Bank of Montreal (TSX:BMO): Should You Buy Before a Big Bank Bounce?

Description

Bank of Montreal (TSX:BMO)(NYSE:BMO) has been one of Canada's most out of favour Big Six bank stocks in 2020. The COVID-19 crisis has hit the banks hard, but with more than its fair share of commercial loans in the oil and gas (O&G) scene, among other COVID-hit sectors of the North American economy, BMO stock has been punished most severely.

Although shares of BMO have recovered some ground from the depths of March (shares lost nearly 50% of their value from peak to trough), the stock remains a country mile away from its pre-pandemic highs. Not having participated to the full extent in the recent market-wide relief rally, BMO, as well as many of its Big Six banking peers, look like great bargains for those looking for a catch-up investment.

So, why is BMO likely the best bank for your buck at this juncture?

It's not just because Bank of Montreal led the downward charge back in February and March. Sure, traditional valuation metrics were the most depressed they've been since the rise out of the Great Financial Crisis, but there are many other things to love when it comes to BMO.

There are two underlooked positives that I think BMO has over its peers in the Big Six:

Bank of Montreal's bruised loan book could be quick to bounce back in a COVID-19 recovery

BMO has racked up the loan losses in the first half. While provisioning is likely to continue for several more quarters, I think it's already more than baked into the share price here. Also, I think many investors may be overdiscounting BMO's resilience in the face of this unprecedented crisis and are overlooking BMO's bounce-back potential should COVID-19 be contained or eliminated within the next two years.

Bad commercial loans could mount, but there's also a chance that peak provisioning is already behind us. And as the economy continues reopening safely in phases, there's a chance that the damage done to BMO stock could prove to be excessive. The stock trades at the slightest discount to book value at the time of writing. As things return to normalcy, I expect Bank of Montreal to command a premium once again and think it could happen within two years, as the world economy heals from COVID-19.

Below-average exposure to the Canadian housing market

Some pundits expect a Canadian housing crash at some point over the next few years. While a gradual cooling of the ridiculously frothy housing market is likely, one must not rule out the possibility of a violent meltdown.

Now, the housing market could easily stay frothy for many more years, but if this COVID-19 pandemic ends up being the pin that bursts the housing bubble, you'll want to limit your exposure to domestic mortgages.

Now, a Canadian housing collapse could send further shock waves through the economy that will drag BMO down further. However, compared to the likes of a **CIBC**, which has more housing exposure and a less attractive valuation, I'd say Bank of Montreal has more of a margin of safety if you're looking to hedge yourself against a Canadian housing meltdown.

Foolish takeaway on Bank of Montreal stock

The pessimism is overblown on BMO stock relative to its peers. If you're looking for a high-quality bank that could have the most room to rise out of its funk, look no further than the name before the banks can bounce back from this crisis.

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Date
2025/08/03
Date Created
2020/08/14
Author
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