



## TMX Group: The Ultimate Bull Market Stock

### Description

**TMX Group Ltd** ([TSX:X](#)), the owner of the Toronto Stock Exchange, provides listing, trading, clearing, settlement, depository and information services for an array of publicly traded and over-the-counter financial instruments.

The business model is simple: TMX collects a fee from companies and investors that wish to engage in any of the activities mentioned above in equities, fixed income, energy products and derivatives instruments. In a business where scale and reputation are important factors, TMX dominates the Canadian market. Bull markets are strongly supportive of most of the activities of the company.

The main sources of the \$701 million 2013 revenue were listing services for equities and fixed income, trading, clearing and settlement for equities, fixed income, derivatives and energy products and data information services. The main trading and settlement platforms provided by the company include the Toronto Stock Exchange (main equities exchange), Montreal Exchange (financial derivatives) and CDS (securities clearing, depository and settlement).

### **A major business merger in 2012 with integration in 2013**

The company underwent a major business combination in 2012 with the merging of the old TMX Group Inc business with Alpha Group and the Canadian Derivatives Clearing Corporation. The 2013 financial results provided the first full year of operation of the combined group.

At the time of the merger, the company indicated that considerable business synergies and cost savings would be derived from the merger. The latest indication given by the firm is that an annualised \$28 million (c 8%) of expenses would be saved during 2014, arising from the combination of trading platforms and the realisation of efficiencies of overlapping functions.

### **Recent results were positive and early 2014 signs are promising**

The company recently reported 2013 full year results that exceeded market expectations. The business produced revenue of \$701 million and profit before interest tax and depreciation of \$330 million. Adjusted earnings per share was \$3.38 and a dividend of \$1.60 per share was paid during the year for a dividend yield of 3.1% at the current price. Operating and free cash flow was solid with the

latter totalling \$220 million or \$4.07 per share, covering the dividend payment multiple times.

Expectations are that the firm will be able to grow its profits considerably during 2014 based on the estimated 2014 cost savings, integration synergies and increased listing, capital raising and trading market activity. The early signs in 2014 are promising with increased listing, capital raising and trading activity reported in January. Further increases in Canadian stock prices and especially the mining companies will provide a welcome boost to the equity trading business activities.

### **The valuation seems reasonable compared to other stock exchanges**

TMX is an integrated exchange that can be compared with some of major stock markets such as the **Singapore Exchange**, **Nasdaq Stock Market** ([Nasdaq: NDAQ](#)), **London Stock Exchange** and the **Australian Securities Exchange**. On most of the valuation measures used for this type of business, TMX seems to be slightly undervalued, especially when the 2014 cost savings and positive profit prospects are taken into account.

### **Foolish bottom line**

The company is a Canadian market leader in the key segments in which it operates and has built a valuable franchise that will be difficult for competitors to replicate. The current valuation of the stock is at a slight discount to other major stock exchanges in other parts of the world. Upside potential may come from the considerable expected cost savings and the improving trading conditions on the Canadian equities market.

### **CATEGORY**

1. Investing

### **TICKERS GLOBAL**

1. NASDAQ:NDAQ (Nasdaq, Inc.)
2. TSX:X (TMX Group)

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### **Date**

2025/08/21

### **Date Created**

2014/02/26

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