STOCKTRADES PREMIUM COMPANY SUMMARY

TMX GROUP LTD.

X.TO

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Stocktrades Premium

TMX Group Ltd is a company that operates several global markets to provide investment opportunities for its clients. TMX Group's key operations include Toronto Stock Exchange, TSX Venture Exchange, TSX Alpha Exchange, The Canadian Depository for Securities, Montreal Exchange, Canadian Derivatives Clearing Corporation, and Trayport, which provides listing markets, trading markets, clearing facilities, depository services, technology solutions, data products, and other services to the global financial community. TMX Group operates offices across North America (Montreal, Calgary, Vancouver, and New York), as well as in key international markets including London and Singapore.

Focus Areas	Score (0/100)	Focus Areas	Score (0/100)
Valuation	43	Dividend	92
Profitability	44	Outlook	100
Risk	92	Debt	59
Returns	42	Growth	50
Overall	63		

*Our Risk Rating: Our opinion of the overall risk an investment presents. Can be shown as Defensive (DEF), Moderate (MOD), or Aggressive (AGG). By no means is this an indication of future potential gains or lower volatility.

PROS

- Significant moat - the largest exchange in the country
- Achieved Canadian Dividend Aristocrat status in 2021. Has since extended its dividend growth streak to 8 years
- Excellent payout ratios - plenty of room for continued dividend growth
- Respectable growth in the high single digits
- Has consistently outperformed the S&P/TSX Composite Index
- Has raised the dividend three times in the last 2 years
- A very consistent & reliable performer, especially considering current market conditions

CONS

- Growth is expected to slow in the next couple of years. The pace of the markets in 2020/2021 was likely unsustainable
- Market volatility and higher policy rates have resulted in lower IPOs over the last few years
- Increased competition from the Cboe (formerly NEO Exchange), the only other senior exchange in Canada, which is now starting to target corporate listings
- Volume on all TMX marketplaces continues to drop, resulting in in lower equity trading volume

OVERALL THESIS

The TMX Group has a considerable moat that is unlikely to be impacted meaningfully despite the emergence of the NEO Exchange. TMX has little competition and remains the preferred exchange for most companies that want to go public.

The pandemic also increased retail interest in the markets. Yes, it has died down because of some pretty rough economic circumstances for Canadians, but when policy rates come down it is likely activity returns. Regardless, the more market activity for TMX Group, the better. The company has flown under the radar as a reliable income stock. We think this will eventually change with its inclusion on the Aristocrat list. The company offers an attractive combination of yield and dividend growth with earnings growth at reasonable values considering the circumstances.

The company has a nice mix of growth through acquisitions and has managed to achieve strong organic growth in the high single to low double-digits over the past handful of years. That trend is expected to continue over the next couple of years. The company is quietly posting good results and doing its thing. Nothing to get excited about, but it has proven to be a reliable stock to own. In the current market environment, this is huge.

The company gained an impressive 32% in 2023, enough to outperform the TSX and S&P 500. 2024 is setting up nicely as well, and we're still bullish.

POTENTIAL RISKS

A significant portion of the company's revenue comes from trading which is highly sensitive to macroeconomic conditions. Given that Canada is also the largest geographic concentration of revenue it is subject to domestic macroeconomic factors such as GDP growth, regulations, interest rates, volatility, and market activity, all impacting business.

The risks are not only limited to Canada. Geopolitical issues globally will impact trading and capital raise volume. We saw how the Russia/Ukraine war impacted the latter as in some cases companies had been materially impacted by sanctions on Russia.

Beta	**0.59**
Alpha	**10.5**
Our Risk Rating	**Mod***
Max Drawdown	**28.9%**

This can lead to delayed or cancelled raises or IPOs, etc. While exchange competition is limited (in Canada at least), it still competes globally with other exchanges for global listings and if it is not competitive, the company can lose business to other more notable exchanges.

Finally, since the Canadian economy is heavily exposed to natural resources and energy-related businesses, the TMX Group is exposed to downturns in these sectors as they can impact capital formation business and the trading and clearing activities.

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VALUATION

	TTM	5 Year Average	Industry Average
P/E	29.8	23.78	N/A
P/S	8.88	7.88	N/A
P/B	1.1	1.98	N/A
P/FCF	22.3	20.58	N/A
PEG Ratio (FWD)	1.96	N/A	N/A

The valuation gap with TMX Group over the last year or so has vanished. As of this most recent update, TMX Group is now trading in line with historical averages, even at a slight premium in some situations.

As a company that typically trades in line with the averages, we had expected this gap to close. Now that it has, this is no longer a value play. That said, getting a reliable company like TMX Group at fair value can still deliver solid returns. We'd expect the company's share price to rise in line with growth. It has gone from a value play to a GARP (Growth At a Reasonable Price) option, which is one of our favourite types of holdings.

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COMPETITOR ANALYSIS

TMX has no real direct competitors trading on the TSX Index, which is why you don't see a competitors chart here. An economic moat like this is something investors are willing to pay a little extra for. You have to go south of the border to find more directly comparable companies. And when you look at companies like Nasdaq (NDAQ), and CME Group (CME) south of the border, TMX Group is still trading at a discount to its US peers.

The company's primary competition at home is the Cboe (formerly NEO Exchange) which is emerging as a legitimate competitor to the TSX Index. That being said, it still pales in comparison to the size of TMX and it is not publicly traded. That means that the TMX Group remains the only legitimate stock option for investors looking for exposure to this industry.

DIVIDEND ANALYSIS

Annual Dividend	Free Cash Flow Payout Ratio	5 Year Dividend Growth %	Dividend Growth Streak
$0.76	40%	11.13%	8

Regarding the safety of the dividend, the TMX Group ranks up there with some of the best. Looking at the dividend against earnings, free cash flow, or operational cash flow, you can see that the dividend is well covered.

Cash flow ratios come between 40-50%, while the payout ratio against earnings is only 49%. This should give investors confidence that the company can handle an adverse event. Its payout ratio in terms of earnings has continued to drop for nearly 3 years straight. This highlights the fact that one-off charges and market-driven headwinds are subsiding. In December 2020, the company's payout ratio was in the 55-57% range.

Furthermore, the company has consistently grown earnings and cash flows year-over-year, so the payout ratios will likely remain stable even with future raises.

TMX Group has consistently grown its dividend on an annual basis. However, the company has been making smaller, more frequent hikes to the dividend. It raised the dividend in February 2023, August 2023, and came through with an additional 6% raise in May 2024.

It will be interesting to see if TMX Group becomes a more frequent raiser or if this is just a situation where they feel they have some excess cash flows at this point and are returning them back to shareholders.

Either way, we're always happy with out-of-the-norm raises to the dividend.

RECENT EARNINGS

Earnings Estimates	2024	2025	2026
EPS	$1.63	$1.83	$2.04
Revenue	$1.43B	$1.54B	$1.64B
EBITDA	$1.629	$1.828	$2.07
EBITDA Margins	55%	56%	56.5%

TMX Group reported a strong third quarter. Revenue of $353.8M came in ahead of expectations for $350.3M, and earnings per share of $0.41 topped estimates for $0.389.

The company has weathered the high interest rate environment and declining new listings. It is now reaping the benefits of a more active equity market.

Organic revenue grew by 12% year-over-year, primarily fueled by Trayport, an oil and gas trading platform that the company acquired before the pandemic. Trayport licenses increased by 27%.

As mentioned, after 18 months of declining equity activity, it is now seeing an 11% increase in equity trading volumes and a 19% increase in derivate trading volumes. Ultimately, the more retail and institutional investors trade on TMX's exchanges, the more revenue the company generates.

The company made a relatively small acquisition on the quarter, purchasing Newsfile Corporation, a Canadian-based dissemination provider. If you've ever read a quarterly earnings report from a company in the form of a press release, there is a good chance Newsfile issued it. Newsfile has sales of around $10M~ in 2024 and operating income of $4.3M. So, as mentioned it is a relatively small acquisition, but a solid one nonetheless.

Strong double digit growth on both the top and bottom lines should allow the company to continue to make small tuck-in acquisitions to fuel further cash flow growth in the future. With the equity markets showing zero signs of slowing down, I do expect volumes to continue improving.

Where the company is still struggling to a degree is its listing revenue. Interest rates remain relatively high, and the environment for initial public offerings isn't as attractive as it was during the COVID lockdowns and low-rate environment. I expect this to improve as rates start to come down and companies start seeing the equity markets as an attractive way to raise capital again.

Overall, the company continues to post exceptional results, and despite being at higher prices valuation-wise, I have confidence it will be able to deliver strong results moving forward.

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