Bank of Montreal (NYSE:BMO) Q1 2024 Earnings Conference Call February 27, 2024 8:15 AM ET

Company Participants

Christine Viau - Investor Relations

Darryl White - Chief Executive Officer

Tayfun Tuzun - Chief Financial Officer

Piyush Agrawal - Chief Risk Officer

Nadim Hirji - Head of BMO Commercial Banking

Ernie Johannson - Head of BMO North American Personal and Business Banking

Conference Call Participants

Ebrahim Poonawala - Bank of America

Meny Grauman - Scotiabank

Mario Mendonca - TD Securities

Gabriel Dechaine - National Bank Financial

Doug Young - Desjardins Capital Markets

Mike Rizvanovic - KBW Research

Darko Mihelic - RBC Capital Markets

Paul Holden - CIBC

Operator

Good morning and welcome to BMO Financial Group's Q1 2024 Earnings Release and Conference Call for February 27, 2024. Your host for today is Christine Viau. Please go ahead.

Christine Viau

Thank you and good morning. We'll begin the 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 today to take questions are Ernie Johansson, Head of BMO North

American Personal and Business Banking; Nadim Hirji, Head of BMO Commercial Banking; Alan Tannenbaum, Head of BMO Capital Markets; Deland Kamanga, Head of BMO Wealth Management; and Darrel Hackett, EMO 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 Typhoon will be referring to adjusted results in their remarks unless otherwise noted.

I will now turn the call over to Daryl.

Darryl White

Thank you, Christine and good morning, everyone. Today, we announced net income of $1.9 billion and adjusted earnings per share of $2.56 and against a challenging economic backdrop, continued to demonstrate the strength and resilience of our diversified businesses.

While the environment has constrained revenue growth in market-sensitive businesses in the near term, the strength of our personal and commercial businesses further enhanced through the integration of strategic acquisitions, delivered revenue growth of 10% and pre-provision pre-tax earnings growth of 3% from last year. We're executing against simple, clear and well-defined plan by optimizing our businesses and balance sheet, controlling costs and growing customer relationships to drive long-term sustainable growth.

We significantly strengthened our capital position with a CET1 ratio of 12.8% and up 30 basis points from last quarter and up 60 basis points since closing the Bank of the West transaction. Through disciplined balance sheet optimization, we've absorbed regulatory impacts and credit normalization and are well positioned to support client growth going forward. Given the outcomes of our actions, the result -- the resulting strong position and consistent internal capital generation, we've removed the DRIP discount as of this quarter. We're delivering against the expense management commitments we announced last year, including the full achievement of the US$800 million run rate cost synergies at Bank of the West as of February 1 and 1 year after closing and 20% higher than our initial plan.

We're also on track to deliver the additional $400 million of expense savings by the end of 2024 from the early actions put in place last year to enhance bank-wide operational efficiency. The benefits of these programs are now accelerating. In fact, we've reduced expenses by 4% from last quarter and remain focused on returning to positive operating leverage beginning next quarter. Credit remains well managed. While impaired loss provisions have increased from very low levels and our consistent and disciplined risk management practices and the expertise within our lending teams and the quality of our client selection are resulting in good overall credit performance in line with our expectations. As we've been saying for several quarters, the near-term growth outlook industry-wide is muted by slowing GDP growth.

We expect North American economic growth to remain subdued in the first half of this year before recovering towards the end of the year on the back of lower interest rates. While directionally similar, we do expect a meaningful difference in the landing between Canadian and U.S. economies. In Canada, real GDP is expected to fall from 3.8% in 2022 to 0.8% in 2024. The U.S., while also slowing is expected to show much better growth of 2.2% in 2024. We foresaw these trends emerging and we're dynamically managing our businesses to succeed and further strengthen our competitive advantage as the environment improves.

In Canada, Personal and Business Banking continues to outperform with net new customer growth up 7% year-over-year. We continue to expand our suite of innovative products, including our new BMO Eclipse RISE Visa card that rewards customers for establishing good financial habits. We're already seeing great traction with over 15,000, new accounts since launching in December. We continue to attract newcomers to Canada with our award-winning digital offerings and services with new accounts up 35% from last year.

In the U.S., we are executing against a very specific plan. We closed, converted and integrated the Bank of the West acquisition during a period of heightened uncertainty in the U.S. banking market where several banks have been challenged to maintain liquidity, capital and customers. Since closing, our total U.S. segment has consistently delivered quarterly PPPT above US$1 billion and contributing 45% to the bank's earnings. We've sustained this performance despite intensified deposit competition and decreased loan demand. We've overachieved our cost synergies and steadily improved our capital ratio in the U.S. banking subsidiary which is up over 80 basis points from a year ago. We're gaining momentum from our initial brand campaign which when combined with targeted marketing, including becoming the official jersey sponsor of the LAFC is driving new customers across our entire footprint, all under the unified BMO brand.

In our new Western markets, we've had over 250,000 customer conversations this quarter, providing valued and trusted advice. In California, new deposit relationships were 38% higher compared to last year as branch productivity continues to build towards our full potential. In North American Commercial Banking, while pressure on loan demand reflects lower utilizations as businesses wait to deploy capital at a lower cost, we continue to see strong momentum in customer acquisition across our integrated North American platform. The U.S. is now contributing 60% of our total new client growth compared to 37% during the same period last year. And we've retained over 90% of Bank of the West clients solid evidence that the BMO brand is strong and gaining traction.

We're actively pursuing revenue synergies across our businesses with early indicators providing confidence that we will outperform the market when the environment becomes more constructive. In our Wealth business, we continue to create new and innovative solutions in the ETF and mutual fund space to help investors achieve their financial goals. BMO Global Asset

Management received top honors across several categories at the 2023 Canada Lipper Fund Awards and led all ETF providers at the 2023 Funddata awards. At BMO Insurance, investments in data and analytics are helping speed up and simplify the underwriting process, improving productivity for financial advisers and helping make life insurance coverage more accessible to Canadians. In BMO Capital Markets, client activity is gaining momentum after a muted start to the year. In Canada, we were number one in completed M&A and ECM this quarter. And in the U.K., BMO was recently designated as a gilt-edged market maker, a natural extension of our global rates business.

We're driving real financial progress for our clients and communities and continuing to deliver on our client -- on our climate ambition. In partnership with the Canada Infrastructure Bank, we launched an innovative program to support the financing of energy retrofits for commercial building owners to deliver certified reductions to greenhouse gas emissions. It's just 1 example of how we're supporting our clients as the air lead partner in the transition to a net zero world. BMO's leadership continues to be acknowledged once again being ranked among the most sustainable companies in the Dow Jones Sustainability Index.

In summary, our first quarter results were impacted by revenues that fell short of expectations due in part to environmental pressure and other specific factors Tayfun will describe in detail. Meanwhile, our core fundamental pillars are strong. Capital is very strong and ahead of expectations. Credit is within our range of expectations and expenses are tightly controlled and we're delivering on our efficiency commitments and driving clear results. We will continue to manage for optimal performance in this environment and also proactively improve our competitive positioning for outperformance as we move to the next stage of the business cycle.

I'll now turn it over to Tayfun.

Tayfun Tuzun

Thank you, Darryl. Good morning and thank you for joining us. My comments will start on Slide 8.

First quarter reported EPS was $1.73 and net income was $1.3 billion. Adjusting items are shown on Slide 38 and included the after-tax impact of the FDIC special assessment of $313 million, the net accounting loss on the sale of a portfolio of recreational vehicle loans related to balance sheet optimization of $136 million and acquisition-related impacts for amortization of intangibles and integration costs of $84 million and $57 million, respectively. The increase in reported net income from last year reflected the loss on fair value management actions related to the Bank of the West acquisition in the prior year.

The remainder of my comments will focus on adjusted results. Adjusted EPS was $2.56, down from $3.06 last year and net income was $1.9 billion, down 12%. Revenue increased 10% and PPPT increased 3% with good growth in Canadian P&, C the benefit of acquisitions and market-related impacts in insurance from the transition to IFRS 17, partly offset by declines in Capital

Markets and Corporate Services. Expenses increased 16%, primarily due to the impact from acquisitions, partly offset by the realization of cost synergies and efficiency initiatives. Total PCL was $627 million, including a $154 million provision for performing loans compared with a total provision of $217 million in the prior year. Piyush will speak to these in his remarks.

Turning to Slide 9. There were some idiosyncratic items within the quarter that had outsized impacts on the total bank revenue growth. First, in Wealth Management, the transition to IFRS 17 resulted in variability from market-related impacts. While quarterly results in the prior year were restated. They are not necessarily representative of our future earnings profile as hedging strategies to mitigate the impact of changes in interest rates on our earnings began to be implemented in the second half of the year. We expect our quarterly insurance revenue stream to be more consistent with the first quarter during the remainder of this year.

Second, Capital Markets revenues reflected a weaker environment and client activity to start the year. In addition, the impact of proposed legislation that eliminates the deductibility of certain Canadian dividends reduced trading revenue by approximately $50 million from the prior year. Activity levels improved at the end of the quarter. And if markets remain constructive, we expect to reach $625 million to $650 million of average quarterly PPPT in Capital Markets during the remainder of the year.

Third, Corporate Services revenues decreased compared with the prior year and prior quarter. About 2/3 of the decline from the prior year was related to the earnings on excess equity that we were holding ahead of the closing of Bank of the West. We are also holding more liquidity on our balance sheet which always comes at a higher cost. In addition, market volatility during the quarter had a negative impact on the valuation of our hedge-derivative positions that runs through our P&L. This item can cause some variability but the cumulative impact converges to 0 over time. This was the largest contributor to lower sequential revenues as well as a lower benefit from purchase accounting market accretion. Barring unexpected market volatility, we expect our average quarterly revenues in corporates to be around negative $200 million to $225 million for the remainder of the year.

Moving to the balance sheet on Slide 10. Average loan growth was 16% year-over-year, driven by Bank of the West and good growth in Canadian P&C and Capital Markets. The sale of the RV loan portfolio in the quarter reduced average loans by $4.8 billion and period-end loans by $9.6 billion. Excluding the impact of the sale and the wind down of the indirect auto portfolio, average loans were up 2% sequentially on a constant currency basis with growth both -- in both business and government and consumer lending. Average customer deposits increased 19% year-over-year due to Bank of the West and higher balances in Canadian P&C and Capital Markets. Sequentially, period-end deposits were up 2% on a constant currency basis.

Turning to Slide 11. On an ex-trading basis, net interest income was up 12% from the prior year and net interest margin was up 3 basis points driven by higher margins in our P&C businesses, partially offset by lower net interest income in Corporate Services. Net interest margin was down 6 basis points from last quarter, reflecting continued pressure from the overall competitive deposit environment and deposit migration, net of benefits from reinvestment at higher rates. The total bank margin was also impacted by lower net interest income related to net accretion of purchase accounting fair value marks and risk transfer transactions, including the sale of the RV loan portfolio. In Canadian P&C, NIM increased 3 basis points, mainly due to favorable balance sheet mix, partly offset by lower deposit margins due to the continued migration to term deposits.

In U.S. P&C, NIM remained flat as favorable changes in balance sheet mix were offset by lower deposit margins as customers migrate to higher cost deposits. During the remainder of the year, we expect relative stability in our overall margin as the benefit of reinvestment of equity and non-maturity deposits at higher yields offset pressures from higher deposit costs.

Moving to Slide 12. Expenses increased 16% from the prior year, mainly due to the impact from acquisitions. The current quarter included an $84 million benefit from the consolidation of certain U.S. benefit plans. Sequentially, expenses were down 4%, mainly reflecting the higher realized Bank of the West cost synergies and additional operational efficiency savings. These more than offset the impact of stock-based compensation for employees eligible to retire and seasonality of benefits that is recognized in the first quarter of each year which had a combined impact of $280 million. As Darryl mentioned earlier, we have been very successful on delivering on our expense commitments. We now have achieved the full US$800 million in the Bank of the West run rate cost synergies per our commitments and we have been progressing well on the remaining enterprise operational efficiencies we announced last year.

To date, we have realized $325 million of the $400 million run rate expense savings that we are targeting to achieve by the end of the fiscal year. Based on our current expectations, the first quarter should be a low point for revenues and a high point for expenses for this fiscal year. And therefore, we remain confident in our ability to deliver positive operating leverage starting the second quarter and for the full fiscal year.

Turning to Slide 13. Our capital position continues to strengthen with a common equity Tier 1 ratio of 12.8%, up 30 basis points from the prior quarter, driven by internal capital generation, shares issued under the dividend reinvestment plan and the benefit from the sale of the RV loan portfolio. These were partially offset by the FDIC special assessment charge and higher source currency RWA, reflecting higher market and operational risks and net asset quality changes. The combined impact of regulatory capital developments and adoption of IFRS 17 effective this first quarter did not have a significant impact on our capital position.

Moving to the operating groups and starting on Slide 14. Canadian P&C delivered net income of $925 million, down 3% year-over-year. PPPT of $1.6 billion increased a strong 8%, offset by higher provisions for credit losses. Revenue of $2.8 billion was up 9%, driven by growth in net interest income reflecting both solid balance growth and higher margins. Noninterest revenue increased 6%, primarily due to the acquisition of AIR MILES. Expenses were up 9% and reflecting the inclusion of AIR MILES and higher technology costs and down 4% from the prior quarter, driven by lower employee-related costs and operational efficiencies. Loans were up 5%

year-over-year with good growth across mortgages and commercial loans and increased 1% from the prior quarter. Deposits were up 11% year-over-year, with retail deposits up 10% and commercial deposits up 12% and reflecting continued growth in term products. Deposits increased 2% sequentially.

Moving to U.S. P&C on Slide 15. My comments here will speak to the U.S. dollar performance. Net income was $475 million, down 4% from the prior year with PPPT growth of 19%, offset by higher provisions for loan losses. Sequentially, revenue was up 1%, driven by an increase in net interest income on higher deposit balances. Expenses declined 4% quarter-over-quarter, reflecting benefits from expense management and our focus on operational efficiencies. Loans were up 48% from the prior year driven by Bank of the West. Excluding the impact of the RV loan portfolio sale, average loans were up 2% sequentially, with growth across both mortgages and commercial loans. Deposits increased 45% year-over-year and 2% sequentially, driven by strong growth in term and money market deposits.

Moving to Slide 16. BMO Wealth Management net income was $241 million, up from $160 million last year. Wealth and Asset Management net income of $188 million decreased 7% from the prior year. Contributions from Bank of the West and growth in new client assets were more than offset by lower net interest income due to migration to term deposits and higher expenses. Insurance net income was $53 million compared with a loss of $43 million in the prior year, primarily due to market-related impacts in the prior year, reflecting the transition to IFRS 17. Expenses were up 8%, mainly due to higher employee-related costs, including impact of Bank of the West and were up 1% sequentially.

Moving to Slide 17. BMO Capital Markets net income was $408 million compared with $495 million in the prior year, reflecting weakness in the market environments. Revenue in Global Markets was down 13%, reflecting lower trading revenue. Investment and corporate banking revenue was up 5% on higher underwriting and advisory fees. Expenses were up 1% driven by technology costs, partially offset by lower performance-based compensation.

Turning now to Slide 18. Corporate Services net loss was $316 million compared with $180 million in the prior quarter and $114 million in the prior year. The widening of the net loss was driven by the revenue items previously discussed, partially offset by lower expenses.

To conclude, the banking environment is at a point in the cycle where the outlook for revenue growth is more constrained in the near term. In response, we are delivering on our committed expense savings to deliver PPPT growth and positive operating leverage. At the same time, we are focusing on investing for growth, allocating additional resources to areas where we have expanded our revenue opportunities through acquisitions and to businesses where we are capturing market share profitably to build continued shareholder value. We are cognizant that we need to execute with discipline and our track record in risk and expense management should be a strong proof point for such accountability.

I will now turn it over to Piyush.

Piyush Agrawal

Thank you, Tayfun and good morning, everyone. Starting on Slide 20. The total provision for credit losses was $627 million or 38 basis points. Impaired provisions for the quarter were $473 million or 29 basis points, up 4 basis points from prior quarter, reflecting the continued impact from tighter monetary policy.

Credit performance remains well within our expectations and was driven by strong risk management discipline across the bank and the benefit from our risk mitigation actions over the last few years. Canadian retail impaired losses were $204 million, up $14 million from prior quarter and U.S. retail impaired loan losses were $80 million, up $20 million. Consumer loan losses in both Canada and the U.S. reflect higher delinquencies in credit cards and other personal loans, reflecting increases in customer insolvencies which in Canada are now above pre-pandemic levels. Also of note, the discontinued indirect auto business provisions are now reported in Corporate Services and have increased in line with industry trends. Canadian commercial impaired loan provisions were $34 million, down $8 million from last quarter and U.S. commercial impaired provisions were $103 million, up $20 million, primarily due to higher losses in the transportation and retail trade sectors. Capital markets impaired losses were $11 million, flat to previous quarter.

Moving to Slide 21. Performing provision for credit losses of $154 million primarily reflected portfolio credit migration and model updates, net of changes in expert credit judgment. Negative credit migration which began in the second quarter of last year is not yet over but we do expect it to slow up late during the remainder of the year. Also of note is an $87 million release of performing allowance related to the RV loan sale. This release is outside of the $154 million build and netted in the noninterest revenue line against the loss on the sale of the RV portfolio that Tayfun referenced in his remarks. We are comfortable that our total performing allowance for Q1 of $3.5 billion provides appropriate coverage of 55 basis points over our performing zones and 2.4x trading 4-quarter impaired losses given the credit profile of our current portfolio and our forecast for impaired losses.

Turning to Slide 22 on impaired loans and formations. Bank-wide impaired formation slowed by $400 million from prior quarter to $1.4 billion. Gross impaired loans increased to $4.3 billion or 65 basis points with the increases coming primarily from health care and manufacturing.

On Slide 23, we provide an overview of our business and government portfolio which remains a key differentiator for the bank. The portfolio is well diversified across geographies and industries, highly secured and well structured. Throughout market cycles, we have maintained consistent and disciplined underwriting standards as evidenced by the portfolio quality and strong performance over time. Our expertise in workout practices consistently results in lower losses on impaired loans with a focus on helping clients return to performing status. As expected, inflation and monetary tightening are impacting businesses and resulting in negative migration. However, 54% of this portfolio continues to be investment grade with low impairment level of less than 1%.

On Slide 24, we provide an overview of the Canadian mortgage portfolio that continues to perform very well. We've provided additional information on the impact of higher interest rates on customer payments, while higher rates are expected to impact borrowers and renewal or refinancing, our internal analytics indicate that customers have the capacity to absorb these higher payments. In fact, over $19 billion of mortgages have now renewed in this higher rate environment and they continue to exhibit good payment performance. Additionally, our outreach to customers continues to be successful with many taking actions, resulting in a significant reduction in mortgages that are in negative amortization by over $7 billion in this quarter alone.

To conclude, we continue to expect that the higher level of interest rates and slowing economic activities will be reflected in somewhat higher impaired loss rates in the range of low 30 basis points for the year with some variability quarter-to-quarter. But given the quality and the diversification of our portfolio, our high allowance coverage and strong risk management capabilities, we remain well positioned to manage the current environment and emerging risks.

With that, I will now turn the call back to the operator for the Q&A portion of this call. Thank you.

Question-and-Answer Session

Operator

[Operator Instructions] And the first question is from Ebrahim Poonawala, Bank of America.

Ebrahim Poonawala

I guess I had a question just around balance sheet positioning, maybe Tayfun. One, talk to us around the U.S. P&C business. I look at the loan-to-deposit ratio everything that I hear from the U.S. banks has significant focus on liquidity, lower loan-to-deposit ratios. Could you give us a perspective on how you are thinking about liquidity within U.S. P&C where that loan-to-deposit ratio should gravitate. And then the second question is the -- from a capital and RWA optimization standpoint, how much more there to go? I mean, I understand banks are constantly optimizing for RWA. But from an investor standpoint, RWA optimization leads to hit to earnings and revenue. So just trying to understand the risk of earnings or revenue tied to these actions?

Tayfun Tuzun

Thank you for both questions. Let me actually start with the second one first. I understand why the question first references in impact of these transactions but we actually look at it differently. We look at this as not necessarily taking away from our revenues but creating the potential for more revenue growth and for expanded relationship growth in all of our businesses, whether it applies to commercial or consumer because these create -- first of all, these are ROE accretive transactions. So in that sense, we are creating more room on our balance sheet, not to sacrifice growth but actually to grow stronger and faster, both in the U.S. and in Canada. So that's important. I think I highlighted last year that during the fiscal year, the impact of these transactions would be about $400 million last year. This year, it will probably be a bit higher because we have more transactions. But the growth impact on our company of these transactions and the optimization of capital is very significant.

On the U.S. side, with respect to the balance sheet positioning, we feel actually very good both on the personal side as well as the commercial side with deposit growth. We have -- obviously, Bank of the West gives us an extra ump in terms of connecting with more customers and growing the deposit base, while also our fairly efficient treasury management platform gives our commercial business expanded opportunities in growing deposits. In an area where we have a bit more muted loan growth compared to our historical levels, we expect this will continue to build liquidity. We've always emphasized over the past year or so that we are positioned very well with respect to our competitors, both from a capital perspective as well as from a liquidity perspective which gives us, I think, opportunities for market share growth.

Ernie and Nadim, I will invite you guys to comment on both questions.

Nadim Hirji

Sure. This is Nadim. Talking about the capacity creation from the risk transfer transactions and a commercial standpoint is extremely important for us. Darryl and Tayfun both mentioned the subdued loan demand environment which does exist. Businesses are still cautious wait and watch mode before making new capital investments, we're optimizing their balance sheet, reducing revolver utilization, especially in the working capital-heavy businesses. But what I will say is that customer sentiment has improved this quarter versus last quarter and I expect that trend to continue. And despite the environmental headwinds, mitigating this is our diversified portfolio and momentum in new client acquisition, including in our integrated treasury and payments platform in both countries.

If you look at Canada, although we showed flat quarter-over-quarter loan growth in the month of January, point-to-point, we had strong momentum and that momentum has continued into Q2. In the U.S. we showed quarter-over-quarter loan growth just under 2% which is at the higher end of our peer growth. And in both countries, our pipelines on loans and deposits has increased. So overall, the capacity creation is extremely welcomed on the commercial side and I believe, positions us extremely well. And as we've done through past cycles, we are now in a strong position to accelerate as the environment rebounds and take share. And this time, it's off of an even bigger platform.

Ebrahim Poonawala

Got it. Just one very quick follow-up, Tayfun, I think you mentioned revenue in Corporate segment negative $200 million to $225 million or $250 million [ph]; that's a pretty meaningful change from last year. If you don't mind, what do you think the net income or net loss contribution from Corp segment will be for the rest of the year?

Tayfun Tuzun

Look, I mean I think I gave you the revenue guidance, Ebrahim. Expenses are on the low end. As I've said before, we will give you some guidance for net income. But overall, I think the guidance on revenues should be a good level to forecast the net income piece as well. There's, of course, is corporate revenues are difficult to analyze from outside. I tried to clarify it with these idiosyncratic items. I'll be happy to give more details on that as well. Purchase accounting accretion does have an impact overall. But on a year-over-year basis, on revenues, the larger portion came from our earnings on equity in the first quarter of last year, that was almost 2/3 of the year-over-year change. And then, there were some higher liquidity costs compared to last year's first quarter.

On a quarter-over-quarter basis, on net interest income in corporates, it was a combination of purchase accounting accretion, change and then higher liquidity cost on net noninterest revenues. The impact came from the market volatility impact on fair market values on a portion of our hedge portfolio which always is sort of related to volatility during a quarter. But over time, that converges back to 0. Some quarters are positive, some quarters are negative. This quarter just happens to be a negative one. So our guidance on revenues is better for the rest of the year, barring any changes in market volatility.

Operator

The next question is from Meny Grauman, Scotiabank.

Meny Grauman

Maybe following up on Ebrahim's question. Darryl, I'm curious, if you look forward, would you say you'd be more cautious pulling the trigger on risk transfer transactions going forward, considering where your capital ratio is and considering the more challenged revenue environment? Maybe it's an obvious answer but I thought I'd pose it curious to your thoughts on that.

Darryl White

Yes. The short answer is we feel like we're in a pretty good spot. You look at our CET1 ratio at 12.8%. It would be inconsistent if we said that we're removing the DRIP discount. And at the same time, we felt capital constrained. We don't feel capital constrained. We're very pleased with the execution of risk transfer transactions. It's put us in part in the position that we're in.

It's helped us create the capacity for when the environment becomes more constructive. So as you know, we always look at these tools to optimize balance sheet performance. It's not just for risk mitigation but it's for the creation of future opportunities as Tayfun summarized just now. But as I look out today, we feel pretty comfortable in the organic capital generation on our balance sheet.

Meny Grauman

And then maybe just a question for Piyush in terms of your guidance on the impaired loan PCL. Just wondering if you could provide a little more guidance in terms of timing? When do you expect to see -- what quarter you expect to see this peak? And if you could talk about your outlook for small business, especially from the impairments perspective, I think it's pretty clear what's happening on the consumer side in terms of the unsecured book of business. But what are you seeing on the small business side? And where is that expected to go?

Piyush Agrawal

Sure. So two parts; let me just first provide the broader impaired guidance. I think I've been guiding to low 30s. And so while we've seen the steady pickup as expected in the credit environment, I think that's going to continue. There will be variability intra-quarter over the years. I would generally guide to say we expect a higher amount in the first 2 quarters. And if the rate cycle plays out as expected, it should start trading off by the end of the year. But again, the macro assumption there is how the rate cycle plays off. As you know, we are beginning -- we are seeing continued resiliency by the Canadian consumer when it comes to the mortgages. So that's been a very good book for us. But then on the unsecured side, the insolvencies that are showing up through the Canadian consumer is what's reflective of the impaired losses.

And the challenge is that even if the rate cycle changes, it will take a couple of quarters for the transmission to flow through. I think the better piece, I would say is even though we don't expect Q2 rates to come down, it's very important for business, government sentiment that if we are closer to rate cycle changes in Q3 and 4, I think you'll start seeing upgrades. So the impaired loan losses, I'm sticking to our guidance of the low 30s. And so I'm very pleased with where we landed at 29 basis points and I expect that's going to continue with some variability, like I said, in that range. On your small business question, it's a very small part of our overall book; there is stress in Canada.

Again, if you look at business banking insolvencies coming out of COVID, there has been a huge pickup but we continue to manage. There are certain sectors that are more stressed but our risk underwriting criteria captures that. And so that's not a big mover of the dial in the overall impaired losses as we go forward.

Operator

The next question, Mario Mendonca, TD Securities.

Mario Mendonca

Tayfun, I appreciate your comments on corporate. Can I ask you to look at it in a slightly different way, more on from a consolidated perspective on Page 15 of your supplement. When you talk about revenue associated with the hedging activity being weaker in the quarter or a drag this quarter, are you specifically referring to that other revenue line the $44 million adjusted this quarter. Is that what you're referring to?

Tayfun Tuzun

It is in noninterest income, Mario. This item is not in net interest income. It's in noninterest income.

Mario Mendonca

Sorry, that's what I meant. I mean noninterest income revenue like the -- I hate to say it but like the other line is what I'm...

Tayfun Tuzun

Correct. Yes.

Mario Mendonca

And so that number can move around a fair bit. Can you talk about the dynamics that caused it to be a fair bit weaker like much lower than previous quarters?

Tayfun Tuzun

Yes. So that will be impacted by the overall interest rate volatility in the markets. And as you know, the November through January period was relatively volatile. But there will be quarters when that number will be positive. This one was a negative quarter. Over the life of the portfolio, it will converge by definition to 0. So that's the reason why we called an idiosyncratic item this quarter. It will not repeat in the same manner. And it's difficult for us to give you some guidance because we don't have a way to necessarily appropriately predict market volatility.

Mario Mendonca

And for clarity, there's no other line income statement sort of revenue line that benefited...

Tayfun Tuzun

No.

Mario Mendonca

No. So that's just purely the effect there. Okay. The next sort of similar type of question relates to the insurance investment result. I would have expected that line to be relatively steady unless there were credit charges or fair value charges in the quarter. So with that investment result looking so weak or negative $9 million. Can you talk about what drove that?

Tayfun Tuzun

I assume you are comparing this quarter to last quarter...

Mario Mendonca

Over the last few quarters.

Tayfun Tuzun

Yes. So this is purely related to the transition in our business from IFRS 4 to IFRS 17. And as the year went on in fiscal year '23, we started hedging our interest rate sensitivity in the second half of the year to prepare for the expected sensitivity levels under IFRS 17 and which has caused an uptick in revenues in the third and fourth quarters of last year. So now that we are firmly in the year having made the transition, our outlook for that line is going to be fairly static going forward. So you will not see a similar volatility and this quarter's level is more indicative for future revenues in our insurance line.

Mario Mendonca

So you'd expect to be close to zero insurance investment income?

Tayfun Tuzun

Yes. I mean, I think overall revenues in insurance was around $80 million or something like that. So that should be our guidance. That is our guidance for the next few quarters.

Mario Mendonca

Understood. Now Darryl, maybe you quickly, I understand that when transactions are done particularly in the U.S., it has the effect of hurting the ROE in the near term and then as synergies are materialize and you're successful in your transaction, ROE in that business should improve. First of all, is that your view on how the U.S. ROE should migrate? And what is an acceptable ROE in that U.S. business over time?

Darryl White

Yes. So it's a good question, Mario. So the answer to your first question is yes. And we're currently, I would say, in the inflection point of the journey on your question. So if you go back and look at the benefits that have come and then the benefits that still are expected to come. Look, the conversion was, by all measures, world-class. The marketing campaigns are in flight. The cost synergies we've talked about. We've exceeded the initial target. And by the way, I just want to clarify on that when we say we're run rating at $800 million of synergies. That's as of February 1. That was not as of the average of the first quarter. So there's more in that tank for all of you as the rest of the year goes on than there was in the first quarter. The capital, as you know, has been built since the acquisition and we've held on to the deposits quite nicely in an environment where deposits have fled the system. So do we expect the ROE to accrete from there?

You bet we do because we haven't yet realized the benefit of the revenue synergies that we've also talked about. And so another way to think about it is that we put out in the window for you all a $2 billion PPPT target for the bank, then known as Bank of the West asset that we bought and we're standing by that because we see all of the various metrics that lead up to that as enablers coming in quite nicely as we speak.

Mario Mendonca

A double-digit ROE in the U.S. then seems entirely reasonable over time.

Darryl White

Yes, we've been there before and we'll be there again when we execute on this.

Operator

The next question is from Gabriel Dechaine, National Bank Financial.

Gabriel Dechaine

First question for Piyush. You talked about your expectation for impaired PCL, the trajectory. I'm maybe putting words in your mouth here, hopefully I'm not but you're sounding like a little bit of an uptick here in Q2 but improving in the second half as rate cuts materialize, correct me if I'm wrong there. I'm wondering about what about the performing provision. If rate cuts keep getting pushed back for whatever reason, is there any upward pressure on your performing provision? Like what's built in there? If you can dumb it down to that level, that would be great, so that we know what to expect?

Piyush Agrawal

Sure, Gabriel. So on the impaired PCL, look, in any quarter, I wouldn't take 1 quarter's number as the number, it's going to be variable quarter-to-quarter as things happen. So this credit cycle has come off for a long time and it's come with a cheaper slope. So it's picked up very quickly which is why you've seen the rapid buildup in impact PCLs. And I think in Q2, my expectation is, as this trend continues, it will be a tad bit up. I can't exactly point to what basis points. We also have, as you know, risk mitigation actions in place, so we benefit from those. And so depending on the name that's impaired versus what's in our risk management, risk mitigation, we will get some benefit. So yes, a tad bit up but I think then down and I look at it over the year and over the year, like I said, I feel very confident about. At the moment, if something changes, obviously, we'll keep you posted.

I think the performing PCL is a little bit of a longer story. Let me take a few seconds to just unpeel or explain the build in the context of what we did this quarter. So the first piece of the $154 million build is, of course, the credit migration that causes the upward build. The second piece is really around a few modest updates. And the model updates are as we completed the integration of Bank of the West models, we got a richness of data that allowed us or guided us in the expected losses of our own existing portfolios under different economic scenarios. We've been considering many of these variables through export credit judgment. This time, we let go of the expert credit judgment because now it's built into the model. And I see this more as a onetime from an M&A and the integration. And so when we have the next M&A, we'll have more data from another bank. But at this time, the expert credit judgment flows into the updated models which I think are good because they inform us of what can happen through different trajectories.

So we'll continue to keep our models in good standing as required but the integration impact, like I said, was a onetime event. And so that's the $154 million. I do want to point out that you will see on Page 21 in our foreign exchange and other, a larger release and that larger release actually includes an $87 million release for our RV portfolio, that typically would have gone and netted against the $154 million but under accounting standards, it's reflected in or gain or loss on sale of the RV book. So that's in the revenue line. And so if I just bring all of this full circle, what's really important is where we land on the outcome. And so our Q1 provision at $3.5 billion is a tad bit lower than where we began the quarter and our coverage is 55 basis points which is very similar to what you've seen in the last few quarters. And so, I feel very good about our prudent coverage of 55 basis points in the credit cycle where we are.

And of course, we'll continue to look at scenarios and look at how the data in our credit portfolio shows up as we get to making decisions every quarter. So just again, to unpeel that to give you some more information how we reach where we reached.

Gabriel Dechaine

Okay, great. I might need to follow up on that but Tayfun in the interest of time. Can you give me the numbers that they're associated with your credit mark. What's been recognized to date as far as, I guess, recoveries? And what the remaining balance is and the time line you expect to see the most impact from that unwind?

Tayfun Tuzun

I assume you're talking about the purchase accounting accretion numbers. Yes, I think we have not necessarily given out actual numbers, Gabriel. But I think the year-over-year change in purchase accounting accretion which may give you some aspects of the impact on revenues is probably $250 million to $300 million.

Gabriel Dechaine

Lower this year.

Tayfun Tuzun

Correct. Compared to last year, full year over full year.

Gabriel Dechaine

Yes. Q1 versus Q1 -- or I'm not sure, I follow you, actually.

Tayfun Tuzun

It's a -- so if you add up purchase accounting accretion for the full year '23 and compare it for the full year of '24, you'll probably see about a $300 million type of decrease in purchase accounting accretion.

Gabriel Dechaine

Okay, here you go. I was overthinking it. And talk to you end of March, Tayfun.

Operator

Next question is from Doug Young, Desjardin Capital Markets.

Doug Young

I'll make it just quick. Tayfun, just that purchase accounting change year-over-year, how much of that is just a normal roll off? How much of that was because of risk transfer transactions or sale of portfolios like the RV book?

Tayfun Tuzun

A portion of that, clearly, what sped up some of the accretion in the earlier parts of the acquisition does relate to the RV transaction because we captured some of that accretion in our net gain calculation. So that's the part of the reason why going forward, accretion numbers have come down. And there is there's a natural degradation because as we continue to capture more of it. And in these types of acquisitions, you tend to capture more at the beginning parts of the cycle and then it just gets reduced as you go down the line. But it did have -- the RV transaction did have a discrete impact.

Doug Young

Okay. And then, Darryl, in your prepared remarks, you talked about the expense savings from Bank of the West and the other $400 million from other actions. And you talked about accelerating and you talked about the $800 million being as a sub first and more to come. You seem excited that there's more to come. Are you indicating that you think you can get more than what you've talked about? And then I guess the flip side of this or to continue on with that discussion around expenses, how confident are you around achieving the positive operating leverage? So I'm just curious about all the different moving pieces on the expense and the revenue side that gives you that confidence.

Darryl White

Yes. No, I wasn't -- Doug, I want to be clear. I wasn't signalling that we think there's necessarily more to come. What I was commenting on is the point that we're at in the trajectory on the delivery and reminding you all that of the $800 million, we're clocking in at that post February 1, not entirely pre-February 1. And then of the $400 million -- and by the way, we mix currencies on you on this. So I'll remind you the $800 million is U.S. and then the $400 million is. And on the $400 million, I think Typhoon explained that we're $325 million through it and then we've got the other $75 million to go. So as -- what I was trying to do for you for your model, Doug, is to emphasize that as you go through Q2 and then particularly into Q3 and Q4, the totality of the expense delivery programs increase for us relative to what we're delivering for you right now. Is that helpful?

Doug Young

That is. Yes.

Operator

The next question, Mike Rizvanovic, KBW Research.

Mike Rizvanovic

Just a quick question on your margin trajectory here. So down at the all bank level and then up in Canada and I think flattish in the U.S. So I'm wondering when you guide to a higher negative

NII line in corporate, is that where we should see the improvement, if, in fact, you are able to get some margin accretion at the all bank level maybe second half of this year or perhaps just heading into 2025. I'm just wondering where those moving parts will end?

Tayfun Tuzun

Yes. I think this quarter, we have seen a little bit of a higher deposit price competition than we were expecting. That's the reason why it came down 6 basis points. In terms of the NII line in Corporate Services, yes, we do expect that line to come down from the Q4 levels which will somewhat contribute to the stability of the margin because this concept of higher reinvestment yields balancing the deposit pricing competition and term migration is real and it's coming through across -- we do reflect that not only on the corporate side but also in businesses. So we're pretty confident that the outlook for the rest of the year is very tight and stable from here.

Mike Rizvanovic

Okay. So you're still confident that you could see margins higher all bank level, even if rates are declining possibly towards the end of the year and heading into 2025. Is that a fair assessment?

Tayfun Tuzun

Yes. Our outlook does contain an interest rate view that the Fed and Bank of Canada will start pulling the short-term rates down. I would not guide you to a significant increase in our margin. If it is, it's a couple of basis points, I'm more guiding you towards a stable enterprise level consolidated NIM outlook.

Mike Rizvanovic

Okay, that's super helpful. And then, just I wanted to quickly ask Darryl. I think in your prepared remarks, sorry, I think you made a reference to rates coming down which should help across different aspects of your business lines. And I'm just wondering if you could sort of qualify that. When you're seeing lower rates, are you just talking about the short end of the curve Bank of Canada? Or are you, in fact, expecting and across the spectrum or across the yield curve duration like an across the board movement in rates downward? I'm just wondering what you're sort of modeling in your own projections there?

Darryl White

Yes. Look, Mike, I'm happy to take you through the sort of base case with the obvious notation that this has been a difficult game for anybody on the planet to be forecasting. But our base case does suggest that in the second half of the year, probably starting around July, we will begin to see a reduction in the short-term administered rates, so both in Canada and in the U.S. As far as the amount that we expect over the course of the second half of the calendar year, if you want to think about it that way, remembering that the calendar year is not the same as the fiscal year for the Canadian banks, of course, we're in the neighborhood of 100 basis points from the July period to the end of the calendar year, not capturing all of that in our fiscal naturally. And look, as you look at the longer end of the curve, I think we should probably see some commensurate reduction there as well but maybe not to the same degree. So you could see some steepening as we go through. That's our base case. And you will all have your own base cases to overlay on that but that's the way we see it relative to the economic performance that we expect in both the Canadian and U.S. economies.

Operator

Next question from Darko Mihelic, RBC Capital Markets.

Darko Mihelic

In the Interest of time, I'll be very quick. You mentioned that the change in taxation on dividends is about a $50 million reduction in trading revenue. I'm assuming that's a 1-month impact, should I just be annualizing that? Or is there a better way to tell me the headwind from that maybe from an earnings perspective for 2024?

Tayfun Tuzun

Actually, it is not just a 1-month impact. It covers most of the quarter. I would suggest that if you are going to add it in your model, I would use like a $60 million type of number for -- on a quarterly basis for the remainder of the year. So the $50 million [ph] doesn't go to $100 million [ph], it just goes to $60 million [ph] on a quarterly basis.

Darko Mihelic

And that's just revenues? Or are you talking about taxes?

Tayfun Tuzun

Revenues in Capital Markets.

Operator

Next question from Paul Holden, CIBC.

Paul Holden

A couple of follow-up questions to what I think are important discussions on the call. First, just with respect to balance sheet or asset growth. Obviously, you've taken a number of actions over the last 12 months to manage assets and RWA. It sounds like maybe we've reached an inflection point, both because you now have the capital to grow the balance sheet again. And b, to the points being raised, you're starting to see improved demand as well. So maybe give us a sense of how the balance sheet may grow from here through '24? And what kind of impact declining interest rates might have on that view as well?

Tayfun Tuzun

Yes. So I mean, look, as both Darryl and I said, we have proactively executed a number of these transactions to create room on our balance sheet for growth. And as -- again, I'm going to turn it over to Ernie and Nadim in terms of asset growth for the future but we believe that we've prepared our balance sheet both from a capital and liquidity perspective for growth in the future. In terms of timing, I'm going to turn it over to you guys.

Erminia Johannson

I can start, it's Ernie. If I think about Canada, we do see us growing probably in the low mid-single digits on mortgages and our card book, et cetera. In the U.S., I would say we're probably in the low single digits on our loan growth, just a reflection of our growth position given our marine RV sale and our indirect auto exit. I'll turn it over to Nadim for his comments.

Nadim Hirji

Okay. For the commercial side, I would say to expect low single-digit loan growth both sides of the border in the near term, building to a more mid-single-digit loan growth as we move into the latter half of the year which is the guidance that we had originally provided last quarter which was mid-single digit by the end of the full year.

Paul Holden

Okay. And then, Darryl, I want to come back to sort of the line of questioning Mario had on the ROE but his question was specific to the U.S. bank. I want to ask a similar question for the Canadian bank, just given all of the changes that have happened with CET1 requirements, Basel III, your increased usage of risk transfer, et cetera. Does anything change in terms of your long-term ROE expectations? Or is this still a bank that should be able to produce a mid-teen ROE when things normalize?

Darryl White

Yes. You'll have seen, Paul and it's a good question. You'll have seen when we updated our medium-term target disclosure at the end of the year. We didn't change the medium-term ROE target. So that's a conscious decision. That's an active decision. So when we say we've got an objective of 15% or higher. That remains the case. So there isn't a question that the industrial changes have had an impact on the ability to deliver that. And it's also the case that if you go back a couple of years, we were closer to 20% than we were at 15%. So with that as a buffer as I look out going forward and we execute against these programs, we're holding that. And I remind everybody that's a medium-term target.

Operator

Thank you. This is all the time we have for questions today. I would now like to turn the meeting over to Darryl White. Please go ahead.

Darryl White

Well, thank you, everyone, for your questions. We apologize for going a little long but we wanted to get your questions in, given that we started a little late. As you've heard this morning, we're proactively positioning ourselves for an environment of future growth and we're confident in the power of this integrated North American franchise that delivers consistent and differentiated performance to help our clients make real financial progress. We look forward to speaking to you all again in May. Thanks, everyone.

Operator

Thank you. The conference has now ended. Please disconnect your lines at this time. And we thank you for your participation.