

CUSP Managers Vote for Status Quo in Industrial Sector

By Kristian Shad and Ethan Hill

We, as CUSP analysts, made three presentations related to the Industrials sector. Cumulatively, we recommended two additions to the portfolio, Deere and Cummins, and two holds among the current portfolio, Boeing and FedEx. The class ultimately voted to hold Boeing and FedEx and voted against adding any other firms to the industrials sector. Our rationale for each recommendation follows.

Deere: We pitched this stock as a “buy” and addition to the CUSP Industrials sector in both February and April 2022. Our investment thesis was as follows: Although its first quarter and valuation were not as favorable as we would like, Deere has strong growth potential and an optimistic future. Our valuation based on discounted free cash flows and analysis of comparable industry companies led us to the conclusion that Deere was trading about at fair value. However, we believe technological innovation will continue to make Deere a leader in its industry. Additionally, its competitive positioning, usage of cash flows and external economic factors all bode well for Deere as a long-term investment. The class votes were close in each presentation but did not meet the class’s required threshold of two-thirds majority to act. Those who voted against the purchase most commonly cited Deere’s relative valuation as a reason to not buy.

Boeing: Boeing is a current holding in the CUSP. We evaluated the stock to see if we should alter the position in April 2022. Our recommendation was to continue holding the company. Our rationale was that despite the bad press and recent airplane malfunctions, Boeing has demonstrated admirable resiliency. Boeing did report a fourth-quarter 2021 loss of \$7.69 per share, but this was largely due to the company taking a \$3.5 billion pre-tax non-cash charge on the 787 Dreamliner program. We believed that the firm was trading at a discount as its valuation metrics were below its peers, and its stock price had fallen due to headline-grabbing airplane crashes and a poor fourth quarter earnings report. The commercial airplane business will continue to face challenges in the short term; however, its defense business, which accounts for almost half of its revenues, is experiencing positive trends. With travel recovering to pre-pandemic levels and defense spending expected to increase, we recommended Boeing remain in the CUSP. The class voted to retain the stock.

FedEx: FedEx is a current holding in the CUSP. We evaluated the stock in April 2022 to see if we should alter the position. Our recommendation was to continue holding the company. Our rationale was as follows: While FedEx has uncertainty revolving around its valuation, there are many promising factors the company has in its favor. Regarding valuation, our estimates led us to a similar conclusion as Deere; the company’s multiples and projections gave strong indications of fair valuation. However, FedEx is in a good position to meet its earnings and revenue projections, while FCF looks good enough to repurchase stock and pay a higher dividend. Furthermore, e-commerce demand should keep growing or stay at its current elevated level, fueling growth for FedEx. All these positive factors led us to the conclusion that FedEx should be retained in the portfolio. The class voted to retain the stock.

Cummins: In February 2022 we pitched this stock as a “buy” and an addition to the CUSP Industrials sector. Our investment thesis was that the firm has expanded its focus from its traditional reliance on manufacturing and distributing gas engines, after-treatment products and components to also leading the industry in New Power products. Cummins’ New Power segment designs, manufactures, sells and supports hydrogen products and electrified power systems, including battery and fuel cell technologies.

This should expand the firm's sales as regulators push for zero-carbon emission engines and as the industry pivots towards environmentally sustainable products. In addition, Cummins is a leader in hydrogen engines, which are a more sustainable and logical replacement for many large commercial vehicles when compared with fully electric commercial vehicles. We believe Cummins to be trading at a discount to or perhaps near its intrinsic value as its valuation metrics were almost all lower than peers. Moreover, we believe the prospects for growth at Cummins exceed those of many of its peers. The class vote again was close but did not support the purchase.