BMO Financial Group

Bank of Montreal at Scotiabank Financials Summit 2019

CORPORATE PARTICIPANTS

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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 2019 and beyond, our strategies or future actions, our targets, expectations for our financial condition or share price, the regulatory environment in which we operate and the results of or outlook for our operations or for the Canadian, U.S. and international economies, and include statements of our management. Forward-looking statements are typically identified by words such as "will", "would", "should", "believe", "expect", "anticipate", "project", "intend", "estimate", "plan", "goal", "target", "may" and "could".

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 or projections. 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; the Canadian housing market; weak, volatile or illiquid capital and/or credit markets; interest rate and currency value fluctuations; changes in monetary, fiscal, or economic policy and tax legislation and interpretation; the level of competition in the geographic and business areas in which we operate; changes in laws or in supervisory expectations or requirements, including capital, interest rate and liquidity requirements and guidance, and the effect of such changes on funding costs; judicial or regulatory proceedings; 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 and to complete and integrate acquisitions, including obtaining regulatory approvals; critical accounting estimates and the effect of changes to accounting standards, rules and interpretations on these estimates; operational and infrastructure risks, including with respect to reliance on third parties; changes to our credit ratings; political conditions, including changes relating to or affecting economic or trade matters; global capital markets activities; the possible effects on our business of war or terrorist activities; outbreaks of disease or illness that affect local, national or international economies; natural disasters and disruptions to public infrastructure, such as transportation, communications, power or water supply; technological changes; information and cyber security, including the threat of 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; and our ability to anticipate and effectively manage risks arising from all of the foregoing factors.

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 see the discussion in the Risks That May Affect Future Results section on page 79 of BMO's 2018 Annual Report, and the sections related to credit and counterparty, market, insurance, liquidity and funding, operational, model, legal and regulatory, business, strategic, environmental and social, and reputation risk, in the Enterprise-Wide Risk Management section on page 78 of BMO's 2018 Annual Report, and the Risk Management section on page 27 in BMO's Third Quarter 2019 Report to Shareholders, 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 our shareholders 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 are set out in the 2018 Annual Report under the heading "Economic Developments and Outlook", as updated by the Economic Review and Outlook section set forth in BMO's Third Quarter 2019 Report to Shareholders. 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. In determining our expectations for economic growth, both broadly and in the financial services sector, we primarily consider historical economic data provided by governments, historical relationships between economic and financial variables, and the risks to the domestic and global economy. See the Economic Review and Outlook section in BMO's Third Quarter 2019 Report to Shareholders.

Non-GAAP Measures

Bank of Montreal uses both GAAP and non-GAAP measures to assess performance. Readers are cautioned that earnings and other measures adjusted to a basis other than GAAP do not have standardized meanings under GAAP and are unlikely to be comparable to similar measures used by other companies. Reconciliations of GAAP to non-GAAP measures as well as the rationale for their use can be found on page 4 of BMO's Third Quarter 2019 Report to Shareholders and on page 27 of BMO's 2018 Annual Report, all of which are available on our website at www.bmo.com/investorrelations.

Examples of non-GAAP amounts or measures include: efficiency and leverage ratios; revenue and other measures presented on a taxable equivalent basis (teb); amounts presented net of applicable taxes; results and measures that exclude the impact of Canadian/U.S. dollar exchange rate movements, adjusted net income, revenues, non-interest expenses, earnings per share, effective tax rate, ROE, efficiency ratio, pre-provision pre-tax earnings, and other adjusted measures which exclude the impact of certain items such as, acquisition integration costs, amortization of acquisition-related intangible assets, decrease (increase) in collective allowance for credit losses, restructuring costs, revaluation of U.S. net deferred tax asset as a result of U.S. tax reform and the remeasurement of an employee benefit liability as a result of an amendment to the plan.

Bank of Montreal provides supplemental information on combined business segments to facilitate comparisons to peers.

PRESENTATION

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

I'm very pleased to welcome to the stage Mr. Darryl White, Chief Executive Officer of the BMO Financial Group. Darryl joined the bank in 1994 and assumed his role as Chief Executive in November of 2017.

Darryl White – Bank of Montreal – CEO

Thank you for having us.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

Thanks again for being here. I wanted to start off by seeing if we can wind our way through the short term and long term when it comes to Bank of Montreal. You've been CEO for just under 2 years. We had an Investor Day at the all bank level about a year ago, and the bank gave us its medium-term objectives, financially speaking, including a 7% to 10% EPS growth goal that you talked about.

We know where you want the bank to be, and we know what the numbers are. How does that medium- and long-term strategy shift, or what are the levers available to the bank, when you think about the macro environment you're operating in right now? Whether that's an inverted yield curve, trade wars, Brexit, market volatility – a lot of macro issues in place here. How do you and your management team adjust to that in the context of these growth objectives you've communicated to your investors?

Darryl White – Bank of Montreal – CEO

Okay. So, there's a lot in your question. And I think what you're getting at is sort of a changing environment and what's the operational thesis that belies the management objectives within that. Look, I think there's a couple of lenses you could look through when you think about this question. And one of them might say, well, let's consider the last two, three years and look at the environment in which we and all the others that will come on the stage were operating over the last couple of three years.

And there, you say, well, we had a pretty interesting tailwind environment, didn't we? And with the benefit of hindsight, I'm not sure everybody appreciates it when you're in the moment, but you had North American economy growing at 2.5%, you had the shape of the yield curve, which worked, you had rising interest rates, you had pretty constructive equity markets and benign credit environment, and inflation, which people don't talk about, that was actually above 1.5% – so we had a very healthy macro. You're talking about macro dynamic, that's been the weather pattern over the last couple of years.

And inside of that, I would say, I'm very proud of some of the work that we've done. We can say, if I look back two or three years, we looked at that probability, and I would add fiscal stimulus to that list. We have a big business, as people know, in the United States. So U.S. fiscal stimulus was important as well. And we said, how are we going to take advantage of that period of time and invest?

And, we said we wanted to increase the share, because we thought shareholders deserved it, of earnings that came from the bank from the United States. We took that from 25% to 35% today, and we said we wanted to take our efficiency ratio, which I always remind people has a numerator and a denominator, and we wanted to work on both our relative revenue growth and our expense – down. And, at the end of 2017 – so that's the period of time we're analyzing here – for 2017, we're at 62.7%. And we said, not good enough. In the quarter we just put out a couple of weeks ago, we're at 59.9%.

So, I'm actually quite pleased with the progress we've made in that environment because we did it while investing. We grew our loans, we grew our deposits, we increased our technology spend, as we talked to you about very significantly, four years of double-digit technology spend increase, which positions us really well for whatever is coming next. And then the question is what's coming next? And how do you operate in it? And the reason I said a minute ago there're two lenses is, one lens says, boy, that was great, those were great times, banks chose to position themselves however they chose to position themselves in a tailwind environment. And now everything is different. So, is everything different is the question. Are we going to have a slower growth environment? I think, for sure, we're going to have a slower growth environment. We don't have fiscal stimulus. We've got declining rates, not increasing rates. And you're smarter than me on what equity markets will do, but I don't know that they'll perform the way they have over the last four years.

And you look at that and say, well, is it exactly the opposite of everything we've had and, therefore, is the music stopping and does the strategy completely change? And I don't take that lens. I take a lens that says, ignore how good it felt over the last three years and just think about starting from T-0 and over the next two to three years, what are we likely to see? I think we're likely to see growth, but lower growth. We might see 1.5%, we might see 2% GDP growth in North American economies over the next two to three years. We'll continue to see low rates, which will stimulate consumer behaviour. Might be a little bit more difficult from the perspective of a banker on the yield curve shape, but it does stimulate consumer behaviour. And we're starting this period of time at all-time low unemployment.

And so, if you look at it and say, is the environment in the next two to three years – to overuse the analogy of the last two to three were a tailwind – is this a gale force headwind? Or is it a slower growth environment, does it feel like a breeze in the face? I think it feels like a breeze in the face. And that's really important because it doesn't mean, therefore, that you put the brakes on investment and you put the brakes on offense, at least from our perspective. It does mean, though, that you start to shift the way you think about benefiting from the investments that you've made over the last two to three years.

And so, if we were defined in the last two to three years at the Bank of Montreal by growing our share in a disciplined way in the United States, driving our ROE up in the United States and our overall bank efficiency down, I think what you'll see in the next two to three years is more of that, at perhaps not the same rate of growth but you'll see our overall efficiency trajectory continue on the trend that you've seen over the last couple of years. We referenced our Investor Day, we were declarative then that we were targeting 58% by the end of 2021. We're sticking to that even in a lower growth environment than we might have forecasted then. We're sticking to that. We're on that trajectory. And we see that as a way station, not as a final destination. And I say that because we're building-in operational discipline that says every day, every quarter, we've got to get all of our businesses thinking about operating leverage, and we drive to that, and we'll drive to that, and we'll drive through that, at that point in time.

And there are a whole bunch of disciplines that I think are in place today that might not have been five or 10 years ago. There are incentives that are in place that might not have been. And, we start to change the whole technology story from inputs to outputs. When you grow your technology stack by 10% a year for four years, you can get to the point where you just say, I'm pleased with the central architecture, but I really have to focus the conversation on outcomes. So that would be the other difference, I think, you'll see in the next two to three years. We're starting to see it now. It takes a while, but we're starting to see it now. We're really proud of our app in Canada is leading in the App Store. Our app in the U.S., by the way, is among leading banks in the United States, now we're collecting deposits in all 50 states in the United States. We are getting those little tangible outputs from the investment that occurs, and when we talked last year about moving our digital banking time to credit approval and funding from 30 days down to 30 minutes, we've done that. We're in this phase of – we say to ourselves at our management team – we've got to stop thinking about the dollars invested, and we've got to start thinking about the outcomes to the customer and the cost per unit. And we're in that phase right now. So I feel it's kind of like one of these things that people say, is this the end of the world as we know it? Absolutely not. I actually feel fine, because we've made these investments, we've set ourselves up for a growing but lower growth environment. And what you'll see from us is consistency through our businesses and our operating disciplines for the next two to three years.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

Thank you for that. You touched on or you introduced some of the topics that I want to delve into more deeply here. In a lot of the conversations we've had, and in my personal view as far as the Bank of Montreal shares are concerned, investors' sentiment has been heavily influenced by what's happening with the U.S. business and what's happening with the trend in efficiency. And as you mentioned, the last couple of years have been very strong in that regard.

When it comes to U.S., and we'll start with the personal and commercial franchise, you've discussed with me and with the group in the past that you feel that the business is more diversified than has been the case, perhaps, in previous cycles, when economic or competitive environment has shifted.

I would say that the market's view is, hey, these guys are a commercial lender, and we've had a major shift in the rate structure, and that's going to weigh on their earnings and revenue performance. Maybe we can get into that, but more bigger picture, again, to go to that term. What in your view speaks to that increased diversification and how do you think that better protects U.S. earnings power in a lower rate, slower growth environment?

Darryl White – Bank of Montreal – CEO

And you're talking particularly to the U.S. business?

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

U.S. P&C, in particular.

Darryl White – Bank of Montreal – CEO

So P&C, in particular. Well, what I was going to say to you, first of all, is that the U.S. business is not just the P&C business.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

Yes. We're going to go to the other ones.

Darryl White – Bank of Montreal – CEO

And we'll get there. So let's talk about the businesses that are 70-ish percent of our U.S. profit pool – P&C businesses.

Why are we more diversified? You should look at that question through the lens of geography and through business mix. So when you look at it from a geographic perspective, I bet you, Sumit, if I polled everybody in this room five years ago and said how much of the U.S. business of the Bank of Montreal is occurring in the Midwest, the Chicago and the concentric circles that go to the states where we have a branch footprint, you'd get a very high market share of people in this room who would say it's probably pretty close to 100% or something like that.

Today, it's 50%. It's 50% of the business that we do in the U.S. comes from that core footprint, two-thirds of our new originations come from outside of that core footprint in the commercial banking business. How does that happen? We started talking to you three years ago about the fact that scaling commercial banking is probably the easiest scale game that you have in a human-centric business and banking because I can open – which we have – commercial banking offices in Columbus and Fort Worth and Dallas and Atlanta, and I can do that with really good bankers who rely on the infrastructure that's been built centrally, you don't have to drag it all with you.

We've done that on the lending side, on the commercial side, and we've been able to grow faster than the market and take share in a business that we're just really good at. We're viewed in the marketplace as a top 10 lender in the United States – 5,000 banks, top 10 lender, with the benefit of the balance sheet that comes with the global franchise.

And then you go to the deposit side, and we said we've got to get better at this, too, because you can't have a lending book that grows so much faster than your ability to fund it with the deposits. And we put in place strategies that said we're going to be really awesome at deposits in our core markets, but also, if we're going to keep up with the lending business, we thought to figure out how to sweep deposits from outside of our core markets, which does actually go to the scale debate, because we then rebuilt our digital bank in the U.S., we call it B2B, and we invested heavily in that. we rolled that out late last year, and through the course of this year, what we've seen is leading deposit growth in the market. We've seen a collection of deposits in all 50 states. And we've seen an ability – not quite, we're actually seeing the loan book grow a little bit faster than deposits now – we're going to see that level out as we go forward into the quarters that come. So, we feel really good about having looked at it as an integrated strategy from a geography perspective, because you can't say I have a broad-based lending strategy and then I have a really narrow deposit strategy, we put it together and we said we have to have one strategy and they have to support each other.

So that's the geography lens. And then you go to sectors on diversification as well. One of the things people ask me all the time, are you worried about the size of your commercial lending book when we get into a downturn, is there concentration risk and all that? We don't have a single sector – and we participated in almost all of the sectors in U.S. commercial lending – we don't have a single sector that accounts for more than 11% of the book, not one. It's very broad-based. It's based on decades of history. By the way, today is the 35th anniversary of the acquisition of the Harris Bank in 1984. We've been in business in the United States for 200 years, 35 years of concerted commercial banking expertise, not a social experiment. It's now cresting on $2 billion of earnings. And we don't have concentration, so when I talk about diversification, it's really supported by all of those facts. And I think that as you go forward, I'd be shocked if we saw it do anything but continue to diversify both geographically and from a sector perspective.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

One of the objectives that under your tenure has been communicated by BMO has been to be a leader in taking risk and managing risk. So, first off, the obvious question that comes to mind, are you of the view that the bank, perhaps, was too risk-averse in the past with respect to whether it was lending or capital markets, particularly given that your credit metrics historically have been some of the best in the sector?

And, secondly, let's overlay that with the credit cycle. About a year ago at this time, or certainly at the end of '18, we had a sell-off on the view that we were late cycle when it came to credit. Credit metrics have been pretty good this year, again, there's been a little bit of noise and some of that's been accounting driven. But what would you say to the pushback that, hey, BMO's corporate and commercial loan growth is 20% year-over-year, and we're getting into a period where by your own admission, it seems like growth is going to slow? I want to know a little bit about that objective of taking and managing risk and how you would communicate that in the context of the current credit environment and economic cycle?

Darryl White – Bank of Montreal – CEO

If you look – there's a page in our investor deck that we sometimes gloss over too quickly – if you look at the credit performance of the Bank of Montreal since 1990, if you look at total PCLs related to total loans, we've had the best performance almost every single year and well better than the average. I think there are only a couple of years where that's -- it's amazing, actually – it's only a couple of years where that's not the case. Do I think we've been too conservative on taking risk? I don't think so. I think that's a built-in competitive distinguished advantage that the Bank of Montreal brings. And the reason I take you all the way back to 1990 when I say that is because we've proven that it's the case through cycles. And so, managing risk in up cycles, managing risk in down cycles, is something that I think is embedded in the DNA, and the underwriting standards and the practices that have gotten us there are true today.

Go back to the commercial lending book. In fact, I would say the diversification of that book is better than it was before, through the course of that period that I just defined for you, and the skills, the technical skills, are way better, just as they are, I think, in most places they should be. And the knowledge of the sectors and the bankers, knowledge of the clients is also better. So I don't think we're at a different place on the risk curve at all. I think we're taking advantage of what is an embedded advantage of the Bank of Montreal in terms of credit risk performance.

And it's interesting, Sumit, you look at – we've been saying for over a year, maybe two years that – our total PCLs, as it relates to the total outstandings, which was in the kind of high teens or let's call it 20 basis points at the upper boundary, we've been saying, if you could go back and listen to our transcripts, call after call after call, that this isn't going to stay forever, and we guided to somewhere in the low 20s. I think that guidance is appropriate going forward, and that will be a little bit higher than what we've seen before, in an environment that's growing more slowly. Why would you expect anything different, I would say to people. And I think it'll continue to be distinguished and better than our peers.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

The 20 to 25 basis points in provisions is still a very constructive level for credit quality and I'd say for your overall growth rates, so this sounds like less recoveries, some normalization, not the start of a full turn of the credit cycle.

Darryl White – Bank of Montreal – CEO

Yes. When we put our earnings out two weeks ago, we surprised on a headline miss – if you mathematically calculate the expectation for credit losses relative to the published credit loss, that accounted for the entirety of the miss. You've actually done a fantastic job just now summarizing what to expect going forward. And we said the credit quality of the book remains very strong, and I said that, when you look at it, we can't see any significant deterioration in the trends and the credit quality of the book at all. Some people scratch their head and say, how are those two things be true when you have $306 million of PCLs at the Bank of Montreal and yet, you're saying the credit quality is not deteriorating? And we took you through it, we didn't have a reversal – we shouldn't pick on a reversal every quarter – we had some collection issues, which we were clear about and we said are behind us, which contributed to it, we had an idiosyncratic situation in the Canadian commercial book, which doesn't happen very often. And, we said, that's the story on the impaired book, which itself is completely reasonable. So, when you look at it, I agree with you, you come back into the, let's say, low mid-20s. Relative to the size of our book and the performance, it does not say there's a shoe dropping here. It doesn't say there's a shoe dropping. It says this is a natural outcome of where we are in the credit cycle. We could have a separate conversation on IFRS 9, but maybe that's fair.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

I'll save that for my private call with Tom Flynn. I won't bore you with that here. Let's move off that. Maybe the only point on Commercial would be – I think the bank has indicated in a few other calls that it's probably not reasonable to expect commercial growth is going to continue to trend at these levels. Is that mostly a commentary on rule of large numbers, that at certain point things start to slow or are you seeing certain pockets, given that historical 30-year outperformance on credit, that you're saying, you know what, maybe it makes sense that, whether it be real estate, whether it be Ag, there are a few pockets that we want to tap the brakes?

Darryl White – Bank of Montreal – CEO

There are pockets that we will continue to grow in, but perhaps not at the rate that we've seen in the last couple of years, that may have some influence from a risk perspective. But I would say, Sumit, that is not the biggest driver as to why we're saying we'll see some slowing. I think it is the law of large numbers, and there's a dynamic in the marketplace that the demand for commercial credit is slowing as the world slows down a little bit. So as the world slows down, the demand for credit, the draw on lines aren't as prevalent, and we're just looking through that and saying, over the next two to three years, do we actually see the marketplace, that itself was benefiting from a fiscal stimulus, a rising rate expectation, which would cause one to go quickly and make their capital investment and borrow the money, relative to where we are today, we'll see the demand taper off, we'll continue, we believe, to, at minimum, protect our share and probably continue to grow our share in a slower growing market. It's not so much a risk-based assessment of continued growth but a demand based assessment.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

Mindset around capital and capital deployment. I mentioned, your CFO Mr. Flynn before, he stated on the call – your CET1 ratio is about 11.4% and, for most of your tenure, the bank had been relatively consistent on share repurchasing activity, have paused the last two quarters, probably in response to the fact that your business loan growth has been so strong – Tom mentioned something along the lines of, we probably want to be solid through 11.5% before getting going on share repurchases in the market again. That's a higher number than we've seen from the bank in the past. Would you say that's a response to the domestic stability buffer that OSFI has increased or is there something else that's changed in how you're thinking about that?

Darryl White – Bank of Montreal – CEO

No, it's not the domestic stability buffer and, any number that you and I can talk about right now, we're well clear of the domestic stability buffer, so I would say no influence there. And I would say, we're at 11.4% published, if Tom said 11.5%, I'd actually put this in the category of splitting hairs. I would say the reality is we're in a range right now that we're comfortable with, we think is a really comfortable range to operate the bank. If you go forward, we build capital at a normal rate of about 10 to 15 basis points per quarter. Some quarters could be higher, could be lower, but on average, over time, you can kind of model that out and say, if we have 10 to 15 basis points of capital build per quarter and then you look at what individual impacts could swing it around in any particular quarter. In Q1, as you know, better than anybody, we've got the capital rule change, that sort of could round-trip that approximate growth. So, you sort of look out over the next couple of quarters and say somewhere around where we are, which we've said is a pretty comfortable position is the right place to go, and then you might see growth in the capital ratio after that, at which point, I think, Tom said and I agree with him, we'd look to get more active over the course of the year. If that capital growth continued, you'd see us get more active through the year than you might right now.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

And I'll do that.

Darryl White – Bank of Montreal – CEO

And, is there anything more to it? No, it's just sort of simple capital planning and accounting for that capital rule in the first quarter of the year.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

I feel like, me, my counterparts, your investors, you've been faced with the U.S. M&A acquisition, even before you officially took the seat. A year ago, I thought you did a good job here in putting some financial parameters out to the market. If I remember correctly, it was EPS accretion in year two and double-digit IRR in year two – were some of the key headline metrics you were working with. So, number one, I'll ask you to confirm that I have that right. And, secondly, historically, this bank hasn't been averse to thinking about M&A in economic backdrops that were far from certain. M&I will go into the history books as a very well-timed acquisition, if we measure these things on what price do you buy and what price could you sell at. Is it fair to say that M&A for BMO, it's not really the backdrop that matters to you as much as the fit that you're going to get on some of the key metrics that you've laid out for us, including strategy and culture?

Darryl White – Bank of Montreal – CEO

We've always said, through that piece that you're summarizing, Sumit, as long as we are comfortable that we have real organic opportunities that we can take advantage of on strategy – that comes first. So, I'd start by taking you back the last two or three years, and you just look at the growth of our business in the United States without the, I'll call it, complexity and risk of executing M&A, which is always the case, there is complexity and risk, and I wouldn't have changed a thing. Our ability to deliver – you asked me earlier about the U.S. P&C business that now has a sub-60% efficiency ratio, a double-digit ROE and is contributing to the earnings growth of the bank, all organically. That's a great story.

Now, as we go forward, you asked me to confirm how we think about M&A, I would say nothing has changed. Those are the criteria. We're pretty disciplined about them. I think I've also said, if something had unicorn value strategically, if we saw that it was just perfect for other reasons, might we explained to you that we had to stretch beyond that criteria a little bit – maybe, there's nothing that we can see right now that we would put in that category. So, we'll stay pretty disciplined to it. And I'm glad you asked at the end of your question about strategy and culture because, I've got to tell you, we see a lot of things, and some of them can be sort of close to the acceptable box on the financial analysis, but not on culture. And we take that stuff pretty seriously, we've operated our bank based on a set of values and culture that are very important and if we don't see that we can port our culture into something that we're picking up, we won't do it. We bought the KGS business in the capital markets vertical – it wasn't very big, but I think it's a really good example of this – we looked at it and we said, we're pretty confident that this will be financially valuable to the shareholders of the Bank of Montreal. And, by the way, it's outperformed all of our base-case expectations since we bought it: ROE, revenues, cost, and we haven't lost one single person. And I bring that last part up because we also assess the culture. We spent a lot of time with them, and we assessed whether or not the fit with our platform was going to work, because we're not really interested in M&A, in the "buy it and leave it alone," we're not really interested in kind of putting things in the corner. We're interested in bringing them on to our culture.

You haven't seen us very active and it's because we don't see many opportunities that fit the valuation equation as well as the strategy and the culture. And I can't tell you whether that's going to change over the next while. When you pointed out M&I, I think you've got it bang on, we bought M&I at book value in 2010, it's one of the first and largest acquisitions post global financial crisis, but we saw the fit, we saw the culture, and we doubled our branch footprint – at book value. Those are not readily available today.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

You've got a $100 billion plus asset franchise in U.S. P&C, a $100 billion plus asset franchise in U.S. capital markets, or wholesale, I always think of the middle ground between those businesses is wealth. There was a period of time when BMO was purchasing select asset managers globally, that's been quiet in the last few years. Maybe more philosophically, how do you view your U.S. wealth opportunity between these two larger U.S. tenets you have in P&C and wholesale?

Darryl White – Bank of Montreal – CEO

In the U.S., we've got an asset management business and we've got a private banking business, so we don't have a full-service distribution business like you do in Canada, and we don't have an ETF capability like we do in Canada, but we have good businesses that operate well. And, you're quite right, we haven't gone out and sought to grow these businesses by acquisition. In fact, we've actually found opportunities to contain, or to sell, our trust outsourcing business, for example, which we just didn't think fit with our client strategy.

So, the lens that we put on it is, where is the client fit? And if there was something we could do to grow those businesses that had a client imperative, we would look at it very hard. We found that asset management businesses and wealth management businesses in the United States, at least up until now, have been very expensive. And we were never really convinced of the imperative of paying that price relative to other opportunities to deploy our capital, and so we haven't moved on them. Now, if the world moves into an affordable range and we see a client imperative, we may do something, but it's not a place you would lurch for growth necessarily at any price, it's got to have a really good fit.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

So, if U.S. is one of those key components that investors and the market have been focused on, efficiency has been another. You've articulated many times that the technology spend has increased to roughly $2 billion annually, but at Investor Day, you message that that's not an area that we're looking to slow the level of spend, it's going to be in the double digits for the foreseeable future. So, in a revenue environment that even in your opening, you articulated, seems to have slowed more quickly than we would have thought a year ago, how does the 58% efficiency objective – which is [by] 2021 – does the technology spend get revisited in the context of this revenue deceleration, or is that off the table?

Darryl White – Bank of Montreal – CEO

When I said that we didn't see it slowing down in the foreseeable future – that was in October of last year – what I meant was this year, and we've been right about that. We'll continue to increase it at a double digit, it's actually well through $2 billion now on the base. I don't look at it, Sumit, and say, all right, how much is enough? You look at it and start to ask the question, is the central architecture sufficient? We believe it's not only sufficient but distinguished. Are we at the stage now where we can move the technology conversation to outcomes, like the ones I talked about earlier, and cost per unit to serve, instead of just talking about whether we've built the architecture and the central stack. And we're absolutely on that trajectory right now, and we've got lots of market-leading examples, some of which I summarized earlier, that we're very proud of.

And so, we will see a decline in the technology spend going forward. I don't mean a decline from the absolute level of spend, a decline in the growth rate. It's absolutely the case that this bank, and I bet every one of them that are here at your conference, are well, well, well inside the efficient frontier on technology spend. It becomes a question on the return on the marginal dollar, and are you at the point where you can assess it and say, we understand the return on the marginal dollar of spend, and we're happy about that. We are. So, I think you'll see a moderation in the rate of growth of spend. It may not be 10%. It may be somewhere between 5% and 10%, for example. And does that get us to our commitment of 58%? For sure, it does. Even in a lower growth environment, because it's not just about moderating the technology spend to get there, right? It's about all the other strategies and the portfolio choices that we make.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

So maybe a two-parter on technology, you've done a good job in communicating in a few different businesses how you think about the return profile and ROE is getting better, specifically in the U.S., but also on all bank level. Do you have a metric or measure as to how the bank thinks about return on investment of your project spend and technology? And then, secondly, a little bit different, earlier this year, you had an interesting announcement that you had started up a financial crimes unit within the bank and, if you think about some of the incidents lately or some of the things we've heard, Desjardins, Capital One, some high-profile breaches, what exactly is the mandate that you've given to that team?

Darryl White – Bank of Montreal – CEO

Okay, so those are two, I guess, related but very different questions, so let's just go through them in order. On the return on the marginal spend, we do go back and we look at – you auction off the best ideas, right? – you auction off the best ideas in technology and you choose the ones that fit strategy. And then what you do is, you go back six months later, a year later, and ask yourself the question, are they returning what the business team said that they thought they were going to return when we made the investment? So, there's a discipline in it in the same way we have discipline in all of the business plans in the bank and people are held accountable to what they project. We don't have a lot of capacity for hundreds of millions of dollars of social experiments. That's not the way we run the business. We figure out whether it's on strategy, does it fit with the objectives that we've talked about with shareholders, and then we go to the outcomes. So, when I talked earlier about the performance of the app in Canada, the app in the U.S., the benefits that we're seeing from data and analytics, the robotics that are improving our AML performance, efficiency and effectiveness, all at the same time, 30 days to 30 minutes on business banking lending – hat's all as a result of the benefit of the technology. And what it's doing is, it's telling us that we understand now our ability to create capacity through that spend, benefit to the consumer, and we understand that the cost of serve is going down. So we can de-particularize it by project, as opposed to looking at it as a big swath all the way across the bank, and you learn from that and you get better as every quarter and as every year goes by. When I said to you earlier that rate of growth will still be high, but it will moderate relative to what we've seen in the last 4 years, it's because we're really confident that we're now in a phase of outputs and capacity creation, not just spend so that we can say that we spend as much as the next guy. That's a ridiculous way to think about technology spend, in my view.

Second part of your question, we did announce earlier this year the creation of what we call the financial crimes unit. Think of it as a triangle between your cybersecurity, your physical security and your investigations. And when you put data and analytics in the middle of that, and we brought in some world-class talent so that we could have all of these people working together, you then have an environment where the connection to your AML capability, your data and analytics capability, the events that occur in the world, aren't either cyber or physical or internal fraud or external fraud – we put the fraud team inside this as well. You get a few hundred people who are completely connected from an operating model perspective. Because you think about it in a different model, where they're all reporting in different places in the org chart, we came to the view that we had information over here that was very valuable to the work that we're doing over here, but it wasn't connected and they didn't know it, but if we put it together, we would have a preventative ability to get ahead of the threat. The threat is ever-increasing, it's global. It needed a world-class response with world-class people. But the real key was putting the unit together, so those people are working together and sharing the information, so that we could get better and smarter at it. And look, touch wood, anybody at your conference could have a bad day any day, and we think what we've done through this is – decreased our risk fairly materially of having that bad day, but you never get it to 0 and you're always chasing it.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

Right on time. Good to plan up.

Darryl White – Bank of Montreal – CEO

You're a good moderator.

Sumit Malhotra – Scotiabank Global Banking and Markets, Research Division – MD of Canadian Financial Services

I still want to thank you for taking the time. I appreciate you giving us those messages, and we will do this again.

Darryl White – Bank of Montreal – CEO

Terrific. Thanks for having me.
