Don't Let Disappointing Numbers Deter You From Investing in the Bank of Montreal

Description

Investors and analysts alike are growing increasingly concerned over the performance of Canada's big six banks with a range of headwinds set to affect their performance.

The impact that these headwinds have had on the big six is indicated in the **Bank of Montreal's** (TSX:BMO)(NYSE:BMO) first-quarter 2015 results. The net income for this quarter declined by 6% year-over-year, but despite this I believe investors should still consider Bank of Montreal as a core holding in their portfolio.

Let me explain.

So what?

The key drivers of the Bank of Montreal's disappointing result include the cumulative impact of the oil rout, lower long-term interest rates, and a weaker Canadian economy. These have all had an impact on the demand for credit and mortgages, which are the bread and butter of the bank business in Canada.

Net income in its core Canadian retail banking unit may have shot up by 6% year-over-year to $708 million, but this can be mostly attributed to lower provisions for credit losses.

The bank's capital markets business also turned in a particularly disappointing result, with net income falling by a whopping 20% year-over-year to $221 million. This can be attributed to the adjustment of credit and funding valuations that were affected by the rout in crude, lower securities gains, and a weak outlook for the Canadian economy.

However, despite the bad news, there is one key reason why I believe the Bank of Montreal is well positioned to continue posting solid performances. That reason is the Bank of Montreal's solid exposure to the rapidly recovering U.S. economy.

For the quarter, the Bank of Montreal's U.S. business saw the net income surge an impressive 14% on the back of stronger credit demand, with year-over-year loan growth up by an impressive 10%.

There are signs that such impressive growth is set to continue.

An increasingly stronger U.S. economy means lower unemployment rates and higher salaries, which will drive greater loan and deposit growth and push the U.S. dollar higher, increasing the revenue derived from this business.

Another positive for the bank is that despite its wealth management business delivering next to no bottom-line growth, its total funds under management surged a massive 43% year-over-year to $852 billion.

Funds-management businesses are typically perceived as “cash cows,” with the managed investments considered to be “sticky money” that allows the business to generate a steadily growing revenue over time, particularly if markets perform well. This is no different for the Bank of Montreal, with this tremendous asset base presenting a range of revenue generating opportunities that will help to boost its bottom line over time.

Finally, let’s not forget about that dividend.

The Bank of Montreal has an impressive dividend history, which has seen it hike its dividend for the last three straight years, giving it a 4.2% yield, the third highest of the big six banks. This yield also certainly appears to be sustainable, with the bank committed to pay out 40% to 50% of its net income.

Now what?

I certainly don’t expect to see any further growth in the bank’s dividend for as long its Canadian operations are facing a broad range of headwinds, but I do expect it to continue rewarding investors with this tasty yield.

This is because the Bank of Montreal’s operations are set on a solid foundation, with the bank being well capitalized and having a high-quality credit portfolio. I believe these reasons, coupled with its ability to benefit from the growing U.S. economy and a stronger U.S. dollar, make it a core holding in any portfolio.

CATEGORY

1. Bank Stocks
2. Investing

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