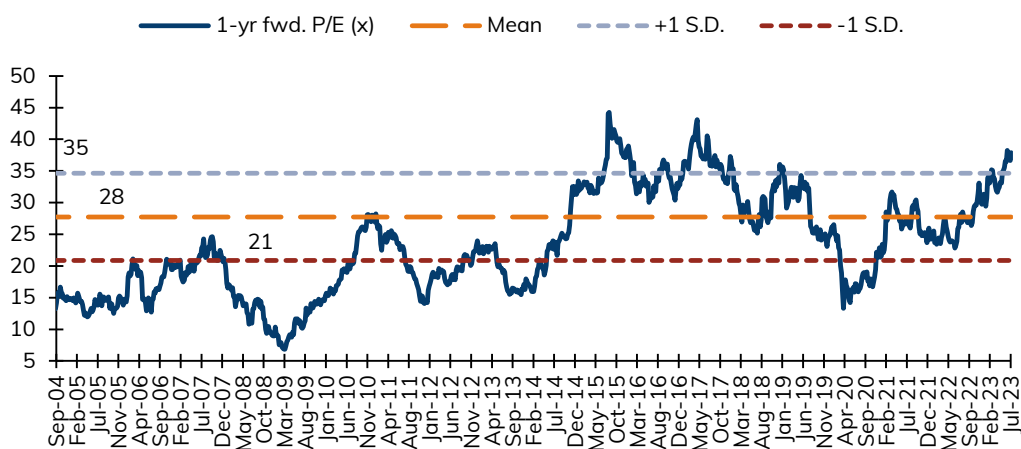
Key risks: i) Delay in passing on of input costs might impact margins, ii) further disruption in the supply chain.

Exhibit 3: Valuation summary

INR mn	FY25E
PAT (X)	15,653
Tax rate (%)	25.5
Interest & dividend income	1,700
Rental Income	1,571
Operating PAT	13,216
P/E multiple (x)	30
Value	3,96,481
Cash & Cash Equivalent	35,894
Gross value	4,32,375
Cummins Standalone value per share (INR)	1,560
Discounted Lease contribution	7,606
Lease contribution value per share (INR)	27
Valvoline PAT	2,228
P/E multiple (x)	30
Valvoline Gross value	66,606
Holding value (50% stake)	33,303
Valvoline value per share (INR)	120
Total value per share (INR)	1,707

Source: I-Sec research

Exhibit 4: Historical P/E



Source: Bloomberg, I-Sec research

Exhibit 5: Earnings revision

INR mn	FY24E			FY25E		
	Previous	Revised	% chg	Previous	Revised	% chg
Revenues*	89,498	89,969	0.5	1,04,901	1,04,820	(0.1)
EBITDA	14,714	13,855	(5.8)	17,995	16,755	(6.9)
Adj PAT	13,306	12,813	(3.7)	16,167	15,653	(3.2)

Source: I-Sec research | *Includes other operating revenue

Exhibit 6: Key assumptions

INR mn	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
PowerGen	13,946	16,000	14,350	11,350	19,690	25,550	32,704	39,572
% YoY		14.7	(10.3)	(20.9)	73.5	29.8	28.0	21.0
Industrial	7,730	9,230	9,960	7,661	8,990	10,460	12,134	14,318
% YoY		19.4	7.9	(23.1)	17.3	16.4	16.0	18.0
Distribution	12,620	13,500	13,400	12,020	14,840	18,720	22,464	26,957
% YoY		7.0	(0.7)	(10.3)	23.5	26.1	20.0	20.0
Domestic	34,296	38,730	37,710	31,031	43,520	54,730	67,302	80,846
% YoY		12.9	(2.6)	(17.7)	40.2	25.8	23.0	20.1
Exports	16,007	16,527	12,906	11,530	16,100	20,500	21,320	22,599
% YoY		3.2	(21.9)	(10.7)	39.6	27.3	4.0	6.0
Total	50,303	55,257	50,616	42,561	60,256	76,123	88,622	1,03,445

Source: Company data, I-Sec research

Exhibit 7: Shareholding pattern

%	Dec'22	Mar'23	Jun'23
Promoters	51.0	51.0	51.0
Institutional investors	35.5	37.8	37.8
MFs and other	21.2	20.2	20.2
FIs/ Banks	0.0	0.0	0.0
Insurance Cos.	3.8	3.3	3.3
FIIIs	12.4	14.3	14.3
Others	13.5	11.2	11.2

Source: Bloomberg, I-Sec research

Exhibit 8: Price chart



Source: Bloomberg, I-Sec research

Financial summary

Exhibit 9: Profit & Loss

(INR mn, year ending Mar-31)

	FY22A	FY23A	FY24E	FY25E
Net Sales	60,256	76,123	88,622	1,03,445
Operating Expenses	11,485	12,709	15,385	17,206
EBITDA	8,851	12,426	13,855	16,755
EBITDA Margin (%)	14.7	16.3	15.6	16.2
Depreciation & Amortization	1,340	1,405	1,461	1,519
EBIT	7,511	11,022	12,394	15,236
Interest expenditure	115	158	200	250
Other Non-operating Income	2,875	4,200	5,005	6,024
Recurring PBT	10,271	15,064	17,199	21,011
Profit / (Loss) from Associates	800	800	800	800
Less: Taxes	2,728	3,623	4,386	5,358
PAT	7,543	11,441	12,813	15,653
Less: Minority Interest	-	-	-	-
Extraordinaries (Net)	1,324	(143)	-	-
Net Income (Reported)	9,667	12,098	13,613	16,453
Net Income (Adjusted)	8,343	12,241	13,613	16,453

Source Company data, I-Sec research

Exhibit 10: Balance sheet

(INR mn, year ending Mar-31)

	FY22A	FY23A	FY24E	FY25E
Total Current Assets	38,133	40,203	46,627	56,529
of which cash & cash eqv.	14,267	13,808	15,963	20,804
Total Current Liabilities & Provisions	13,391	15,253	17,137	19,684
Net Current Assets	24,742	24,950	29,489	36,845
Investments	15,939	21,042	23,368	25,883
Net Fixed Assets	11,954	11,698	11,563	11,544
ROU Assets	-	-	-	-
Capital Work-in-Progress	804	413	413	413
Total Intangible Assets	-	-	-	-
Other assets	1,122	1,647	1,712	1,779
Deferred Tax assests	-	-	-	-
Total Assets	54,660	59,867	66,663	76,582
Liabilities				
Borrowings	3,933	3,500	3,000	2,500
Deferred Tax Liability	971	1,057	1,057	1,057
provisions	799	1,016	1,016	1,016
other Liabilities	430	614	330	330
Equity Share Capital	554	554	554	554
Reserves & Surplus	47,972	53,125	60,705	71,124
Total Net Worth	48,527	53,680	61,259	71,679
Minority Interest	-	-	-	-
Total Liabilities	54,660	59,867	66,663	76,582

Source Company data, I-Sec research

Exhibit 11: Cashflow statement

(INR mn, year ending Mar-31)

	FY22A	FY23A	FY24E	FY25E
Operating Cashflow	9,345	12,137	11,741	14,840
Working Capital Changes	331	752	(1,073)	(813)
Capital Commitments	(910)	(1,609)	(1,500)	(1,500)
Free Cashflow	10,255	13,746	13,241	16,340
Other investing cashflow	(2,509)	(4,704)	(2,096)	(2,515)
Cashflow from Investing Activities	(3,418)	(6,313)	(3,596)	(4,015)
Issue of Share Capital	868	483	0	0
Interest Cost	(115)	(158)	(200)	(250)
Inc (Dec) in Borrowings	3,777	(433)	(500)	(500)
Dividend paid	(5,128)	(6,542)	(5,234)	(5,234)
Others	1,796	5,070	2,040	2,515
Cash flow from Financing Activities	1,197	(1,579)	(3,894)	(3,469)
Chg. in Cash & Bank balance	7,124	4,245	4,251	7,356
Closing cash & balance	16,776	18,512	18,059	23,319

Source Company data, I-Sec research

Exhibit 12: Key ratios

(Year ending Mar-31)

	FY22A	FY23A	FY24E	FY25E
Per Share Data (INR)				
Reported EPS	27.2	41.3	46.2	56.5
Adjusted EPS (Diluted)	34.9	43.6	49.1	59.4
Cash EPS	39.7	48.7	54.4	64.8
Dividend per share (DPS)	18.5	23.6	18.9	18.9
Book Value per share (BV)	175.1	193.7	221.0	258.6
Dividend Payout (%)	68.0	57.2	40.8	33.4
Growth (%)				
Net Sales	41.6	26.3	16.4	16.7
EBITDA	52.7	40.4	11.5	20.9
EPS (INR)	22.1	51.7	12.0	22.2
Valuation Ratios (x)				
P/E	66.0	43.5	38.9	31.8
P/CEPS	45.2	36.9	33.0	27.7
P/BV	10.3	9.3	8.1	6.9
EV / EBITDA	53.3	37.5	33.3	27.1
P / Sales	8.3	6.5	5.6	4.8
Dividend Yield (%)	1.0	1.3	1.1	1.1
Operating Ratios				
Gross Profit Margins (%)	33.7	33.0	33.0	32.8
EBITDA Margins (%)	14.7	16.3	15.6	16.2
Effective Tax Rate (%)	26.6	24.0	25.5	25.5
Net Profit Margins (%)	12.5	15.0	14.5	15.1
NWC / Total Assets (%)	19.2	18.6	20.3	20.9
Net Debt / Equity (x)	(0.5)	(0.6)	(0.6)	(0.6)
Net Debt / EBITDA (x)	(3.0)	(2.5)	(2.6)	(2.6)
Profitability Ratios				
RoCE (%)	15.8	21.1	21.3	22.9
RoE (%)	18.0	24.0	23.7	24.8
RoC (%)	15.8	21.1	21.3	22.9
Fixed Asset Turnover (x)	5.3	6.5	7.7	9.1
Inventory Turnover Days	51	47	45	45
Receivables Days	87	84	81	81
Payables Days	70	60	57	56

Source Company data, I-Sec research

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