Alerus Financial (ALRS)

Updated October 31st, 2024 by Aristofanis Papadatos

Key Metrics

Current Price:	$21	**5 Year CAGR Estimate:**	5.5%	**Market Cap:**	$413 M
Fair Value Price:	$16	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date:**	12/24/24[1]
% Fair Value:	135%	**5 Year Valuation Multiple Estimate:**	-5.8%	**Dividend Payment Date:**	1/10/25
Dividend Yield:	3.8%	**5 Year Price Target**	$23	**Years Of Dividend Growth:**	19
Dividend Risk Score:	B	**Retirement Suitability Score:**	B	**Rating:**	Hold

Overview & Current Events

Alerus Financial is a financial services company headquartered in North Dakota. Its operations date back to 1879, when it was originally founded as the Bank of Grand Forks, one of the first banks in Dakota. In 2000, it changed its name to Alerus Financial to reflect its evolution from a traditional community bank to a financial services company. Alerus Financial provides financial solutions to businesses and consumers through four distinct business segments—banking, retirement and benefit services, wealth management and mortgage. Instead of focusing on the broader population, it targets specific business and consumer segments, which offer significant growth potential. The bank has a market cap of $413 million and is characterized by prudent management. As a result, it has raised its dividend for 19 consecutive years.

On July 1st, 2022, Alerus Financial acquired Metro Phoenix Bank for $85.3 million in an effort to grow its presence in Arizona. As the deal value is 21% of the current market cap of Alerus Financial, it is obviously significant for the bank.

On May 15th, 2024, Alerus Financial agreed to acquire HMN Financial (HMNF) for ~$116.4 million in an all-stock deal. As per the terms of the deal, the shareholders of HMNF will receive 1.25 shares of Alerus Financial for each share they own. The combined company will have 29 branches in the Midwest and Arizona and will enjoy economies of scale. The deal is expected to be immediately accretive to earnings and closed in October-2024.

On October 29th, 2024, Alerus Financial reported results for Q3-2024. It grew its loans 3% and its deposits 1% sequentially. Net interest margin contracted from 2.39% to 2.23% and thus net interest income dipped -6%, in sharp contrast to the trend observed in most banks. As a result, earnings-per-share remained flat at $0.31, missing the analysts' estimates by $0.13. The stock slumped -14% due to the disappointing results. It also came under pressure last year due to the broad sell-off of regional banks, which resulted from the collapse of some banks. However, Alerus Financial has endured the financial turmoil, which has subsided, and thus its stock has retrieved most of its losses.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	$1.48	$1.21	$1.00	$1.07	$1.84	$1.91	$2.52	$2.97	$2.10	$0.58	***$1.30***	***$1.91***
DPS	$0.38	$0.42	$0.44	$0.48	$0.53	$0.57	$0.60	$0.63	$0.72	$0.76	***$0.80***	***$1.00***
Shares[2]	13.9	13.9	14.0	14.0	14.1	15.1	17.4	17.5	20.2	20.0	***20.0***	***25.0***

Alerus Financial has exhibited a decent performance record over the last decade. During this period, the bank grew its earnings-per-share at a 4.1% average annual rate until 2022, though it posted 10-year low earnings-per-share last year due to its losses from the sale of bonds amid high interest rates. The bank is trying to grow primarily via the acquisition of smaller peers. The recent acquisition of HMN financial, which is the largest and marked the 26th acquisition in the history of the bank, is likely to prove a material growth driver in the upcoming years. Alerus Financial may incur additional losses from the sale of securities this year but it is likely to recover in the upcoming years, assisted by the interest rate reductions expected by the Fed. Overall, given the low comparison base formed this year, we assume 8.0% average annual growth of earnings-per-share over the next five years.

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[1] Estimated date.

[2] In millions.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

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Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	12.4	16.2	17.7	18.0	13.0	10.6	8.2	10.1	11.7	31.7	***16.2***	***12.0***
Avg. Yld.	2.1%	2.1%	2.5%	2.5%	2.2%	2.8%	2.9%	2.1%	2.9%	4.1%	***3.8%***	***4.4%***

Due to its low earnings this year, Alerus Financial is trading at a price-to-earnings ratio of 16.2, which is higher than the 10-year average price-to-earnings ratio of 15.0 of the stock. We assume a fair earnings multiple of 12.0 for the stock, in line with the norm for banks. If the stock trades at this valuation level in five years, it will incur a -5.8% annualized drag.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	26%	35%	44%	45%	29%	30%	24%	21%	34%	131%	***62%***	***52%***

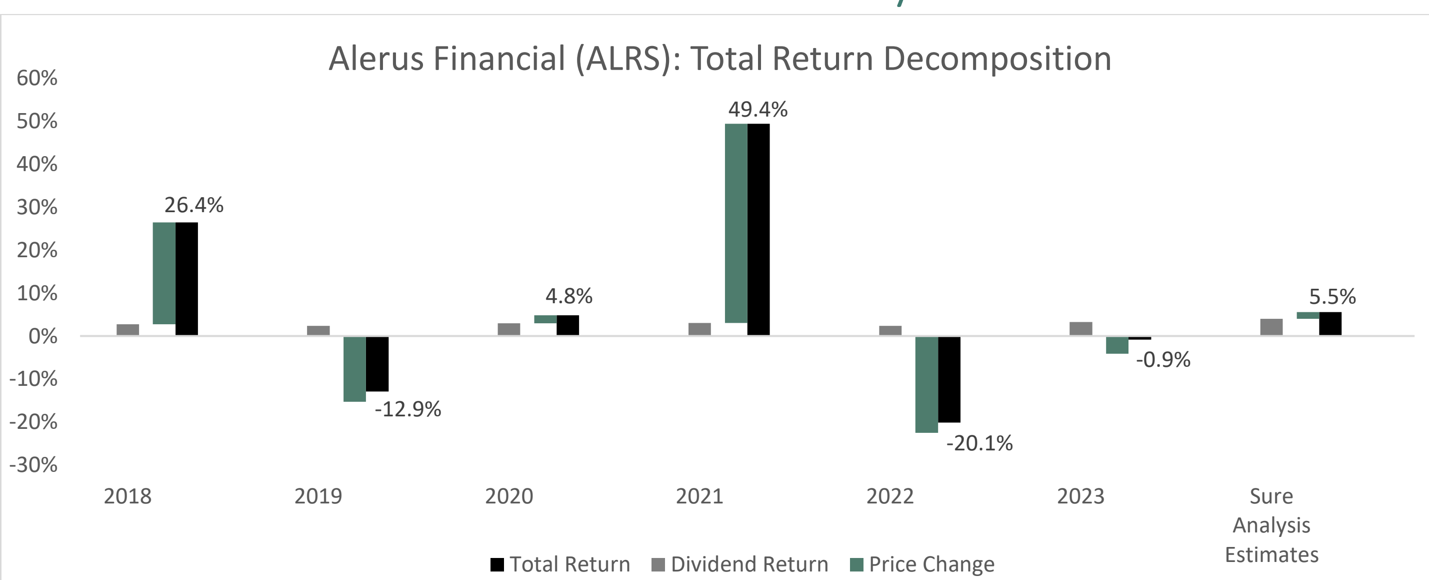
Alerus Financial has fairly prudent management, which is focused on maintaining healthy credit quality metrics. During the last 25 years, the bank has maintained an average net loan charge-off ratio of only 0.3%. Thanks to its cautious strategy, the company has proved resilient to recessions. Most banks faced material loan losses due to the pandemic in 2020, but Alerus Financial proved resilient to this crisis thanks to its defensive business model. The bank grew its earnings-per-share in both 2020 and 2021, though its earnings have now dipped due to the decrease in the value of the fixed-income investments of the bank caused by nearly 23-year high interest rates.

Alerus Financial has raised its dividend by 5.2% this year. As a result, it has raised its dividend for 19 consecutive years and is currently offering a dividend yield of 3.8%. Given its healthy payout ratio of 62% and its reliable business performance, the bank can continue raising its dividend for many more years.

Final Thoughts & Recommendation

Alerus Financial has promising growth prospects thanks to its acquisition of Metro Phoenix Bank and HMN Financial, which marked the largest acquisition in the history of the bank. In addition, the bank has endured the turmoil caused by the collapse of a few banks. The stock has rallied 50% in the last 18 months and hence it has become less attractive. It could offer a 5.5% average annual return over the next five years thanks to 8.0% earnings-per-share growth and its 3.8% dividend, partly offset by a -5.8% valuation headwind. The stock maintains its hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	123	137	166	168	176	186	228	230	209	166
SG&A Exp.	68	81	89	71	73	77	92	97	84	79
D&A Exp.	8	9	11	10	9	9	9	9	8	9
Net Profit	21	17	14	15	26	30	45	53	40	12
Net Margin	17.0%	12.5%	8.5%	8.9%	14.7%	15.9%	19.6%	22.9%	19.1%	7.2%
Free Cash Flow	19	20	32	45	50	16	(26)	147	101	26
Income Tax	9	7	7	18	7	9	14	16	12	4

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	1,488	1,745	2,051	2,136	2,179	2,357	3,014	3,393	3,780	3,908
Cash & Equivalents	46	266	207	122	41	144	173	242	58	130
Goodwill & Int. Ass.	26	25	65	59	54	50	58	54	72	66
Total Liabilities	1,317	1,562	1,882	1,956	1,982	2,071	2,684	3,033	3,423	3,539
Long-Term Debt	21	69	58	88	58	58	58	59	432	373
Shareholder's Equity	171	183	169	180	197	286	330	359	357	369
LTD/E Ratio	0.13	0.38	0.34	0.49	0.29	0.20	0.18	0.16	1.21	1.01

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	1.4%	1.1%	0.7%	0.7%	1.2%	1.3%	1.7%	1.6%	1.1%	0.3%
Return on Equity	13.6%	9.7%	8.0%	8.6%	13.7%	12.2%	14.5%	15.3%	11.2%	3.2%
ROIC	11.3%	7.7%	5.9%	6.1%	9.9%	9.9%	12.2%	13.1%	6.6%	1.5%
Shares Out.	13.9	13.9	14.0	14.0	14.1	15.1	17.4	17.5	18.9	20.1
Revenue/Share	8.80	9.80	11.83	12.03	12.50	12.32	13.05	13.17	11.06	8.25
FCF/Share	1.38	1.47	2.31	3.21	3.54	1.08	(1.50)	8.43	5.36	1.28

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.