7σ SQUIRERA

Executive Summary

While the acquisition strengthens BMO's U.S. presence and market position, its success hinges on effective integration, synergy realization, and prudent risk management to justify the premium paid.

BMO's Acquisition of Bank of the West

Strategic Rationale for the Acquisition

- The $16.3 billion acquisition significantly bolsters BMO's U.S. footprint, particularly in high-growth markets like **California**, increasing access to **1.8 million new customers** and expanding its deposit base.
- The deal increases BMO's total assets to **$938.8 billion**, with a **57% rise in U.S. deposits** and an **$80 billion boost** in loans, enhancing revenue streams and market competitiveness.
- Expected **cost synergies of $670 million** and revenue synergies approaching **$1 billion** through cross-selling opportunities in commercial banking, wealth management, and capital markets.

Challenges & Potential Downsides

- At **1.5x book value** and 14x estimated earnings, BMO paid a significant premium, which increases the risk of longer-than-expected breakeven timelines. Historical bank M&A transactions have ranged from 1.2x to 1.4x book value, the premium raises concerns about long-term value creation.
- Differences in customer base behavior: Bank of the West had a **42% concentration** of retail customers in California, whereas BMO has a historically more diversified portfolio.
- Expected ROIC (Return on Invested Capital) of **10% post-synergies,** but any slowdown in loan growth or unexpected credit losses could push this lower.

Strategic Fit & Expansion

BMO's $16.3B acquisition of Bank of the West accelerates its U.S. expansion, adding 514 branches and $105B in deposits, success hinges on $670M in cost synergies and seamless integration.

Expansion in High Growth US Markets

California Opportunity

- California has the **largest state economy in the U.S. (~$4 trillion GDP)**, with strong business activity and high-net-worth clients.
- BMO's market share in California before the acquisition was negligible, but with this deal, it now holds **over $105 billion in U.S. deposits**, a **40% increase** from pre-acquisition levels.

Diversification

- The acquisition strengthens BMO's **presence in high-growth Western states**, such as **Colorado, Arizona, and Nevada**, where population and business expansion rates have outpaced national averages.

- BMO's capital markets division now has **greater access to West Coast businesses**, facilitating M&A advisory, underwriting, and capital raising.

Growth & Profitability targets

Projected Revenue Growth

- The deal is expected to add **$2 billion** in **annual revenue by 2025**, fueled by cross-selling opportunities and expanded lending capabilities.

- BMO forecasts an internal rate of return (IRR) of **14% post-synergy realization.**

Synergies

- Bank of the West's **$80 billion loan portfolio** (focused on commercial, industrial, and real estate lending) aligns well with BMO's existing strengths, creating a **stronger pipeline for corporate banking revenues**.
- Bank of the West's private banking and investment services strengthen BMO's **wealth management segment**, which generates **35% of its total revenue**.

Strategic Rationale

U.S. Presence

BMO

BANK OF THE WEST

- The **$16.3 billion acquisition** of Bank of the West marks BMO's **largest expansion into the U.S. market**, significantly increasing its customer base and geographic reach.
- The deal expanded BMO's branch network by **514 locations**, giving it a **direct presence in 32 states**, with a **dominant market share in California**, one of the most lucrative banking markets in the U.S
- BMO's U.S. commercial banking division saw a **57% growth in deposits**, boosting its ability to fund large-scale corporate lending activities.

Considerations

1. Operating under stricter U.S. regulations may increase compliance expenses by **$200-$300 million annually**.

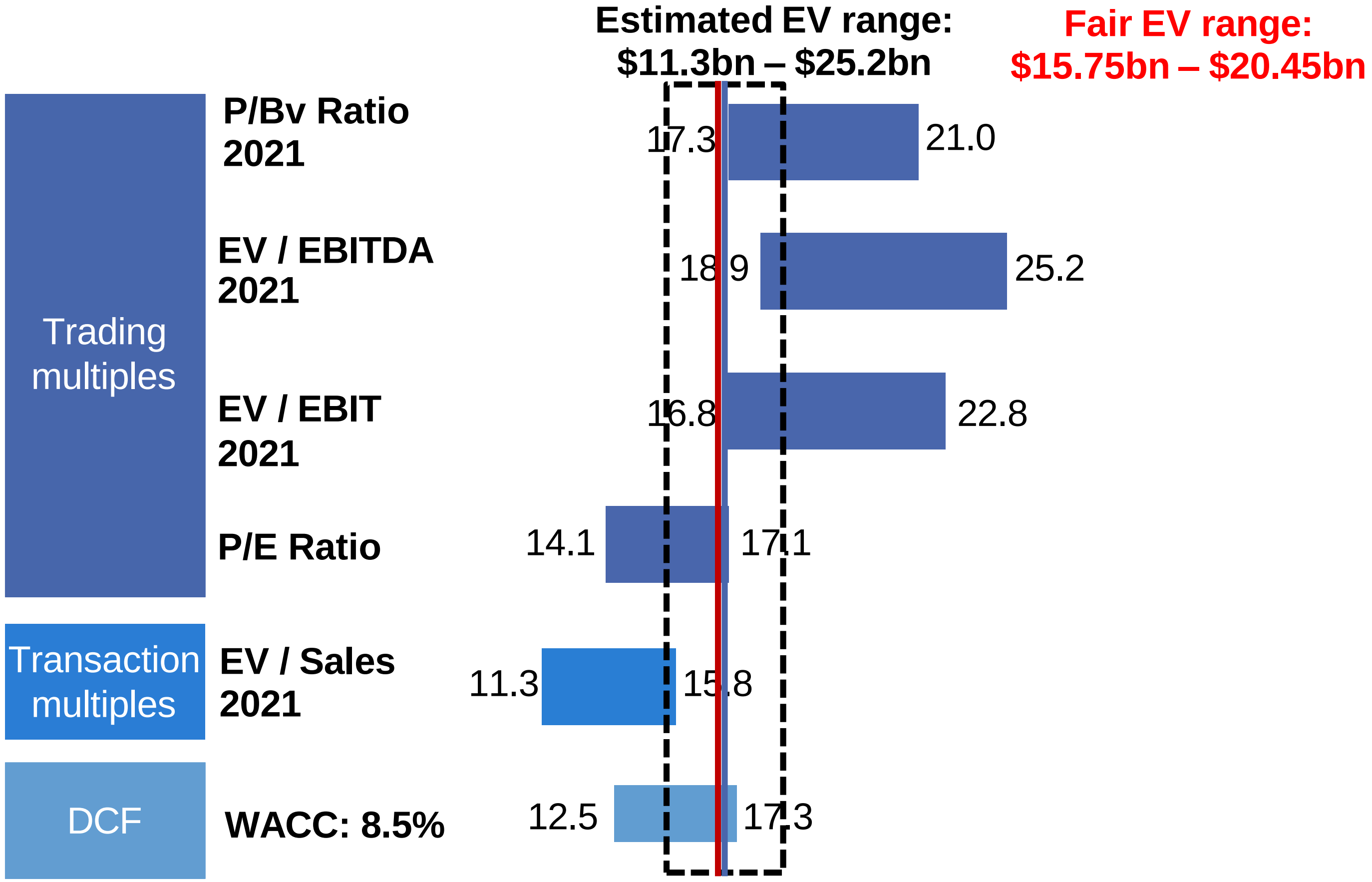
2. Bank of the West has **$20 billion in real estate loans**, with potential risks due to interest rate fluctuations and economic downturns.

Valuation & Enterprise Value

The fair enterprise value of Bank of the West is estimated to be in the range of **$15.75bn – $20.45bn**, aligning closely with the actual acquisition price of **$16.3bn**.

Football field

Bank of the West Enterprise Value, in billion USD



Weight* / Implied multiples from valuation

	Weight*	Peer Multiples Low	Peer Multiples High	BMO Multiples Bank of the West
P/Bv Ratio 2021	25%	1.5x	1.9x	1.6x
EV / EBITDA 2021	20%	10.5x	14.3x	12.8x
EV / EBIT 2021	15%	14.0x	19.0x	17.5x
P/E Ratio	15%	12.5x	16.0x	14.3x
EV / Sales 2021	10%	2.5x	3.5x	3.2x
WACC: 8.5%	15%			

BMO Financial Group announced the **$16.3 billion all-cash acquisition** of **Bank of the West** from **BNP Paribas** on **December 20, 2021**. The deal, which closed on **February 1, 2023**, was valued at approximately **1.5x tangible book value (TBV)**, aligning with historical banking M&A multiples

Note: *: P/BV (25%) and EV/EBITDA (20%) were given the highest weight due to their relevance in banking acquisitions, showcasing asset value and profitability.

Source: BMO Financial Group Press Release, BMO's 2023 Annual Report, Wilary Winn White Paper

Risk & Threat Assessment

The acquisition of Bank of the West presents macroeconomic, regulatory, operational, and competitive risks, which could impact BMO's financial performance and integration success.

	Description	Areas of concern following the Bank of West acquisition	Threat assessment	*Threat level*	Overall threat
Valuation Risk	• The valuation of **$16.3 billion** for Bank of the West was based on expected **cost synergies of $800M annually** and growth in **BMO's U.S. footprint**.	• **Overestimation of future profitability** • Goodwill & Asset Impairment • Macroeconomic Conditions	• Valuation Overstatement (**impact $2.5bn - $4.0bn**) • Revenue Miss & Goodwill Impairment (**impact $1.5bn - $3.0bn**) • Macroeconomic Uncertainty	Low Medium Low	
Operational Risk	• Merging two banks of different sizes and operational structures presents risks. Integration failures have been a major cause of post-M&A underperformance in the banking sector.	• Disruptions in IT and digital banking services can result in **customer dissatisfaction and regulatory penalties**. • Operational Efficiency Loss	• **IT & Tech Integration Failure** • Operational Inefficiencies, inconsistent lending policies • Loss of key talent and employee attrition	High Medium Medium	
Regulatory & Compliance Risk	• Banking mergers are **heavily scrutinized by financial regulators**, particularly in the U.S., where consolidation can **raise anti-competition concerns.**	• Regulatory Approval Delays • Capital Adequacy Requirements • Compliance with **GDPR, CCPA, and U.S. banking data protection laws**	• Regulatory delays and fines • Capital Adequacy compliance cost (**Tier 1 capital ratio** above 10.5% to meet Basel III guidelines.) • Data Privacy Breach Risk	Low Low Medium	
Market Risk	• BMO's expansion into the U.S. increases **competition risk** as it faces dominant players like **JPMorgan Chase, Wells Fargo, and Bank of America**.	• If high-value clients leave, BMO may struggle to achieve **expected revenue synergies**. • U.S. banks have established brand recognition, making **customer acquisition difficult**.	• Customer Attrition & Revenue loss • Competitive Pressure and loan pricing strategies • Interest rate impact on lending demand, Fed rate hikes could impact **loan demand** and profitability.	Medium High Medium	

Low threat High threat

Post-Acquisition Strategy

BMO's post-acquisition strategy focuses on **cost synergies, revenue expansion, and digital transformation**, driving improvements in **EPS, ROE, and Cost-to-Income ratios**.

A. Cost Synergies & Operational Efficiency (Target: $800M in annual cost synergies by Year 3)

Branch Consolidation:

~200+ overlapping branches to be closed or merged, reducing **operational costs by 15%**.

Back-Office Optimization:

25% reduction in redundant corporate functions (HR, IT, Risk, Compliance).

IT System Integration:

Migration to **BMO's digital banking infrastructure** to streamline operations and reduce maintenance costs by **$200M annually**.

📌 **Financial Impact:**

1. Expected **cost-to-income ratio to improve from 58.6% → 52.0%** post-integration.
2. EPS accretion of **10-12% in Year 1**, with full synergies by **Year 3**.
3. **Efficiency Ratio Improvement:** 59.3% → **56.0%**

C. Enhancing Revenue Synergies & Growth (Improves P/E, ROE, NIM)

Loan Book Expansion:

Grow SME and mortgage lending by **8% YoY**, adding **$50B in new loans** by 2026.

Wealth Management Cross-Selling:
Monetize **$105B in deposits**, boosting fee-based revenue by **$500M annually**.

Commercial Lending Market Share:

Expand in **California, Texas, and Florida**, increasing loan origination fees by **$250M annually**.

📌 **Financial Impact:**

1. **Net Interest Margin (NIM) Growth:** 2.75% → **3.1%**
2. **Loan-to-Deposit Ratio:** 89.4% → **85.0% (Optimized for liquidity)**
3. **Revenue Synergies Contribution to EPS Growth:** +6% by Year 3

B. Digital Transformation & Operational Efficiency (Improves Cost-to-Income, ROE, P/E)

Target: 70% Digital Banking Adoption by 2026

- **AI-Driven Credit Scoring:** Reduce loan default rates by **10%**, improving risk-adjusted returns.
- **Cloud-Based Banking Migration:** Save **$250M annually** by eliminating on-premise IT costs.
- **Expanding Digital-Only Banking:** Capture **2M+ new customers** in underpenetrated markets, driving **$500M in annual digital revenue**.

D. Capital Optimization & Multiple Expansion (Improves P/BV, CET1 Ratio, ROA)

Target: Maintain CET1 at 11.5%+ and Strengthen Asset Quality

- **Divesting Low-Yielding Assets:** Offload **$5B in underperforming loan portfolios**, improving ROA by **0.25%**.
- **Tier-2 Capital Raise:** Issue **$2B in bonds** to maintain a strong capital buffer and reduce equity dilution.
- **Optimizing Deposit Mix:** Shift **15% of deposits** to lower-cost commercial accounts, reducing funding costs by **$100M annually**.