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Q1FY22 result review and earnings revision

Capital Goods

Target price: Rs995

Earnings revision

(%)	FY22E	FY23E
Sales	↑ 1.7	↑ 1.7
EBITDA	↑ 5.9	↑ 4.4
PAT	↑ 14.3	↑ 7.8

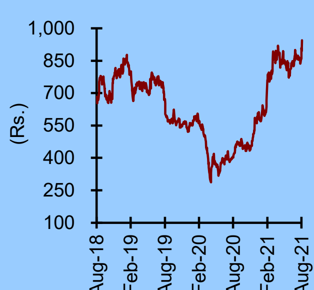
Target price revision
Rs995 from Rs927

Shareholding pattern

	Dec '20	Mar '21	Jun '21
Promoters	51.0	51.0	51.0
Institutional investors	35.2	36.2	36.1
MFs and others	17.1	15.9	16.5
FIs/Banks/Ins	9.1	9.3	7.7
FIIs	9.0	11.0	11.9
Others	13.8	12.8	12.9

Source: NSE

Price chart



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INDIA

Cummins India

ADD
Maintain
Rs945

Healthy growth aided by revival in exports

Cummins India's (Cummins) revenue grew 137% YoY to Rs11.8bn (Isec:Rs10.6bn) in Q1FY22, aided by 144% YoY growth in exports at Rs3.1bn and domestic growth recovery by 140% YoY to Rs8.6bn. Despite the overall logistical and other oxygen-related bottlenecks, demand has been strong. The export growth recovery is likely to continue given the overall uptick in demand from most geographies. Government is likely to adhere to emission norm deadline and this can result in market consolidation in medium to long term. Factoring in beat in performance, we raise FY22E and FY23E earnings by 14.3% and 7.8%, respectively. Given the revival in exports and beat in domestic execution, we maintain ADD with a revised SoTP-based target price of Rs995 (previously: Rs927).

- **Strong execution indicates pent-up demand and revival in investments:** Revenue grew 137% YoY and declined 5% QoQ to Rs11.8bn vs ISec estimate of Rs10.6bn. Exports grew 144% YoY and 21% QoQ to Rs3.1bn, while domestic grew 140% YoY and declined 11% QoQ to Rs8.6bn. Despite the second wave of pandemic leading to oxygen shortage in foundry and logistical bottlenecks in exports, the beat in revenue implies healthy demand.
- **Sequential improvement in gross margin indicates better mix and pricing:** Despite the sharp increase in commodity prices, gross margin improved 80bps QoQ to 34.4% implying favourable mix and price hikes. Due to normalisation of fixed overheads, EBIDTA margin stood at 12.6% vs our estimate of 12.4% despite gross margin improvement. With gradual increase in revenue growth, we believe, EBIDTA margin is likely to improve further.
- **Export outlook is healthy albeit at a gradual pace:** Demand from China and ASEAN countries had been healthy and continues to remain strong. The overall lull in the global economy under powergen is showing signs of turning around with a medium- to long-term perspective.
- **Maintain ADD on export recovery and control on margins:** Despite higher commodity prices, the company improved gross margin, and export demand is showing signs of recovery. We believe long-term growth potential is intact with likely introduction of CPCB-IV+ norms. We revise our SoTP-based target price to Rs995 (previously: Rs927) and maintain ADD.

Market Cap	Rs262bn/US$3.5bn
Reuters/Bloomberg	CUMM.BO/KKC IN
Shares Outstanding (mn)	277.2
52-week Range (Rs)	920/341
Free Float (%)	49.0
FII (%)	11.9
Daily Volume (US$/'000)	16,430
Absolute Return 3m (%)	13.9
Absolute Return 12m (%)	123.8
Sensex Return 3m (%)	11.6
Sensex Return 12m (%)	43.5

Year to Mar (Std)	FY20	FY21	FY22E	FY23E
Revenue (Rs mn)	51,577	43,293	49,960	57,206
Net Income (Rs mn)	6,432	6,179	6,762	7,843
DEPS (Rs)	23.2	22.3	24.4	28.3
% Chg YoY	(11.0)	(3.9)	9.4	16.0
P/E (x)	33.3	34.6	31.6	27.3
CEPS (Rs)	27.0	26.8	29.1	33.3
EV/E (x)	35.2	34.7	28.5	23.2
Dividend Yield (%)	1.8	1.9	1.9	2.6
RoCE (%)	17.2	17.8	19.5	22.0
RoE (%)	15.5	14.4	14.9	16.6

Valuation and outlook

Factoring in growth and margin improvement, we raise earnings by 14.3% and 7.8% for FY22E and FY23E, respectively. Any likely development regarding the merger of the unlisted group entities will give rise to synergies and thus, weigh favourably towards valuation re-rating. Factoring the same, we have core earnings target multiple of 35x FY23E earnings.

We believe Cummins' long term structural story is intact given the change in emission norms, technological leadership, testing, other preparedness and investments done by the company. Taking account of Cummins India's higher other income due to lease rentals and high cash position, we value its core earnings and lease rental income separately and add back the cash. Given the strong cashflow, we assign core earnings valuation multiple of 35x FY23E and add back the cash and discount the lease rentals @6% for 10 years. This works out to a target price of Rs995.

Table 1: Earnings revision

(Rs mn)

	FY22E			FY23E		
	Previous	**Revised**	**% chg**	**Previous**	**Revised**	**% chg**
Revenues	49,960	50,811	1.7	57,206	58,183	1.7
EBITDA	7,044	7,462	5.9	8,581	9,036	5.3
PAT	6,762	7,730	14.3	7,843	8,515	8.6

Source: Company data, I-Sec research

Table 2: Valuation summary

(Rs mn)

	FY23E
PAT	8,515
Tax rate (%)	*24.0*
Interest & dividend income	1,400
Rental Income	1,602
Operating PAT	6,233
P/E (x)	35
Value	2,18,167
Cash & Cash Equivalent	16,763
Gross value	2,34,930
Cummins Standalone value per share (Rs) (A)	**848**
Discounted Lease contribution	12,770
Lease contribution value per share (Rs) (B)	**46**
Valvoline PAT	1,876
P/E multiple (x)	30
Valvoline Gross value	56,268
Holding value (50% stake)	28,134
Valvoline value per share (Rs) (C)	**101**
Total value per share (Rs) (A+B+C)	**995**

Source: Company data, I-Sec research

Table 3: Result highlights

(Rs mn)	Q1FY21	Q1FY22E	YoY(%)	Q4FY21	QoQ(%)	Isec est	Var(%)	FY20	FY21	YoY(%)
Total Revenue	**4,982**	**11,845**	***137.8***	**12,465**	***(5.0)***	**10,650**	***11.2***	**51,577**	**43,293**	***(16.1)***
EBITDA	29	1,488	*5,030.7*	1,675	*(11.2)*	1,321	*12.6*	5,863	5,795	*(1.2)*
Margin	0.6	12.6	1198bps	13.4	-87bps	12.4	16bps	11.4	13.4	
Depreciation	303	309	*1.9*	306	*1.0*	305	*1.3*	1,187	1,255	*5.8*
Finance Cost	43	18	*(59.4)*	33	*(46.3)*	45	*(61.1)*	203	162	*(20.1)*
Other Income	1,022	549	*(46.3)*	1,116	*(50.8)*	600	*(8.5)*	3,315	3,701	*11.6*
Extraordinary income	-	1,324		-		-		(199)	-	
PBT	705	3,034	*330.6*	2,452	*23.7*	1,571	*93.1*	7,591	8,080	*6.4*
Tax	179	668	*273.2*	595	*12.1*	393	*70.0*	1,297	1,901	*46.5*
tax rate	*25.4*	*22.0*	-339bps	*24.3*	-227bps	*25.0*	-299bps	*17.1*	*23.5*	
Reported PAT	526	2,366	*350.2*	1,857	*27.4*	1,178	*100.8*	6,293	6,179	*(1.8)*
Adjusted PAT	**526**	**1,374**	***161.3***	**1,857**	***(26.0)***	**1,178**	***16.6***	**6,432**	**6,179**	***(3.9)***
EPS (Rs)	1.9	5.0		6.7		4.3		23.2	22.3	*(3.9)*

Source: Company data, I-Sec research

Financial summary

Table 4: Profit & loss statement

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Total Income	**51,577**	**43,293**	**50,811**	**58,183**
Operating Expenses	45,715	37,497	43,349	49,147
EBITDA	**5,863**	**5,795**	**7,462**	**9,036**
% margins	*11.4*	*13.4*	*14.7*	*15.5*
Depreciation & Amortisation	1,187	1,255	1,318	1,384
EBIT	**4,676**	**4,540**	**6,144**	**7,652**
Gross Interest	203	162	150	150
Other Income	3,315	3,702	3,655	3,702
PBT before exceptionals	**7,789**	**8,080**	**9,649**	**11,204**
Add: Extraordinaries/Exceptionals	(199)	-	1,324	-
Add: Share in associates				
PBT	**7,591**	**8,080**	**10,973**	**11,204**
Less: Taxes	1,297	1,901	2,316	2,689
Less: Minority Interests				
Net Income (Reported)	**6,293**	**6,179**	**8,657**	**8,515**
Adjusted Net Income	**6,432**	**6,179**	**7,730**	**8,515**

Source: Company data, I-Sec research

Table 5: Balance sheet

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Assets				
Total Current Assets	33,609	32,317	37,742	41,635
of which cash & cash eqv.	12,353	12,919	15,603	16,763
Total Current Liabilities & Provisions	12,137	11,922	12,770	14,475
Net Current Assets	**21,472**	**20,395**	**24,972**	**27,160**
Investments	10,793	10,625	10,793	10,793
Other Non-Current Assets	2,465	1,865	1,931	1,999
Net Fixed Assets	**12,674**	**12,163**	**11,851**	**11,567**
Goodwill				
Total Assets	**47,403**	**45,047**	**49,546**	**51,519**
Liabilities				
Borrowings	4,854	156	156	156
Deferred Tax Liability	800	823	823	823
Minority Interest				
Equity Share Capital	554	554	554	554
Face Value per share (Rs)	2.00	2.00	2.00	2.00
Reserves & Surplus	41,195	43,513	48,012	49,985
Net Worth	**41,750**	**44,067**	**48,567**	**50,540**
Total Liabilities	**47,404**	**45,047**	**49,546**	**51,519**

Source: Company data, I-Sec research

Table 6: Cashflow statement

(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Operating Cashflow	**4,333**	**5,637**	**8,801**	**10,049**
Working Capital Changes	1,855	2,242	(1,958)	(1,097)
Capital Commitments	(1,079)	444	(1,006)	(1,100)
Free Cashflow	**5,110**	**8,323**	**5,838**	**7,852**
Cashflow from Investing Activities	**(1,056)**	**(289)**	**(653)**	**(784)**
Issue of Share Capital				
Buyback of shares				
Inc (Dec) in Borrowings	1,762	(4,697)	-	-
Interest paid	203	162	150	150
Dividend paid	(4,579)	(4,158)	(4,158)	(6,542)
Extraordinary Items/Others	**1,108**	**1,226**	**1,508**	**484**
Chg. in Cash & Bank balance	**2,546**	**566**	**2,685**	**1,160**

Source: Company data, I-Sec research

Table 7: Key ratios

(Year ending March 31)

	FY20	FY21	FY22E	FY23E
Per Share Data (in Rs.)				
Diluted adjusted EPS	23.2	22.3	27.9	30.7
Recurring Cash EPS	27.0	26.8	36.0	35.7
Dividend per share (DPS)	14.0	15.0	15.0	20.0
Book Value per share (BV)	150.6	159.0	175.2	182.3
Growth Ratios (%)				
Operating Income	(8.9)	(16.1)	17.4	14.5
EBITDA	(32.2)	(1.2)	28.8	21.1
Recurring Net Income	(11.0)	(3.9)	25.1	10.1
Diluted adjusted EPS	(11.0)	(3.9)	25.1	10.1
Diluted Recurring CEPS	(10.2)	(0.6)	34.2	(0.8)
Valuation Ratios				
P/E	40.7	42.4	33.9	30.8
P/CEPS	35.0	35.2	26.3	26.5
P/BV	6.3	5.9	5.4	5.2
EV / EBITDA	43.4	43.0	33.0	27.1
EV / Operating Income	4.9	5.8	4.8	4.2
EV / Operating FCF (pre -Capex)	41.1	31.6	36.0	27.4
Operating Ratios				
Raw Material/Sales (%)	65.3	63.8	64.0	63.5
SG&A/Sales (%)	11.1	11.1	10.2	10.0
Other Income / PBT (%)	42.6	45.8	37.9	33.0
Effective Tax Rate (%)	16.7	23.5	24.0	24.0
NWC / Total Assets (%)	17.7	15.1	16.7	17.3
Inventory Turnover (days)	41.3	47.8	47.8	47.7
Receivables (days)	80.1	90.6	85.0	84.0
Payables (days)	49.3	61.5	55.0	55.0
Net D/E Ratio (x)	(0.2)	(0.3)	(0.3)	(0.3)
Return/Profitability Ratios (%)				
Recurring Net Income Margins	12.5	14.3	15.2	14.6
RoCE	17.2	17.8	20.7	22.5
RoNW	15.5	14.4	16.7	17.2
Dividend Payout Ratio	60.3	67.3	53.8	65.1
Dividend Yield (%)	1.5	1.6	1.6	2.1
EBITDA Margins	11.4	13.4	14.7	15.5

Source: Company data, I-Sec research

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