Farmers & Merchants Bancorp, Inc. (FMAO)

Updated March 27th, 2023, by Yiannis Zourmpanos

Key Metrics

Current Price:	$25.4	**5 Year CAGR Estimate:**	10.8%	**Market Cap:**	$346.6 M
Fair Value Price:	$23.1	**5 Year Growth Estimate:**	10.0%	**Ex-Dividend Date:**	03/30/2023
% Fair Value:	110%	**5 Year Valuation Multiple Estimate:**	-1.9%	**Dividend Payment Date:**	04/20/2023
Dividend Yield:	3.3%	**5 Year Price Target**	$37	**Years Of Dividend Growth:**	15
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Rating:**	Buy

Overview & Current Events

Farmers & Merchants Bancorp, Inc. (FMAO) or F&M is a bank holding company headquartered in Archbold, Ohio, USA. It was founded in 1897 and currently operates in Ohio, Indiana and Michigan. FMAO caters to a diverse set of customers, including individuals, businesses, and farmers, and offers a range of financial services, including deposit accounts, loans, credit cards, and online banking. FMAO faces significant competition from other regional and national banks, but its strong customer relationships and commitment to personalized service help it maintain a competitive position in the market. The company has a competitive position in the community banking market and holds a market share of 10%. FMAO's revenue segments are retail banking, commercial banking, and agricultural lending.

On February 8th, 2023, the company announced results for the fourth quarter ending December 31st, 2022. F&M reported Q4 Non-GAAP EPS of $0.65, missing market estimates by $0.02. The company reported revenues of $22.56 million for the quarter, up 12.59% year-over-year. For 2022, F&M reported revenue of $870.2 million, up 22% from the previous year. The company also reported a net income of $7.2 million, down 6.5% from the $7.7 million profit in the previous year.

The bigger scale, high asset quality, and careful expense control of F&M contributed to profitability for the fourth quarter and full year of 2022. The Company's efficiency ratio increased to 50.45% in the fourth quarter of 2022 and 55.95% for the entire 2022 calendar year. High profitability also contributed to better yearly returns, and after adjusting for one-time, tax-adjusted acquisition expenses, ROAA, ROAE, and ROATCE all increased year over year. Total deposits on December 31, 2022, were $2.47 billion, up 12.6% from December 31, 2021. Also, as deposits have expanded since the COVID-19 crisis started, F&M continues to observe an increasing trend among customers toward safer and more reliable saving instruments.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	$0.96	$1.04	$1.12	$1.26	$1.38	$1.61	$1.66	$1.80	$2.01	$2.46	***$2.10***	***$3.38***
DPS	$0.41	$0.42	$0.44	$0.46	$0.50	$0.56	$0.61	$0.66	$0.71	$0.80	***$0.84***	***$1.18***
Shares	9.3	9.2	9.2	9.1	9.2	9.2	11.0	11.1	11.6	13.1	***13.6***	***16.7***

In the last quarter of 2022, the loan portfolio increased by 10% due to the purchase of Peoples-Sidney Financial Company. Also, the loan portfolio is well-diversified among many industries, including agriculture, consumer real estate, and commercial real estate. Following the acquisition of Peoples-Sidney Financial Company the margins have dropped, however we expect margins to resume its upward trajectory in the foreseeable future.

Thus, we forecast an EPS of $2.10 in 2023 in-line with analysts' estimates, and amidst the rising interest rate environment, the bank can grow faster in the following years, with a projected annual EPS growth of 10.0%, FMAO's EPS can reach $3.38 by 2028. F&M's DPS had a nine-year and five-year CAGR of 7.7% and 26.5%, respectively. Considering the company's 5-year payout ratio of 35.2%, we believe there is room for further DPS growth in light of EPS' expansion due to margin expansion. Recently the company has increased its dividend by 10.5% from the first quarter of 2022, supporting its increasing dividend trajectory.

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Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Avg. P/E	11.2	12.1	11.8	11.9	21.6	25.8	17.3	12.9	12.1	13.0	***12.1***	***11.0***
Avg. Yld.	1.6%	1.4%	1.3%	1.3%	1.2%	1.3%	1.5%	1.7%	1.8%	2.1%	***3.3%***	***3.2%***

F&M is trading at a forward P/E of 12.1, lower than its nine-year and five-year average P/E of 15.0 and 16.2, respectively. Following the banking turmoil and fears of the contagion effect in the sector, the stock has plunged but has strongly recovered lately. Considering the bank's resiliency, we have assumed a stable P/E of 11.0 to value the company in 2028, slightly lower than its historical averages, which accounts for the higher uncertainty attached to the sector, suggesting a target price of $37, and a 46% upside from current levels.

Safety, Quality, Competitive Advantage, & Recession Resiliency

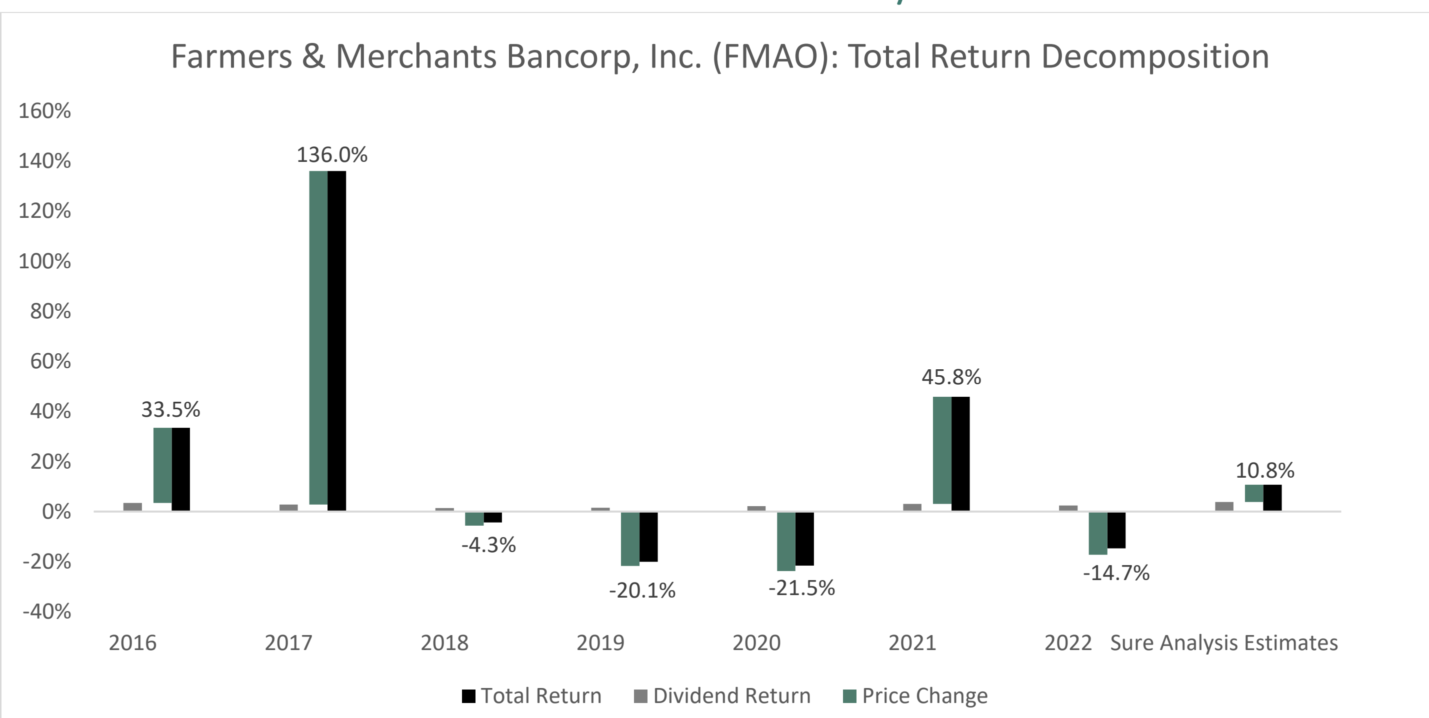
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	43%	40%	39%	37%	36%	35%	37%	37%	35%	33%	***40%***	***35%***

The company's competitive advantage lies in its longstanding reputation for providing quality financial services to its customers, along with its strong presence in the communities it serves. During the recession of 2008, F&M, performed well due to its conservative lending practices and strong capital position.

Final Thoughts & Recommendation

The loan pipeline and the margins are performing better; thus, we anticipate increasing dividend distributions in 2023, especially given that interest rates are currently expected to support profit growth. Following the banking crisis, the sector outlook remains uncertain. However, F&M's strong financial position is robust which leads to our buy rating, premised upon the 10.8% annualized total returns for the medium term, derived from the forecasted earnings-per-share growth of 10.0% and 3.3% dividend yield.

Total Return Breakdown by Year



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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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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	38	40	41	44	46	49	64	75	85	100
SG&A Exp.	19	20	21	20	21	23	30	32	38	42
D&A Exp.	2	2	2	2	2	2	4	4	5	4
Net Profit	9	10	10	12	13	15	18	20	23	33
Net Margin	24.0%	24.3%	25.3%	26.8%	27.9%	30.3%	28.9%	26.8%	27.7%	32.4%
Free Cash Flow	15	16	13	10	16	8	20	24	33	38
Income Tax	4	4	4	5	5	3	4	5	6	8

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	966	941	989	1,056	1,107	1,116	1,607	1,910	2,638	3,015
Cash & Equivalents	18	22	21	29	37	42	54	103	146	88
Goodwill & Int.	6	6	6	6	6	6	50	51	84	90
Total Liabilities	857	827	869	930	973	973	1,377	1,660	2,341	2,717
Long-Term Debt	5	-	10	10	5	-	25	18	99	172
Total Equity	109	114	120	126	134	143	230	249	297	298
LTD/E Ratio	0.04	-	0.08	0.08	0.04	-	0.11	0.07	0.33	0.58

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	0.9%	1.0%	1.1%	1.1%	1.2%	1.3%	1.4%	1.1%	1.0%	1.2%
Return on Equity	8.2%	8.6%	8.8%	9.5%	9.8%	10.8%	9.9%	8.4%	8.6%	10.9%
ROIC	7.7%	8.5%	8.5%	8.8%	9.3%	10.6%	9.2%	7.7%	7.1%	7.5%
Shares Out.	9.3	9.2	9.2	9.1	9.2	9.2	11.0	11.1	11.6	13.1
Revenue/Share	4.04	4.33	4.45	4.77	4.98	5.37	5.72	6.72	7.27	7.60
FCF/Share	1.61	1.77	1.43	1.10	1.72	0.88	1.84	2.17	2.81	2.88

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