



Bank of Montreal (BMO)

Updated September 1st, 2024 by Kay Ng

Key Metrics

Current Price:	\$84	5 Year CAGR Estimate:	11.8%	Market Cap:	\$61B
Fair Value Price:	\$84	5 Year Growth Estimate:	7.0%	Ex-Dividend Date:	10/30/24
% Fair Value:	99%	5 Year Valuation Multiple Estimate:	0.2%	Dividend Payment Date:	11/26/24
Dividend Yield:	5.5%	5 Year Price Target	\$118	Years Of Dividend Growth¹:	11
Dividend Risk Score:	B	Retirement Suitability Score:	A	Rating:	Buy

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 the West branches) in North America. 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 Q3 2024 financial results on 08/27/24. For the quarter, compared to a year ago, adjusted net revenue was flat at C\$8.2 billion, while adjusted net income fell 8% to C\$2 billion. Adjusted diluted earnings per share ("EPS") declined by 10% to C\$2.64. Higher adjusted provision for credit losses ("PCL") of C\$906 million (versus C\$492 million a year ago) weighed on earnings. The PCL on impaired loans to average net loans and acceptances was 0.50% for the quarter, up from 0.21% a year ago.

Average net loans & acceptances, and average deposits rose 3.7% and 8.8%, respectively, to C\$665 billion and C\$962 billion. The bank's common equity tier 1 ratio remained solid at 13.0%, up from 12.3% a year ago. The adjusted return on equity was 10.6%, down from 12.5% in the prior year's quarter.

For the fiscal year to date, adjusted revenue rose 4% to C\$24 billion, while adjusted net income fell 9% to C\$5.9 billion. Adjusted diluted EPS fell 12% to C\$7.78. Due to higher PCL, we lowered our fiscal 2024 EPS estimate to \$7.68.

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	\$7.68	\$10.77
DPS	\$2.82	\$2.60	\$2.56	\$2.72	\$2.94	\$3.06	\$3.15	\$3.37	\$4.03	\$5.32	\$4.59	\$6.14
Shares¹	649	643	646	648	639	640	646	650	677	721	730	759

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, actual results will be affected by forex fluctuations between the C\$ and US\$. Due to the recent higher PCL, BMO has underperformed. On a rebound to normalization, the stock could deliver better results through 2029, so for this period we use a 7% EPS growth and 6% DPS growth rate.

Although in fiscal Q2 2024, BMO only raised its dividend by 2.6%, notably, it typically increases its dividend twice a year. So, the trailing-12-month increase was 5.6%. 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: This analyst has a position in the security discussed in this research report.



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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	10.9	11.0
Avg. Yld.	3.9%	4.5%	3.6%	3.4%	4.5%	4.0%	5.3%	3.5%	3.9%	4.5%	5.5%	5.2%

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 11.0 would make sense if BMO achieved a higher EPS growth rate of ~7% through 2029. The current P/E of 10.9 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

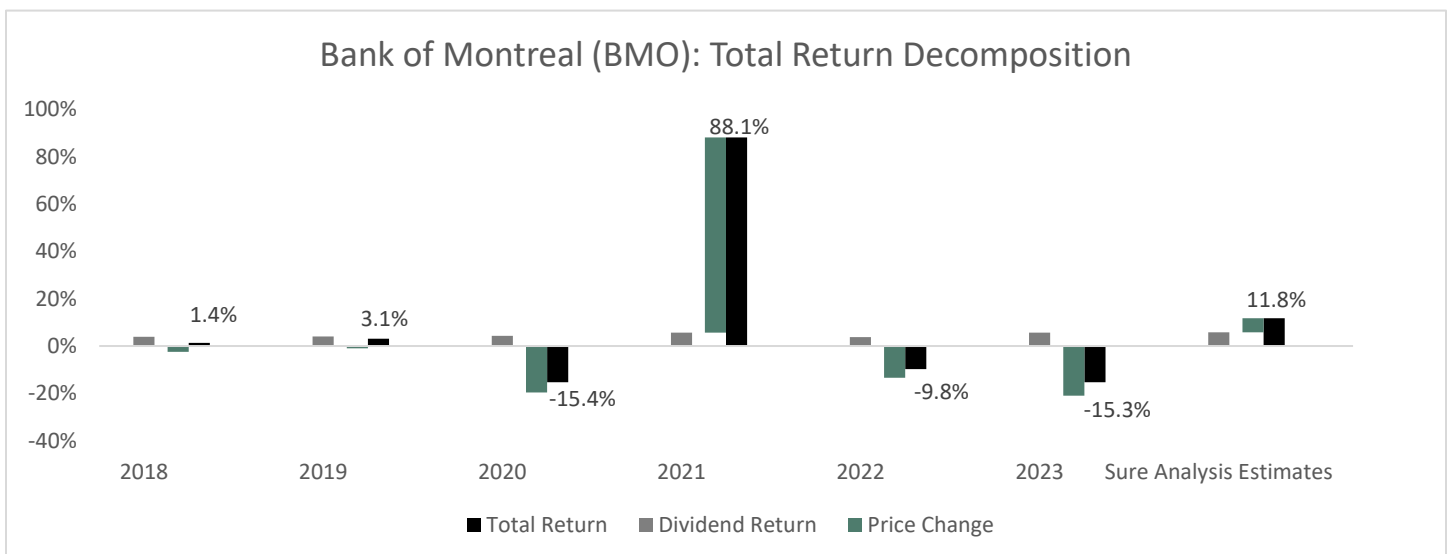
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	49%	50%	45%	43%	43%	43%	53%	33%	41%	61%	60%	57%

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 eight quarters during the COVID-19 pandemic. BMO came out with a dividend increase as soon as the ban was lifted. BMO's dividend policy is for 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 macroeconomic 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 five 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 11.8% in total annualized returns over the next five years for an investment in BMO at current prices, consisting of a yield of 5.5%, 7.0% earnings-per-share growth, and a 0.2% tailwind from a higher price-to-earnings ratio. Currently, we rate Bank of Montreal as a buy.

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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