

## Caterpillar Inc

# Largest CAT dealer down under – look for key insights from upcoming event

Maintain Rating: BUY | PO: 363.00 USD | Price: 339.19 USD

## We look for key insights from one of CAT's largest dealers

We are hosting one of Caterpillar's largest dealers – Seven Group Holdings (SVW) - for a virtual event this week (March 13<sup>th</sup> EST). The event includes Ryan Stokes, MD & CEO, and Richard Richards, CFO. SVW core businesses include WesTrac – sole CAT dealer in Western Australia & New South Wales. Additionally, SVW includes other businesses across Industrial Services, Energy and Media. We look for insights into a range of debate topics: end-market demand in Australia post commodity volatility (mining, infrastructure, construction), inventory management, tech adoption (autonomous mining, electrification), parts demand at WesTrac, and Coates's shift to an asset light strategy.

## Public dealer commentary around inventories

Public dealer commentary (Finning, Seven Group) through earnings season highlighted a build up in inventories through the end of 2023 (see exhibit 1-3) to support a positive growth outlook. The good news is that most of this inventory is committed to customers (WesTrac notes 75% committed) and supports a positive outlook. Dealers – particularly in the mining arena – see visibility to high levels of rebuild activity. That said, we sense the public dealers are focusing on unlocking working capital through 2024. Inventories are likely to be a headwind to Caterpillar, albeit the demand environment remains healthy.

## Other comments: pricing, mining vs construction vs power

i) pricing: indications of low single digit pricing in 2024, ii) Construction: Canadian dealers cite some softening in construction markets given completion of major projects, iii) Power: power systems consistently cited as an area of strength – back up power, standby, utility, data centers – with availability still constrained. Iv) mining: high level of rebuild activity across Chile, Australia, and Canada given the aged fleet. We maintain our Buy rating as we continue to see strength in certain verticals (mining, power, infrastructure) that provides a level of earnings stability as we wait for leading industrial indicators to inflect through 2024.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	13.84	21.21	22.00	24.00	26.50
GAAP EPS	12.64	20.12	21.24	23.59	26.07
EPS Change (YoY)	28.0%	53.3%	3.7%	9.1%	10.4%
Consensus EPS (Bloomberg)			21.18	22.09	23.43
DPS	4.71	5.10	5.50	5.94	6.42
Valuation (Dec)					
P/E	24.5x	16.0x	15.4x	14.1x	12.8x
GAAP P/E	26.8x	16.9x	16.0x	14.4x	13.0x
Dividend Yield	1.4%	1.5%	1.6%	1.8%	1.9%
EV / EBITDA*	17.2x	12.2x	12.0x	11.4x	10.7x
Free Cash Flow Yield*	2.9%	5.8%	5.2%	5.3%	6.2%

\* For full definitions of *IQmethod*<sup>SM</sup> measures, see page 5.

11 March 2024

### Equity

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### Stock Data

Price	339.19 USD
Price Objective	363.00 USD
Date Established	6-Feb-2024
Investment Opinion	B-1-7
52-Week Range	204.04 USD - 344.50 USD
Mkrt Val (mn) / Shares Out (mn)	173,869 USD / 512.6
Free Float	99.8%
Average Daily Value (mn)	860.67 USD
BofA Ticker / Exchange	CAT / NYS
Bloomberg / Reuters	CAT US / CAT.N
ROE (2024E)	65.5%
Net Dbt to Eqty (Dec-2023A)	22.2%
ESGMeter™	Medium

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Timestamp: 11 March 2024 05:30AM EDT

# iQprofile<sup>SM</sup> Caterpillar Inc

## iQmethod<sup>SM</sup> – Bus Performance\*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	19.3%	31.5%	31.1%	30.8%	30.6%
Return on Equity	42.4%	65.9%	65.5%	61.2%	56.7%
Operating Margin	14.9%	20.8%	21.2%	21.1%	21.4%
Free Cash Flow	5,079	10,064	9,089	9,224	10,695

## iQmethod<sup>SM</sup> – Quality of Earnings\*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	0.9x	1.1x	1.1x	1.0x	1.0x
Asset Replacement Ratio	0.9x	1.2x	1.8x	1.5x	1.6x
Tax Rate	24.1%	20.9%	23.0%	23.0%	23.0%
Net Debt-to-Equity Ratio	21.2%	22.2%	22.0%	14.2%	6.7%
Interest Cover	20.5x	26.6x	27.1x	29.1x	31.2x

## Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	56,574	63,869	65,247	68,923	72,778
% Change	17.4%	12.9%	2.2%	5.6%	5.6%
Gross Profit	15,218	21,093	21,727	23,055	24,708
% Change	20.1%	38.6%	3.0%	6.1%	7.2%
EBITDA	10,550	14,951	15,203	15,941	16,964
% Change	15.7%	41.7%	1.7%	4.9%	6.4%
Net Interest & Other Income	10	(268)	(510)	(500)	(500)
<b>Net Income (Adjusted)</b>	<b>7,339</b>	<b>10,893</b>	<b>10,933</b>	<b>11,509</b>	<b>12,296</b>
<b>% Change</b>	<b>23.7%</b>	<b>48.4%</b>	<b>0.4%</b>	<b>5.3%</b>	<b>6.8%</b>

## Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	7,339	10,890	10,933	11,509	12,296
Depreciation & Amortization	1,439	1,361	1,371	1,371	1,371
Change in Working Capital	(2,015)	(11)	(18)	(1,014)	(214)
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	(405)	(552)	(750)	(575)	(575)
Capital Expenditure	(1,279)	(1,624)	(2,447)	(2,068)	(2,183)
<b>Free Cash Flow</b>	<b>5,079</b>	<b>10,064</b>	<b>9,089</b>	<b>9,224</b>	<b>10,695</b>
<b>% Change</b>	<b>-16.6%</b>	<b>98.1%</b>	<b>-9.7%</b>	<b>1.5%</b>	<b>16.0%</b>
Share / Issue Repurchase	(4,179)	(4,963)	(6,600)	(5,445)	(6,389)
Cost of Dividends Paid	(2,440)	(2,563)	(2,735)	(2,850)	(2,979)
Change in Debt	(172)	(10)	0	0	0

## Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	6,042	6,106	5,860	6,788	8,116
Trade Receivables	3,710	3,971	4,022	4,343	4,985
Other Current Assets	18,758	20,892	21,065	22,674	23,555
Property, Plant & Equipment	8,186	8,694	9,770	10,466	11,279
Other Non-Current Assets	17,133	14,015	14,493	15,143	15,807
<b>Total Assets</b>	<b>53,829</b>	<b>53,678</b>	<b>55,210</b>	<b>59,416</b>	<b>63,742</b>
Short-Term Debt	123	1,044	1,044	1,044	1,044
Other Current Liabilities	19,303	20,028	20,338	21,529	23,126
Long-Term Debt	9,529	8,626	8,626	8,626	8,626
Other Non-Current Liabilities	7,880	7,904	7,904	7,904	7,904
<b>Total Liabilities</b>	<b>36,835</b>	<b>37,602</b>	<b>37,912</b>	<b>39,103</b>	<b>40,700</b>
<b>Total Equity</b>	<b>16,994</b>	<b>16,076</b>	<b>17,299</b>	<b>20,313</b>	<b>23,041</b>
<b>Total Equity &amp; Liabilities</b>	<b>53,829</b>	<b>53,678</b>	<b>55,210</b>	<b>59,416</b>	<b>63,742</b>

\* For full definitions of iQmethod<sup>SM</sup> measures, see page 5.

## Company Sector

Construction Machinery

## Company Description

Caterpillar (CAT), the largest manufacturer/marketer of construction equipment worldwide, is also a leading manufacturer of engines and turbines for transport, energy, and industrial applications.

## Investment Rationale

CAT is a global powerhouse in mining, construction, oil and gas, rail, and power systems equipment. We believe CAT is well positioned with trough earnings notably higher than in prior downturns. As we look to towards the next cycle, CAT's earnings power and multi-year growth prospects are positive: capex is higher following years of underinvestment, older fleets require replacement, and shift in construction spending towards heavy/infrastructure projects.

## Stock Data

Average Daily Volume 2,459,439

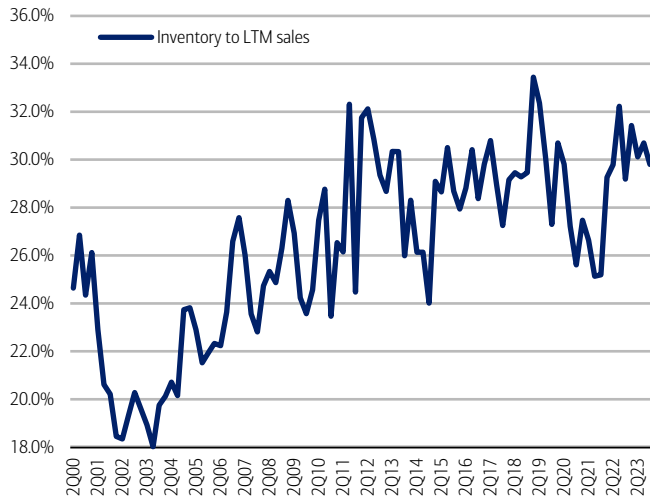
## Quarterly Earnings Estimates

	2023	2024
Q1	4.91A	5.11E
Q2	5.55A	5.66E
Q3	5.52A	5.61E
Q4	5.23A	5.62E

# CAT Dealer Inventory charts

## Exhibit 1: Finning Inventory to LTM sales

Finning Inventory to LTM sales is moderating

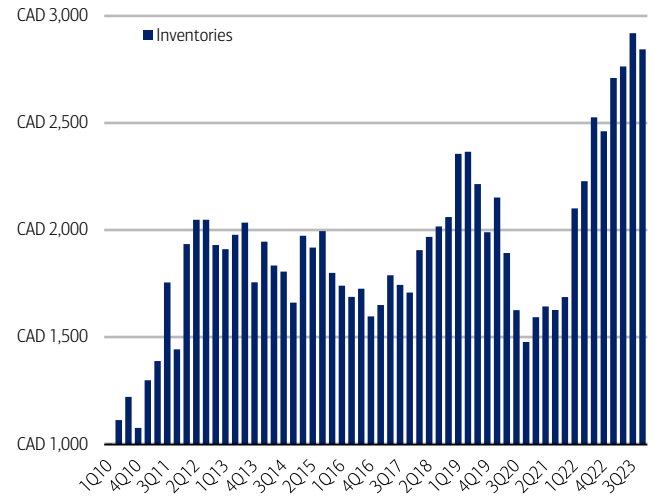


Source: Company Filings

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## Exhibit 2: Finning Inventory Levels

Finning Inventories remain elevated

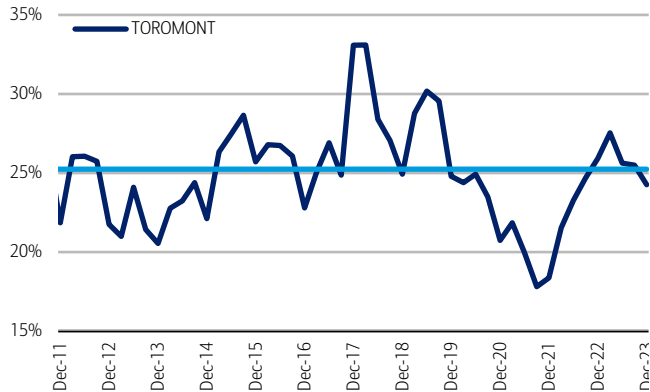


Source: Company Filings

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## Exhibit 3: Toromont Inventory to LTM sales

Toromont inventory to LTM sales is below the 10 year average



Source: Company Filings

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## Price objective basis & risk

### Caterpillar Inc (CAT)

Our \$363 PO on CAT is on based on 16.5x 2024e EPS which is in-line with the long term historical range of 15-17x. While we see some headwinds that are likely to slow growth (higher inventories, capex plateauing, pricing moderating, backlog softening), there are unique macro and business cycle factors that are underpinning stronger cycle over cycle earnings: infrastructure, construction spending mix shifts towards heavy vs light, higher miner free cash flow generation, aging fleets, and data centers.

Downside risks to our PO: 1) widening global coronavirus pandemic that tilts global economy into recession, 2) a greater-than-expected reduction or delay in capital spending among large mining, and oil and gas customers, 3) intensifying pricing pressure in the construction and mining equipment industries, 4) greater than expected dealer destocking, 5) ongoing deterioration in dealer sales growth.

Upside risks: 1) a faster recovery in the global economy, 2) firming earthmoving construction equipment market, 3) stronger-than-expected fleet replacement, 4) continuing recovery in commodity prices, 5) stronger-than-expected demand trends in gas compression, 6) quicker-than-expected resolution to the pandemic.

## Analyst Certification

I, Michael Feniger, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

### US - Machinery Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
<b>BUY</b>				
	AECOM	ACM	ACM US	Michael Feniger
	Blue Bird Corp	BLBD	BLBD US	Sherif El-Sabbahy
	Caterpillar Inc	CAT	CAT US	Michael Feniger
	CNH Industrial NV	CNHI	CNHI US	Michael Feniger
	Construction Partners Inc.	ROAD	ROAD US	Michael Feniger
	ESAB Corp	ESAB	ESAB US	Sherif El-Sabbahy
	Finning International Inc.	YFTT	FTT CN	Sherif El-Sabbahy
	H&E Equipment Services Inc	HEES	HEES US	Sherif El-Sabbahy
	Knife River Corp	KNF	KNF US	Sherif El-Sabbahy
	Republic Services	RSG	RSG US	Michael Feniger
	Techtronic Industries Co Ltd	TTNDF	669 HK	Michael Feniger
	Techtronic Industries Co Ltd	TTNDY	TTNDY US	Michael Feniger
	United Rentals Inc	URI	URI US	Michael Feniger
	Vulcan Materials	VMC	VMC US	Michael Feniger
	Waste Connections Inc	WCN	WCN US	Michael Feniger
	WillScot Mobile Mini	WSC	WSC US	Sherif El-Sabbahy
<b>NEUTRAL</b>				
	AGCO Corp	AGCO	AGCO US	Michael Feniger
	Deere & Co	DE	DE US	Michael Feniger
	Fluor	FLR	FLR US	Michael Feniger
	GFL Environmental Inc	GFL	GFL US	Michael Feniger
	GFL Environmental Inc	YGFL	GFL CN	Michael Feniger
	Jacobs Eng.	J	J US	Michael Feniger
	Kennametal Inc.	KMT	KMT US	Michael Feniger
	Martin Marietta Materials	MLM	MLM US	Michael Feniger
	NV5 Global Inc.	NVEE	NVEE US	Michael Feniger
	PACCAR Inc	PCAR	PCAR US	Michael Feniger

**US - Machinery Coverage Cluster**

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	RB Global, Inc	RBA	RBA US	Michael Feniger
	Waste Management	WM	WM US	Michael Feniger
<b>UNDERPERFORM</b>				
	Allison Transmission Holdings Inc.	ALSN	ALSN US	Sherif El-Sabbahy
	Casella	CWST	CWST US	Michael Feniger
	Cummins Inc	CMI	CMI US	Michael Feniger
	Herc Holdings Inc	HRI	HRI US	Sherif El-Sabbahy
	IPG Photonics	IPGP	IPGP US	Michael Feniger
	Oshkosh Corp.	OSK	OSK US	Michael Feniger
	Snap-on	SNA	SNA US	Sherif El-Sabbahy
	Terex Corp.	TEX	TEX US	Michael Feniger
	Timken Company	TKR	TKR US	Michael Feniger

**iQmethod<sup>SM</sup> Measures Definitions****Business Performance**

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

**Quality of Earnings**

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

**Valuation Toolkit**

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

**Numerator**

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

**Numerator**

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash &amp; Equivalents

EBIT

**Numerator**

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

**Denominator**

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization

Shareholders' Equity

Sales

N/A

N/A

**Denominator**

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

**Denominator**

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

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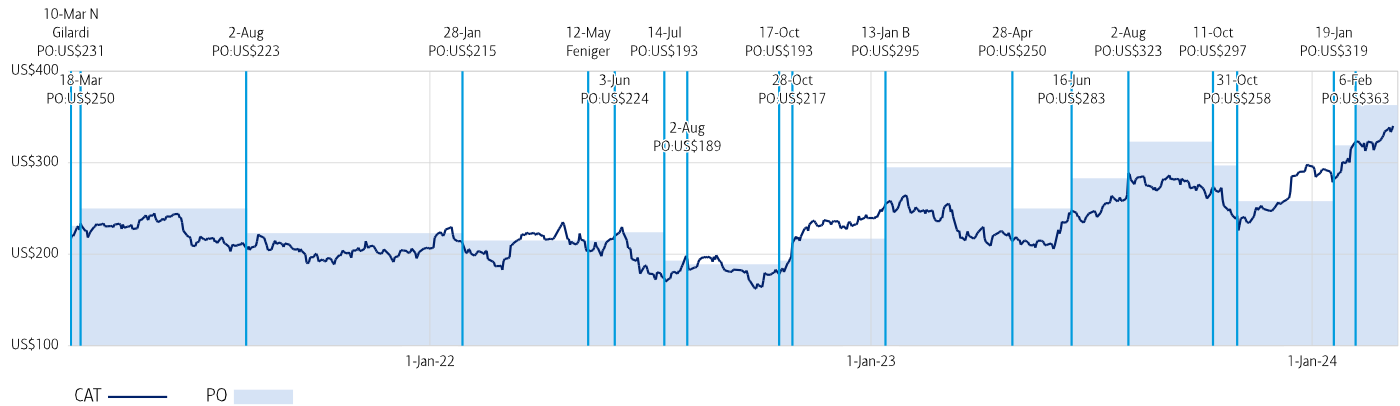
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### Caterpillar Inc (CAT) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

### Equity Investment Rating Distribution: Machinery/Diversified Manufacturing Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	27	42.19%	Buy	8	29.63%
Hold	17	26.56%	Hold	8	47.06%
Sell	20	31.25%	Sell	8	40.00%

### Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

<sup>R1</sup> Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster <sup>R2</sup>
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

<sup>R2</sup> Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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