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Q4 2022 Earnings Call

Company Participants

- Jamie Dimon, Chairman and Chief Executive Officer
- Jeremy Barnum, Chief Financial Officer

Other Participants

- Andrew Lim, Analyst
- Betsy Graseck, Analyst
- Ebrahim Poonawala, Analyst
- Erika Najarian, Analyst
- Gerard Cassidy, Analyst
- Glenn Schorr, Analyst
- John McDonald, Analyst
- Ken Usdin, Analyst
- Matthew O'Connor, Analyst
- Mike Mayo, Analyst
- Steven Chubak, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. Welcome to JPMorgan Chase's Fourth Quarter 2022 Earnings Call. This call is being recorded. Your line will be muted for the duration of the call. We will now go live to the presentation. Please standby.

At this time, I would like to turn the call over to JPMorgan Chase's Chairman and CEO, Jamie Dimon; and Chief Financial Officer, Jeremy Barnum. Mr. Barnum, please go ahead.

Jeremy Barnum {BIO 15409544 <GO>}

Thank you very much. Good morning, everyone. The presentation is available on our website, and please refer to the disclaimer on the back.

Starting on Page 1, the firm reported net income of $11 billion, EPS of $3.57 on revenue of $35.6 billion, and delivered an ROTCE of 20%. This quarter, we had two significant items in corporate, a $914 million gain on the sale of Visa B shares, offset by $874 million of net investment securities losses.

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Touching on a few highlights, combined credit and debit spend is up 9% year-on-year, with growth in both discretionary and non-discretionary spending. We ended the year ranked number one for global IB fees with a wallet share of 8%, and credit continues to normalize, but actual performance remains strong across the company.

On Page 2, we have more on our fourth quarter results. Revenue of $35.6 billion was up $5.2 billion or 17% year-on-year. NII ex Markets was up $8.4 billion or 72%, driven by higher rates. NIR ex Markets was down $3.5 billion or 26%, predominantly driven by lower IB fees, as well as management and performance fees in AWM, lower auto lease income, and home lending production revenue. And Markets revenue was up $382 million or 7% year-on-year.

Expenses of $19 billion were up $1.1 billion or 6% year-on-year, primarily driven by higher structural expense and investments. And credit costs of $2.3 billion included net charge-offs of $887 million. The net reserve build of $1.4 billion was driven by updates to the firm's macroeconomic outlook, which now reflects a mild recession in the central case, as well as loan growth in card services, partially offset by a reduction in pandemic-related uncertainty.

Looking at the full year results on Page 3. The firm reported net income of $37.7 billion, EPS of $12.09, and record revenue of $132.3 billion. And we delivered an ROTCE of 18%.

On the balance sheet and capital on Page 4, we ended the quarter with a CET1 ratio of 13.2%, up 70 basis points, primarily driven by the benefit of net income, including the sale of Visa B shares less distributions, AOCI gains, and lower RWA. RWA declined approximately $20 billion quarter-on-quarter, reflecting lower RWA in the Markets business, which was partially offset by an increase in lending, primarily in card services. Recall that we had a 13% CET1 target for the first quarter of 2023, which we have now reached one quarter early. So, given that, we expect to resume share repurchases this quarter.

Now, let's go to our businesses, starting on Page 5. Starting with a quick update on the health of US consumers and small businesses based on our data. They are generally on solid footing, although sentiment for both reflects recessionary concerns not yet fully reflected in our data. Combined debit and credit spend is up 9% year-on-year. Both discretionary and non-discretionary spend are up year-on-year, the strongest growth in discretionary being travel. Retail spend is up 4% on the back of a particularly strong fourth quarter last year. E-commerce spend was up 7%, while in-person spend was roughly flat. Cash buffers for both consumers and small businesses continue to slowly normalize, with lower income segments and smaller businesses normalizing faster. Consumer cash buffers for the lower income segments are expected to be back to pre-pandemic levels by the third quarter of this year.

Now, moving to financial results, this quarter, CCB reported net income of $4.5 billion on revenue of $15.8 billion, which was up 29% year-on-year. You'll notice in our presentation that we renamed Consumer & Business Banking to Banking & Wealth Management. Starting there, revenue was up 56% year-on-year, driven by higher NII on higher rates.

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Deposits were down 3% quarter-on-quarter, as spend remains strong and the rate cycle plays out, with outflows being partially offset by new relationships. Client investment assets were down 10% year-on-year, driven by market performance, partially offset by net inflows, where we are seeing good momentum, including from our deposit customer. Home lending revenue was down 46% year-on-year, largely driven by lower production revenue.

Moving to card services and auto, revenue was up 12% year-on-year, predominantly driven by higher card services NII on higher revolving balances, partially offset by lower auto lease income. Card outstandings were up 19%. Total revolving balances were up 20%, and we are now back to pre-pandemic levels. However, revolving balances per account are still below pre-pandemic levels, which should be a tailwind in 2023. And in auto, originations were $7.5 billion, down 12%. Expenses of $8 billion were up 3% year-on-year, primarily driven by investments, as well as higher compensation, largely offset by auto lease depreciation from lower volumes. In terms of credit performance this quarter, credit costs were $1.8 billion, reflecting reserve build of $800 million in card and $200 million in home lending; and net charge-offs of $845 million, up $330 million year-on-year.

Next, the CIB on Page 6. CIB reported net income of $3.3 billion on revenue of $10.5 billion for the fourth quarter. Investment banking revenue of $1.4 billion was down 57% year-on-year. IB fees were down 58%, in line with the market. In advisory, fees were down 53%, reflecting lower announced activity earlier in the year. Our underwriting businesses were affected by market conditions, resulting in fees down 58% for debt and down 69% for equity.

In terms of the outlook, the dynamics remain the same. Pipeline is relatively robust, but conversion is very sensitive to market conditions and sentiment about the economic outlook. Also, note that it will be a difficult compare against last year's first quarter.

Moving to Markets, revenue was $5.7 billion, up 7% year-on-year, driven by the strength in our macro franchise. Fixed income was up 12%, as elevated volatility drove strong client activity, particularly in rates and currencies and emerging markets, while securitized products continue to be challenged by the market environment. Equity markets was relatively flat against a strong fourth quarter last year. Payments revenue was $2.1 billion, up 15% year-on-year. Excluding the net impact of equity investments, it was up 56%, and the year-on-year growth was driven by higher rates. Security services revenue of $1.2 billion was up 9% year-on-year, predominantly driven by higher rates, largely offset by lower deposits and market levels. Expenses of $6.4 billion were up 10% year-on-year, predominantly driven by the timing of revenue-related compensation. On a full year basis, expenses of $27.1 billion were up 7% year-on-year, primarily driven by higher structural expense and investments, partially offset by lower revenue-related compensation.

Moving to the Commercial Bank on Page 7. Commercial Banking reported net income of $1.4 billion. Record revenue of $3.4 billion was up 30% year-on-year, driven by higher deposit margins, partially offset by lower investment banking revenue and deposit-related fees. Gross investment banking revenue of $700 million was down 52% year-on-year, driven by reduced capital markets activity. Expenses of $1.3 billion were up 18% year-on-year. Deposits were down 14% year-on-year and 1% quarter-on-quarter, primarily reflecting

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attrition of non-operating deposits. Loans were up 14% year-on-year 3% [ph] sequentially. C&I loans were up 4% quarter-on-quarter, reflecting continued strength in originations and revolver utilization. CRE loans were up 2% quarter-on-quarter, reflecting a slower pace of growth from earlier in the year due to higher rates, which impacts both originations and prepayment activity.

And then to complete our lines of business, AWM on Page 8. Asset & Wealth Management reported net income of $1.1 billion, with pretax margin of 33%. Revenue $4.6 billion was up 3% year-on-year, driven by higher deposit margins on lower balances, predominantly offset by reductions in management, performance and placement fees linked to this year's market declines. Expenses of $3 billion were up 1% year-on-year, predominantly driven by growth in our private banking advisory teams, largely offset by lower performance-related compensation. For the quarter, net long-term inflows were $10 billion, positive across equities and fixed income, and $47 billion for the full year. And in liquidity, we saw net inflows of $33 billion for the quarter and net outflows of $55 billion for the year. AUM of $2.8 trillion and overall client assets of $4 trillion were down 11% and 6% year-on-year, respectively, driven by lower market levels.

Finally, loans were down 1% quarter-on-quarter, driven by lower securities-based lending, while deposits were down 6% sequentially, driven by the rising rate environment, resulting in migration to investments and other cash alternatives.

Turning to Corporate on Page 9. Corporate reported a net gain of $581 million. Revenue of $1.2 billion was up $1.7 billion year-on-year. NII was $1.3 billion, up $2 billion year-on-year due to the impact of higher rates. NIR was a loss of $115 million and reflects the two significant items I mentioned earlier. And expenses of $339 million were up $88 million year-on-year.

With that, let's pivot to the outlook for 2023, which I will cover over the next few pages, starting with NII, on Page 10. Okay. We expect total NII to be approximately $73 billion and NII ex Markets to be approximately $74 billion. On the page, we show how the significant increases in quarterly NII throughout 2022 culminated in the $81 billion run rate for the fourth quarter and how we expect that to evolve for 2023.

Going through the drivers, the outlook assumes that rates follow the forward curve. Combination of the annualization of the hike in late December, the hikes expected early in the year, and the cuts expected later in the year should be a net [ph] tailwind. Offsetting that tailwind is the impact of deposit repricing, which includes our best guess of rate paid in both wholesale and consumer.

In addition, looking at balance sheet growth and mix, we expect solid overall card spend growth, as well as further normalization of revolving balances per account and modest loan growth across the rest of the company. We expect that this tailwind will be offset by lower deposit balances, given modest attrition in both consumer and wholesale. But it's very important to note that this NII outlook is particularly uncertain. Specifically, Fed funds could deviate from forwards, balance attrition and migration assumptions could be meaningfully different, and deposit product and pricing decisions will be determined by customer behavior and competitive dynamics as we focus on maintaining and growing primary bank relationships, and may be quite different from what this outlook assumes.

And further, the timing of all these factors could significantly affect the sequential trajectory of NII throughout the year. That said, as we continue executing our strategy of investing to acquire new customers, as well as deepen relationships with existing ones, and as we see the impact of loan growth, we would expect sequential NII growth to return, all else being equal. And just to finish off on NII, as the guidance indicates, we expect Markets NII for the year to be slightly negative as a result of higher rates. But remember, this is offset in Markets NIR.

Now, turning to expenses on Page 11. We expect 2023 adjusted expense to be about $81 billion, which includes approximately $500 million from the higher FDIC assessment. Going through some of the other drivers, we expect increases from labor inflation, which, while it seems to be abating on a forward-looking basis, is effectively in the run rate for 2023. An additional labor-related driver is the annualization of 2022 headcount growth, as well as our plans for a modest headcount increase here, all of which are primarily in connection with executing our investments. And on investments, while we are continuing to invest consistent with what we told you at Investor Day, it's a more modest increase than last year.

The team has remained consistent, and we will continue to give you more detail throughout the year, including at Investor Day in May. Of course, as is always true, this outlook includes continuing to generate efficiencies across the company. And finally, while volume and revenue-related expense was ultimately a tailwind for 2022, we are expecting it to be close to flat in 2023, which will be completely market-dependent, as always.

Moving to credit on Page 12. On the page, you can see how exceptionally benign the credit environment was in 2022 for the company across wholesale, card, and the rest of consumer. Turning to the 2023 outlook for card net charge-off rates, specifically, Marianne gave quite a bit of detail about this on a recent conference, and our outlook hasn't really changed.

So, to recap that story, the entry to delinquency rate is the leading indicator of future charge-offs and it is currently around 80% of pre-pandemic levels. We expect that to normalize around the middle of the year, with the associated charge-offs following about six months later. As a result, loss rates in 2023 will still be normalizing. So, while we anticipate exiting the year around normalized levels, we expect the 2023 card net charge-off rate to be approximately 2.6%, up from the historically low rate of 147 basis points in 2022, but still well below fully normalized levels.

So, let's turn to Page 13 for a brief wrap-up before going into Q&A. We are very proud of the 2022 results, producing an 18% ROTCE and record revenue in what was a quite dynamic environment. Throughout my discussion of the outlook, I've emphasized the uncertainty in many of the key drivers of 2023 results. And while we are ready for a range of scenarios, our expectation is for another strong performance. So, as we look forward,

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we expect to continue to produce strong returns in the near term, and we remain confident in our ability to deliver on our through-the-cycle target of 17% ROTCE.

And with that, operator, let's open up the line for Q&A.

Questions And Answers

Operator

Please standby. (technical difficulty) coming from the line of John McDonald from Autonomous Research. You may proceed.

Q - John McDonald {BIO 21440002 <GO>}

Hi, good morning, Jeremy. I wanted to ask about the NII outlook, Slide 10. The range of outcomes on deposit costs is quite wide. As you mentioned, it looks like 1.5% to 2% demonstrated there. Does the $74 billion NII line-up was kind of the midpoint of that? Maybe you could give some color about kind of the drivers of the $74 billion and where that lines up on this range of deposit cost outcomes?

A - Jeremy Barnum {BIO 15409544 <GO>}

Sure, John. I mean, I wouldn't take the chart on the bottom left too literally. That's supposed to give us stylized indication of the fact that relatively small changes in deposit rate paid for the company on average, as you well know, can produce quite significant impacts on the NII. And also, there's, as we have already talked about, a meaningful (technical difficulty). The outlook is our best guess, as Jamie says, and the drivers within that are the usual drivers. In wholesale, we would expect to see a little bit of continued attrition, especially of the non-operating type balances, and you're going to see some internal migration there out of noninterest-bearing into interest-bearing over time. In consumer, CDs are flowing right now and we're seeing good new CD production. We've got a 4% CD in the market as of this morning. And so, continued CD production and internal migration there will be a driver. And the rest of it is, well -- and of course, as I said in the prepared remarks, we do expect across the company modest deposit attrition as we look forward as a function of duty and the rate cycle and so on.

So, we've got best guesses for all of those in the outlook. And of course, the actual outcome will be different in one way or another, and we'll just run the business this year.

Q - John McDonald {BIO 21440002 <GO>}

Okay. Thanks. And on buybacks, how will you think about approaching buybacks and putting it in that mix of capital decisions that you have? And any thoughts on kind of the size or quantifying the potential buybacks?

A - Jeremy Barnum {BIO 15409544 <GO>}

Yeah, sure. So, sort of in the mode of like helping you guys out and put a number in the model, if you sort of look at the way we're seeing things, obviously, we've got another

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GSIB stuff coming next year, so, say, 13.5% target. And the -- sort of using your estimates, organic capital generation minus dividends, et cetera, and all of the elements of uncertainty there, I think a good number to use is something like $12 billion of buybacks for this year -- for 2023. But you know, of course, that buybacks are always at the end of our capital hierarchy.

So, we have better uses for the money. Those will come first, and the timing and the conditions of how much we do when is entirely at our discretion. And also, noting that we are potentially going to see a Basel III NPR sometime in the first quarter or maybe in the second quarter, and while that would be an NPR and it will only cover part of the surface area and it won't be final, so it's unlikely that it meaningfully shapes short-term decision-making. There will be some information content of that release that could shape our decisions as well.

Q - John McDonald {BIO 21440002 <GO>}

Got it. Thank you.

Operator

The next question is coming from the line of Erika Najarian from UBS. You may proceed.

Q - Erika Najarian {BIO 17048573 <GO>}

Hi, good morning. Jeremy, my first question is just, as you can imagine, following up on the NII line of questioning. Appreciate that there is a significant amount of uncertainty in this year's NII forecast, in particular. But to follow up with John's question, I'm wondering if you could give us sort of more specific guardrails with regards to what you are expecting for deposit attrition and deposit beta, in terms of the terminal deposit beta. I think the feedback I'm getting very early from investors is that they appreciate the headwinds that's occurring for NII this year. At the same time, you have been consistently beating what seemed like conservative NII expectations for 2022, including printing a giant $20.3 billion number in the fourth quarter. So, that's why I think the more specific guardrails could be very helpful, as investors try to figure out what their own expectations are versus that.

A - Jeremy Barnum {BIO 15409544 <GO>}

Thanks, Erika. So, look, I totally appreciate the desire for more specific guardrails. I would want that too if I were you. I do think that we're trying to be quite helpful by giving you a full year number, which, if we're honest, involves a lot of guessing about how things will evolve throughout the year. I think once you start giving guardrails, you implicitly assume that outcomes outside of the guardrails are very unlikely, and that's just a level of precision that we're just not prepared to get into, especially because in the end, as I said, a lot of the repricing decisions that we'll be faced with as a company are respond to data in the moment at a granular level in connection with the strategy, which is about growing and maintaining primary bank relationships, rather than chasing every dollar of balances at any cost.

So, in that context, we do expect modest balance attrition across the company for deposits, as I said. Jamie, you want to?

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A - Jamie Dimon {BIO 1484062 <GO>}

Yes. Erika, thank you. I just want to give a big picture about why -- and I do not consider $74 billion conservative. So, the Federal Reserve reduces balance sheet by $400 billion. $1.5 trillion came out of bank deposits. And so, investors can invest in T-Bills, money market funds and, of course, banks are competing for the capital money now. And banks are all in different places. Some banks start to compete heavily, some have a lot of excess cash and maybe compete less. But if you look at prior -- and forget what happened in 2016. I think you will make a huge mistake looking at that. We've never had cued [ph] this zero rates. We've never had rates go up this fast. So, I expect there will be more migration to CD, more migration to money market funds. Lot of people out there competing for it, and we're going to change savings rates.

Now, we can do it at our own pace and look at what other people are doing. We don't know the timing, but it will happen. And I just also want to point out that even at $74 billion, we're earning quite good returns. And that's not -- and we've always pointed out to you, sometimes you're over-earning and sometimes are under-earning. I would say, okay, this time we're over-earning on NII this quarter. We're maybe over-earning on credit, but maybe under-earning in something else. So, these are still very good numbers, and we're going to wait and see and we'll report to you. But I don't want to give you a false notions how secure it is.

Q - Erika Najarian {BIO 17048573 <GO>}

And my follow-up is exactly in that line of questioning. Let's zoom out for a second here to your point, Jamie. The returns are still good. You mentioned that your outlook already captures a mild recession. And I'm going to re-ask the question I asked in the third quarter. As you think about 2023, do you think JPMorgan can hit that 17% ROTCE that you laid out in Investor Day, even with the headwind in NII and a headwind in the provision?

A - Jamie Dimon {BIO 1484062 <GO>}

Yes, we can. But a lot of factors determine that, but yes we can. I think when we do Investor Day in May, we may give you a more interesting number, which is, what do we think our ROTCE will be if we have a real recession, which, I think, even in a real recession, it would probably equal the average industrial company, which is good. So, we're going to give you some detail around that, and those are still good returns and we can still grow. And 17% -- remember, 17% is very good if you can compound; some growth is [ph] 17%. Those are extraordinary numbers. And I also want to point out, we don't know exactly what the capital needs to be at this point, and we have to modify that at one point.

A - Jeremy Barnum {BIO 15409544 <GO>}

And Erika, let me just add a very minor clarifying point, as I want to be crystal clear about this. So, as you know and as we discussed a lot, like, through the pandemic in terms of the way we construct and build the allowance, well, it's anchored around our economists' central case forecast, which, as you correctly say, is a mild recession. Through the way we weigh the different scenarios and a range of other factors, the de facto scenario that's embedded in the forecast is actually more conservative than that from an allowance perspective. So, we just want to be clear about that.

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Q - Erika Najarian {BIO 17048573 <GO>}

Perfect. Thank you.

Operator

The next question is coming from the line of Ebrahim Poonawala from Bank of America Merrill Lynch. You may proceed.

Q - Ebrahim Poonawala {BIO 17612305 <GO>}

Good morning. I guess, maybe Jeremy, just following up on the credit assumptions underlying, if you could give us a sense of what's assumed in that reserve ratio at the end of the year, be it in terms of the unemployment rate and your outlook around just a lot of chatter around commercial real estate, the struggles to reprice in the current rate backdrop, are you concerned about that? Are you seeing pain points in CRE customers, given what's happening with cap rates and then just the overall backdrop today?

A - Jeremy Barnum {BIO 15409544 <GO>}

Sure. Let me just do CRE quickly, Ebrahim. As you know, our sort of multifamily commercial term lending business is really quite different from the classic office type business. Our office portfolio is very small, Class A, best developers, best location. So, the vast majority of the loan balances in commercial real estate are that sort of affordable multifamily housing, commercial term lending stuff, which is really quite secure from a credit perspective for a variety of reasons. So, we feel quite comfortable with the loss profile of that business.

And so -- yeah, so then you were asking about the assumptions in credit overall. So, yeah, as I said, like, the central case economic forecast has a mild recession. And if I remember correctly, unemployment peaking at something like 4.9%. The adjustment that we make to the scenarios to reflect slightly more conservative outlook have us imply a peak unemployment that's notably higher than that. So, I think we have appropriately conservative assumptions about the outlook embedded in our current balances. And then the trajectory that we talked about in the presentation, they're definitely -- can capture something more than a very mild soft lending, but of course, it wouldn't be appropriate to reflect a full-blown hard lending in our current numbers, since the probability of that is clearly well below 100%.

Q - Ebrahim Poonawala {BIO 17612305 <GO>}

Noted. And I guess, just as a follow-up on -- you've managed RWA growth pretty well, when you look at, like, loan growth year-over-year versus RWA stayed relatively flat. As we think about just managing capital, how should we think about the evolution of RWA? Are there still opportunities to optimize that going into whatever the Fed comes out with on Basel? Thank you.

A - Jeremy Barnum {BIO 15409544 <GO>}

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Yeah. So, there are definitely still opportunities to optimize. We're continuing to work very hard, and it's a big area of focus. Some of that is reflected in this quarter's numbers, but some the other drivers of this quarter are what you might call more passive items, particularly in market risk RWA. And yeah, but we should be clear that although we said that the effects of capital optimization are not a material economic headwind for the company, they are also not zero. There are real consequences to the choices that we're making as a result of this capital environment, and in a Basel III outcome, that is unreasonably punitive from a capital perspective there will be additional consequences (technical difficulty). We obviously are hoping that's not the case and believe that it's not appropriate, but we'll see what happens.

Q - Ebrahim Poonawala {BIO 17612305 <GO>}

Got it. Thank you.

Operator

The next question is coming from the line of Glenn Schorr from Evercore ISI. You may proceed.

Q - Glenn Schorr {BIO 1881019 <GO>}

Hi, thank you. I'm curious, I want to talk levered loans for a second. You've done a good job avoiding some of these -- put on these loans for the -- like, the better half of the last half year. So, good call on your part. Things have gotten a lot cheaper. However, bank balance sheets, not yours, are still kind of kind of muck it [ph] up with a lot of the back book. I'm curious to see if things have gotten cheap enough. Do you consider yourself back in? And how important is this, in general, for activity levels to pick back up to have available funding from the big banks?

A - Jeremy Barnum {BIO 15409544 <GO>}

Yeah. A couple of things there, Glenn. So, short answer is, we're absolutely open for business there. Terms are better, pricing is better. We have the resources needed. We're fully there. No overhang and no issue. Also, I think there's a bit of a narrative that, like, activity in the market needs to overcome overhang. We're not convinced that that's true. We think that the overhang is in the numbers and people need to look forward and the system has the capacity to handle the risks. So, I recognize your point. I think it's an interesting point. But we are wide open for business and not particularly concerned about the overhang from the perspective of bank's ability to finance activity.

Q - Glenn Schorr {BIO 1881019 <GO>}

Interesting. So, maybe a bid/ask thing, more so. Okay. Maybe, Jamie, while we have you, in the last annual letter, you talked about low competitive moats and intense competition from all angles, not just fintech. And I was just trying to think out loud. Is that better or worse, that competitive landscape in a much higher rate backdrop? Maybe I'll just leave it at that to see where you go with it.

A - Jamie Dimon {BIO 1484062 <GO>}

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I think it's the same. You have the Apples, who are basically doing a lot of banking services and Walmart starting theirs. And obviously, higher rates will hurt some of the folks in the fintech world and maybe even help some of the folks. So, we expect tough competition going forward.

Q - Glenn Schorr {BIO 1881019 <GO>}

Okay. Thanks.

Operator

The next question is coming from the line of Gerard Cassidy from RBC Capital Markets. You may proceed.

Q - Gerard Cassidy {BIO 1505265 <GO>}

Thank you. Hi, Jeremy.

A - Jeremy Barnum {BIO 15409544 <GO>}

Hey, Gerard.

Q - Gerard Cassidy {BIO 1505265 <GO>}

Jeremy, you mentioned in your payments business that if you took out the equity investment write-downs, the growth was over 50%. Can you share with us on the equity write-downs -- obviously, private equity is going through some challenging times. And I'm assuming --

A - Jeremy Barnum {BIO 15409544 <GO>}

It was a gain last year. It wasn't a write-down this year.

Q - Gerard Cassidy {BIO 1505265 <GO>}

Oh, I got it. Okay. I thought there was a write-down there. Okay.

A - Jamie Dimon {BIO 1484062 <GO>}

Let me make that clear. Sorry about that.

Q - Gerard Cassidy {BIO 1505265 <GO>}

Very good. Thank you, Jamie. Can you -- sticking just with private equity for a moment, can you share with us where the risks are in the private equity markets to JPMorgan? Is there -- when you think about it from your loan book, or is it really just in equity investments? And maybe expand upon that.

A - Jeremy Barnum {BIO 15409544 <GO>}

Sorry, do you want me to take that? Okay, just a couple of things. So, Jamie is right. The headwind year-on-year is primarily a function of the fact that this is an investment that just

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because of the management [ph] alternative accounting standard, we were forced to mark up previously. This is an investment that we got payment in kind as part of the sale of some of our internally developed initiatives. So, anyway, it's fine. The point is there is a small write-down this quarter. And the important point there is that the core business is performing exceptionally well, both because of higher rates, but also because of the strategy that Takis talked a lot at Investor Day, paying off across fees and value-added services and so on and so forth.

And I guess, Gerard, your question is, like, private equity in general and how are we feeling about that space? Did I hear that correctly?

Q - Gerard Cassidy {BIO 1505265 <GO>}

That's correct, Jeremy. And just in terms of any lending -- obviously, so many of these companies have seen their valuations come down considerably. Is there any elevated risk lending to some of these companies, considering the struggles they're having?

A - Jeremy Barnum {BIO 15409544 <GO>}

Yeah. I mean, I think that's a risk that we manage quite tightly as a company. Our exposure to the sort of non-bank financial sector are broadly defined. And of course, as we thought a little bit about what normalized wholesale charge-offs could look like through the cycle. They're obviously higher than effectively zero, which is what we have now. But we feel confident with our credit discipline and what we have on the books.

Q - Gerard Cassidy {BIO 1505265 <GO>}

Great. And then as a follow-up question, you guys did a good job building up that loan loss reserve this quarter. Two questions to that. First, the Shared National Credit exam results are always released in February. Does the reserve buildup take some of that into account? And second, how much of the reserve build was more of a management overlay versus your base case, the quantitative part of the decision-making for building up the reserve?

A - Jeremy Barnum {BIO 15409544 <GO>}

Yeah. I mean, I'll give you that answer, but I'm oversimplifying a lot. I would say that.

A - Jamie Dimon {BIO 1484062 <GO>}

Oversimplifying.

A - Jeremy Barnum {BIO 15409544 <GO>}

Yeah. Yeah, I know. I got it. The sort of conservatism of the management overlay did not change for all intents and purposes quarter-on-quarter. I think that's the best way to think of that, Gerard.

Q - Gerard Cassidy {BIO 1505265 <GO>}

Oh, and the Shared National -- yeah, go ahead.

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A - Jamie Dimon {BIO 1484062 <GO>}

The National Shared Credit thing will not affect our results materially.

Q - Gerard Cassidy {BIO 1505265 <GO>}

Very good. Thank you, Jamie.

Operator

The next question is coming from the line of Ken Usdin from Jefferies. You may proceed.

Q - Ken Usdin {BIO 3363625 <GO>}

Hi, thanks. Good morning. I was just wondering if you can help us understand the ongoing efforts on your mitigation for the RWAs in advance of all the points we've made already about the pending capital regime. How do we -- can you help us understand what type of effects that has, if any, on parts of the income statement, whether it's NII or the trading business?

A - Jeremy Barnum {BIO 15409544 <GO>}

Yeah. So, if I just take that one. Just assume we're going to have modest growth in RWA. And in every single businesses, mortgages, loans, derivatives, how we hedge CVA and stuff like that, we take actions to manage RWA. Do not -- it does not really affect the business that much. It might one day, but it doesn't affect it today. And so, we don't build in somehow we lose a little bit of this, a little bit of that. And they're -- and the biggest opportunity down the road will be a reopening of the securitization markets. And they're still very tight, and I think one day, they will reopen.

Q - Ken Usdin {BIO 3363625 <GO>}

Okay. And then on the -- one follow-up. Just coming back to the reserving process, can you help us understand, relative to the 5% peak in 3Q that you gave for your unemployment rate quarterly average in the 3.9% average baseline, just where does this fourth quarter reserve get you to? And just does that rule of thumb that you kind of gave us last quarter still stand in terms of a scenario analysis on potential builds ahead of this mild recession?

A - Jamie Dimon {BIO 1484062 <GO>}

Can I just make it real simple? The base case, okay, is where it hits almost that 5% unemployment. Then you probability-weight other scenarios. That's why Jeremy is saying the reserve is higher than the base case. We didn't change the probabilities in our weighting. But of course, it got worse since the base case got worse. That's all it is, which still is a good benchmark, you'll keep in mind. If we got to a relative adverse case, all that, a 6% unemployment, we -- and then once you get there, you assume the average weighting, you have wins. It could get better or it could get worse. At that case, we would need about $6 billion more.

When the base case itself deteriorates, we're moving closer to the relative adverse. That's all it is. These are all probabilities and possibilities and hypothetical numbers. If I were you, I'd just look at charge-offs, like, actual results. And so -- and we break this out, but it's hard to describe, and every bank does it slightly differently and every bank has a slightly different base case and slightly different weighting of adverse cases, et cetera. And so, we're just trying to make it as simple as possible.

Q - Ken Usdin {BIO 3363625 <GO>}

Yeah, I hear you. The challenge this time is that we're going to have the income statement effect way ahead of that charge-off. So, we're all trying to just fit for that. But I appreciate that. Thanks, Jamie.

A - Jamie Dimon {BIO 1484062 <GO>}

And once the ME [ph] base case gets to where you expect relative adverse, you'd be adding the $6 billion of reserves before you have charge-offs.

Q - Ken Usdin {BIO 3363625 <GO>}

Exactly. Right.

A - Jeremy Barnum {BIO 15409544 <GO>}

Hey, Ken. And maybe just out of interest, implied to your question might be a little bit, to what extent does this quarter's build sort of is a down payment on the $6 billion. And the answer to that question is, much less than all of it, because a lot of it was driven by loan growth. But some of it, as Jamie says, is driven by the flow-through of the downward provision in the central case. You could say, subject to the caveat that this is a little bit odd, not science, that there's some down payment on that $6 billion.

Q - Ken Usdin {BIO 3363625 <GO>}

Yeah. Understood. Thank you for all that.

Operator

The next question is coming from the line of Betsy Graseck from Morgan Stanley. You may proceed.

Q - Betsy Graseck {BIO 4799503 <GO>}

Hi, good morning.

A - Jamie Dimon {BIO 1484062 <GO>}

Hey, Betsy.

Q - Betsy Graseck {BIO 4799503 <GO>}

I wanted to understand a little bit about how you're thinking about managing the expense line as you go through this year. I know we talked already about how -- it's hard to predict

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NII. Obviously, markets has pushes and pulls. Can you help us understand how you're thinking about delivering operating leverage, where the elements of the expense base are needing to be invested in so you really can't touch, and where there are opportunities to potentially peel back such that if you get a weaker rev line, you can still deliver positive operating leverage?

A - Jeremy Barnum {BIO 15409544 <GO>}

Sure. So, I mean, as we've -- as you know, obviously, we tend to break down our expenses across all three categories. And in some sense, the category that you're addressing is the volume and revenue-related expense, which we highlight, because it should pre-symmetrically respond to a better or worse environment and thereby contribute to operating leverage.

So for example, in this year's ultimate outcome and the number that we want on printing for '22 [ph], the year-on-year change in volume and revenue-related expense, still we're finding the numbers, we'll probably show you more at the Investor Day, but it's probably close to $1 billion. In other words, year-on-year decline, whereas next year, we're assuming something more like flat. So, while the sort of year-on-year dollar change in the outlook sort of '21 to '22, '22 to '23 is comparable, the mix is quite different actually.

And so, for example, if we wound up being wrong about the type of environment that we're budgeting for, you would expect a significant drop in the volume and revenue-related expense number that's in the current outlook, and that would contribute to operating leverage. For the rest of it, we're always generating efficiency. And we worked just as hard at that, whether the revenue environment is good or bad. And as you know, we invest through the cycle. And so broadly, our investment plans really shouldn't be that sensitive to short-term changes in the environment.

Of course, certain types of things, like marketing investments in the card business, in particular, the math of what we expect the NPV of those things to the cycle may change in a downturn, and that could produce lower investment, all else equal. But the core strategic investments that we're making to secure the future of the company are not going to get modified because of the ups and downs of the environment.

Q - Betsy Graseck {BIO 4799503 <GO>}

Okay. And part of the reason for asking is, one of the debate points on JPMorgan stock has been around the capital charges, the capital march, and will capital be a bigger burden for you to bear as we go through the next couple of years. As you deliver on the positive operating leverage side, it gives you room to absorb some more capital, obviously, and still hit those IRR and ROTCE target on incremental investments. Maybe you could help us understand what level of capital increase you could absorb, given the operating leverage you're expecting to generate? And maybe that's an unfair question today and it's a better question for Investor Day, but that's kind of the debate that's out there on the stock.

A - Jeremy Barnum {BIO 15409544 <GO>}

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I got it. I mean it's a fair question. It's a good question. I'm not going to answer it super-specifically, and Jamie may have some views there too. But let me just quickly say, we've kind of said that we feel quite confident about this company's ability to generate 17% in the cycle. And that's incorporating our sense of the current environment, the operating leverage that you talked about, and the expectation of higher capital requirements with the 13.5% target in the first quarter of '24.

The question of whether Basel III end game and other factors increase that number and how much of that we can absorb and still produce those returns is, of course, impossible to answer right now. But I would remind you that it's not just denominator expansion. Unreasonable capital outcomes will increase costs into the real economy, which goes into the numerator too. It's not what we want, but that is a possible outcome.

Q - Betsy Graseck {BIO 4799503 <GO>}

Thank you.

Operator

The next question is coming from the line of Mike Mayo from Wells Fargo Securities. You may proceed.

Q - Mike Mayo {BIO 1494617 <GO>}

Hi. Yeah, I recognize you're evolving your business model and you're spending money to make more money and that your track record last decade was strong there. But as it relates to Frank acquisition that's been in the news, I'm just wondering what that says about the financial discipline for the 15 deals that you pursued, the $7 billion of investing each year and the one-fifth increase in expenses over three years to your guide of $81 billion in 2023. So, it's really a question about financial discipline. And I know you can't go in details on the Frank deal. And -- but you earn the purchase price in two days, okay? So, I get that. And if there's fraud, there's only -- you can't do anything about fraud, but still, it's diverse management resources and attention.

So maybe just in the specifics, as it relates to the acquisition strategy, like who sources them? Who negotiates them? Who does the due diligence? Who runs it? And ultimately, who's accountable for all these 15 different deals? And when you have investments going across business lines, which is a strength of you guys, but who's ultimately accountable when these investments don't go the way you want to? And Jamie, you recognized, a couple of years ago at Investor Day, you said, look, sometimes you're going to waste money as you're innovating and you're growing. But ultimately, who's accountable when investment doesn't go right, like the Frank deal or another deal or some of the other $81 billion that you expect to spend this year?

A - Jamie Dimon {BIO 1484062 <GO>}

Yeah. Obviously, Mike, that's a very good question, which we're always concerned of that. We've always talked about complacency and all things like that. So, obviously, when you're getting up to bat 300 times a year, you are going to make -- have errors. And we don't want our company to be terrified of errors that we don't do anything and that the

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complacency is then burdened by bureaucracy, which is stasis in-depth. So, you got to -- you have to be very careful when you make an error, like, you cripple the firm.

We are very disciplined, and you see that in a lot of different ways. You see it in our leverage lending book. You see it in the success of our investments. You see it in the quality of our products and services. You see it in our -- in all these things. And it's no different for an acquisition. There are -- so, the acquisitions are done by the businesses, but it's also a centralized team that does extensive due diligence. So, the business does it, the centralized team does it. We've been doing it for 20 years, like, we just started doing something like that. But -- and obviously, there are always lessons learned. And at one point, we'll tell you the lesson we learned here when this thing is out of litigation.

But we're quite comfortable. And the people who are responsible are the people in the business. So, they -- that business did the acquisition, they are responsible, they report back. And we expect people, when they talk to all of us, is the good, the bad, the ugly. We're never looking for how great everything was. And obviously, this thing, in one way or another, was a huge mistake.

Q - Mike Mayo {BIO 1494617 <GO>}

Let me follow up on that. So, that relates to the inorganic growth. As it relates to the organic growth, such as in the payments business, which I know is a focus, that cuts across a lot of different business lines. So, as you invest more in payments, which is -- can be a 20 or 30 P/E [ph] business, which could be great if you got there. Who is responsible for that sort of organic investment that cuts across? Sometimes, the way you aggregate the data, it's consumer, it's the investment bank, it could be asset management, it could be commercial, it can be everything, in the payments. Who's responsible for those?

A - Jamie Dimon {BIO 1484062 <GO>}

So, just to be clarified, so I would say that Marianne and Jen when it comes to credit, debit, checks and all the consumer-related stuff; and Takis, which I think you saw the presentation about payments at Investor Day, reporting to Daniel, and that is on the wholesale payments, merchant processing, a whole bunch of stuff. And those are direct responsibilities. It's quite clear, this is an area that cuts across the company. So, it's a payments working group that just spends time on that. That working group has not done an acquisition, okay? And if they make -- if they want to invest, which there are cases, by the way, which you -- and you'll see more this year, we decide it jointly and all the way up to Daniel and me.

Q - Mike Mayo {BIO 1494617 <GO>}

And then last follow-up to my first start, the general comment. I mean, this is the third year in a row of about $5 billion of expense growth, and you have Slide 11 there. But I mean, that's a lot of certain front-loaded expenses for less certain back-ended benefits. How is your comfort level that you're going to see those back-ended benefits relative to the past?

A - Jamie Dimon {BIO 1484062 <GO>}

Totally. And we try to show you guys at Investor Day, for every branch we open, for every bank that we hire, for every tech thing we do, we're pretty comfortable. There are certain

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things, just more like infrastructure, like getting to the cloud and stuff like that, which -- you can't identify all of that, but we're pretty comfortable that we -- if they weren't working, we change them. So, we're -- we ask ourselves that question every day, when you're adding wealth managers or branches or certain things. So -- and marketing is half of that -- not quite half, but half of that number. That's a very specific -- for the most part, very specific dollar in, how many dollars out. Not a guess, and we're pretty accurate at that kind of stuff. And again, if we -- if there's $1 billion that we were spending didn't give us the return, we cut the $1 billion.

Q - Mike Mayo {BIO 1494617 <GO>}

All right. Thank you.

Operator

The next question is coming from the line of Steve Chubak from Wolfe Research. You may proceed.

Q - Steven Chubak {BIO 18457976 <GO>}

Hi, good morning. So, I wanted to start off with a question on the outlook for trading in the investment banking businesses. Just Jeremy, given the strong pipelines you cited, I was hoping you can provide some additional color just in terms of what you're hearing from corporate clients, especially in the context of the mild recession scenario you outlined, when you would expect to see some inflection in investment banking activity. And similar question on the trading side. You are facing difficult comps in the coming year. We still have QT, rate volatility proxy still elevated. Do you anticipate a significant moderation in trading activity or not?

A - Jeremy Barnum {BIO 15409544 <GO>}

Sure. Thanks, Steve. So, let's do banking first. So, I think the thing that's interesting about banking right now is that the declines have been so significant, obviously, from very elevated levels. But even relative to just 2019, 2022 was a relatively weak year. And as we look into 2023, it's possible that the actual economic environment will be worse than it was in '22 [ph]. That could conceivably make you pessimistic about the investment banking wallet outlook.

And to be sure, it's not as if we're super-optimistic. But it's important to note that part of the issue here is how quickly things changed in 2022, specifically with respect to rates, as that affects the debt business, and valuations, as it affects M&A and ECM as well. And one of the sort of necessary conditions for people to do deals or decide to raise capital is just getting comfortable with valuations in the low local [ph] market. So, I think there's a chance that that actually winds up helping in 2023 in the investment banking world. Of course, we don't know. But those are some of the things that we're thinking about.

Similarly, on the Markets side, obviously, markets had another very strong year, better than we'd expected, since the numbers were so strong. Coming out of the pandemic, we were expecting more normalization than what we actually saw. And 2022 had a lot of themes. I think the active management community did well. That always helps us a little bit. And we

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had volatility with relatively orderly and continuing Markets. As we look towards 2023, maybe some of those themes will be a little bit less obvious, and that could be a little bit of a headwind. But on the other hand, it's not like the volatility is going away, and Markets seem to continue to be quite orderly. And a 4.5%, 5% rate environment is probably one where there is more trading opportunities than the zero percent rate environment.

So, of course, we don't know. We'll see. I think you would have to probably expect some normalization there. It's -- the numbers are really very strong in Markets, but we'll see. We'll see what happens.

Q - Steven Chubak {BIO 18457976 <GO>}

That's really helpful color. And just for my follow-up on finalization of Basel III. Sorry, Jeremy, I couldn't help myself here. But in Barr's December speech, he strongly hinted at capital requirements moving higher for you and peers. You also alluded in your comments or in response to one of the questions that the finalization of Basel III can potentially be very punitive. Given the absence of the proposal, I was really just hoping you could speak to how you are scenario-planning for the eventual finalization, and any additional detail you can offer on the areas of mitigation? I think the one issue or area of confusion is that one of the biggest sources of RWA inflation is op risk, which can't really be mitigated. So, what are the actions that you can take to really offset some of those potential headwinds?

A - Jeremy Barnum {BIO 15409544 <GO>}

Yeah. So, Steve, I'd love to get into detail here, but I just think that the question of how to mitigate is really hard to discuss in a lot of detail until we see an actual proposal. And the reason that we talk about potentially punitive increases -- I mean, you studied this issue closely, is just to point out that under the version of the world where you get the worst outcome in all of the different moving parts of this thing, it's a very significant increase to the capital requirements of the system as a whole. And given how strong the system is today, that just, like, doesn't make sense to us. So, we just want to say that.

But yeah, Jamie, please.

A - Jamie Dimon {BIO 1484062 <GO>}

Just, look, you guys know the operators' capital, the trading book, the CCAR, G-SIFI, all those moving parts, let's just see what they are. We'll deal with them when we get there and then we'll figure out what we have to modify our business and stuff like that. We don't think it's necessary to increase capital ratio, and we're quite clear on that. One of the new numbers we put on the top of the press release was our total loss-absorbing capacity. So, we have now almost $500 billion. I mean, really, like, at one point, when is $500 billion of that, of $1 trillion liquidity, all those things enough.

And so -- but let's just see what it is. They're going to work it through their international laws, their international requirements. We're hoping that America is the same as international. That would be nice. G-SIFI is supposed to be corrected. We'll see if that happens. So, let's just see. We don't have to guess. And if the number's too high, we're going to tell you what we're going to do about it.

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A - Jeremy Barnum {BIO 15409544 <GO>}

(multiple speakers) Just a minor expansion -- just to expand a bit on Jamie's point that it's important to be clear, there will be time to adjust, like, there's a long road from the NPR to -- so, to sort of supports Jamie's point, let's see what it is and then we'll --

Q - Steven Chubak {BIO 18457976 <GO>}

Fair enough. Thanks so much for taking my questions.

Operator

Your next question is coming from the line of Matthew O'Connor from Deutsche Bank. You may proceed.

Q - Matthew O'Connor

Good morning. How do you guys think of the managing the securities book, given the outlook of lower deposits? Obviously, the yield curve is quite inverted, depending on what part you're looking at or most part, frankly. And at the same time, the securities book is cash flowing a lot less than it was a couple of years ago, just given the rate environment.

A - Jamie Dimon {BIO 1484062 <GO>}

Yeah. So, remember, the securities book is an outcome of investing, basically, excess deposits. And you have like $2.4 trillion deposits and $1 trillion of loans and things like that. So -- and we manage it to manage interest rate exposure, all these various things. And so -- and then when you say the size of it, we forecast -- which I'm not going to give you the numbers, we forecast every quarter what we're going to buy, what we're going to sell, how much is coming in, how much we need to liquidity, and we adjust it all the time based upon deposits coming down and loans and stuff like that. Obviously, what you get to invest in is at much higher rates today. And you see JPMorgan's loss in HTM loan book as the percent is much lower than most other people. We're kind of conservative there too.

Q - Matthew O'Connor

And I guess, a bigger picture question. We've seen such a drop in really a five -- 10-year part of the curve and even further out. And banks aren't really buying, the Fed is selling. And I guess, I was wondering if you had thoughts on who's buying and what's driving the rates so much lower than most people think they should be at.

A - Jamie Dimon {BIO 1484062 <GO>}

Yeah, we do. But you -- we should get the answer, of course, to get that. We look at what everybody is doing, pension plans, governments. We look at every part of the curve. We look what other banks are doing. I think I mentioned earlier in this call, banks are in different positions. Some have -- some may have to sell securities to finance their loan books. We obviously don't. So, people are in a different position. And as Jeremy pointed out, it's very important, that yield curve will not be the same six months from now that it is today. While we use that to kind of look forward, it's not actually our forecast. We know it

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will be wrong. And with the investment portfolio, we'd be invested when there are opportunities. We bought a lot of Ginnie Maes when there was a 60 OAS spread. We sold -- one of the reasons we take securities loss is because that gives you $10 billion plus you can reinvest when you think of more attractive securities.

Q - Matthew O'Connor

Got it. Thank you.

Operator

The final question is coming from the line of Andrew Lim from Societe Generale. You may proceed.

Q - Andrew Lim {BIO 15232581 <GO>}

Hi, good morning. Thanks for taking my questions. So, the first one on credit quality, thanks for giving us commentary on the shape of NCOs, I guess, specifically for credit cards, topping out at the end of this year. Could you give us a bit more color on how reserve builds should shape out this year, I guess, with respect to CECL? I'm guessing that it should top out quite soon. That's my first question. This is assuming all your macro assumptions are unchanged and -- all the macro assumptions are unchanged and the (multiple speakers) --

A - Jeremy Barnum {BIO 15409544 <GO>}

So, yeah, Andrew.

Q - Andrew Lim {BIO 15232581 <GO>}

-- unchanged and so forth.

A - Jeremy Barnum {BIO 15409544 <GO>}

But I think we've talked about CECL, like, quite a bit, and I think there's some decent color there in terms of Jamie's $6 billion over a few quarters in a world where the economic outlook is worse than it is today. We're definitely not going to get into the business of giving you an outlook for a sequential evolution of the loan loss allowance. But it's appropriate today, and it will evolve as a function of the environment.

Q - Andrew Lim {BIO 15232581 <GO>}

Sure. Okay. Let's drill down into NII then. I just want to square a few comments you made there, Jeremy. So, if I heard you correctly, I think you're still talking about sequential increases in NII. So, I guess, looking towards, like, $20 billion plus for 1Q, maybe even 2Q. So, I guess, we're hitting about $40 billion for 1H and then a sharp drop-off as, say, deposit costs increase and maybe we get a few Fed fund rate cuts as well. Is that the way we should be thinking about it?

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A - Jeremy Barnum {BIO 15409544 <GO>}

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Yeah, no. So, let me uncontroversially say no there, Andrew, you just really wouldn't doubt. So, the -- my comments about sequential increases were to address the sort of obvious conclusion, which we're somewhat correctly drawing from the slide, which is that in a world where we're exiting the fourth quarter run rate at $81 billion, and we're telling our ADX markets [ph] or whatever, we're telling you $74 billion for the full year. There are obviously some sequential declines in there somewhere as a function of what plays out. We are simply saying, don't project those into the future in perpetuity. Once things adjust, we will return to normal sequential growth. Does that make sense?

Q - Andrew Lim {BIO 15232581 <GO>}

Right. Yeah. No, no, absolutely. That makes sense. That's great. Thanks for that.

A - Jeremy Barnum {BIO 15409544 <GO>}

Yeah. Thanks.

Operator

We have no additional questions in queue. I would now like to hand the call back to Mr. Barnum.

A - Jeremy Barnum {BIO 15409544 <GO>}

That's it. Thank you very much.

A - Jamie Dimon {BIO 1484062 <GO>}

Well, thank you very much. We'll talk to you all soon.

Operator

That concludes today's conference. Thank you all for participating. You may disconnect at this time.

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