



Commerce Bancshares (CBSH)

Updated October 22nd, 2020 by Jonathan Weber

Key Metrics

| | | | | | |
|-----------------------------|------|--|-------|----------------------------------|-----------------------|
| Current Price: | \$63 | 5 Year CAGR Estimate: | 0.5% | Market Cap: | \$6.9B |
| Fair Value Price: | \$43 | 5 Year Growth Estimate: | 6.0% | Ex-Dividend Date: | 12/04/20 ¹ |
| % Fair Value: | 146% | 5 Year Valuation Multiple Estimate: | -7.3% | Dividend Payment Date: | 12/22/20 ² |
| Dividend Yield: | 1.7% | 5 Year Price Target | \$58 | Years Of Dividend Growth: | 10 |
| Dividend Risk Score: | B | Retirement Suitability Score: | D | Last Dividend Increase: | 3.8% |

Overview & Current Events

Commerce Bancshares is a bank holding for Commerce Bank. It offers general banking services to its customers, which include businesses as well as individuals. Its services include retail and corporate banking, as well as asset management, investment banking, and other offerings. The company was founded in 1865 and operates branches in Colorado, Kansas, Missouri, Illinois and Oklahoma. Commerce Bancshares is headquartered in Kansas City, Missouri.

Commerce Bancshares reported its third quarter earnings results on October 20. The company generated revenues of \$346 million during the quarter, which was up 2% from the previous year's quarter. At the end of the quarter, Commerce Bancshares' loan portfolio totaled \$16.4 billion, while deposits stood at \$25.7 billion at the same time. These were increases by double-digits on a year over year basis, a trend that has been visible in the results of other banks as well. Commerce Bancshares' provisions for loan losses declined versus Q2, which is why profits improved meaningfully.

Commerce Bancshares generated earnings-per-share of \$1.11 during the third quarter, which was up by 20% compared to the previous year's quarter. It is expected that this year's profits will be well below 2019's level, due to higher credit losses. We believe that this will reverse over the coming years though, and that Commerce Bancshares' underlying earnings power (\$3.60), which we use to calculate fair value, is higher than this year's forecasted earnings.

Growth on a Per-Share Basis

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2025 |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| EPS | \$1.79 | \$2.10 | \$2.27 | \$2.24 | \$2.25 | \$2.32 | \$2.49 | \$2.89 | \$3.60 | \$3.58 | \$2.50 | \$4.82 |
| DPS | \$0.64 | \$0.65 | \$0.69 | \$0.71 | \$0.74 | \$0.78 | \$0.82 | \$0.86 | \$0.94 | \$1.04 | \$1.08 | \$1.51 |
| Shares³ | 122 | 119 | 117 | 117 | 112 | 107 | 107 | 107 | 117 | 114 | 110 | 103 |

Commerce Bancshares has grown its earnings-per-share by 7% annually since 2008, which is a solid growth rate. During the financial crisis, Commerce Bancshares' profitability declined, but the company remained highly profitable, unlike many other American banks. Compared to its peers, Commerce Bancshares is a relatively stable performer and a lower-risk stock during times when the economy is not in good shape.

Commerce Bancshares' profits are driven by several factors. The bank's net interest income depends on the amount of outstanding loans as well as the spread between the interest rates the bank pays and the interest rates it earns. During recent years the bank's loan book grew regularly, and the bank was able to grow its net interest income continuously. Net interest margins will likely come under pressure a bit from the Fed's policy of lowering interest rates. Commerce Bancshares also keeps growing the trust fees it receives, which is positive for its revenue growth. Commerce Bancshares has repeatedly done share repurchases, which have lowered the bank's share count considerably over the last decade. This was partially offset by some stock dividends that the bank issued over the last two years, though, which is why the share count has gone up again. In 2020, the coronavirus crisis will have a huge impact on Commerce Bancshares' profits, but we believe that a recovery to "normal" profitability will not take a long time.

¹ Estimated date

² Estimated date

³ In Millions

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Valuation Analysis

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | Now | 2025 |
|-----------|------|------|------|------|------|------|------|------|------|------|------|------|
| Avg. P/E | 14.7 | 13.5 | 12.8 | 15.0 | 16.4 | 16.6 | 17.6 | 18.7 | 14.3 | 19.0 | 17.5 | 12.0 |
| Avg. Yld. | 2.4% | 2.3% | 2.4% | 2.1% | 2.0% | 2.0% | 1.9% | 1.6% | 1.6% | 1.5% | 1.7% | 2.6% |

Commerce Bancshares trades at more than 17 times our 2020 earnings power estimate right now, although actual reported profits will be lower. The longer-term median earnings multiple is in the mid-teens, but we believe that shares would be fairly valued at a 12 times price to earnings multiple, which results in substantial downside potential.

Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2025 |
|--------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Payout | 35.8% | 31.0% | 30.4% | 31.7% | 32.9% | 33.6% | 32.9% | 29.8% | 26.1% | 29.1% | 30.0% | 31.4% |

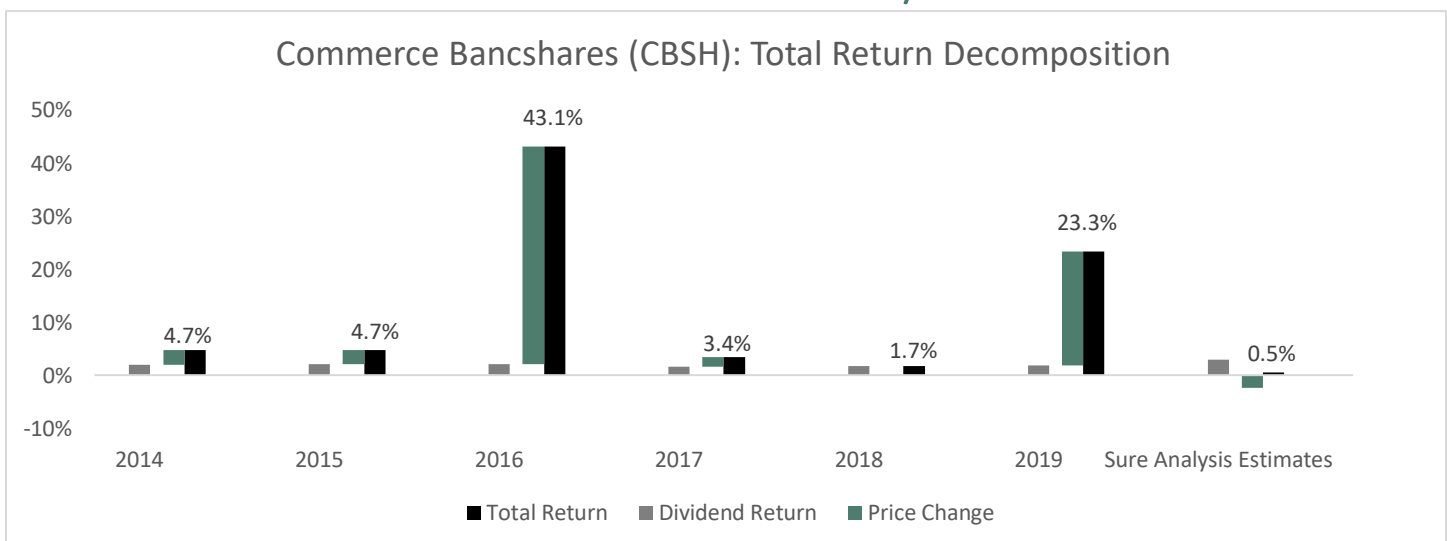
Commerce Bancshares' dividend payout ratio has never been particularly high, even during the last financial crisis when the company's profits took a hit. The dividend payout ratio has declined further during the last decade, and is now at a low level of around 30%. We believe that the payout ratio will expand going forward, but the dividend will still be rather safe, as Commerce Bancshares will continue to pay out significantly less than half of its profits.

Commerce Bancshares is not an overly large bank, but the company has strong fundamentals. This includes an above-average return on equity, which was 14% during 2019, and which is quite attractive versus the ROEs that many of the bank's peers achieve. Commerce Bancshares' capitalization is strong as well, the company has a tier 1 leverage ratio of 10.8%. Commerce Bancshares' credit quality is strong, as net charge-offs are at a below-average level compared to most peers. The current crisis will have an impact, but we see a recovery over the next couple of years.

Final Thoughts & Recommendation

Commerce Bancshares is not among the largest players in the banking industry, and the company has not produced overly high earnings growth rates in the past. Commerce Bancshares is a high-quality company with compelling fundamentals, though, and it has been more resilient than many peers in the past. We believe that shares are trading above fair value right now, even when using underlying earnings power instead of this year's artificially low forecasted net profits. Due to its high valuation, we rate Commerce Bancshares a sell for now.

Total Return Breakdown by Year



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Income Statement Metrics

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Revenue | 1,054 | 1,050 | 1,044 | 1,033 | 1,071 | 1,089 | 1,127 | 1,220 | 1,325 | 1,350 |
| SG&A Expense | 479 | 466 | 483 | 493 | 513 | 536 | 560 | 582 | 607 | 635 |
| D&A Expense | 49 | 47 | 43 | 42 | 42 | 43 | 41 | 40 | 39 | 41 |
| Net Profit | 222 | 256 | 269 | 261 | 262 | 264 | 275 | 319 | 434 | 421 |
| Net Margin | 21.0% | 24.4% | 25.8% | 25.3% | 24.4% | 24.2% | 24.4% | 26.2% | 32.7% | 31.2% |
| Free Cash Flow | 653 | 386 | 349 | 338 | 317 | 259 | 430 | 396 | 519 | 470 |
| Income Taxes | 96 | 121 | 127 | 123 | 122 | 117 | 124 | 111 | 106 | 109 |

Balance Sheet Metrics

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|-------------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Total Assets | 18,502 | 20,649 | 22,160 | 23,072 | 23,994 | 24,605 | 25,641 | 24,833 | 25,464 | 26,066 |
| Cash & Equivalents | 451 | 506 | 752 | 1,226 | 1,068 | 488 | 767 | 469 | 1,198 | 887 |
| Goodwill & Int. | 137 | 133 | 131 | 148 | 146 | 146 | 146 | 147 | 148 | 148 |
| Total Liabilities | 16,479 | 18,479 | 19,988 | 20,858 | 21,660 | 22,238 | 23,140 | 22,115 | 22,527 | 22,927 |
| Long-Term Debt | 112 | 112 | 104 | 107 | 104 | 104 | 102 | 2 | 9 | 2 |

Profitability Metrics

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Return on Assets | 1.2% | 1.3% | 1.3% | 1.2% | 1.1% | 1.1% | 1.1% | 1.3% | 1.7% | 1.6% |
| Return on Equity | 11.4% | 12.2% | 12.4% | 11.9% | 11.9% | 12.0% | 12.1% | 13.0% | 16.2% | 14.6% |
| ROIC | 9.3% | 11.6% | 11.8% | 11.4% | 11.0% | 10.7% | 10.9% | 12.0% | 15.3% | 13.8% |

Note: All figures in millions of U.S. Dollars unless otherwise noted.

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