



Bank of Montreal (BMO)

Updated February 28th, 2024 by Kay Ng

Key Metrics

Current Price:	\$90	5 Year CAGR Estimate:	9.2%	Market Cap:	\$64.7B
Fair Value Price:	\$88	5 Year Growth Estimate:	5.0%	Ex-Dividend Date:	04/26/24
% Fair Value:	101%	5 Year Valuation Multiple Estimate:	-0.3%	Dividend Payment Date:	05/28/24
Dividend Yield:	5.0%	5 Year Price Target	\$113	Years Of Dividend Growth¹:	11
Dividend Risk Score:	B	Retirement Suitability Score:	A	Rating:	Hold

Overview & Current Events

Bank of Montreal was formed in 1817, becoming Canada's first bank. The past two centuries have seen Bank of Montreal grow into a global powerhouse of financial services and today, it has about 2,000 branches (including Bank of West branches) in North America. In a normal year, Bank of Montreal produces about C\$14 billion in net income. It generates about 45% of earnings from the U.S. (including Bank of the West) and the rest primarily from Canada. The bank is cross listed in both New York and Toronto; we use U.S. Dollars throughout the report unless otherwise noted.

Bank of Montreal reported its fiscal Q1 2024 financial results on 02/27/24. For the quarter, compared to a year ago, adjusted net revenue rose 10% to C\$7.85 billion, while adjusted net income fell 12% to C\$1.89 billion. Adjusted diluted earnings per share ("EPS") declined by 16% to C\$2.56. Higher provision for credit losses (PCL) of C\$627 million (versus C\$217 million a year ago) as well as a 16% jump in non-interest expense to \$4.78 billion weighed on earnings. Notably, the PCL on impaired loans to average net loans and acceptances is still low at 0.29% for the quarter, although it's up from fiscal 2023's 0.19%.

Average net loans & acceptances, and average deposits both jumped ~16% year over year to C\$651 billion and C\$922 billion, respectively. The bank's common equity tier 1 ratio remained solid at 12.8%, down from 18.2% a year ago. The adjusted return on equity was 10.6%, down from 12.9% in the prior year's quarter.

BMO completed the integration of the Bank of the West, which it acquired in February 2023. Importantly, it achieved the US\$800 million run-rate cost synergies to start the second quarter. It's also improving operational efficiencies that should lower expense. In light of the Q1 results, we lowered our fiscal 2024 EPS estimate to \$8.50.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	\$5.79	\$5.23	\$5.66	\$6.27	\$6.81	\$7.09	\$5.95	\$10.13	\$9.85	\$8.68	\$8.50	\$10.85
DPS	\$2.82	\$2.60	\$2.56	\$2.72	\$2.94	\$3.06	\$3.15	\$3.37	\$4.03	\$5.32	\$4.51	\$5.76
Shares¹	649	643	646	648	639	640	646	650	677	721	725	754

From 2014 to 2023, the bank increased EPS by 6.6% in C\$ but when translated to US\$, the growth rate dropped to 4.6% per year. The company estimates medium-term EPS growth of 7-10% per year. However, the actual result would be affected by forex fluctuations between the C\$ and US\$. Through 2029, we use a 5% growth rate for the EPS and DPS, to be cautious.

In December 2021, after the regulator, Office of the Superintendent of Financial Institutions, approved of dividend increases again, BMO raised its quarterly dividend by 25.5% (the highest increase versus the other Big Six Canadian banks) to C\$1.33. This is a vote of confidence in BMO's strong capital position. We set our 2024 dividend estimate based on the forex rate at writing. Keep in mind that the fluctuations in the forex between U.S. dollars and Canadian dollars will affect the effective yield for U.S. shareholders.

¹ Years of Dividend Growth in Canadian dollars; Shares in millions.

Disclosure: Kay Ng owns shares of BMO.



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Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	11.5	11.4	11.0	11.7	12.0	10.6	10.0	11.2	10.4	9.8	10.5	10.4
Avg. Yld.	3.9%	4.5%	3.6%	3.4%	4.5%	4.0%	5.3%	3.5%	3.9%	4.5%	5.0%	5.1%

From 2014-2023, BMO's average price-to-earnings ratio was 11. From 2019 to 2023, it was 10.4. We think a P/E of 10.4 is more conservative for the expected longer term EPS growth rate of about 5%. The current P/E of 10.5 makes the stock fairly valued. We think BMO's yield will not stray far away from a 4-5% yield range in the long run. As a Canadian stock, BMO's dividends may be subject to a 15% dividend withholding tax for U.S. investors. This tax can potentially be avoided by investing in BMO through a retirement account.

Safety, Quality, Competitive Advantage, & Recession Resiliency

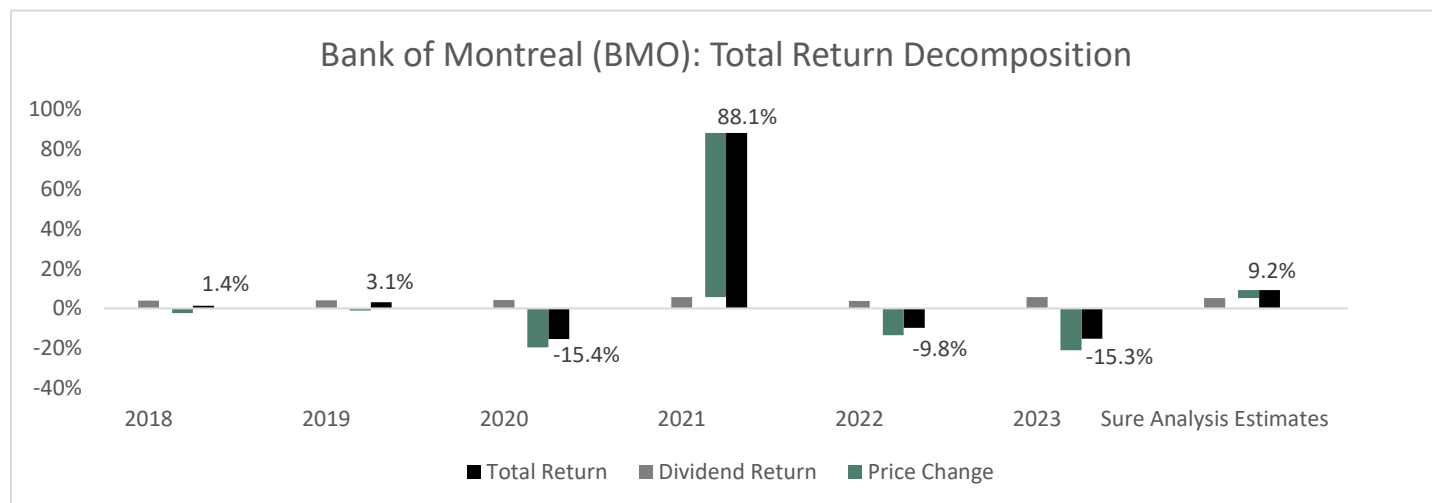
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	49%	50%	45%	43%	43%	43%	53%	33%	41%	61%	53%	53%

During the Great Recession, BMO maintained the same dividend from fiscal 2009 to 2011 before resuming dividend growth afterwards. Similarly, the regulator restriction led to a dividend freeze of 8 quarters during the COVID-19 pandemic. The solid bank came out with a dividend increase as soon as the ban was lifted. BMO's dividend policy is a payout ratio of 40%-50%. Its payout ratio was higher than normal in 2020 and 2023 due to higher provision for credit losses from a more negative macro outlook. We expect BMO's payout ratio to stay within its target payout ratio range in most years. The bank's competitive advantage is in the long history and reputation of its brand, its large size. It's a top 10 U.S. bank by assets with a footprint in 32 states, a top 5 commercial lender in North America, and one of the Big Six banks, in a smaller market like Canada. Recessions are tough for banks, but BMO performed admirably during the last two (including the one during the pandemic) by maintaining its dividend in the Canadian currency.

Final Thoughts & Recommendation

We forecast 9.2% in total annualized returns over the next five years for an investment in BMO at current prices, consisting of a yield of 5.0%, 5.0% earnings-per-share growth, and a 0.3% headwind from a lower price-to-earnings ratio. Currently, we rate fairly valued Bank of Montreal as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	16569	15457	15798	16608	17673	19060	18615	21388	19996	24490
SG&A Exp.	7110	6716	6731	6886	6850	8376	7180	8042	6702	10570
D&A Exp.	686	635	624	670	702	744	1057	1133	1075	1555
Net Profit	3925	3521	3486	4081	4238	4332	3791	6163	10514	3235
Net Margin	23.7%	22.8%	22.1%	24.6%	24.0%	22.7%	20.4%	28.8%	52.6%	
Free Cash Flow	-3363	1391	-2518	1619	13233	21199	37047	34230	2726	5865
Income Tax	829	754	830	988	1524	1139	931	1990	3378	1101

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets (B)	525.6	487.6	512.8	553.1	589.4	647.2	712.5	797.4	837.1	935.1
Cash & Equivalents	30803	36219	26910	30469	38451	43130	49873	81953	68482	59340
Accounts Receivable	6719	5844	6732	6036	3413	3518	3520	4121	4903	7054
Goodwill & Int. Ass.	6612	6288	6380	6550	6589	6656	6738	6168	5495	15870
Total Liabilities (B)	494.0	457.3	481.2	518.5	554.6	608.4	670.1	751.0	784.9	879.4
Accounts Payable	7825	7381	8249	8658	8716	9501	9410	11149	12441	14260
Long-Term Debt	24447	19819	116458	132181	124845	148195	138567	150945	161511	177320
Shareholder's Equity	27925	27487	28671	31268	31541	35229	38959	43471	50251	53300
D/E Ratio	0.80	0.66	3.69	3.82	3.58	3.82	3.26	3.25	3.09	3.18

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	0.8%	0.7%	0.7%	0.8%	0.7%	0.7%	0.6%	0.8%	1.3%	0.4%
Return on Equity	14.4%	12.7%	12.4%	13.6%	13.5%	13.0%	10.2%	15.0%	22.4%	6.2%
ROIC	7.1%	6.6%	3.5%	2.6%	2.6%	2.5%	2.1%	3.3%	5.1%	1.4%
Shares Out.	648	647	646	652	645	640	642	649	666	711
Revenue/Share	25.55	23.88	24.45	25.47	27.40	29.76	28.99	32.97	30.04	34.47
FCF/Share	-5.19	2.15	-3.90	2.48	20.52	33.10	57.69	52.77	4.09	8.25

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

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