Farmers & Merchants Bancorp, Inc. (FMAO)

Updated February 28th, 2024, by Yiannis Zourmpanos

Key Metrics

Current Price:	$21	**5 Year CAGR Estimate:**	7.1%	**Market Cap:**	$298.9 M
Fair Value Price:	$16.50	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date:**	03/29/2024[1]
% Fair Value:	127%	**5 Year Valuation Multiple Estimate:**	-4.7%	**Dividend Payment Date:**	04/19/2024[2]
Dividend Yield:	4.2%	**5 Year Price Target**	$24	**Years Of Dividend Growth:**	16
Dividend Risk Score:	D	**Retirement Suitability Score:**	C	**Rating:**	Hold

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 13th, 2024, the company announced results for the fourth quarter of 2023. F&M reported Q4 GAAP EPS of $0.41, beating estimates by $0.09. Additionally, the company reported revenues of $23.86 million for the quarter, down 10.6% year-over-year.

The results demonstrate the good asset quality maintained by FMAO, with a nonperforming loan rate of only 0.87% of total loans and net charge-offs to average loans amounting to a tiny 0.03%. The allowance for credit losses was robust at 111.95% of the nonperforming loans, with the Tier 1 leverage ratio at 8.20%. Important strategic activities during the quarter included the opening of FMAO's first bank office in Michigan and a new regional headquarters in Fort Wayne, Indiana. The company also appointed Ian D. Boyce to the Company and Bank boards for governance enhancement. FMAO also reorganized its organizational structure to support future growth effectively and enhance profitability.

The full year 2023 witnessed many key-year metrics at all-time highs by FMAO. Total loans witnessed a 9.5% gain, coming in at $2.58 billion, while total assets also increased by 8.9% to $3.28 billion. Deposits grew by 5.6% to a record level of $2.61 billion, and stockholders' equity increased by 6.2% to a record high of $316.5 million. Even after net interest income was down 3.1%, to $79.7 million after the provision for credit losses, net income for the year remained strong at $22.8 million or $1.67 per basic and diluted share. The return on average tangible equity was an impressive 12.17%.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	$1.04	$1.12	$1.26	$1.38	$1.61	$1.66	$1.80	$2.01	$2.46	$1.67	***$1.50***	***$2.20***
DPS	$0.42	$0.44	$0.46	$0.50	$0.56	$0.61	$0.66	$0.71	$0.80	$0.85	***$0.88***	***$1.23***
Shares[3]	9.2	9.2	9.1	9.2	9.2	11.0	11.1	11.6	13.1	13.6	***14.2***	***17.9***

We have revised downwards our EPS forecast to match analysts' estimate of $1.50 for 2024. The forecasts suggest lower interest rates in the following years despite the high-interest rate environment. With a projected annual EPS growth of 8.0%, FMAO's EPS can reach $2.20 by 2029. F&M's DPS had a 10-year and five-year CAGR of 5.4% and 1.8%, respectively.

[1] The ex-div date is estimated based on historical data.
[2] The dividend payment date is estimated based on historical data.
[3] In millions.

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Considering the company's five-year average payout ratio of 37.9%, we believe there is room for further DPS growth considering EPS should grow due to margin expansion.

Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Avg. P/E	12.1	11.8	11.9	21.6	25.8	17.3	12.9	12.1	13.0	13.3	***14.0***	***11.0***
Avg. Yld.	3.3%	3.3%	3.1%	1.7%	1.3%	2.1%	2.9%	2.9%	2.5%	3.8%	***4.2%***	***5.1%***

F&M is trading at a forward P/E of 14.0, lower than its 10-year and five-year average P/E of 15.2 and 13.7, respectively. Considering the bank's resiliency, we have assumed a stable P/E of 11.0 to value the stock, slightly lower than its historical averages as this accounts for the uncertainty attached to the sector. This suggesting a target price of $24.

Safety, Quality, Competitive Advantage, & Recession Resiliency

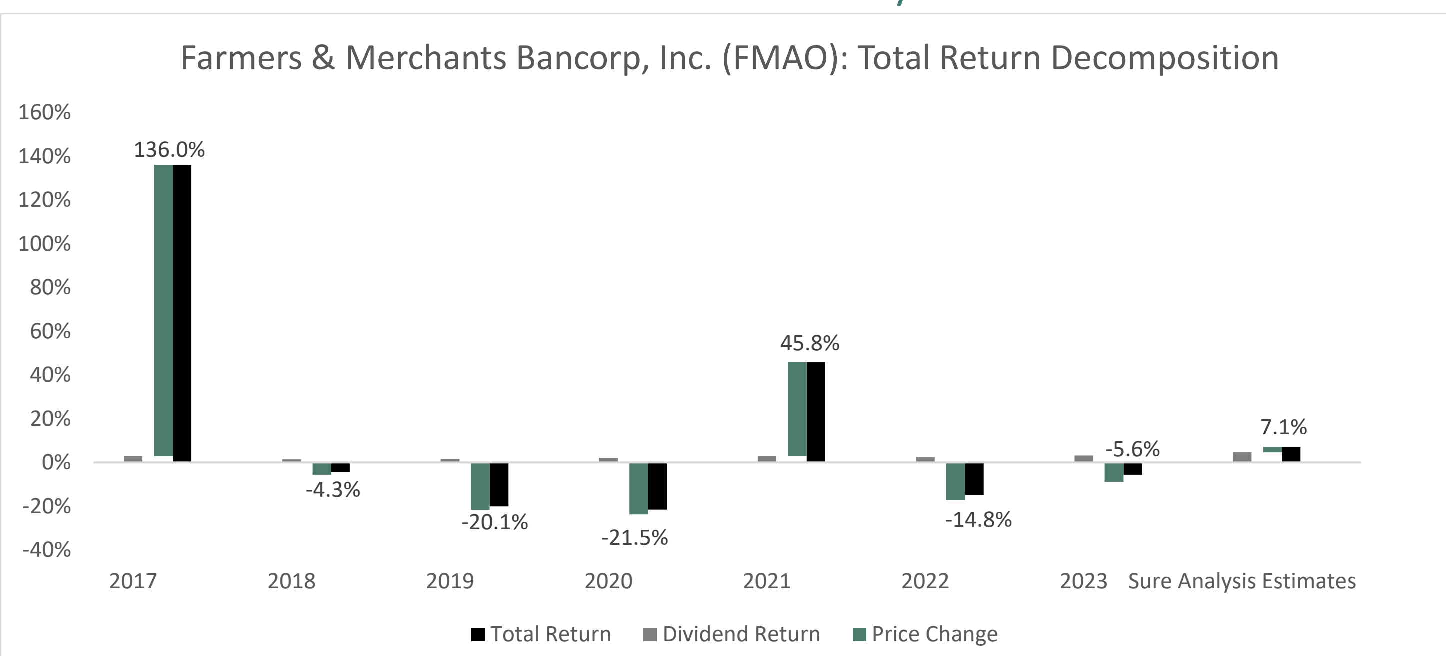
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	40%	39%	37%	36%	35%	37%	37%	35%	33%	51%	***59%***	***56%***

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. In general, F&M has a stable dividend payout ratio, and we expect it to hover above its historical average of 38.0%, at around 59%.

Final Thoughts & Recommendation

The loan pipeline and the margins are performing better; thus, we anticipate increasing dividend distributions in 2024, especially given that interest rates are expected to support profit growth. Following the banking crisis, the sector outlook remains uncertain. Following FMAO's pullback recently and considering its strong financial position, we have revised our rating to hold, premised upon the 7.1% annualized total returns for the medium-term, derived from the forecasted earnings-per-share growth of 8.0%, 4.2% dividend yield, and a valuation headwind.

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.