# BMO Financial Group

# Q2 2023 Conference Call

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### Caution Regarding Forward-Looking Statements

Bank of Montreal's public communications often include written or oral forward-looking statements. Statements of this type are included in this document and may be included in other filings with Canadian securities regulators or the U.S. Securities and Exchange Commission, or in other communications. All such statements are made pursuant to the "safe harbor" provisions of, and are intended to be forward-looking statements under, the United States Private Securities Litigation Reform Act of 1995 and any applicable Canadian securities legislation. Forward-looking statements in this document may include, but are not limited to, statements with respect to our objectives and priorities for fiscal 2023 and beyond, our strategies or future actions, our targets and commitments (including with respect to net zero emissions), expectations for our financial condition, capital position or share price, the regulatory environment in which we operate, the results of, or outlook for, our operations or for the Canadian, U.S. and international economies, the closing of our proposed acquisition of Bank of the West, including plans for the combined operations of BMO and Bank of the West and the financial, operational and capital impacts of the transaction, customer growth and support, sustainable lending and underwriting targets, net zero financed emissions targets, reducing operational greenhouse-gas (GHG) emissions and inclusivity and diversity, and include statements made by our management. Forward-looking statements are typically identified by words such as "will", "would", "should", "believe", "expect", "anticipate", "project", "intend", "estimate", "plan", "goal", "commit", "ambition", "aim to", "target", "may", "might", "schedule", "forecast", "outlook", "timeline", "suggest", "seek" and "could" or negative or grammatical variations thereof.

By their nature, forward-looking statements require us to make assumptions and are subject to inherent risks and uncertainties, both general and specific in nature. There is significant risk that predictions, forecasts, conclusions or projections will not prove to be accurate, that our assumptions may not be correct, and that actual results may differ materially from such predictions, forecasts, conclusions, projections, targets, commitments, ambitions, plans or goals. We caution readers of this document not to place undue reliance on our forward-looking statements, as a number of factors – many of which are beyond our control and the effects of which can be difficult to predict – could cause actual future results, conditions, actions or events to differ materially from the targets, expectations, estimates or intentions expressed in the forward-looking statements.

The future outcomes that relate to forward-looking statements may be influenced by many factors, including, but not limited to: general economic and market conditions in the countries in which we operate, including labour challenges; the severity, duration and spread of the COVID-19 pandemic, and possibly other outbreaks of disease or illness, and their impact on local, national or international economies, as well as their heightening of certain risks that may affect our future results; information, privacy and cybersecurity, including the threat of data breaches, hacking, identity theft and corporate espionage, as well as the possibility of denial of service resulting from efforts targeted at causing system failure and service disruption; benchmark interest rate reforms; technological changes and technology resiliency; political conditions, including changes relating to, or affecting, economic or trade matters; climate change and other environmental and social risk; the Canadian housing market and consumer leverage; inflationary pressures; global supply-chain disruptions; changes in monetary, fiscal, or economic policy; changes in laws, including tax legislation and interpretation, or in supervisory expectations or requirements, including capital, interest rate and liquidity requirements and guidance, and the effect of such changes on funding costs; weak, volatile or illiquid capital or credit markets; the level of competition in the geographic and business areas in which we operate; exposure to, and the resolution of, significant litigation or regulatory matters, our ability to successfully appeal adverse outcomes of such matters and the timing, determination and recovery of amounts related to such matters; the accuracy and completeness of the information we obtain with respect to our customers and counterparties; failure of third parties to comply with their obligations to us; our ability to execute our strategic plans, complete proposed acquisitions or dispositions and integrate acquisitions, including obtaining regulatory approvals; critical accounting estimates and judgments, and the effects of changes to accounting standards, rules and interpretations on these estimates; operational and infrastructure risks, including with respect to reliance on third parties; the possibility that our proposed acquisitions, including our acquisition of Bank of the West, do not close when expected, or at all, because required regulatory approvals and other conditions to closing are not received or satisfied on a timely basis, or at all, or are received subject to adverse conditions or requirements; the anticipated benefits from proposed acquisitions, including Bank of the West, such as potential synergies and operational efficiencies, are not realized; our ability to manage exposure to capital arising from changes in fair value of assets and liabilities between signing and closing; our ability to perform effective fair value management actions and unforeseen consequences arising from such actions; changes to our credit ratings; global capital markets activities; the possible effects on our business of war or terrorist activities; natural disasters and disruptions to public infrastructure, such as transportation, communications, power or water supply; in respect of sustainability matters, availability of comprehensive and high-quality GHG data, the evolution of our lending portfolios over time, the need for active and continued participation of stakeholders (including enterprises, financial institutions and governmental and non-governmental organizations), the development and deployment of new technologies and industry-specific solutions, international cooperation, the development of regulations internationally, our ability to successfully implement various initiatives under expected time frames, the compliance of various third parties with our policies and procedures and legal requirements and those other factors set out on page 17 of BMO's 2022 Annual Report; and our ability to anticipate and effectively manage risks arising from all of the foregoing factors. In addition, our climate risk analysis and net zero strategy remain under development, and the data underlying our analysis and strategy remain subject to evolution over time, and, as a result, we expect that certain disclosures made in this document are likely to be amended, updated or restated in the future as the quality and completeness of our data and methodologies continue to improve.

We caution that the foregoing list is not exhaustive of all possible factors. Other factors and risks could adversely affect our results. For more information, please refer to the discussion in the Risks That May Affect Future Results section, and the sections related to credit and counterparty, market, insurance, liquidity and funding, operational non-financial, legal and regulatory, strategic, environmental and social, and reputation risk, in the Enterprise-Wide Risk Management section of BMO's 2022 Annual Report, as updated by quarterly reports, all of which outline certain key factors and risks that may affect our future results. Investors and others should carefully consider these factors and risks, as well as other uncertainties and potential events, and the inherent uncertainty of forward-looking statements. We do not undertake to update any forward-looking statements, whether written or oral, that may be made from time to time by the organization or on its behalf, except as required by law. The forward-looking information contained in this document is presented for the purpose of assisting shareholders and analysts in understanding our financial position as at and for the periods ended on the dates presented, as well as our strategic priorities and objectives, and may not be appropriate for other purposes.

Material economic assumptions underlying the forward-looking statements contained in this document include those set out in the Economic Developments and Outlook section of BMO's 2022 Annual Report, as updated by quarterly reports, as well as in the Allowance for Credit Losses section of BMO's 2022 Annual Report, as updated by quarterly reports. Assumptions about the performance of the Canadian and U.S. economies, as well as overall market conditions and their combined effect on our business, are material factors we consider when determining our strategic priorities, objectives and expectations for our business. Assumptions about Bank of the West's balance sheet, product mix and margins, and interest rate sensitivity were material factors we considered in estimating the fair value and goodwill and intangibles amounts at closing, and assumptions about our integration plan, the efficiency and duration of integration and the alignment of organizational responsibilities were material factors we considered in estimating pre-tax cost synergies. In determining our expectations for economic growth, we primarily consider historical economic data, past relationships between economic and financial variables, changes in government policies, and the risks to the domestic and global economy.


### Non-GAAP Measures and Other Financial Measures

Results and measures in this document are presented on a GAAP basis. Unless otherwise indicated, all amounts are in Canadian dollars and have been derived from our audited annual consolidated financial statements prepared in accordance with International Financial Reporting Standards (IFRS). References to GAAP mean IFRS. We use a number of financial measures to assess our performance, as well as the performance of our operating segments, including amounts, measures and ratios that are presented on a non-GAAP basis. We believe that these non-GAAP amounts, measures and ratios, read together with our GAAP results, provide readers with a better understanding of how management assesses results.

Management considers both reported and adjusted results and measures to be useful in assessing underlying ongoing business performance. Adjusted results and measures remove certain specified items from revenue, non-interest expense and income taxes, as detailed on slide 37. Adjusted results and measures presented in this document are non-GAAP. Presenting results on both a reported basis and an adjusted basis permits readers to assess the impact of certain items on results for the periods presented, and to better assess results excluding those items that may not be reflective of ongoing business performance. As such, the presentation may facilitate readers' analysis of trends. Except as otherwise noted, management's discussion of changes in reported results in this document applies equally to changes in the corresponding adjusted results.

Non-GAAP amounts, measures and ratios do not have standardized meanings under GAAP. They are unlikely to be comparable to similar measures presented by other companies and should not be viewed in isolation from, or as a substitute for, GAAP result.

Examples of non-GAAP amounts, measures or ratios include: efficiency and leverage ratios calculated using revenue presented net of CCPB; revenue and other measures presented on a taxable equivalent basis (teb); pre-provision pre-tax income; amounts presented net of applicable taxes; adjusted net income, revenues, non-interest expenses, earnings per share, effective tax rate, ROE, efficiency ratio, and other adjusted measures which exclude the impact of certain items such as acquisition and integration costs, amortization of acquisition-related intangible assets, impact of divestitures, restructuring costs and management of fair value changes on the purchase of Bank of the West. Bank of Montreal provides supplemental information on combined operating segments to facilitate comparisons to peers.

Certain information contained in BMO's Management's Discussion and Analysis dated May 24, 2023 for the fiscal quarter ended April 30, 2023 ("Second Quarter 2023 MD&A") is incorporated by reference into this document. Quantitative reconciliations of non-GAAP and other financial measures to the most directly comparable financial measures in BMO's financial statements for the period ended April 30, 2023, an explanation of how non-GAAP and other financial measures provide useful information to investors and any additional purposes for which management uses such measures, can be found in the Non-GAAP and Other Financial Measures section of the Second Quarter 2023 MD&A. Further information regarding the composition of our non-GAAP and other financial measures is provided in the "Glossary of Financial Terms" section of the Second Quarter 2023 MD&A. The Second Quarter 2023 MD&A is available on SEDAR at www.sedar.com and on our website at www.bmo.com/investorrelations.

**PRESENTATION**

**Christine Viau –** *Bank of Montreal – Head of Investor Relations*

Thank you and good morning. We will begin today's call with remarks from Darryl White, BMO's CEO, followed by Tayfun Tuzun, our Chief Financial Officer and Piyush Agrawal, our Chief Risk Officer. Also present to take questions today are Ernie Johannson, Head of BMO North American Personal & Business Banking; Nadim Hirji, Head of BMO Commercial Banking; Dan Barclay, Head of BMO Capital Markets; Deland Kamanga, Head of BMO Wealth Management and Dave Casper, BMO U.S. CEO.

As noted on slide 2, forward-looking statements may be made during this call, which involve assumptions that have inherent risks and uncertainties. Actual results could differ materially from these statements. I would also remind listeners that the bank uses non-GAAP financial measures to arrive at adjusted results. Management measures performance on a reported and adjusted basis and considers both to be useful in assessing underlying business performance. Darryl and Tayfun will be referring to adjusted results in their remarks unless otherwise noted as reported. I will now turn the call over to Darryl.

**Darryl White** – *Bank of Montreal – CEO*

Thank you, Christine and good morning, everyone.

I'd like to begin by acknowledging the hardship faced by our communities in Alberta impacted by the devastating wildfires that threaten their homes and livelihoods. We're committed to standing alongside our clients and doing our part to make sure that they get the help that they need.

I'd also like to welcome Nadim Hirji, Group Head, BMO Commercial Banking, who's joining the call for the first time. Nadim has a long track record of serving our clients, including leadership positions in risk management and commercial banking, where most recently, he was Co-Head of the Canadian Commercial Bank.

Now let me turn to the quarter.

Against the backdrop of a shifting environment, BMO delivered solid performance, including the benefit of a full quarter of results from Bank of the West. Earnings per share were $2.93 and net income was $2.2 billion for the quarter and $4.5 billion year-to-date.

Second quarter pre-provision pre-tax earnings were up 7% year-over-year and grew [to] $6.2 billion year-to-date.

Our performance reflects the continued strength of our highly-diversified business mix with good PPPT growth in our Canadian and U.S. personal and commercial banking businesses, up 8% and 29% year-to-date, respectively, while our wealth and capital markets businesses were impacted by weaker markets and lower client activity.

While credit trends are beginning to normalize from historically low levels as expected, credit performance remains strong across our portfolios, reflecting our long-standing track record of superior risk management, a culture that is shared by our Bank of the West colleagues.

Our CET1 ratio of 12.2% remains very strong even after closing the largest acquisition in Canadian [banking] history.

ROE for the quarter was 12.6%, while return on tangible common equity improved to 17.2%. We also announced a dividend increase of 4 cents, up 6% from last year to $1.47 per share.

Since we spoke last quarter, the impact of persistent inflation, rising rates, a slowing global economy, and increasing deposit competition on the industry has accelerated. We're not immune to these market forces, which are putting pressure on revenue growth and near-term operating leverage. After delivering five consecutive years of positive operating leverage, these factors, along with the higher efficiency Bank of the West brings pre-synergies, are now expected to result in negative operating leverage this year.

We're focused on resetting our expense outlook in line with the revenue headwinds to regain positive operating leverage and continue the improvement in our efficiency ratio. Tayfun will elaborate on this in his remarks. Our commitment to positive operating leverage through time remains firm even in this environment.

The last few months have reinforced the importance of a strong foundation and the trust built over time with our stakeholders. Our bank is highly diversified by customer, sector and geography and we fortified our balance sheet and significantly expanded our customer deposit base with Bank of the West.

Liquidity, funding and capital are well-managed and ratios are strong, well above both regulatory requirements and internal targets.

The strength and stability of our bank, that has delivered resilient performance through economic cycles, is being noticed.

We have a differentiated position in the U.S. market that has been enhanced with the Bank of the West. As a high-performing national U.S. bank, we rank in the top 10 of diversified banks with assets over US$250 billion. Our combined U.S. segment has over US$400 billion in assets and offers customers a full range of integrated banking, wealth and capital markets products and services with presence in leading markets and digital platforms that extend nationally.

Our clients further benefit from the strength of BMO's $1.25 trillion North American balance sheet investment capacity and the stability of a Canadian bank. We're advantageously positioned within a small number of large banks in the U.S. that have sufficient size, scale and a full range of capabilities, including our premium top five North American commercial banking franchise, a one-client approach and a North-South business model unlike any other bank.

We believe that this will contribute to outsized gains in customer and deposit acquisition as customers seek to partner with banks who are willing and able to support them through the cycle. Since the market disruption in early March, leveraging our leading North American treasury and payment solutions and enhanced digital onboarding capabilities, we opened several thousand new commercial deposit accounts and continued to add retail customers across our expanded U.S. footprint.

Our U.S. segment has been a key contributor to our growth and success over time with a long track record of combining organic growth with successful acquisitions. The contribution of Bank of the West to BMO's performance is in line with our expectations, adding 10% to BMO's pre-provision pre-tax earnings in the first quarter, and we are on track to increase that contribution as our run rate, expense and revenue synergies come through.

We're well prepared and on track to convert systems and branding over the Labour Day weekend. I remain confident that by the end of 2025, the Bank of the West acquisition will add over US$2 billion in run rate pre-provision pre-tax earnings, as I discussed with you last quarter.

This quarter, we also continued to make progress on our strategic priorities: to continue building a digitally enabled bank, enhancing customer loyalty and being our clients' lead partner in the climate transition, benefiting from the investments we've made in technology, marketing and sales force expansion.

We continue to support newcomers to Canada, launching industry-leading digital pre-arrival account opening capabilities through our expanded NewStart program. The combination of digital transformation and helping customers make real financial progress was recognized by Celent with two Model Bank awards.

Earlier this month, we announced the approval of our acquisition of the Air Miles reward program, an opportunity to reinvigorate one of Canada's largest and most celebrated loyalty programs.

We're helping customers address the challenges of climate change through thought leadership, such as our participation in the UN-convened Nature Target-setting working group, as well as the launch of our Greener Future Financing program to help agriculture businesses build future-ready, climate-resilient operations.

In BMO Wealth Management, even in a challenging market environment, our focus on client advice and product innovation is bringing net new clients and assets to BMO, including our continued leadership in ETF flows and improved mutual fund market share.

BMO Capital Markets continued to perform well despite muted client activity with record results in M&A and in our digital and liquid trading businesses, reflecting the benefits of our diversified business model.

All that we do is guided by our Purpose to boldly grow the good in business and life and underpinned by our core values. We continue to be acknowledged for our ethical business practices, recognized for the sixth consecutive year as one of the World's Most Ethical Companies by Ethisphere, the only bank in Canada to receive this award since its inception in 2007.

Our resilient and tested strategy is designed to deliver sustained performance through the cycle. As we move towards finalizing the integration of Bank of the West, we're equally focused on continuing to drive performance in all of our businesses and are uniquely situated to offer integrated North American banking, wealth and capital markets products and leading digital experiences that differentiate us from our competitors and drive long-term value for our shareholders.

I'll now turn it over to Tayfun.

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**Tayfun Tuzun** – *Bank of Montreal – CFO*

Thank you, Darryl. Good morning and thank you for joining us.

My comments will start on slide 10. Second quarter reported EPS was $1.30 and net income was $1.1 billion.

Adjusting items are shown on slide 40 and include Bank of the West acquisition-related impacts for the initial provision for credit losses on performing loans and integration costs, which decreased net income by $517 million and $545 million, respectively. The remainder of my comments will focus on adjusted results.

Adjusted EPS was $2.93 and net income was $2.2 billion, up 1% from last year, including a $230 million contribution from Bank of the West. Excluding the addition of Bank of the West, net income declined due to higher PCLs. Revenue increased 3% and PPPT declined 4%, reflecting good growth in net interest income from our P&C businesses, offset by weaker results in Wealth and Capital Markets due to continued muted market environment.

Total PCL was $318 million, including a $75 million provision for performing loans, compared with a total provision of $50 million in the prior year.

Piyush will speak to these in his remarks.

Turning to slide 11. The acquisition of Bank of the West contributed $230 million to net income, $1.1 billion to revenue and $755 million to expenses. Results this quarter have come in-line with our internal expectations.

On closing, we recognized purchase accounting fair value marks on Bank of the West's loans and deposits and discounts on securities on our balance sheet, which accretes to net interest income.

As previously disclosed, to manage the exposure to the impact of higher interest rates on capital from changes in the fair value of the assets and liabilities of Bank of the West between the announcement and closing of the acquisition, we entered into interest rate swaps that resulted in cumulative mark-to-market gains of $5.7 billion. These swaps were largely offset from an interest rate risk perspective through the purchase of a portfolio of matched duration U.S. treasuries and other balance sheet instruments. On closing, the swaps were unwound and replaced with hedges which, in effect, crystallized the unrealized loss position on our balance sheet. The amortization of the fair value hedge is reflected as interest expense.

The net impact of these two items increased Bank of the West net interest income in the quarter by $103 million and was recorded in Corporate Services. Going forward, we expect this discrete benefit to reduce as the legacy of Bank of the West securities portfolio is managed within the overall bank and replaced within our underlying earnings.

Plans remain on track to complete systems conversion and brand unification on Labour Day weekend. We remain confident in achieving the previously announced US$670 million expense synergies to be fully executed by the start of the second quarter in 2024, the same timeline that we guided to at announcement. Overall, we are very pleased with what we have seen during the first quarter post-closing and excited about our opportunities associated with our expanded U.S. presence.

Moving to the balance sheet on Slide 12, average loan growth was 28% year-over-year and 14% quarter-over-quarter. Bank of the West added $79 billion to loan balances in the current quarter.

On a constant currency basis, underlying Business and Government loans increased 11% from the prior year with good growth across all operating groups and Consumer loans increased 8% reflecting diversified growth in Canadian P&C and Wealth.

Average customer deposits increased 25% year-over-year and 16% sequentially, including $86 billion from Bank of the West. On an underlying basis, deposits were up 8% year-over-year and flat quarter-over-quarter.

On slide 13, we provide a view of deposit trends in our Canadian and U.S. P&C and Wealth businesses.

In Canada, strong balance sheet growth continues, which reflects our continued success in capturing market share in our Personal and Business Banking business. Within retail deposits, we do see ongoing migration to term deposits as customers seek higher returns given the significant rise in interest rates.

In the U.S., our underlying deposit levels remain well diversified and above pre-pandemic levels. Although we are not immune to the impact of quantitative tightening and rate competition from money market funds on bank deposits, BMO's size and stability continues to be an attractive offer for our clients. Our digital deposit platform in Personal Banking is now supported with a larger retail branch base as a result of the Bank of the West acquisition and our advanced Treasury Management platform capabilities position us well in this environment. We expect to see a return to sequential growth in the second half of the year as we continue to optimize our pricing strategy balancing growth and returns.

Turning to Slide 14, on an ex-trading basis, net interest income was up 36% and net interest margin was up 15 basis points from prior year driven by the Bank of the West, strong balance sheet growth and margin expansion in the underlying businesses. Year-over-year growth was partly offset by the impact of risk transfer transactions and higher low-yielding assets for liquidity purposes.

Net interest margin was up nine basis points from last quarter. The acquisition and net purchase accounting accretion benefit added 15 basis points and four basis points, respectively, while Corporate Services reduced the margin by eight basis points, mostly due to lower earnings on equity held in advance of closing the acquisition.

In Canadian P&C, NIM remained stable as higher loan margins were offset by lower deposit spreads and the changing deposit mix reflecting continued flows into term deposits. In U.S. P&C, margins widened by four basis points sequentially due to a five-basis-point benefit from Bank of the West as well as wider loan margins and other favourable impacts in the quarter, partially offset by lower deposit margins reflecting competitive pricing.

With the transitory impacts of the pre- and post-close balance sheet movements behind us, which generated more quarterly volatility in our margin, especially in Corporate during the first two quarters of this year, we expect our margin to remain relatively stable during the second half of the year.

Moving to our interest rate sensitivity on slide 15, rate sensitivity for the quarter has decreased quarter-over-quarter with the addition of Bank of the West's longer-duration assets and reduction of short-term liquidity balances that we held in preparation for the acquisition close. Our risk metrics now reflect a relatively neutral position consistent with our strategy, and we believe that we are well-positioned for the current environment.

Moving to slide 16, excluding the impact of Bank of the West and the stronger U.S. dollar, expenses increased 6% from last year, driven by the follow-through impact of targeted investments last year, including salesforce expansion, technology and marketing as well as inflation. In addition, we incurred certain one-time expenses during the quarter, including legal provisions and severance, which added approximately $80 million or 2% to our expense growth. Sequentially, expenses declined 5% due to the impact of seasonal items in the first quarter and fewer days in the current quarter.

The impact of the acquisition and slower revenue growth have resulted in negative operating leverage for the quarter and year-to-date. We expect that expense growth will continue to moderate and operating leverage and efficiency will improve in the second half of the year as most of the follow-through impact of last year’s expense increases are behind us.

While weakness in the revenue environment may persist in the near term, we have identified additional discrete expense management actions focusing on the entire expense base with a targeted reduction in our efficiency ratio. Dynamic expense management, positive operating leverage and improving our relative efficiency ratio continues to be management's priority focus. These actions, in addition to our confidence in meeting the targeted cost synergies at Bank of the West, are expected to result in meaningful positive operating leverage in 2024.

Our capital position remains very strong with a Common Equity Tier 1 Ratio of 12.2%. The Bank of the West acquisition reduced the ratio by 680 basis points, partially offset by internal capital generation, shares issued under the dividend reinvestment plan and the benefit from the implementation of the first phase of Basel III reforms this quarter. Lower source currency RWA primarily reflected the elimination of the capital floor in the quarter.

Our current capital position, which now exceeds our pre-COVID level after closing the largest bank acquisition in our history, complements the strength of our balance sheet and gives us a distinct competitive advantage. We remain confident that our CET1 ratio will remain above 12% for the remainder of the fiscal year.

Moving to the operating groups and starting on slide 18, Canadian P&C delivered net income of $864 million, down 8% from the prior year due to higher provision for credit losses with strong pre-provision pre-tax earnings growth of 7%. Revenue was up 7% from the prior year. Net interest income increased 12% reflecting strong balance growth and higher margins. Expenses were up 6% reflecting investment in the business, including salesforce expansion, technology and higher salaries and remained relatively flat quarter-over-quarter, in-line with the broader trends in our consolidated results.

Loans were up 10% with 9% growth in residential mortgage lending and 12% in commercial loans. Deposits increased 13% year-over-year and 3% sequentially across both retail and commercial businesses with strong growth in term deposits.

Moving to U.S. P&C on slide 19, my comments here will speak to the U.S. dollar performance. Net income was $638 million, up 37% due to the contribution from Bank of the West which added $163 million in the current quarter. Underlying results were up 2%, driven by pre-provision pre-tax earnings growth of 11%, partially offset by higher provisions for credit losses compared with a recovery in the prior year.

Revenue was up 9%, excluding Bank of the West, reflecting a 14% increase in net interest income due to higher margins and loan balances, partly offset by a decline in non-interest revenue. Excluding Bank of the West, expenses increased 7% due to higher employee and operating costs, and were down 1% quarter-over-quarter.

On the balance sheet, Bank of the West added $55 billion to both loans and deposits. Underlying loans grew 3% from the prior year and declined 3% quarter-over-quarter, primarily in Commercial. Underlying deposits declined 5% year-over-year and 2% sequentially.

Moving to slide 20, BMO Wealth Management net income was $285 million, down from $315 million last year. The Bank of the West added $26 million in the current quarter. Wealth and Asset Management net income was $222 million compared with $248 million in the prior year. Contributions from Bank of the West and growth in net interest income and new client assets were more than offset by weaker global markets, lower online brokerage transactions and higher expenses. Insurance net income was $63 million compared with $67 million in the prior year. Excluding Bank of the West, expenses were up 6% mainly due to the impact of investments made in the business last year, and down 2% quarter-over-quarter.

BMO Capital Markets net income was $388 million compared to $453 million in the prior year. Revenues in Global Markets remained relatively flat as higher foreign exchange and equities trading revenue were offset by lower issuance activity and interest rate trading revenue.

Revenues in Investment and Corporate Banking were up 2%, mainly due to higher corporate banking revenues and advisory fees, partly offset by lower underwriting activity. Expenses were up 14%, including the impact of the stronger U.S. dollar, higher technology costs and a legal provision, and down 3% quarter-over-quarter.

Turning now to slide 22, Corporate Services net loss was $187 million compared with $111 million in the prior year. The current quarter reflects lower earnings on the investment of excess capital that is now being deployed in the business, partially offset by the net accretion of purchase accounting fair value marks. Per my comments earlier on the impact of pre- and post-closing activities, Corporate can experience some variability following an acquisition of this size, which resulted in higher net losses over the last two quarters compared with our normal range. We expect Corporate to normalize in the second half of the year.

To conclude, our operating performance this quarter reflects the benefits of our diversified business that is now operating at a larger scale with a strong balance sheet and expanded growth opportunities in North America. With the benefit of a $1.3 trillion balance sheet, the strength of our capital position and the scope of our diversified businesses, we are very well positioned in the current evolution of the banking industry that favours scale participants. While we will always focus on long-term growth strategies, we are not losing sight of the need to align our operating performance with our long-term commitment to positive operating leverage.

I will now turn it over to Piyush.

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**Piyush Agrawal** – *Bank of Montreal – CRO*

Thank you, Tayfun, and good morning, everyone. Our risk performance continued to reflect strong risk management discipline across the bank this quarter despite market volatility and economic headwinds.

Starting on Slide 25, the total provision for credit losses was $1 billion, including the initial performing allowance of $705 million related to the Bank of the West purchased portfolio. Adjusting for this one-time charge, total PCL was $318 million or 20 basis points, up five basis points from prior quarter. Impaired provisions for the quarter were $243 million or 16 basis points, two basis points up from prior quarter, consistent with the expected trend to more normal loss rates.

Moving to slide 26, excluding the initial provision for Bank of the West, the $75 million provision for credit losses on performing loans for this quarter reflected portfolio credit migration, model changes and economic uncertainty, partially offset by a modest improvement in some macroeconomic variables over the forecast horizon. We remain comfortable that our $3.3 billion of performing loan allowances provides good loss coverage, over 4x coverage on trailing four quarters impaired losses and approximately 2x coverage against 2020 losses.

Turning to the impaired loan credit performance in the operating groups, Canadian Retail impaired loan losses were $163 million or 32 basis points, up from 26 basis points in Q1. In U.S. Retail, impaired loan losses were $41 million or 32 basis points, up from 24 basis points in the prior quarter. This PCL increase in Retail was due to continued normalization in both insolvencies and on delinquency rates in unsecured loans and credit cards.

For residential real estate secured lending, we continue to view the risk from higher rates as modest given our high credit quality borrower base and low LTVs. As you can see on slide 31, the riskier segment renewing over the next 12 months is nominal given our portfolio quality.

In our Commercial and Corporate businesses, we continue to see strong credit performance. In Canadian Commercial, impaired loan provisions were $10 million or

four basis points, down three basis points from the previous quarter. Our U.S. Commercial business had impaired loan provisions of $25 million or six basis points, down five basis points from the last quarter. Our Capital Markets business had very strong impaired loan results as well, with impaired losses of one basis point. The strong impaired performance in our Corporate and Commercial businesses remain below historical averages. And given the environment, we do expect Corporate and Commercial losses to normalize from these low levels.

On slide 27, bank-wide impaired formations at $843 million increased $322 million relative to Q1. The formations rate remains below our pre-pandemic experience. Gross impaired loan balance was $2.6 billion or 41 basis points, including an increase of $436 million related to the acquired Bank of the West portfolio. Although slightly up over the prior quarter, the gross impaired loan rate continues to be well below pre-pandemic levels.

As you see on slide 30, we are providing additional information on our commercial real estate portfolio given investor interest. Our portfolio is well-diversified across geographies and property types. Although the higher interest rates and office vacancies are headwinds for the sector, we have maintained consistent and disciplined underwriting standards and client selections throughout market cycles. The office subsegment exposure represents only 1% of our overall loan portfolio and is monitored closely. We have reviewed a large part of the portfolio on a deal basis and are comfortable with our exposure. Overall, our commercial real estate portfolio quality is strong. And while we have seen expected migration in the portfolio, impaired formations and losses continue to be modest and in line with expectations.

This was a significant quarter as we closed the Bank of the West acquisition. On slide 29, we provide an overview of the Bank of the West legacy portfolio, which further diversifies our portfolio across segments, sectors and U.S. regions. The Bank of the West portfolio fair valuation included a credit mark of $1.1 billion. The $705 million initial allowance provides additional provisioning on this portfolio.

Looking back at the quarter, we have seen both intended and unintended consequences from the pace of monetary policy tightening. The failure of some U.S. regional banks added to market volatility this quarter. While we continue to closely monitor, our risk management approach and strong liquidity position resulted in solid risk performance throughout the second quarter. As we look ahead, we are cautious about the economic environment. Together with the Bank of the West portfolio, we expect impaired loss rates to trend towards low- to mid-20 basis points. Given the quality of our portfolio, high allowance coverage and strong risk management capabilities, we are well-positioned to manage current and emerging risks.

I will now turn the call back to the operator for the Q&A portion of the call.

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**QUESTIONS AND ANSWERS**

**John Aiken** – *Barclays*

Not surprisingly, there's a lot of interest in the U.S. deposits and Tayfun, you did a great job in terms of demonstrating the flows. But I was wondering if we could have someone talk to the performance of Bank of the West-specific deposits during the quarter and then secondly, the performance of your digital deposit platform through the quarter, please?

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**Tayfun Tuzun** – *Bank of Montreal – CFO*

Let me just make a very brief comment, and then I'll turn it over to Ernie. John, I think we are obviously very excited about having the Bank of the West expanded branch network and the ability to connect our digital banking platform with their physical presence, and they're doing quite well. I think we had the opportunity to obviously work with them early after we closed and Ernie and her team are focusing on bringing their operations to the same targets that we have.

I'll turn it over to Ernie for her comments on how that's going.

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**Ernie Johannson –** *Group Head, N.A. Personal and Business Banking*

Thanks, Tayfun. Just a couple of comments on the legacy Bank of the West franchise. We did experience balances deteriorating largely due to some pricing and product choices that existed at that time. Remember, now they are not on our core platform. That will happen in September. But regardless of the fact that they’re not on our platform, we are able to adjust a few things in the franchise, and we were able to adjust some pricing, some product offerings, some campaigns, and marketing to be able to introduce some changes that are more effective for that marketplace, and in fact, I've seen very strong results as a result of those changes.

We've reduced the attrition rates, or migration out of various products, being able to support growth of dropping reductions by 30%, 40% because we've offered out different products at different price points. That's been continuing through March to April and even through the past few weeks as we continue to monitor that. We're impressed by the receptivity of the market and to the colleagues in the field that are able to present these offers to customers and be able to retain balances and grow at the same time.

Bank of the West represents about a 50% increase in the overall retail balances that we have in the U.S. and just a point back to the digital deposit taking, BMO standalone as a business or branch network performed very well over the past quarter, growing quarter-over-quarter and outperforming the market in terms of retaining balances.

We have not yet fully deployed our digital deposit-taking capabilities across the 50 states. We've done a slow ramp-up. We'll continue to ramp that up over the remaining quarters as necessary and that is proving to be very profitable and at the same time is driving balances into the franchise. More to come on that front, but I'm really encouraged to see what's possible in the Bank of the West franchise with partial capabilities that BMO brings in and it only gets strengthened as we move past September through the conversion time period. A good overall strategy in the U.S. between the 1,000 branches we now have and the digital capabilities. Hopefully, John, that answers part of your question.

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**Meny Grauman –** *Scotiabank Global Banking and Markets*

There is a lot of interest in the outlook for your U.S. business, broadly speaking, the U.S. P&C business. Is the U.S. still as attractive a market as it was when you first announced Bank of the West back in December ‘21? What's your perspective on that?

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**Darryl White –** *CEO*

Thanks for the question, Meny. My perspective is unambiguously yes. We play the long game, as you know. The U.S. is the largest and most profitable banking market on the planet. You have to make a decision, I suppose, in the first place, do you want to play there or not and if you do, our view is that if you have a meaningful presence and you execute against that as we have for the last several years, where you've seen us run a P&L that runs the same ROE and the same efficiency ratio in the U.S. as Canada, then you want to grow that. It will go through cycles and some cycles will be a little bit more difficult than others.

But my view is through time, and I think you're going to see it's going to get particularly exciting as we ramp up the next few quarters, the answer to your question is emphatically, yes. When I step back from it, Meny, let me tell you, if I were to clean sheet it, I would say, what would you want in terms of your positioning in the U.S. market? You'd want to operate at scale and so there, I'd refer you to page 6 of our presentation where we show that we're in a pretty unique category of participants in the industry structure, number one. Number two, you'd want to be in markets where business is good and you can grow and you're good at it, and we point out that we're in three of the five largest markets in the U.S. and 50 states digitally, and that is differentiated. I give you my word on that relative to most of our regional banking competitors.

Thirdly, ideally, you'd like it to be fully integrated into a bigger and broader North American business and balance sheet and that's what we bring. And so with the Bank of the West -- that's a general comment, I suppose, Meny. In particular, when we look at the comment I made to you last quarter when we had this conversation that the expectation is that we would deliver an incremental US$2 billion of PPPT by the end of 2025, it's as a result of all of those things as we combine those businesses. And so far, keep in mind, we've owned that business for 79 business days, [excluding] U.S. weekends and holidays and as I look out to fully synergizing the expenses by the end of only three quarters from now, first quarter of 2024, and then starting to build in the revenue synergies as we go through 2024 and 2025, I couldn't be more confident. I would say, I'm more confident today despite the environment. I'm more confident today than I was when we made the acquisition announcement.

**Meny Grauman –** *Scotiabank Global Banking and Markets*

Understood and just a follow-up, just on the regulatory side, which is definitely a concern for investors, it seems pretty reasonable that the Fed is going to have a regulatory response to the crisis that we've seen. I'm just wondering how you view those risks specifically for BMO? There's regulatory uncertainty, but do you have a sense of how impactful the regulatory blowback, if you want to call it that, will be on BMO?

**Darryl White –** *CEO*

Yes, I know what you're getting at, Meny. I would say as we've said to you, we are moving to a Category III bank in the U.S. I'd also take you back to the fact that we've said we were always built in the U.S. for more scale and more customer throughput and more assets, and that's what we've brought to it. Therefore, whatever regulatory implications there are with the current environment, I feel very confident that we're built to be able to handle them as they come. I don't think you're going to see a radical shock to our architecture in the U.S. at all. In fact, we think we're built for it in the first place.

**Meny Grauman –** *Scotiabank Global Banking and Markets*

Are there any regulatory changes that you're expecting?

**Darryl White –** *CEO*

None particularly, but it's always an evolving -- I mean I don't have any announcements to make on behalf of the Fed if that's what you're asking.

**Gabriel Dechaine –** *National Bank Financial*

I'd like to follow up with that line of questioning, I guess. I know you can't talk about future regulation; if you have any thoughts there, I'd love to hear them. But just the FDIC levies that were announced a couple of weeks ago, I get to about a US$250 million cumulative impact to BMO; was that in the ballpark? You're also saying you're moving to Category III and that you're already built for that; that would suggest that you don't need to build additional liquidity.

And then finally, on Bank of the West, I'm just looking at the total balance sheet, loans plus deposits, I net out the fair value marks on loans and deposits. I'm still coming, I guess, 4% to 5% below where you expected it to be at least in the Q1 slide deck. Is that in the ballpark? And if so, how does that affect your accretion outlook?

**Tayfun Tuzun** – *Bank of Montreal – CFO*

Gabriel, this is Tayfun. So a series of questions there. In terms of the impact of the proposed FDIC assessment, that's probably going to be closer to US$300 million. In terms of any expected changes on liquidity management related to new regulatory restrictions, we operate our balance sheet as a $1.3 billion balance sheet and our liquidity management approach is really not based on only our U.S. presence. I don't believe that there's going to be a significant change in the way we manage liquidity, whatever may come our way.

In terms of the transition from a Category IV bank to a Category III bank, there will be some investments mostly related to operational readiness because there's going to be a change in the frequency of data transfers and there's going to be a change in the way we track single counter-party credit exposures; those will require some operational investments, but we know what they are, and we are well prepared to do that.

In terms of the size of the Bank of the West balance sheet, most of that change occurred prior to closing day and what happened in 2022 is, as you know, Bank of the West had significant excess liquidity on their balance sheet with their transactional deposits. They had no wholesale funding supporting the asset side. They basically were focused on maintaining and growing their margin, and they were willing to let go some of the deposits. That really is what constitutes the difference between their previous numbers versus the closing day balances. But again, from our perspective, that is not a huge impact. We're basically looking at a similar type of expectations in terms of their overall performance and contribution to BMO. As Ernie articulated, we now obviously have a much different focus going forward in terms of growing both the deposit side of the balance sheet as well as the loan side of the balance sheet across all businesses.

**Doug Young –** *Desjardins Securities*

Just maybe to clarify on the Bank of the West versus last quarter and what we saw on page 39 and the deposit side, I kind of get. The loan side looks a little bit lower than what you kind of threw into the last quarter slide deck and so I'm just confused as to what the difference would be on the loan side.

**Tayfun Tuzun** – *Bank of Montreal – CFO*

So there is an impact on the mark, which is, I believe, a couple of billion dollars. And then in general, I would say there's really nothing unique or different about the loan side of the balance sheet, except that they're facing the same type of environment that we all are, a little bit of softer loan growth. Also, I would point out that transitions like these with large acquisitions, always tend to slow down new customer onboarding acquisition. They're going to be a little bit slow out of the gate, but we expect that activity, especially post-conversion on Labour Day to normalize from the current level. This is nothing unusual in terms of what we have been expecting.

**Doug Young** – *Desjardins Securities*

Okay. I guess that's what I was looking for. Tayfun, just on the hedge unwind and the impact, you walked through the details in your prepared remarks and so maybe I'm a little confused on this. I kind of get -- you get a negative hit from the unwind of the unrealized loss because you're kind of crystallizing that, but you're going to spread it over the period of time in which you flow through the marks. I thought that negative hit would be kind of closely matched with the loss -- or sorry, with the gain on the mark, but you're saying it's a net positive impact and it will...

**Tayfun Tuzun** – *Bank of Montreal – CFO*

Yes, it is -- it was a net positive this quarter. It will be net positive. It's probably going to get smaller and smaller as we go forward. And basically, what happened is the combination of the hedge position and unwinding those initial swaps, booking the gain against a higher amount of goodwill and then overlaying new swaps against the treasuries that we had, brought us back really to the Day 1 announcement accretion numbers. All that's left now for the next few years is for the net amount to accrete back. It's going to get smaller and smaller as the calendar moves forward.

**Doug Young** – *Desjardins Securities*

Can you remind me of the dollar figure you said; what was that dollar figure?

**Tayfun Tuzun** – *Bank of Montreal – CFO*

It was $103 million pre-tax this quarter.

**Doug Young** – *Desjardins Securities*

Pre-tax. Yes. Okay. When I think of the -- for Bank of the West, I think it was $317 million pre-tax pre-provision earnings from Bank of the West alone, that $103 million is embedded in that. Is that correct?

**Tayfun Tuzun** – *Bank of Montreal – CFO*

Yes.

**Doug Young** – *Desjardins Securities*

Okay and then just clarification lastly, I apologize for the number of questions here but negative operating leverage, sounds like that's what you expect in fiscal 2023, but I'm a little confused. Do you expect to show some positive movement towards positive operating leverage toward the back half of this year or is it just going to be negative and in that fiscal 2024 you're anticipating material positive operating leverage? Just want to get some clarification on how to think of it in the back half of this year.

**Tayfun Tuzun** – *Bank of Montreal – CFO*

Yes, so let me provide some clarification because with Bank of the West and without Bank of the West, these numbers tend to differ from each other. With Bank of the West in 2023, clearly, there is a larger negative operating leverage because of the dynamic of their expense base. And on a standalone basis, we still had negative operating leverage this quarter.

Overall, the expense trends actually are very much in line with what we expected coming to this year. We did actually say very early this year, we significantly curtailed headcount expansion. We changed the timing of some of our technology investments so we anticipated that on a quarter-over-quarter basis this year, we would see either flat or declining expenses, and that's what we exactly have seen in the first quarter. Now in the second quarter, quarter-over-quarter, our expenses have declined.

What you're seeing in our negative operating leverage numbers is really the follow-through impact of the expenses that we added to our base last year. Once we -- those are true, and they're going to be very shortly, we're going to be through them; our expense growth will decline towards low single digits and on a BMO stand-alone basis.

On top of it, you also now have the cost synergies that, especially towards the end of this year and to the first quarter of next year that are going to show up, which by itself has -- is going to create positive operating leverage. What we are now saying is, as we look at our expense base in a relatively weaker revenue environment, we also tend to make other expense decisions at BMO standalone in order to get back to our targeted efficiency ratio, which always was around 55%. We will continue to assess those. We'll make those decisions. Combined with the Bank of the West synergy pickup, these additional decisions that we are looking at we expect those to generate meaningful positive operating leverage in 2024.

**Scott Chan** – *Canaccord Genuity Corp.*

Maybe Tayfun just a couple of cleanup questions. I'm still going through it. But in terms of the Bank of the West contribution, they just hit your wealth management and U.S. P&C segment. Did that hit any other segment at all?

**Tayfun Tuzun** – *Bank of Montreal – CFO*

No, those are the two main points. And corporate obviously has some impact as well.

**Scott Chan –** *Canaccord Genuity Corp.*

Just on corporate, I noticed the preferred equity dividend shot up $95 million. In total, it was $127 million versus $38 million last quarter. Was that due to Bank of the West and how do we see that going forward?

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**Tayfun Tuzun –** *Bank of Montreal – CFO*

Yes, I think that really is dependent upon the frequency of the preferred dividend payments. Some of them are semi-annual, some of them had different frequency. We actually are happy to share with you the details as to, on a quarterly basis, what amount of preferred dividends we pay out. So we'll be able to give you the details for you to track that.

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**Scott Chan –** *Canaccord Genuity Corp.*

Yes, that would be super helpful; just knowing the nuances on every other quarter. Just lastly on capital – you talked about the first phase of the Basel III reforms this quarter. Looking out to future quarters, do you have visibility if there's going to be net -- or negative -- net positive or negative impact on further phases?

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**Tayfun Tuzun –** *Bank of Montreal – CFO*

The next important date is the first quarter of next year. That's when the trading rules will come in and then as you know, between now and the first quarter of 2026, the floor factor will go up by 2.5% every year. But the more important quarter of all for the next three years is probably going to be next year's first quarter, which is going to have a negative impact on capital and we will shortly share with you our assessment of what that may be once we conclude the work that's currently underway.

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**Paul Holden –** *CIBC Capital Markets*

A couple of questions for you. I guess, first, thanks for the additional detail on the CRE portfolio on slide 30. On that point, just hoping you can provide some more colour around the exposure in California, just given the focus in that market, maybe you can give us context of how much is office, how much might be more exposed to like San Francisco, L.A., sort of those regions that we're reading a whole lot about?

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**Piyush Agrawal –** *Bank of Montreal – CRO*

Sure. Thanks, Paul. We've given the CRE portfolio overall; I would say is that on page 30, you see 14% of our total CRE of $67 billion is in California.

We haven't broken down within that specifically office or other areas, but I would say you can take a general mix of the broader portfolio of what we have. However, when I step back, I would say that the strength of our CRE portfolio remains pretty strong.

Within that, we've got a deep dive across all of our large properties and exposures and the office for BMO is 1% of the total book. As you've seen in the disclosure, 10% of our CRE is office, which equates to 1%. We will, over time, obviously, provide more disclosure but I think the jump-off point of the strength of the relationships we've built over the last 20, 30 years, both at BMO as well as at Bank of the West, actually, positions us very well. And so again, we added some California with the Bank of the West portfolios but I feel very good about the quality. You can see that in our impairment book, there's a very normalized trend coming in and we're watching the news and tracking with our borrowers what's going on, so I wouldn't highlight any significant area of concern.

I would just also add that we've got the credit marks from the Bank of the West portfolio. We've got the opening provision so despite a very high provision coverage overall, we have a significantly higher coverage on commercial real estate that we've been carrying for the past few quarters.

Obviously, we'll track this. I think this is a topic which all of you and us are interested in given all of the news but where we are today, I feel very confident about the quality of our book.

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**Paul Holden –** *CIBC Capital Markets*

Got it. Okay. Second question is with respect to commercial and corporate loan growth. It would be great to hear an update on how you're viewing or what your growth appetite looks like right now. Hearing a lot about regional -- U.S. regional banks pulling back in terms of credit underwriting standards. Wondering if you're slowing growth intentionally or if you're seeing less demand in certain pockets, maybe just a broad update there on the U.S. and Canada would be helpful.

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**Piyush Agrawal –** *Bank of Montreal – CRO*

Yes, sure. Let me begin and then maybe I'll ask Nadim to jump in from a business perspective. I think overall, you've seen our risk underwriting criteria, we're through the cycle lenders with deep relationships and I think that continues the trend. We are not walking away from new lending or new relationships. It's really a function of the economy and so you're seeing business activity slow down. Within that loan portfolio growth, there's a lot of recycling happening.

We are growing the book. I think growth will be slow coming off the back of all of the things you're hearing and seeing, probably in the mid-single digits, and then more focused on some of the other sectors, again, just from a balanced portfolio growth but I'm pretty confident, just given the quality that growth will continue, albeit slower, just in line with any of the other banks.

I think with closing the Bank of the West acquisition now, you can see we are again in a position of capital strength and so I think our relationship lending continues. I think we've said to you in the past, 90% of those are sole bank, lead bank, and we expect we'll continue to capitalize on that.

Nadim, would you add something?

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**Nadim Hirji –** *Group Head, BMO Commercial Bank*

Yes, sure. I would say that if you look at the countries, North and South, U.S. is definitely slower than what we see in Canada but we're still doing deals and we're still doing loans. There are pockets that when you look at agriculture, you look at food, we're still seeing good volumes there; dealer finance, media finance, there's good volumes in those as well but areas where, leverage finance or CRE, those are areas, of course, that have slowed down dramatically in the U.S. and will affect our growth. In Canada, those areas have slowed down as well, just not to the same degree.

As Piyush said, we're still growing and we're still doing deals. The volumes are down as they would be in any cycle, but our risk appetite, as Piyush said, and I'll just back up one more time and say it, is that we go through cycles, we're not in and out of industries but we are looking at capital, we are looking at risk optimization and return, and we are looking at long-term relationships, and that's how we get through cycles time and time again.

**Mario Mendonca –** *TD Securities*

In the past, when a particular asset class came under some pressure, the banks have given us some outlook on the loss content in that particular asset class. Comments were around in a stressed environment, we could see x100 basis points of loss content or some of that effect. Is there any way to size that in the context of commercial real estate as a whole and maybe office specifically? In a stressed environment, have you given some thoughts to what the loss content in those businesses could be? I appreciate that these are not massive parts of BMO's portfolio or overall loans, but it would be helpful to get some outlook there.

**Piyush Agrawal –** *Bank of Montreal – CRO*

Yes. Thanks again, Mario. It's Piyush. I would begin by saying that we've come off a very benign cycle and so in the early parts of this year, we've been hinting to you or telling you actually outright that we're normalizing and so these trends are really normalizing versus stress. Now having said that, from a risk management perspective, we have a good discipline of regularly stress testing our portfolios over time, when the normal loss rates have been zero to one basis point in commercial real estate for us over the last eight or 10 years. I just said, we are significantly over-provisioned compared to that loss rate. I feel pretty good about where we are headed.

Unlike some of the news items you hear, there is a large stratification within commercial real estate; the preponderance of multifamily, which is doing very well, single family, but yes, we have looked at office. Again, I'll reiterate, office is 1% of our book. Within the 1%, as you look at the disclosure between REITs and medicals that are doing extremely well, I can then segment down to certain office Classes, A, B or C in urban and suburban, and we've done a deep dive. In our stress test, we don't see any immediate worries now, but we know there is blood in the water. There will be impacts as rates rise, as cap rates change and so in due course, we'll come back, and you'll see those in the results if there is something that is of a higher concern.

If you go back to the 30-year history, our loss rates overall are 30 basis points across the portfolio. In that, some stresses here and there but at the moment, I don't have much more to offer other than we feel very confident about our overall portfolio.

**Mario Mendonca –** *TD Securities*

Did you say 13 or 30 basis points of losses over the last 30 years in commercial real estate?

**Piyush Agrawal –** *Bank of Montreal – CRO*

No, we said overall across the entire portfolio, it's 3-0, 30 basis points and we're coming off the benign cycle, and so you're seeing our loss rate this quarter at 16 basis points on impaired. We are still a long way to the normalized average before we start thinking about stress.

**Mario Mendonca –** *TD Securities*

Well, I don't want to put words in your mouth, but it sounds like what you're saying is that the loss content on your commercial real estate and on office based on the work you've done to date, the loss content is still very, very modest. That seems to be the message you're sending, unless I'm misinterpreting it.

**Piyush Agrawal –** *Bank of Montreal – CRO*

No, that is correct. The loss content from the performance we have seen and the formations and the early watchlist we have, we feel pretty strongly about it.

**Lemar Persaud –** *Cormark Securities*

Maybe just to start off, I just want to summarize one of the prior answers to the loan growth question. Would it be -- I'm going to ask you very directly, would it be fair to suggest that BMO has not changed any of its underwriting standards in the U.S. or Canada? And then if that's true, then would it be fair to suggest that in the commercial loan growth in the U.S., excluding Bank of the West, so that sequential decline, I think it was 4%, should reverse in future quarters because sometimes since we've seen commercial loan growth this soft excluding perhaps some like one-time negative impacts in the U.S. like PPP runoff, so I just want to be really clear on that part.

**Piyush Agrawal –** *Bank of Montreal – CRO*

Yes. Piyush, again. I'd say that the risk appetite is a through-the-cycle risk appetite and our risk underwriting hasn't changed. Now in that, given seasonality, given cyclical trends, we'll tend to overstress more of the underwriting at origination but this really is much more a function of the market than it is a function of us in that market and so loan growth demand is slowing down. You're seeing that across the banks, you're seeing across sectors and so as economic activity picks up, as there's more confidence in the market, I think we'll start to see more originations, and we'll be there for our clients.

We continue to, like I said, managed through the cycle in that risk appetite. We managed through our concentration risk management and all of those have held us in good stead over the many years, and we don't plan to change any of that.

**Darryl White –** *CEO*

Otherwise put -- Lemar, it's Darryl, just to help on the question. I think in time, you'll be exactly right. The question is how much time will it take for you to be exactly right? Meaning, the vast majority of the catalyst for the decline in loan growth is, in fact, if not the entirety of it, is demand, it's the market. We haven't changed underwriting standards, and we don't change our approach to managing our clients.

As we work through this phase of softening economic activity, that should be the outcome. As that phase turns, then you should see a return to positive loan growth for us, particularly in commercial and as you know, our strategy has always been in good markets when loans are growing broadly in the industry and commercial in both Canada and the U.S. Our strategy is to outperform that market when that occurs and that would be our intent today. No change.

**Lemar Persaud –** *Cormark Securities*

And then my next question, I want to turn to U.S. P&C margins. If I'm looking at your waterfall on slide 14, it seems to suggest that excluding Bank of the West, margins have turned negative on the stand-alone business, if you will. It looks like it was a rapid shift in deposit margins comparing this waterfall versus last quarter's. Deposit margins turned to a negative drag on NIMs. Was this directly related to the U.S. regional bank turmoil and then could you talk to the outlook for U.S.-specific retail NIMs, just as a means for my modeling?

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**Tayfun Tuzun –** *Bank of Montreal – CFO*

Yes, so there are two elements here. You are seeing actually what the Bank of the West contribution was to U.S. P&C NIM. We're quite pleased with pretty healthy contribution to our margins. The impact of faster deposit repricing clearly has an element of very strong competitive markets in the U.S. with respect to deposit rates. We try to sort of maintain a stable approach to how we price our deposits but the market over the past 90 days has accelerated and we are feeling the impact of that on our margins.

There's also an element of migration to term deposits, which looks a bit more stronger in Canada. But in Canada, it's actually coming slowly to an end. Probably, over the next couple of quarters, we'll run through the migration impact on Canadian margins. In the U.S., my expectation is that until the market achieves that balanced picture, we will probably continue to see more, faster repricing of both commercial and retail deposits. I suspect by the end of this year, with also the Fed hopefully coming to the end of their rate increase cycle, that pressure will come off.

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**Lemar Persaud –** *Cormark Securities*

It sounds like then relative to that 3.96%, we could see that come down a bit and then hopefully, switch course in 2024. Is that fair?

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**Tayfun Tuzun –** *Bank of Montreal – CFO*

Yes, but not meaningfully. I mean, as I look ahead, both in Canada as well as in the U.S., we are seeing a fairly stable net interest margin in our P&C businesses and the same message holds true for our consolidated margin as well so we're not expecting significant pressure on these margins.

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**Darryl White –** *CEO*

Well, thank you, operator, and thank you all for your questions. I have two important thoughts to close the meeting with. One is to remind us all that BMO's highly-diversified business mix and strong foundation, built on the strength, size, stability of our balance sheet, and fortified by our superior risk, liquidity and capital management is built to perform in any environment.

Second, before we close the call, I want to take a moment to recognize while he's here with us in the room, Dave Casper, who is retiring next month after over 40 years of service with BMO. Dave, as you all know, has been instrumental in BMO's growth, particularly, but not exclusively, in the United States and under his leadership, our commercial banking businesses have become a top five commercial lender on the continent. Dave has also played, as you all know, a very key role in the acquisition of the Bank of the West and has been a staunch supporter of all the communities we serve, but particularly the great city of Chicago so I'll always be grateful for Dave's legacy of outstanding leadership at BMO.

With that, I thank you all for participating and we look forward to speaking to you again in August. Thanks, everyone.