The past two years have been among the most extraordinary and challenging in

recent history for JPMorgan Chase, the financial services industry and the global

economy. We have endured a once-in-a-generation economic, political and social

storm, the impact of which will continue to be felt for years or even decades to come.

As we see signs of recovery and the debates about financial reform wage on, it’s

easy for us to forget the fear and panic we felt a year ago. The market was down an

astonishing 50% from its 2008 highs to its low on March 9, 2009. More important,

as I write this letter, our country has lost 8.4 million jobs in what has turned out to

be a more serious, sustained economic crisis than most of us have ever experienced

before — or may experience again.

For JPMorgan Chase, these past two years have been part of a challenging, yet

defining, decade. We began it as three separate companies: Bank One, Chase and

J.P. Morgan, with each facing serious strategic and competitive challenges. Today, our

strategic position is clear, and JPMorgan Chase is a leader in all of its businesses.

If you had been a Bank One shareholder from 2000 to year-end 2009 (this represents

approximately 40% of the current company) and you held on to your stock, you

would have received a total return on your investment of 131%. Over the same time

period, if you were a Chase or J.P. Morgan shareholder, your returns would have been

12% and 70%, respectively. By comparison, the Standard & Poor’s 500 Index was

down 9% over the same period.

Throughout this decade, we made and executed on many transformative decisions.

When the global financial crisis unfolded in 2008, the people of JPMorgan Chase

understood the vital role our firm needed to play and felt a deep responsibility to our

many stakeholders. It is this sense of responsibility that enables us to move beyond the

distractions of the moment and stay focused on what really matters: taking care of our

clients, helping the communities in which we operate and protecting our company.

It is because of this focus — even amid the daunting and ongoing challenges — that

we are able to weather this economic crisis and continue to play a central, if sometimes

misunderstood, role in rebuilding the U.S. economy. This is a testimony to the

collective strength of character and commitment of our people. Since those first

chaotic days in early 2008, many of our people have worked around the clock, seven

days a week, for months on end. On March 16, 2008, we announced our acquisition of Bear Stearns at the request

of the U.S. government; on September 25, 2008, 10 days after the collapse of

Lehman Brothers, we bought Washington Mutual. We loaned $70 billion in the

global interbank market when it was needed the most. With markets in complete

turmoil, we were the only bank willing to commit to lend $4 billion to the state of

California, $2 billion to the state of New Jersey and $1 billion to the state of Illinois.

Additionally — and, frequently, when no one else would — we loaned or raised for

our clients $1.3 trillion, providing more than $100 billion to local governments,

municipalities, schools, hospitals and not-for-profits over the course of 2009.

Our industry and our country are continuing to face some serious challenges, but

we believe that the strengths of our nation — our resiliency, ability to reform and

innovate, work ethic and culture — will put us on the right track again to global

financial soundness. JPMorgan Chase will remain focused, and we will continue

doing our part.

In the following sections of this letter, I’ll talk about a range of issues that bear on

our company, our industry and our country:

I. How our company fared in 2009 — with a focus on what we *actually* do as a

bank to serve our clients and customers and what we did to respond to the

crisis and help the communities in which we operate

II. How we manage our people — JPMorgan Chase’s most valuable asset

III. Our support of financial reform that will strengthen the financial system

IV. Our responsibility and America’s success

Overall results — performance improved from

2008 but still was not great

Our revenue this year was a record $100

billion, up from $67 billion in 2008. The large

increase in revenue was due primarily to the

inclusion for the full year of Washington

Mutual (WaMu) and the dramatic turnaround

in revenue in our Investment Bank. Profits

were $12 billion, up from $6 billion in the

prior year but down from $15 billion in the

year before that. While these results represent

a large improvement over 2008, they still are

an inadequate return on capital – a return on

tangible equity of only 10%. Relative to our

competition, our company fared extremely

well. We did not suffer a loss in any single

quarter over the two-year crisis (we may have

been one of the few major global financial

firms to achieve this). In absolute financial

terms, however, our results were mediocre.

Maintaining our fortress balance sheet and

commenting on our dividend

During this difficult year, the strategic imperatives

that have defined and distinguished

our company continued to serve us well. We

maintained our focus on risk management;

high-quality capital; strong loan loss reserves;

honest, transparent reporting; and appropriately

conservative accounting. We maintained

an extremely strong Tier 1 Common

ratio, which stood at 8.8% at year-end. We

also increased our loan loss reserves over the

course of the year from $23.2 billion to $31.6

billion, an extremely strong 5.5% of total

loans outstanding. Our relentless focus on our

balance sheet has always enabled us to prevail

through tough times and seize opportunities

while continuing to invest in our businesses.

It served us extremely well over this period.

Early in 2009, we cut our annual dividend

from $1.52 to $0.20 per share – a drastic move

premised on the need to be prepared for a

prolonged and potentially terrible economy.

We hope to be able to increase the dividend to

an annual range of $0.75 to $1.00 per share. To

do so, we would like to see three specific things

happen: several months of actual improvement

in U.S. employment; a significant reduction

in consumer charge-offs (which improves

earnings and diminishes the need for additional

loan loss reserves); and more certainty

around the regulatory requirements for bank

capital levels. Possible changes in capital and

liquidity requirements as well as some tax

proposals are creating uncertainty around our

future capital needs. We hope there will be

more clarity regarding these issues soon.

Many companies had to measurably dilute

their shareholders because of this crisis. We

did not. The only time we issued a material

amount of stock was when we did it offensively

to finance the WaMu purchase (and

maintain our very high capital ratios). We also

hope to be in a position to resume stock buybacks

in the near future. But our first priority

is – and always has been – to invest our

capital to grow our businesses organically and,

secondarily, to make valuable acquisitions. We

buy back stock only when we think it is a good

value for our shareholders relative to the value

of other opportunities. And if we use our stock

in an acquisition, we do so because we believe

the value we’re getting is at least equal to the

value we’re giving.

Increasing our efficiency

Overall, we are a far more efficient company

than we were five years ago, following the

JPMorgan Chase -Bank One merger. Since then,

we’ve consolidated virtually all of our operating

platforms, networks and data centers,

and we have excellent technology and best-in-

class financial and risk systems. We also

have exceptional legal, finance, compliance,

risk, human resources and audit staff. Today, the cost of this improved level of operation

and service per dollar of revenue is significantly

lower than in the past. To give just

one example, our total technology and operations

and corporate overhead costs would be

more than $9 billion higher today if they were

running at the same cost per dollar of revenue

as in 2005.

Continuing to invest

Through the worst of the past two years, we

never stopped investing. This has included

acquisitions, foremost among them Bear

Stearns and Washington Mutual; investments

in infrastructure, including systems and technology;

new products, for example in Card

Services; and the addition of bankers and

branches around the world. These investments

set us up for continued organic growth.

Preparing for tougher global competition

The competitive landscape is rapidly changing.

Many companies did not make it or had to

be dramatically restructured. We expect this

trend to continue in both the United States

and Europe. We and others who survived

benefited from market share gains (in fact,

we gained market share in virtually all of our

businesses). But we must be prepared for all

of our competitors to come roaring back. With

certain competitors and in certain parts of the

world, this already is happening. We do not

take this lightly.

Protecting the company in uncertain times

You read about it every day: continued global

trade imbalances, higher fiscal deficits run

by governments around the world, uncertain

interest rate movements and potential regulatory

changes, among other issues. I could go on

for pages. Rest assured, we are paying very close

attention to the difficult issues we still face.

Following is a recap of our line of business

results. In this section, I will focus on

describing what we as a bank actually do,

which seems to be so often misunderstood.

As you read these results, I hope you will feel

as I do – that we have excellent franchises,

focused on doing a great job for our customers

(even though we do make mistakes), and that

we have been continuously and deliberately

investing for future growth.

Results by line of business:

Great leadership amid great challenges

The Investment Bank reported net income of

$6.9 billion with an ROE of 21%

Overall results

The Investment Bank (IB) delivered record

performance across the board: net income of

$6.9 billion on revenue of $28.1 billion. These

results were led by best-ever Global Markets

revenue of $22 billion and record investment

banking fees of $7.2 billion. The IB generated

a return on equity of 21% on $33 billion of

allocated capital, our best result in five years.

We clearly benefited from higher bid-offer

spreads and higher volumes as the industry

consolidated and vulnerable companies

were distracted. In terms of market share,

we achieved a #1 ranking in every major

global capital-raising league table category.

We do not, however, take this position for

granted and understand that maintaining

and growing our market share will undoubtedly

be tough going forward. We believe

our success was due to the dedication of our

25,000 employees, who were working hard to

serve our clients every day.

What we do in Corporate Finance

Globally, we have more than 2,000 investment

bankers, who serve the corporate finance needs

of 5,000 institutions around the world. More

than 1,000 of these clients are sovereign governments,

state and municipal governments, international

quasi-government agencies, hospitals,

schools and not-for-profits; the others are generally

corporations and financial institutions.

Our job is to help these clients find appropriate

financing, make strategic acquisitions or divestitures,

and help manage their balance sheets and

other exposures – such as exposure to interest

rates, foreign exchange or commodity prices.

In 2009, among their many activities, our

investment bankers:

• Advised on 322 mergers and acquisitions

globally – more than any other bank.

• Loaned or syndicated loans of more than

$200 billion to 295 companies, helping them

grow and create jobs.

• Raised $620 billion of equity or bonds in

public markets for clients around the world.

• Raised $178 billion for the financial industry,

or nearly 10% of the capital needed to

rebuild the financial system.

• Raised $102 billion for states, municipalities,

hospitals, schools and not-for-profits

– to help build roads and bridges, improve

social services, renovate local hospitals

and train people for employment. This

financing included $19 billion to educational

organizations and $14 billion to

healthcare organizations.

• Committed to provide financing when others

were not able to do so; for example:

– $4 billion to California;

– $2 billion to New Jersey; and

– $1 billion to Illinois.

• Arranged $60 billion to restructure stressed

companies and help them recover (and keep

their employees at work).

• Invested in 58 U.S. wind farms spread across

16 states. This portfolio can produce 5,843

megawatts of capacity – enough energy

to power some 1.6 million U.S. homes. We

also are a leader in sourcing, developing

and trading emission-reduction credits,

primarily through our investments in

ClimateCare and EcoSecurities.

In difficult times, extending this level and

type of credit is exceedingly risky and

costly. For example, in 2008 and 2009, we

wrote off or reserved for approximately

$8.9 billion of credit-related losses related

to IB lending activities. What we do in Sales and Trading

Trading is perhaps the least understood area

of our investment banking activities. We have

6,500 professionals on approximately 120

trading desks in 25 trading centers around

the world; these professionals include more

than 800 research analysts who educate

investors on nearly 4,000 companies and

provide insight on 40 developed and emerging

markets. The job of our sales and trading

professionals is to provide 16,000 investor

clients globally with research expertise, advice

and execution capabilities to help them buy

and sell securities and other financial instruments.

These investors range from state and

municipal pension plans to corporations and

governments. We have experienced specialists

who are prepared to buy or sell large

amounts of stocks and bonds, foreign currencies

or commodities for clients and to give

them immediate cash or liquidity when they

need it – something we never stopped doing

even at the most trying moments of the

financial crisis. Additionally, we help organizations

manage and hedge their risk through

providing a range of derivatives products.

Although we run our sales and trading business

to support clients, it is a risky business.

We execute approximately 2 million trades

and buy and sell close to $2.5 trillion of cash

and securities each day. On an average day,

we own, for our account, approximately $440billion in securities – to us this is akin to the

inventory of a store. We hold the securities

so we can meet client demand. Our sales and

trading functions not only play a critical role

in helping to maintain large, liquid and well-functioning

markets, but they are indispensable

to institutions of all types seeking to raise

capital in the first place.

As more clients chose to work with us in 2009,

our sales and trading teams gained market

share. We estimate that our market share

of the top 10 players in Fixed Income and

Equity Markets combined grew from approximately

9% in 2008 to more than 12% in 2009.

Deservedly, these groups also received a lot

of accolades – most gratifyingly, from client-based

surveys.

How we intend to grow

In 2010, we will continue to focus on the

fundamentals of investment banking: advising

companies and investors, raising capital,

making markets and executing for our clients

worldwide. If we do this well, we are helping

not only our clients but the global economic

recovery as well.

We also are aggressively and organically

growing many parts of our business. For

example, the Prime Services business we

acquired from Bear Stearns – which provides

mostly large investors with custody, financing

and trade execution – largely was concentrated

in the United States. We now are growing this

business in Europe and Asia. Across the business,

we will continue to invest in enhancing

our technology, spending $1 billion this year

on upgrades and innovations. We also are

expanding our coverage in key markets,

including China, India and Brazil – essentially

by adding investment banking and trading

professionals and providing them with the

corresponding support they need (i.e., credit and

systems) to cover more corporate and investor

clients in these markets. For example, in the last

five years in India, we have gone from covering

36 companies to 180 companies. We will simply

grow with the emerging economies.

Cazenove

At the end of 2009, we announced that our

U.K. joint venture with Cazenove Group

Limited would become a wholly owned part of

J.P. Morgan. Our initial investment in Cazenove

in 2005 was extremely successful – among

other things, it increased our U.K. investment

banking market share\* from 5% to 13%. We

welcome all of these employees to J.P. Morgan –

Cazenove’s long tradition of integrity and client

service sets a standard for all of us.

Commodities

We continue to build out our Commodities

franchise. Price fluctuations in commodities

like oil, gas and electricity affect many companies

throughout the world. We help our corporate

clients manage this risk by enhancing

our trading and warehousing capacity. Since

2006, our Commodities business has more

than doubled its revenue from serving clients.

In February 2010, we announced our agreement

to purchase a portion of RBS Sempra’s

commodities business for $1.7 billion. This

acquisition will give us the ability in Europe to

trade oil, gas and electricity far more extensively

than we can now; it will enhance all of

our prior U.S. capabilities; and it will add a

capability to warehouse metals for clients. It

also will nearly double the number of corporate

clients we serve in Commodities, to more

than 2,000.

Retail Financial Services reported net income

of $97 million with an ROE of 0%

Overall results

Retail Financial Services (RFS) continued to

be a tale of two cities. Retail Banking, which

includes Consumer and Business Banking,

earned $3.9 billion, primarily by serving

customers through bank branches in 23 states.

Consumer Lending lost $3.8 billion because

of continued high charge-offs in the home

lending business.

In our fastest conversion ever, we upgraded

1,800 Washington Mutual branches and

more than 40 million accounts to Chase’s

systems, products and branding. As a result

of these conversions, customers today have

full access to 5,154 Chase branches across

the country (from New York and Florida to

California). Former WaMu customers have

received greater access to better systems and

products, and we did it at greatly reduced

cost to the firm (approximately $2 billion

firm-wide). We now have one of the most

attractive franchises in the country, with

enormous opportunities to grow.

What we do in Retail Banking

Last year, our 61,000 people in 5,154 Chase

branches in 23 states served more than 30

million U.S. consumers and small businesses by

providing checking and savings accounts and

investments, as well as home, business, auto

and student loans. For our RFS professionals,

2009 was a year of numerous accomplishments:

• Retail operations teams processed 700

million teller transactions, 3.5 billion debit

card purchases, 100 million ATM deposits,

close to 6 billion checks and more than

1.3 billion statements.

• Investment advisors oversaw $120 billion in

assets under management to help consumers

toward their goals.

• We added 4.2 million mobile banking

customers and another 5.2 million new

online banking customers. We also added 2,400 branch sales staff last

year – personal and business bankers, mortgage

officers and investment representatives

– to better serve our customers.

In addition, we are revamping our overdraft

policies to meet regulatory requirements, to

make them clearer and simpler, and to give

customers more control. Customers now can

choose if they want overdraft services for their

debit cards, and they will have a real-time

ability to see their balances over the course

of the day. These changes are ongoing and

complex. We hope to complete them with

minimal disruption and maximum consumer

satisfaction. While costly (we estimate these

changes will reduce our after-tax income by

approximately $500 million annually), we

believe these moves will strengthen our long-term

relationship with our customers.

What we do in Small Business Banking

In 2009, our nearly 2,000 business bankers

provided approximately $2.3 billion in new

loans (our total outstanding loans are $17

billion) and other services to help 2 million

business owners nationwide manage their

businesses. Loan origination in 2009 was

down 58%, as customer demand decreased

significantly and our underwriting standards

became more disciplined. We expect a

substantial turnaround in 2010, and, in fact,

we already are seeing increased demand from

more qualified customers.

We are renewing our efforts to get more credit

into the marketplace, including adding 375

small business bankers to our current workforce.

In late 2009, we committed to boosting

lending to small businesses by $4 billion

in 2010 (to a total of $10 billion) through

increased access to working capital, term loans

for expansion, commercial mortgages, lines of

credit and business credit cards.

What we do in Consumer Lending

Our Consumer Lending business includes

home and auto loans for consumers. In terms

of overall results, it was another difficult year

for Consumer Lending, with losses of $3.8

billion, driven by increased charge-offs and

additions to loan loss reserves in our home

lending portfolios. As discussed last year, these

losses were the result of departures from our

traditional (and well-tested) underwriting

standards, sharply falling home prices and the

deepening recession. While there has been

some improvement in delinquencies and home

prices in some markets, we believe that significant

improvement will depend largely on an

improving economy.

As expected, charge-offs in Home Lending

continued to rise during 2009, and we added

$5.2 billion in reserves to our portfolio. We

anticipate that this portfolio will continue to

lose money for the next three years (excluding

reserve changes) as we work through a

backlog of problem loans. The losses come

not only from charge-offs but from the costs

of managing delinquencies and foreclosures

(though we were able to reduce the number

of homes that we own from 12,700 in 2008

to 7,400 in 2009).

More positively, we took a leadership role in

helping American homeowners through the

most difficult housing market of a generation.

We added 6,000 people just to help homeowners

through modification programs and

other actions to prevent foreclosure. We also

opened 34 Chase Homeownership Centers

to allow struggling borrowers to talk with

loan counselors face to face and have begun

opening 17 more in early 2010. These efforts

have allowed us to begin the mortgage modification

process for nearly 600,000 homeowners

(approximately one-third of which are modifications

under the government’s new Home

Affordable Modification Program, or HAMP).

The mortgage business essentially has

returned to the more disciplined underwriting

of many years ago: 80% loan-to-value ratios

and income verification. In 2009, we originated

more than $150 billion in new home loans, much of it refinancing that allowed

homeowners to lower their payments by

taking advantage of historically low interest

rates. Most of the loans that we originate are

sold to Fannie Mae, Freddie Mac or Ginnie

Mae. We still underwrite jumbo loans (those

with loan amounts larger than those permitted

in government programs), but we have been

very cautious. The home lending business will

one day return to being a good business – it

certainly is critical to the proper functioning of

America’s financial markets – and we intend to

be a leader in it.

In 2009, we also became the largest U.S. auto

lender, financing more than 1.1 million auto

loans for consumers, up 25% from 2008. Our

auto loans outstanding totaled $46 billion at

the end of 2009.

How we intend to grow

To provide better service to our millions of

customers, we plan to add 2,700 personal

bankers and more than 400 investment sales

representatives in 2010. These efforts should

help us earn new customers and broaden our

relationships with existing customers beyond

checking accounts and other basic services. In

addition, we expect to open at least 120 more

branches in 2010 and to ramp up our pace of

openings in 2011 and 2012 – especially in California

and Florida, two of the fastest-growing

U.S. markets, which were introduced to us

through the WaMu acquisition.

Card Services reported a net loss of

$2.2 billion

Overall results

By all measures, 2009 was a terrible year

for our credit card business. The economic

environment drove charge-off rates to all-time

highs. Card Services lost $2.2 billion

(compared with last year’s profit of $780

million). While I don’t want to diminish the

negative overall results, there were some positives.

We were able to grow market share in

terms of accounts and customer spending;

and our credit loss performance – 8.5% on

Chase cards – while poor, was better than our

competitors’ performance.

What we do in Card Services

Our 23,000 Card Services employees around

the world provide financial flexibility and

convenience to customers who, in 2009, used

Chase credit cards to meet more than $328

billion of their spending needs. With more

than 145 million cards in circulation held by

approximately 50 million customers with

$163.4 billion in loan outstandings, Chase is

among the largest U.S. card issuers, with a

wide variety of general purpose credit cards

for individual consumers and small businesses.

We also issue cards with a number of partner

organizations, such as the American Association

of Retired Persons (AARP), Continental

Airlines, Marriott, Southwest Airlines, United

Airlines and Walt Disney.

How we dealt with new regulation

In 2009, in addition to the terrible environment,

the U.S. credit card business faced

fairly dramatic changes because of a new

law enacted by Congress in May. The new

law restricts issuers’ ability to change rates

and prohibits certain practices that were not

considered consumer-friendly. These changes

alone are expected to reduce our after-tax

income by approximately $500 million to

$750 million – but this could possibly change

as both consumers and competitors change

their behavior. We believe that many, but not all, of the

changes made were completely appropriate.

In fact, we had voluntarily eliminated certain

of the targeted practices – like double-cycle

billing, which resulted in greater interest

charges for customers who revolve a balance

for the first time (2007); and universal default

pricing, in which creditors consider credit

histories with other lenders in setting rates

(2008). However, because the new law makes

it harder to raise rates on customers who have

become far riskier and because all payments

now must go toward reducing users’ highest rate

balances (vs. lower-rate balances), we and

other competitors have had to make some

fairly drastic changes in the business:

• We have substantially reduced very low

introductory or promotional balance

transfers. This change alone reduced our

outstanding balances by $20 billion.

• In the future, we no longer will be offering

credit cards to approximately 15% of the

customers to whom we currently offer them.

This is mostly because we deem them too

risky in light of new regulations restricting

our ability to make adjustments over time as

the client’s risk profile changes.

• We reduced limits on credit lines, and we

canceled credit cards for customers who

had not done business with us over an

extended period.

In fact, the industry as a whole reduced limits

from a peak of $4.7 trillion to $3.3 trillion.

While we believe this was proper action to

protect both consumers and card issuers, doing

so in the midst of a recession did reduce a

source of liquidity for some people. Ultimately,

however, the change may make the card business

a more stable and better business.

How we intend to grow

Aggressive product innovation is fundamental

to the development of the credit card business.

Even through the recent tumultuous times,

we never stopped investing in new products

and services to meet our customers’ needs. In

2009, Chase launched more products at one

time than any other issuer. New products and

services included two Chase-branded card

programs, a rewards platform, and a new

feature to help better manage spending and

borrowing. Here are some of the highlights:

• The Chase SapphireSM card was developed

from the ground up to address the needs of

affluent consumers, with premium rewards

and exceptional service.

• InkSM from Chase is a suite of business

cards offering flexible payment options and

resources for small business owners.

• Our new Ultimate RewardsSM program offers

countless redemption options through a

single website: www.ultimaterewards.com.

• BlueprintSM is an industry-first set of features

to improve the way Chase customers manage

their spending and borrowing, with tools to

help consumers take charge of their finances,

pay down balances and manage spending.

These new products\* and programs would

be considered major innovations at any time;

but the fact that we launched them in one of

the worst-ever U.S. consumer environments is

especially noteworthy. By delivering convenience,

customization and great service, we will

build stronger customer relationships. Even

as the credit card business has seen more than

its share of difficulties during the past year, we

believe our new products will help us rebuild

trust with our customers. It’s a process that

will take time, but if we focus on delivering

useful products and making financing easier

for our customers, Card Services will return to

being a business that is good for our customers

and profitable for our company. Commercial Banking reported net income of

$1.3 billion with an ROE of 16%

Overall results

In 2009, Commercial Banking overcame many

challenges to deliver exceptional financial

performance. Even as substantially higher

credit costs negatively affected quarterly

results, the business exceeded its annual plan

by focusing on client selection, marketing

its business aggressively, managing risks

and expenses, and excelling in client service.

Highlights included a 20% boost in revenue to

$5.7 billion; a 25% improvement in operating

margin to $3.5 billion; double-digit increases

in both average liability balances, up 10%, and

average loan balances, up 30%; and a 20%

jump in gross investment banking revenue

to $1.2 billion – a full 25% above plan. These

were fabulous results in any environment.

What we do in Commercial Banking

More than 1,400 bankers help fulfill the

financing needs of nearly 25,000 clients and

over 30,000 real estate investors and owners.

The average length of a Commercial Banking

client relationship with us is more than 18 years.

In 2009, we added over 1,700 new Commercial

Banking clients and expanded more than 7,600

relationships. With a team of banking, treasury

and client service professionals situated in local

markets coast to coast and around the world,

Commercial Banking delivers financial services

while steadfastly supporting communities. Last

year, Commercial Banking extended more than

$73 billion in new financing, which included

nearly $8 billion to the government, not-for-profit

and healthcare (GN PH) and education

sectors. For example: We helped finance the construction of a

$22.3 million healthcare center in the Bronx,

New York, to serve an additional 18,000

patients per year.

• As part of more than $384 million in new

and renewed commitments to GNPH and

educational entities in Ohio, we provided

Kent State University with needed financing.

• We assisted Children’s Memorial Hospital

in Chicago in financing the construction

of a new $915 million building with a

$196 million credit facility.

How we intend to grow

Having successfully completed the conversion

of commercial client accounts acquired

through Washington Mutual, Commercial

Banking is well-positioned to grow. The business

already is taking advantage of Chase’s

retail branch network to expand its offerings

into five new states – California, Washington,

Oregon, Georgia and Florida. We’ll now cover

these new markets by supporting a full range

of clients, from middle market companies to

large corporations. We are achieving this by

hiring exceptional commercial bankers – more

than 50 employees by the end of 2010 alone –

to serve these additional markets. Several years

from now, when this expansion ultimately is

completed, we expect it will generate hundreds

of millions of dollars in additional profits

annually.

On another front, when JPMorgan Chase and

Bank One merged, we set a target of more than

$1 billion in revenue from investment banking

products sold to Commercial Banking clients

(up from $552 million). This year, we exceeded

the goal and are poised to continue growing

this business. Treasury & Securities Services reported net

income of $1.2 billion with an ROE of 25%

Overall results

Treasury & Securities Services (TSS) delivered

solid but lower results, producing 2009 profits

of $1.2 billion vs. $1.8 billion in the prior year.

The business delivered net revenue of $7.3

billion, down 10% from the previous year. We

describe TSS as our “Warren Buffett-style”

business because it grows with our clients

and with inflation; delivers excellent margins

and high returns on capital; and is hard for

would-be competitors to replicate because of

its global scale, long-term client relationships

and complex technology.

Our 2009 performance largely was driven

by weakened market conditions and lower

interest rates. Securities lending and foreign

exchange volumes and spreads, in particular,

saw significant declines. TSS also saw

deposits level off after an exceptional period

in late 2008 and early 2009, when we were

a huge beneficiary of the markets’ flight

to quality. Despite the headwinds of 2009,

the underlying business drivers remained

strong: International electronic funds transfer

volumes grew 13%, assets under custody

increased 13% and the number of wholesale

cards issued grew 19%.

What we do in Treasury & Securities Services

More than 6,000 TSS bankers serve more than

40,000 clients from all of our other lines of

business in 60 locations around the world.

TSS provides clients with critical products and

services, including global custody in more than

90 global markets, holding nearly $15 trillion

in assets; corporate cash management, moving

an astounding $10 trillion a day of cash transactions

around the world for clients; corporate

card services, providing 27 million cards to

more than 5,000 corporate clients and government

agencies; and trade services, guaranteeing

international payments for our clients,

who are many of the world’s largest global

companies. Following are some specific examples

of how TSS supports a range of clients:

• We delivered unemployment and other

benefits to more than 12 million individuals

in 2009, as the national leader in bringing

electronic banking services to low-income

households through electronic benefits

transfer and debit and stored-value cards.

• We were selected by the Federal Reserve

to serve as custodian for its program to

purchase up to $1.25 trillion in mortgage-backed

securities in order to provide support

to the mortgage and housing markets.

• We are the leading cash management

provider to the U.S. Postal Service,

providing cash and check depository

services to nearly one-third of the U.S.

Postal Service’s 80 districts.

How we intend to grow

TSS essentially grows by following its clients

around the world, which means opening

new branches and constantly improving

products. In 2009, TSS opened new branches

in China, Denmark, Finland, Norway and

Sweden; launched new services in Tokyo,

South Korea, Brazil and Mexico; and expanded

capabilities in Australia, India, Europe, the

Middle East and Africa. We will continue this

expansion for the foreseeable future.

In addition, more than three years ago, TSS

and the Investment Bank formed a joint

venture to create our Global Corporate Bank.

With a team of more than 100 corporate

bankers, the Global Corporate Bank serves

multinational clients by giving them access

to TSS products and services and certain

IB products, including derivatives, foreign

exchange and debt. We intend to expand the

Global Corporate Bank aggressively over the

next several years by opening 20-30 locations

and adding 150 corporate bankers, allowing

us to cover approximately 1,000 new clients

(3,100 total, up from 2,100). Asset Management reported net income of

$1.4 billion with an ROE of 20%

Overall results

Asset Management, with assets under supervision

of $1.7 trillion, saw earnings increase by

5% in a year that began with strong negative

headwinds and finished with a market rally.

Overall, the year’s results reflected several

trends, including strong investment performance,

continued growth in Private Banking,

excellent investment performance from Highbridge

Capital Management and a breakout

year for our U.S. retail mutual funds business.

All of these trends reflected an improving

story from the challenges of the past two years.

What we do in Asset Management

Our Asset Management franchise consists

of two primary businesses. The first is Investment

Management, in which 6,500 employees

help institutions and retail investors worldwide

manage their cash; provide equity, fixed income

and alternative investment strategies; and

administer 401(k) services for large and mid-size

U.S. employers. Overall, we manage more than

$1.2 trillion in assets for our clients.

Our second primary business is Private

Banking. Our 1,900 private bankers help the

world’s wealthiest individuals and families

grow, manage and sustain their wealth with

investing, portfolio structuring, capital advisory,

philanthropy and banking services.

Throughout 2009, our Asset Management

professionals advised institutions on how to

strengthen pension plans for the benefit of

their employees; advised more than 1.6 million

401(k) participants on achieving a secure

retirement; executed comprehensive financial

plans for family enterprises and business

owners; distributed more than $100 million

to charities on behalf of fiduciary clients; and

brought market insight and top-performing

products to financial advisors who guide

millions of individual investors worldwide.

Within Asset Management, our Fixed

Income group solidified its position as the

#1 provider of global liquidity (we manage

$590 billion), and our U.S. Equity platform

had 82% of assets under management in the

top two quartiles of peer fund group investment

performance over five years. Our U.S.

retail business had an exceptional year despite

clients’ broadly based risk aversion, bringing

in record net asset flows and ranking third in

net new long-term flows in the industry – due

principally to the sale of strong-performing

fixed income products.

Private Banking experienced record revenue

due to inflows from clients and solid investing,

lending and banking activity, as well as the

addition of nearly 100 client advisors and five

new Private Wealth Management offices (in

Miami, Philadelphia, San Francisco, Seattle

and Washington, D.C.).

In mid-2009, J.P. Morgan assumed 100%

ownership of Highbridge Capital Management,

one of the largest alternative asset managers

in the United States, with $21 billion in client

assets. We acquired Highbridge in 2004 to

augment our alternative investment offerings

for clients. Highbridge delivered the best

investment performance in its history in 2009,

and just five years into our partnership, its

assets have grown threefold.

Importantly, rigorous risk management

enabled Asset Management to provide valuable

support to our clients and avoid many

of the negative developments that surfaced

during the financial crisis and damaged an

untold number of investors.

How we intend to grow

Our Investment Management business is

developing new global strategies, including

funds focused on maritime investments,

commodities, distressed debt and China. We

also plan to enhance Investment Management’s

global distribution with the addition

of more than 200 employees and increased

budgets for marketing and client outreach. In 2010, we plan to expand Private Banking

globally by adding more than 500 bankers,

investors and client service employees. In addition,

we intend to continue to invest in the

growth of the brokerage business we acquired

from Bear Stearns. We anticipate a slowly

improving but volatile investment environment

in 2010 – yet, nonetheless, we expect

Asset Management to continue to thrive by

helping millions of individuals, families and

institutions achieve their financial goals.

The Corporate sector reported net income

of $3.7 billion

Our Corporate sector, excluding merger-related

items, produced net income of $3.7

billion compared with $768 million in the

prior year. The Corporate sector comprises

three segments: Private Equity, unallocated

corporate expenses and our corporate investment

portfolio. Our Private Equity segment

reported a net loss of $78 million vs. a net loss

of $690 million in 2008. Remember, however,

in 2007, we had an outstanding year with

pretax Private Equity gains of more than $4

billion. We know that Private Equity returns,

by their nature, are lumpy, but we expect to

average 20% returns over the years.

Our corporate investment portfolio, which

we own in order to manage excess cash, our

collateral needs and interest rate exposure,

grew from a low of $91 billion in March 2008

to an average of $324 billion in 2009. Our

investment portfolio produced exceptional

performance, the result of both managing

interest rate exposures and buying securities

that we thought were extremely safe investments

and were trading at large discounts to

fair value (e.g., mortgage ABS, Triple-A credit

card ABS and Triple-A CLOs). The pretax

unrealized gain of this portfolio went from a

loss of $3.4 billion at the beginning of 2009 to

a gain of $3.3 billion at year-end. It’s important

to note that your company manages its

interest rate exposure extremely carefully and

believes that taking this exposure is fundamentally

not how we make our money. Any

investor can take on interest rate exposure –

we do not consider that a business. We do not

borrow “cheap” from the Federal Reserve or

any other source; we borrow at market rates,

like everyone else does.

We may realize some of these Corporate

investment gains in 2010, but we do not expect

these exceptional results to continue. Over

the course of the year, Corporate quarterly

net income (excluding Private Equity, merger-related

items and any significant nonrecurring

items) is expected to decline to approximately

$300 million. Nothing is more vital to the long-term growth

of JPMorgan Chase than our ability to attract

and retain talented and dedicated employees.

Ours is a complicated business. Managing it

requires complex systems, extensive quantitative

skills and risk discipline. The pressure

can be enormous and wide-ranging – from a

trader dealing with large positions to a call

center employee helping a customer modify

a mortgage loan that no longer is affordable.

Being smart is not enough; it also takes a high

level of social intelligence and skill to handle

all types of customers facing all kinds of

challenging circumstances.

Success at our firm requires that employees

treat clients and customers respectfully and

fairly and stay true to the values embedded in

our culture: personal commitment, honesty,

teamwork, diversity and community awareness.

Ensuring we have the best people, training and

leadership requires that we do many things

right, from recruiting and training to recognizing,

rewarding and developing leaders.

This is what enables us to attract, retain and

develop the best people.

Recruiting and training talent

The breadth, complexity and variety in the

work our people do are impressive by any

measure but are not well-understood. We have

220,000 employees around the world. While

some of us have high-profile jobs and receive

great attention – not always for the better

these days – many others are not in the public

eye. These individuals are essential to our

global operations and include:

• Nineteen thousand programmers, application

developers and information technology

employees who tirelessly keep our 80 data

centers, 55,000 servers, 225,000 desktops

and global network up and running – and

who were a major part of completing the

Bear Stearns and WaMu conversions in

record time.

• Eighty thousand employees fulfilling operations

functions globally and thousands

of customer service colleagues. In 2009,

they responded to more than 245 million

phone calls – to help customers stay in their

homes, understand credit card payment

plans and avoid financial problems during

these difficult times.

• Thirteen thousand people in Legal & Compliance,

Risk, Audit, Human Resources and

Finance in 60 countries who rigorously

analyze facts and figures, thoughtfully

review the policies we have and address the

issues we face. For example, we rely upon

hundreds of credit risk officers to manage

our various exposures, including $2 billion of

new loans we make on average every day.

• Thousands more of our colleagues working

behind the scenes to keep our operations safe

and efficient, including mailroom attendants,

mechanics and engineers, executive assistants,

receptionists, security personnel and those

who manage our facilities worldwide.

To fill these jobs, we hire thousands of

employees each year, all of whom must be

trained in our products, services and procedures

in order to do their jobs well. Annually,

we hire 1,800 people with advanced degrees

(including M.B.A.s and Ph.D.s). Thousands of

our people have advanced degrees in math,

science and physics. While many of these

people work in the Investment Bank, others

work in Asset Management, Credit and Risk

Analysis, Consumer Lending and Treasury &

Securities Services, as well as in data centers

across the firm.

Employees of JPMorgan Chase receive ongoing

training and development to ensure they are

well-equipped to manage the complex systems,

risk management disciplines and client relationships

that are critical to our franchise.

Additionally, many are prepared to assume

managerial and leadership roles over time.

Our company has 94 management development programs and more than 20,000 training

programs (including online courses) that

enable our people to hone and expand their

skills in a rapidly changing business.

Ongoing assessment and development

At JPMorgan Chase, we are fortunate to attract

world-class talent. We owe it to our employees,

our customers and our shareholders to create

an environment in which our people can do

their best work. Toward this end, we believe

in assessing their strengths and weaknesses

and regularly giving them honest and thorough

feedback. Additionally, we know that

in order to sustain our strong competitive

position, we must focus on developing exceptional

leaders. This starts with a clear and

shared understanding about the attributes we

value most in senior managers. These qualities

must be intentionally fostered and reinforced

through a rigorous talent assessment process.

This process now is embedded as part of how

we operate. We also are developing a general

management program for M.B.A. students to

help us add to our bench and build general

management talent on an ongoing basis.

Encouraging mobility and multiple careers

Talent mobility and optimization are key to our

long-term success. We have to clearly outline

what people need to do to move to the next

level at JPMorgan Chase. We are working to

do away with statements such as, “My boss

won’t let me go … or my boss won’t let me

look at positions in other divisions.” People

have the right to explore different career

opportunities and follow their dreams. While

it’s also an individual’s responsibility to

manage his or her own career, it’s our job to

help facilitate that. We strive to be proactive

and thoughtful in that regard.

Intense focus on succession

We need to be honest and thoughtful about

potential successors, particularly for senior

jobs. We have redoubled our efforts to

ensure that we have people in the pipeline

who are capable of assuming senior levels of

responsibility three, five or even seven years

out or right away if necessary (the “hit by a

truck” emergency scenario). This is true for

my job as well.

Poor CEO succession has destroyed many a

company. CEO and management succession

often seems more like a psychological drama

or a Shakespearean tragedy than the reasoned

and mature process it should be. It is in our

best interest to avoid such drama.

I want to assure you, our shareholders, that

your Board believes that we have within the

organization some outstanding people who

could do my job today; and we will continue to

rotate some of our senior people across the business

to ensure that others are fully developed to

take my job in the future. The Board of Directors

not only believes that this is a priority but

that it is of the utmost importance. And you can

rest assured that your Board members are on

the case. They personally know all of the Operating

Committee members of the company (and

many others), and the Board members periodically

review – with and without me – your

company’s key succession plans.

Getting compensation right

Compensation is one of the most complex

issues we confront – it is important to our

employees, our company, our shareholders

and, increasingly, the public at large. A poorly

conceived compensation strategy can devastate

a company by attracting the wrong people

and incenting them to do the wrong things

for the wrong reasons. At JPMorgan Chase,

we put a great deal of time and thought into

designing compensation plans that attract

and motivate good people and reward good

behavior. Of course, compensation aside, we

always expect our people to do the right thing.

A badly designed compensation plan never is

an excuse for bad behavior.

Many people are concerned and angry about

compensation practices across the financial

services industry – and many of these

concerns are quite legitimate. Senior leaders

at some companies made a great deal of money while their companies failed and, in

the process, helped contribute to the crisis in

our country. This angers me, too. But not all

companies were reckless – and not all companies

had bad compensation practices.

In this section, I’m going to describe how our

overall 2009 compensation related to other

industries, present some overall principles

that guide us and explain how we apply these

principles in compensating our people.

Comparing JPMorgan Chase with other

industries

In 2009, JPMorgan Chase’s total expenses were

$52 billion. The total compensation (salaries

and benefits and incentives) your company

paid out was $27 billion.

As seen above, we paid salaries and benefits

of approximately $74,000 per person and

incentive compensation on average of $46,000

per person for a total of $120,000 per person.

These salary and benefit numbers are generally

in line with other major companies –

financial and non-financial.

The incentive awards come in various forms

(cash, commissions, restricted stock, options,

etc.). Approximately 32% of the incentive

compensation for 2009 was in restricted stock

and options that vest over a number of years.

At JPMorgan Chase, the use of stock options

is very restricted – we only use stock options

for approximately 500 people a year – and

represents just 1%-2% of the company’s total

compensation expense.

Many commentators, in an attempt to measure

fairness and reasonableness of a company’s

compensation payouts, have looked at total

compensation as a percentage of revenue. On

this basis, JPMorgan Chase’s total compensation

(salaries, benefits and bonuses) was 27%

for 2009; this number averaged 33% over

the previous several years. For our Investment

Bank alone – the part of the company

receiving the most scrutiny – compensation

was 33% of revenue, down from an average

of 44% over the last five years.

The chart on the next page compares these

same percentages with a wide mix of businesses.

For the average U.S. business, total

compensation as a percentage of revenue is

approximately 16%. In general, at businesses

that are people-intensive and not capital- or

intellectual property-intensive, such as professional

services companies, a high percentage

of the company’s revenue is paid out to the

employees. Law firms, for example (which

are not included in the following table), pay

out more than 80% of their revenue to their

employees. In highly capital-intensive companies,

like telecommunications or certain

manufacturing companies, payout ratios are

considerably lower.

Some commentators also have looked at total

compensation as a percent of profits. Here you

see a similarly wide range of results.

Essentially, the financial dynamics and structures

of various businesses are very different,

and looking at these ratios always will produce

divergent conclusions – they alone do not

reveal very much.

It also is important to point out that at many

companies, a significant amount of incentive

compensation generally is paid regardless

of whether or not the overall company does

well. Many companies pay certain individuals

based on their specific performance (sales and

service employees) and not necessarily on the

performance of the company.

JPMorgan Chase does employ a number of

highly compensated individuals, probably

more than in many other industries – but not all. We are unable to find real comparisons.

Much of the anger about highly compensated

individuals at banks relates to the argument

that all of these companies would have failed,

which we do not believe is true (more detail

on this in the next section). Finally, the more

highly paid the individual is at JPMorgan

Chase, the higher the percentage of compensation

awarded in restricted stock and options.

Before we speak specifically about how we

compensate individuals at JPMorgan Chase,

it’s appropriate to outline our principles.

Some key compensation principles at

JPMorgan Chase

We believe the compensation principles we

use are best practices and compare favorably

with those outlined by outside authorities,

such as the G-20, the Financial Services

Authority, the Financial Stability Board, the

Federal Reserve and the U.S. Treasury. Our

principles are as follows:

• Pay a significant percentage of our incentive

compensation in stock: at least 67% for the

Operating Committee members and approximately

50% for the remainder of our senior

management team.

• Structure the stock we grant – restricted stock

units or options – to vest over multiple years.

• Require Operating Committee members to

retain and hold approximately 75% of the

stock they receive from the company after

the stock vests.

• Generally do not provide multi-year guarantees

to new hires and almost never to

current employees.

• Institute meaningful recoupment policies,

some of which we enhanced in 2008 and

2009 and are progressively more stringent

at higher levels of management. For

all employees, if anyone causes material

financial or reputational harm to the firm

or its business activities, we can recoup the

employee’s incentives, including stock.

• For approximately 500 senior individuals,

unvested stock also can be recouped for

failure to properly identify, raise or assess, in

a timely manner and as reasonably expected,

material risks to the firm.

• For the Operating Committee and for me,

unvested stock or options can be recouped

not only for the reasons mentioned above but

also if reasonable progress toward personal

and company goals is not met. This is at the

discretion of the Board of Directors. Pay our people for performing well over

multiple years and for helping to build

enduring performance.

• Ensure that financial results – a key metric

(but not the only one) we use to pay our

people – always include profits adjusted

for risk; that is, the more capital a business

uses, the more it is assessed a charge for

that capital.

• Recognize revenue for complex and long dated

trades or products over multiple years

to properly reflect the risk. Try to be as

conservative as possible regarding accounting

– aiming not to recognize profits at all when

we think doing so is inappropriate.

Some of our other compensation principles go

beyond what regulators have asked for but, we

believe, are equally important. For example:

• We do not have change-of-control agreements,

special executive retirement plans or

golden parachutes, or special severance packages

for senior executives.

• We do not pay bonuses for completing

a merger, which we regard as part of the

job. When the merger has proved to be

successful, compensation might go up.

• We feel strongly that financial outcomes

alone do not represent a comprehensive

picture of performance. Broader contributions

– such as continually honing leadership

skills; maintaining integrity and compliance;

recruiting and training a diverse, outstanding

workforce; building better systems; and

fostering innovation, to name just some

important qualities – matter a great deal. In

fact, in our business, basing compensation

solely on financial or quantitative measures,

and ignoring qualitative measures, can be

disastrous. Good performance in a particular

year does not necessarily indicate that the

individual did a good job.

• We are mindful that a rising tide lifts all

boats so we take into account how much a

strong market, as opposed to the initiative

of the individual or group, contributed to

the results.

• We must be highly competitive on compensation,

which is absolutely crucial to being

a great company. While we aim to be a

company that pays its employees well, it

should be because we have been a well-performing

company.

• We want our employees to be shareholders.

All of the policies described above have

been effective in this regard: Our employees

own 488 million shares and options, a

significant portion of which is unvested –

i.e., of no value to the individual if he or she

were to leave the company for a competitor.

Ownership does not guarantee that

our employees will act like owners, but it

certainly improves the odds.

How we pay individuals

Our starting point when it comes to compensation

is, as it should be, risk-adjusted financial

performance. We keep thousands of profit-and-loss

statements (by branch, by trading desk, etc.).

While we don’t maintain incentive compensation

pools at such a granular level, we do have

hundreds of such pools; we try to maintain a

very disciplined approach to relate compensation

as closely as possible to performance.

However, we do not stop there. We make

adjustments based on our own judgments

about how the company is doing (in absolute

and in competitive terms) and for very specific

business decisions, such as additions to staff

or large, new investments that affect profits. In

some cases, the impact of these sorts of discretionary

factors will be negligible. In other

cases, the discretion we exercise may have a

significant effect on the size of an incentive

compensation pool. If we feel the pool amount

was not earned, we do not pay it. Some individuals are paid incentive compensation

based on very specific metrics; for

example, people in our call centers, retail

branches and operating centers. These metrics

may be increased or reduced somewhat by

the company’s performance. There also are

a few senior people who are paid on specific

metrics. For example, bankers who manage

money for our clients have their compensation

tightly tied to the kind of job they did for

their clients. I think you would agree that this

is completely appropriate.

Most of our senior people are not paid by

formula – we use multiple metrics to assess

performance and then apply a great deal of

judgment. In general, the more senior the

executive, the more the compensation should

relate to the company’s performance overall.

This is especially true for the leadership team

of each business.

When it comes to an individual, we look at his

or her performance, the unit results and the

overall performance of the company. Since

we generally know these individuals well, we

evaluate their performance over a multi-year

period. It is important that we recognize our

best people – many of those in senior positions

have generally proved themselves over

many, many years.

We also are keenly aware of our competition

and know what it would take to replace

a person if we had to hire someone new. We

cannot operate in a vacuum.

Our most senior people – members of our

Operating Committee – have their compensation

tightly tied to the company’s performance,

and they also are evaluated on their leadership

skills. In 2008, when the company’s earnings

were down 64%, your senior management’s

compensation was down 67% (this doesn’t

include me; I received no year-end incentive).

We know there are people in this industry

who have been extraordinarily well-paid – and,

in some cases, overpaid. Some of these people

have benefited from profits that turned out

to be ephemeral or were the result of excessive

leverage in the system. Some benefited

from extreme competition for their specific

talents, often from hedge funds and other

such businesses. While no firm can claim it

gets compensation right every time, we at

JPMorgan Chase do think we have generally

been disciplined when it comes to our decisions.

We believe we have the right compensation

practices, but that is only one part of

building a great company. The most important

part is developing great leaders.

Developing leaders

Earlier in this section, I mentioned that my

number one priority is to put a healthy and

productive succession process in place. As I

will be increasingly focused on this process,

I would like to share my thoughts about the

essential qualities a leader must have, particularly

as they relate to a large multinational

corporation like JPMorgan Chase.

Leadership is an honor, a privilege and a deep

obligation. When leaders make mistakes, a lot

of people can get hurt. Being true to oneself

and avoiding self-deception are as important

to a leader as having people to turn to for

thoughtful, unbiased advice. I believe social

intelligence and “emotional quotient,” or

EQ, matter in management. EQ can include

empathy, clarity of thought, compassion and

strength of character.

Good people want to work for good leaders.

Bad leaders can drive out almost anyone who’s

good because they are corrosive to an organization;

and since many are manipulative and

deceptive, it often is a challenge to find them

and root them out.

At many of the best companies throughout

history, the constant creation of good leaders

is what has enabled the organizations to stand

the true test of greatness – the test of time.

Below are some essential hallmarks of a good

leader. While we cannot be great at all of these

traits – I know I’m not – to be successful, a

leader needs to get most of them right. Discipline

This means holding regular business reviews,

talent reviews and team meetings and

constantly striving for improvement – from

having a strong work ethic to making lists and

doing real, detailed follow-up. Leadership is

like exercise; the effect has to be sustained for

it to do any good.

Fortitude

This attribute often is missing in leaders: They

need to have a fierce resolve to act. It means

driving change, fighting bureaucracy and politics,

and taking ownership and responsibility.

High standards

Abraham Lincoln said, “Things may come

to those who wait … but only the things left

by those who hustle.” Leaders must set high

standards of performance all the time, at a

detailed level and with a real sense of urgency.

Leaders must compare themselves with the

best. Huge institutions have a tendency toward

slowing things down, which demands that

leaders push forward constantly. True leaders

must set the highest standards of integrity

– those standards are not embedded in the

business but require conscious choices. Such

standards demand that we treat customers

and employees the way we would want to be

treated ourselves or the way we would want

our own mother to be treated.

Ability to face facts

In a cold-blooded, honest way, leaders emphasize

the negatives at management meetings

and focus on what can be improved (of course,

it’s okay to celebrate the successes, too). All

reporting must be accurate, and all relevant

facts must be reported, with full disclosure and

on one set of books.

Openness

Sharing information all the time is vital –

we should debate the issues and alternative

approaches, not the facts. The best leaders kill

bureaucracy – it can cripple an organization

– and watch for signs of politics, like sidebar

meetings after the real meeting because people

wouldn’t speak their mind at the right time.

Equally important, leaders get out in the field

regularly so as not to lose touch. Anyone in a

meeting should feel free to speak his or her

mind without fear of offending anyone else.

I once heard someone describe the importance

of having “at least one truth-teller at the table.”

Well, if there is just one truth-teller at the

table, you’re in trouble – everyone should be

a truth-teller.

Setup for success

An effective leader makes sure all the right

people are in the room – from Legal, Systems

and Operations to Human Resources, Finance

and Risk. It’s also necessary to set up the right

structure. When tri-heads report to co-heads,

all decisions become political – a setup for

failure, not success.

Morale-building

High morale is developed through fixing

problems, dealing directly and honestly with

issues, earning respect and winning. It does

not come from overpaying people or delivering

sweet talk, which permits the avoidance

of hard decision making and fosters passive aggressive

behaviors.

Loyalty, meritocracy and teamwork

While I deeply believe in loyalty, it often is

misused. Loyalty should be to the principles

for which someone stands and to the institution:

Loyalty to an individual frequently is

another form of cronyism. Leaders demand a

lot from their employees and should be loyal

to them – but loyalty and mutual respect are

two-way streets. Loyalty to employees does not

mean that a manager owes them a particular

job. Loyalty to employees means building a

healthy, vibrant company; telling them the

truth; and giving them meaningful work,

training and opportunities. If employees fall

down, we should get them the help they need.

Meritocracy and teamwork also are critical but

frequently misunderstood. Meritocracy means

putting the best person in the job, which

promotes a sense of justice in the organization

rather than the appearance of cynicism: “Here

they go again, taking care of their friends.”

Finally, while teamwork is important and often

code for “getting along,” equally important is

an individual’s ability to have the courage to

stand alone and do the right thing.

Fair treatment

The best leaders treat all people properly and

respectfully, from clerks to CEO s. Everyone

needs to help everyone else at the company

because everyone’s collective purpose is to serve

clients. When strong leaders consider promoting

people, they pick those who are respected and

ask themselves, Would I want to work for him?

Would I want my kid to report to her?

Humility

Leaders need to acknowledge those who came

before them and helped shape the enterprise

– it’s not all their own doing. There’s a lot of

luck involved in anyone’s success, and a little

humility is important. The overall goal must

be to help build a great company – then we

can do more for our employees, our customers

and our communities.

The grey area of leadership

There are many aspects of the leadership

process that are open for interpretation. This

grey area contributes to the complexity of the

challenges that leaders – and those who govern

them – face. I would like to share with you where

I stand with regard to a few of these issues.

Successful leaders are hard to find

There are examples of individuals who have

been thrust, wholly unprepared, into positions

of leadership and actually perform well

– I think of President Harry Truman, among

others. I would submit, however, that relying

on luck is a risky proposition. History shows

that bad or inexperienced leaders can produce

disastrous results. While there are possibly

innate and genetic parts of leadership (perhaps

broad intelligence and natural energy), other

parts are deeply embedded in the internal

values of an individual; for example, work

ethic, integrity, knowledge and good judgment.

Many leaders have worked their entire lives to

get where they are, and while perhaps some

achieved their stature through accident or

politics, that is not true for most. Anyone on a

sports team, in government or in virtually any

other endeavor knows when he or she encounters

the rare combination of emotional skill,

integrity and knowledge that makes a leader.

Successful leaders are working to build something

Most leaders I know are working to build

something of which they can be proud. They

usually work hard, not because they must

but because they want to do so; they set high

standards because as long as leaders are going

to do something, they are going to do the best

they can. They believe in things larger than

themselves, and the highest obligation is to

the team or the organization. Leaders demand

loyalty, not to themselves but to the cause for

which they stand.

Nonetheless, compensation does matter

While I agree that money should not be the

primary motivation for leaders, it is not

realistic to say that compensation should not

count at any level. People have responsibilities

to themselves and to their families. They

also have a deep sense of “compensation

justice,” which means they often are upset

when they feel they are not fairly compensated

against peers both within and outside

the company. There are markets for talent,

just like products, and a company must pay a

reasonable price to compete.

Big business needs entrepreneurs, too

The popular perception is that entrepreneurs

– those who believe in free enterprise – exist

only in small companies and that entrepreneurs

in small companies should be free to

pursue happiness or monetary gain as appropriate.

Free enterprise, entrepreneurship and

the pursuit of happiness also exist in most

large enterprises. And you, our shareholders,

should insist on it. Without the capacity to

innovate, respond to new and rapidly changing

markets, and anticipate enormous challenges,

large companies would cease to exist. The

people who achieve these objectives want to

be compensated fairly, just as they would be if

they had built a successful start-up. Performance isn’t always easy to judge

Managers responsible for businesses must

necessarily evaluate individuals along a spectrum

of factors. Did these individuals act with

integrity? Did they hire and train good people?

Did they build the systems and products that

will strengthen the company, not just in the

current year but in future years? Did they

develop real management teams? In essence,

are they building something with sustainable,

long-term value? Making these determinations

requires courage and judgment.

Sometimes leaders should be supported and paid

even when a unit does poorly

If a company’s largest, and perhaps most

important, business unit is under enormous

stress and strain, unlikely to earn money

regardless of who is running it, a manager

might ask his best leader to take on the job.

This may be the toughest job in the company,

one that will take years to work through before

the ship has been righted. When the manager

asks a leader to take on the responsibility,

she quite appropriately will want to know

whether she will be supported in the toughest

of times: “Will you make sure the organization

doesn’t desert me?” “Will you stop the politics

of people using my unit’s poor performance

against me?” “Will you compensate me fairly?”

My answer to all of these questions would be

yes. And as long as I thought she were doing

the job well, I would want to pay her like our

best leaders, profits aside. Conversely, we all

know that a rising tide lifts all boats. When

that’s the case, paying that leader too much is

possibly the worst thing one can do – because

it teaches people the wrong lesson.

Evaluating the CEO

The CEO should be held strictly accountable

by the Board of Directors. The Board should

continually review the CEO’s performance

and give feedback (and coaching). The Board

alone should determine the compensation for

the CEO. At every regularly scheduled Board

meeting at JPMorgan Chase, the directors also

have a private meeting without me. Compensation

committees and the Board need to be

independent thinkers – and yours are. They

review lots of data to evaluate the performance

of the company, including reviewing competitors’

performance and their compensation

practices. Our Board members do not rely on

compensation consultants to make decisions

for them. The Board members believe that

determining how to compensate the CEO (and

all of our senior management) is their responsibility

and cannot be outsourced.

In two of the last 10 years, I received no bonus,

which I thought was absolutely appropriate. In

2000, Bank One was in terrible shape – we had

to lay off approximately 10,000 people, and I

thought it completely inappropriate that I take

a bonus. That year, my first at Bank One, I had

a guarantee – I gave it up. The second time

was in 2008, and our financial results were just

too mediocre to contemplate a bonus for the

CEO. Since we did pay many other people in

those two years, we also lived by the principle

that the CEO does not have to be the highest

paid person in the company.

In all the years I’ve worked at this company,

much of my compensation (approximately

65%) has been in stock. I’ve never sold a share

and do not intend to do so as long as I’m in this

job. In fact, when I joined Bank One, I bought

a lot of stock outright, not because I thought it

was cheap (in fact, I thought it was overvalued)

but because I wanted to be tethered tightly to

the company and its performance. We need rational policies based on facts and

analysis

The recent financial crisis has caused great

distress across the country and around the

world, but it also has provided us with a path

for going forward. The era of bailouts must

end, and the oversight of system-wide risk

must increase, among other changes. David

Hume said, “Reason is … slave of the passions

…” But if we rewrite the rules for banks out

of anger or populism, we’ll end up with the

wrong solutions and put barriers in the way

of future economic growth. Good policy and

financial reform must be based on facts and

analysis and need to be comprehensive, coordinated,

consistent and relevant.

As New York Times columnist Thomas L.

Friedman noted earlier this year, “We need a

new banking regulatory regime that reduces

recklessness without reducing risk-taking,

which is the key to capitalism.” In striking

this regulatory balance, the details matter. We

should focus on building good regulation – not

simply more or less of it. The last thing we

need is to enact new policies that over-regulate

and work at cross-purposes without reducing

system-wide risk. None of us can afford the

costs of unnecessary or bad regulation.

While we acknowledge that making good

decisions takes time, we think it is important

to complete financial reform this year. The

lack of regulatory clarity is creating problems

for banks and for the entire economy. Businesses

need confidence and certainty to grow

(and to create jobs). Passing sensible financial

reforms will provide some of the certainty

the business sector needs. With this in mind,

I would like to discuss the critical lessons

learned and how they are central to getting

regulatory reform right.

The crisis had many causes

In my 2008 letter to shareholders, I discussed

the fundamental causes and contributors to

the financial crisis. I won’t repeat them in

detail here, but, broadly speaking, they were

as follows:

• The burst of a major housing bubble, caused

by bad mortgage underwriting, a somewhat

unregulated mortgage business and some

misguided government policies.

• Excessive, pervasive leverage across the

system, including banks, investment banks,

hedge funds, consumers and the shadow

banking system.

• The dramatic growth of structural risks and

the unanticipated damage they caused (the

flaws of money market funds and the repo

system). Remember, we had a “run” on the

capital markets.

• Regulatory lapses and mistakes: Basel capital

rules that required too little capital and

didn’t account for liquidity and relied too

much on rating agencies; the Securities and

Exchange Commission allowing U.S. investment

banks to get too leveraged; and poor

regulation of Fannie Mae and Freddie Mac,

among many elements of an archaic, siloed

regulatory system. However, we should not

and do not blame regulators for the failures

of individual companies, ever – management

is solely to blame.

• The pro-cyclical nature of virtually all

policies, actions and events (e.g., loan loss

reserving, capital requirements and the

market itself).

• The impact of huge trade and financing

imbalances on interest rates, consumption

and speculation levels. The heart of the problem – across all sectors

– was bad risk management. Many market

participants improperly used value-at-risk

(VaR) measurements; they did not run stress

tests to be prepared for the possibility of a

highly stressed environment; they excessively

relied on rating agencies; they stretched too

much for current earnings; and they didn’t

react quickly when markets got bad.

At JPMorgan Chase, we never overly relied on

VaR, and we regularly ran stress tests to make

sure we were prepared for bad environments.

Our goal was and is to remain profitable

every quarter.

While it is tempting to identify a scapegoat

– banks, businesses, the government or

consumers – it is pretty obvious that no one

was solely to blame and that no one should be

completely absolved from blame.

Yes, we made mistakes …

… and we have identified and described them

in great detail in prior years’ chairman’s letters.

Our two largest mistakes were making too

many leveraged loans and lowering our mortgage

underwriting standards. While our mortgage

underwriting was considerably better

than many others’, we did underwrite some

high loan-to-value mortgages based on stated,

not verified, income. We accept complete

responsibility for any and all mistakes we

made or may have made.

There also are many mistakes that we did not

make, among them: structured investment

vehicles (SIVs), extreme leverage, excessive

reliance on short-term funding, collateralized

debt obligations and improper management of

our derivatives book.

Some of the mistakes we made may have

contributed to the crisis. For those, of course,

we are sorry – to both the public and our

shareholders. However, it would be a huge

stretch to say that these mistakes caused the

crisis. In fact, at the height of the crisis, we

aggressively took actions that we believed

helped mitigate some of the fallout from the

crisis and contributed to the stabilization and

recovery (e.g., our purchase of Bear Stearns

and WaMu and our interbank lending; that is,

loans that banks make directly to each other).

Yes, we should thank the government for its

extraordinary actions

As noted in last year’s letter, we think the

government acted boldly and urgently in

dealing with a complex and rapidly changing

situation. Without many of these actions, we

believe the outcome could have been much

worse. A great number of the actions that the

Treasury and the Federal Reserve took, directly

and indirectly, benefited a number of institutions

and may have saved many from failure

and bankruptcy.

Without these actions, however, not all banks

would have failed

The premise that all banks would have failed

had it not been for the government’s actions

is incorrect. This premise is behind much of

the anger toward banks and some of the policy

recommendations that are meant to punish

banks. We should acknowledge that the worst

offenders among financial companies no

longer are in existence. And while it is true

that some of the surviving banks would not, or

might not, have survived, not all banks would

have failed. I know I speak for a number of

banks when I say that some of us accepted

the Troubled Asset Relief Program (TARP)

capital not because we needed it to survive but

because we believed we were doing the right

thing to help the country and the economy.

We were told the government wanted even

the healthy banks to take TARP to set an

example for all banks and to make it easier for

the weaker institutions to accept the capital

without being stigmatized. JPMorgan Chase

and many other banks were in a position to try

to help, and that is what we did. At the worst point in the crisis, we

aggressively provided credit

Throughout the financial crisis, JPMorgan

Chase never posted a quarterly loss. We served

as a safe haven for depositors, worked closely

with the federal government and remained an

active lender.

Our fortress balance sheet enabled us to buy

Bear Stearns in March 2008, adding $289

billion in assets; then we acquired Washington

Mutual just six months later, adding a further

$264 billion of assets. Through it all, JPMorgan

Chase absorbed the stress of higher consumer

and wholesale credit losses while maintaining

high liquidity and acceptable growth in our

capital. We acquired Washington Mutual just

10 days after Lehman Brothers’ collapse on

September 15, 2008, and, in order to maintain

our fortress balance sheet, immediately sold

$11.5 billion in common stock the following

morning. The takeover of Bear Stearns and

WaMu provided essential credit and support

to the system and minimized a potentially

disastrous disruption that could have resulted

from their failures. In the several months

after Lehman’s failure, our interbank lending

grew from almost nothing to as high as $70

billion, and our average lending was approximately

$100 billion per month, even higher

than it had been in the prior months. We also

purchased, at one point, a net $250 billion of

securities, which helped facilitate much-needed

liquidity in the marketplace.

We consistently maintained extremely

high capital levels

As the chart below shows, we ended 2008 with

Tier 1 Common Capital of 7.0% (the critical

measure used by the Federal Reserve for its

bank stress tests), and we ended 2009 with

Tier 1 Common Capital of 8.8%.

In May 2009, the U.S. government ran a stress

test on 19 banks. The test assumed an adverse

environment of 10.4% unemployment and a

48% peak-to-trough decline in the housing price

index across a two-year time span. Upon completion

of the test, the results required 10 banks

to raise common equity to maintain 4% Tier 1

Common Capital through the end of the stress

scenarios. Under the government’s test, JPMorgan

Chase always had common equity of $40 billion

in excess of the 4% minimum (for the record,

the $25 billion of TARP capital we accepted was

preferred stock and, therefore, never was part

of this calculation). The bottom line is that we

passed the stress test with flying colors

We kept our liquidity extremely high

As we entered the most tumultuous financial

markets since the Great Depression, we experienced

the opposite of a “run on the bank”

as deposits flowed in (in a two-month period,

$150 billion flowed in – we barely knew what

to do with it). At JPMorgan Chase, our deposits

always exceeded our loans; deposits always

have been considered one of the safest sources

of funding for a bank. The average bank has

loans that are generally greater than 110% of

its deposits. For JPMorgan Chase, loans were

approximately 75% of deposits. In fact, our

excess deposits greatly reduced the need to

finance ourselves in riskier wholesale markets.

In the long-term wholesale unsecured markets,

we borrowed on average $270 billion. Only $40

billion was borrowed unsecured in the short-term

credit markets – an extraordinarily low

amount for a company of our size. When we

borrow in the secured markets, we do so under

the assumption that we would have access to

some, not all, of that funding in a crisis.

We always maintained excess liquidity at the

bank holding company. We had and continue to

have enough cash or cash equivalents on hand

to fund ourselves for more than two years, even

in the event that we are unable to borrow from

the unsecured credit markets at all.

We were prepared for things to get even worse

While the economic environment had become

as bad as any of us had ever seen, we reluctantly

prepared for the situation to get worse,

with a possible U.S. unemployment rate of

15% or higher. Such an adverse environment

would have required drastic actions: a large

headcount reduction, elimination of marketing

and other investments, and a decrease in

lending to preserve capital. Steps like these

would have saved more than $12 billion in

expenses and created considerable additional

capital. However, it also would have imposed

deep hardship on many of our employees,

suppliers and customers. Fortunately, we never

had to execute such a drastic plan. This was

precisely what the government was trying to

avoid, and I believe its actions helped prevent

many companies from taking steps like those

mentioned above.

Government programs were a mixed blessing

While we deeply appreciate the government’s

actions – and they clearly had benefits for the

system and for JPMorgan Chase – they also

were a mixed blessing.

In June 2009, we paid back the TARP capital

in full. The $25 billion we borrowed for eight

months cost us money, because we never were

able to lend the $25 billion and earn a rate

higher than the 5% coupon we were paying on

the preferred shares. In addition, we gave the

government warrants worth almost $1 billion –

a direct cost to our shareholders.

We did participate in the Federal Deposit

Insurance Corporation (FDIC) guarantee

program, under which we issued $40 billion of

debt with an FDIC guarantee. Many banks that

used this program would not have had access

to the capital markets without this guarantee

and possibly could have failed. For JPMorgan

Chase, it was not a question of access or need –

to the extent we needed it, the markets always

were open to us – but the program did save us

money. As part of this program, we have paid

the FDIC $1.3 billion, and, after paying the

FDIC, it will save us a significant amount of

money over the next few years.

Our company was highly criticized for

accepting the TARP capital and for using

the FDIC program. After April 1, 2009, even

though we were eligible to continue using the

FDIC program, we stopped using it. There

were many other government programs (with

acronyms such as TALF and PPIP) that we

believe were beneficial to the capital markets,

but that we did not need and chose not to use,

so as to avoid the stigma. (We did use the Term

Auction Facility (TAF), a special government

sponsored

depository facility, but this was

done at the request of the Federal Reserve to

help motivate others to use the system.)

While no one knows what would have

happened in the absence of all these government

programs, there is a strong argument

that those that entered the crisis in a position

of strength may have gathered huge benefits

at the expense of failing competitors – but it is

hard to argue that this would have been good

for the country.

We did not anticipate the anger or backlash

the acceptance of TARP capital would evoke

from the public, politicians and the media –

but, even with hindsight, I think we would

have had to accept TARP capital because doing

so was in the best interest of the country. I do

wish it would have been possible to distinguish

between the healthy and unhealthy banks in

a way that didn’t damage the success of the

program – so as not to create a situation where

the public was left with the impression that all

banks were bailed out. Last, I do regret having

used the FDIC guarantee because we didn’t

need it, and it just added to the argument that

all banks had been bailed out and fueled the

anger directed toward banks.

The government runs the FDIC, but the banks

pay for it

While the FDIC is a government institution

that insures bank deposits, our shareholders

should know that the costs associated with

failed banks are borne in full by the banks,

not by taxpayers. We think this is completely

appropriate. Even if the FDIC’s special Temporary

Liquidity Guarantee Program (TLGP)

had lost money, those losses would have been

charged back to the surviving banks. Therefore,

it is these surviving banks that have paid

for the cost to the FDIC of the approximately

200 bank failures since the beginning of 2008.

Of those failures, the largest one, WaMu (with

assets exceeding $260 billion), has cost the

FDIC nothing. That is because JPMorgan Chase

bought WaMu. All of the other banks that have

failed were far smaller (the next largest failure

was IndyMac, with $32 billion). All of these

failures combined have cost the FDIC an estimated

$55 billion.

Between deposit insurance and TLGP funding

for 2008 and 2009, plus estimates for our

share of assessments over the next three years,

JPMorgan Chase alone will have given the

FDIC a total of approximately $6 billion to

cover the cost of failed banks.

Banks are lending — a little less but more

responsibly

A great deal of media attention recently has

focused on what it will take to get banks

lending again. The reality is that banks

never have stopped lending: As of the end

of February 2010, according to the latest data

from the regulatory reports, total loans held

by commercial banks stood at $6.5 trillion –

higher than at the end of June 2007 and more

than 30% higher than in 2004.

How is it that businesses and consumers

clearly feel they have less access to bank credit

while the banks claim they are still lending?

This disconnect can be explained as follows:

1. T he flow of non-bank lending, which has

accounted for 65% of the credit supplied

in the United States, dried up. Many nonbank

lenders (think of the shadow banking

system, SIVs, the asset-backed commercial

paper market and the securitization

markets) virtually collapsed. These sources

of credit alone – and they were funded by

insurance companies, pension plans, and

corporate and foreign investors – reduced

the credit they were providing to the system

by nearly half a trillion dollars.

2. Bank lending did go up in the months

immediately after Lehman’s collapse, but

during the course of 2009, bank lending

started to decline in total. While more than

100 banks, including JPMorgan Chase,

stepped up and acquired failing banks,

they could not and did not fully replace the

extension of credit the failing banks had

been providing. For example, at JPMorgan

Chase, we did not continue the subprime

lending and option-ARM mortgages that

WaMu had been providing.

3. M any banks also tightened their loan standards,

which further reduced new loans.

4. Additionally, customer demand for loans

decreased across large and small businesses.

In fact, at JPMorgan Chase alone, loans to

large companies dropped (from $85 billion

to $50 billion). This was not due to our

reluctance to make the loans but rather

to large companies taking advantage of

the ability to finance at lower rates in the

reopened capital markets.

Banks have a responsibility to make sound

loans. Bad loans are one of the things that

got us into this mess in the first place. And,

unfortunately, making good loans often

means declining applications for loans that

do not meet safe and sound lending criteria.

While it may not seem obvious at the time,

turning down an application that fails to

meet these criteria actually may be in both

our and our client’s best interest. We have a

responsibility to lend only to those who can

handle the debt. Unlike many other businesses,

this puts us in the unpopular position

of saying no to some of our customers.

Banks are not fighting regulation

We at JPMorgan Chase and at other banks have

consistently acknowledged the need for proper

regulatory reform, and I also spoke about this

topic in great detail in last year’s letter.

Looking back, one of the surprising aspects

about the recent crisis is that most of the

specific problems associated with it (global

trade imbalances, the housing bubble, excessive

leverage, money market funds, etc.) were

individually well-known and discussed. But

no one, as far as I know, put together all of the

factors and predicted the toxic combination it

would become – and the crisis it would cause.

So what can we do to help fix the situation

going forward? We must focus on the

problem: bad risk management. This not only

caused financial institutions to fail, but it also

revealed fundamental flaws in the system

itself. These flaws existed at both a macro level,

where the interplay of the numerous critical

factors was missed, and a micro level: for

example, the failure to prevent AIG from taking

excessive, one-sided positions in trading derivatives

and the failure to limit mortgages to families

who could afford them and to keep loan-to-value

ratios to a more reasonable 80%-90%.Over the last 50 years, we have allowed our

regulatory system to become dangerously

outdated. The structure is archaic and leaves

huge gaps in the system. Today, in America,

banks account for only one-third of the credit

outstanding, with all kinds of non-banks taking

and trading risks and providing credit to the

system. So the idea that banking is confined

to deposit-holding entities is inaccurate and

deceptive. The failure of so many firms in

a range of sizes and categories – from Bear

Stearns and Lehman Brothers to IndyMac and

WaMu to Fannie Mae, Freddie Mac and AIG,

as well as local community banks – proves that

regulation needs to be administered by product

and economic substance, not by legal entity. We

have a chance to simplify and strengthen our

regulatory system, and, if we do it right, it will

not only be able to handle the complex challenges

we face today but will be able to do so in

a way that will be flexible enough to continuously

adapt to our changing world.

We support a systemic regulator

Going forward, we will need a systemic regulator

charged with effectively monitoring the

spread and level of risk across the financial

system in its entirety. Think of it as a “super

risk” regulator. Such a regulator would not eliminate

all future problems, but it would be able to

mitigate them. If we had eliminated just some

of the problems, it might have stopped the crisis

from getting this bad. Congress appears to be

well on its way to creating just such a regulator,

and we hope it succeeds.

Some issues the systemic risk regulator should

keep in mind are the following:

• Focusing the process on managing risk. This

should not be a political process. It should

function like a strong risk management

committee.

• Eliminating gaps and overlaps in the system.

For example, mortgages were regulated

by multiple entities, some of which did a

terrible job, causing a “race to the bottom”

as even good companies started to do bad

things to maintain market share.

• Analyzing areas like the mortgage market

and other elements of the consumer-finance

system to ensure that when new rules are

written, they create a sound, safe, effective

and consumer-friendly mortgage market.

• Carefully tracking new products, as they

often are the source of many problems.

• Reviewing credit across the whole system –

including “hidden” extensions of credit, such

as enhanced money market funds and SIVs.

• Aggressively monitoring financial markets

and potential excesses, or bubbles. It may be

hard to detect bubbles, and it may be inadvisable,

once detected, to exert a direct influence

on them with macro economic policy.

However, it is appropriate to try to minimize

the collateral damage bubbles can cause. It

also would be appropriate to try to manage

bubbles, not by using monetary policy but by

restricting credit on specific markets (i.e., it

would have been appropriate to ask lenders

to reduce loan-to-value ratios in mortgages

or to minimize speculation in the financial

markets by reducing the leverage used in the

repo markets).

• Recognizing distortions as they develop in

the broader economy (fiscal deficits, trade

imbalances, structural state budget deficits)

and forcing policy bodies to anticipate the

problems that may result.

• Encouraging international coordination as

much as possible – not only so companies

compete on a level playing field but also

because crises don’t stop at national borders.

These are just some of the ways a systemic

regulator could help fix the flaws in our regulatory

framework and create a system that

continually adapts and improves itself.

We support an enhanced resolution

authority — and the elimination of

“too big to fail”

Even if we achieve the primary goal of regulating

financial firms to prevent them from

failing, we still have to get government out of

the business of rescuing poorly managed firms.

All firms should be allowed to fail no matter

how big or interconnected they are to other

firms. That’s why we at JPMorgan Chase have

argued for an enhanced resolution authority

that would let regulators wind down failing

firms in a controlled way that minimizes

damage to the economy and will never cost the

taxpayer anything. Fixing the “too big to fail”

problem alone would go a long way toward

solving many of the issues at the heart of the

crisis. Just giving regulators this authority, in

and of itself, would reduce the likelihood of

failure as managements and boards would

recognize there is no safety net. Think of this

enhanced resolution as “specialized bankruptcy”

for financial companies. The principles

of such a system would be as follows:

• A failure should be based on a company’s

inability to finance itself.

• The regulator (or specialized bankruptcy

court) should be able to terminate managements

and boards.

• Shareholders should be wiped out when a

bank fails – just like in a bankruptcy.

• The regulator could operate the company

both to minimize damage to the company

and to protect the resolution fund.

• The regulator could liquidate assets or sell

parts of the company as it sees fit.

• Unsecured creditors should recover money

only after everyone else is paid – like in a

bankruptcy. (In fact, the resolution authority

should keep a significant amount of the

recovery to pay for its efforts and to fund

future resolutions.)

• In essence, secured creditors should be

treated like they are treated in a bankruptcy.

• The resolution fund should be paid for

by the financial industry (like the FDIC is

today).

• All institutions under this regime should live

with the exact same rules.

• Regulators should make sure that companies

have enough equity and unsecured debt

to prevent the resolution fund from ever

running out of money. To give an example,

while Lehman had $26 billion in equity, it

also had $128 billion in unsecured debt. A

resolution regulator, in my opinion, would

clearly have been able to let Lehman meet

its obligations, wind it down and/or sell it off

and still have plenty of money left over to

return some money to the unsecured creditors.

Had this been done wisely, the economy

would have been better off.

• If a firm fails, there should be enough clarity

about the financial, legal and tax structures

of that firm to allow regulators, cooperating

across international boundaries, to wind it

down in a controlled manner – what some

refer to as “living wills.”

• While there is no argument about who

should pay for the resolution (i.e., banks), there

are some technical issues about how it should

be funded. The resolution regulator does need

to be able to fund these companies while they

are being wound down, and there are plenty of

appropriate ways to accomplish this.

Once it is established that any firm can fail,

firms of all sizes and shapes should be allowed

to thrive. It is wrong to assume that big firms

inherently are risky. Banks shouldn’t be big for

the sake of being big, but scale can create value

for shareholders and for consumers who are

beneficiaries of better products that are delivered

more quickly and less expensively. These

benefits extend beyond individuals to include

businesses that are bank clients, particularly

those that are global in scale and reach, and

the economy as a whole. banks’ capabilities, size and diversity

enabled them to withstand the crisis

and emerge from it as stronger firms. This

strength, in turn, made it possible for many

firms to acquire weaker firms at the government’s

request and help to alleviate potential

damage to the economy.

Closing comments on regulation

While we support the general principles

behind enhanced regulation of derivatives,

securitizations and enhanced consumer protections,

we do not support each and every part

of what is being recommended. The devil is

in the details, and it is critical that the reforms

actually provide the important safeguards

without unnecessarily disrupting the health of

the overall financial system.

We also believe there are some serious ideas

that need attention if the system is to be made

more fail-safe:

• Repo markets could be better structured,

monitored and controlled.

• Loan reserving could be made far less

pro-cyclical.

• Securitization markets could be fixed so that

both originators and distributors have skin

in the game.

• A system could be put into place to prevent

a “run” on money market funds.

• The ability to buy shareholder or creditor

voting rights without owning and being

exposed to the risks of owning the underlying

securities should be extremely limited.

Investors should not have the ability to vote

the capital securities actually owned if the

investors are voting for the failure of the

company and stand to gain more on their

short positions than on their long positions.

• Finally, we support strong controls on

so-called “naked short selling.”

During the past year’s discussion among regulators

and legislators, many other ideas have

been proposed or recommended – from the

Volcker Rule to new bank taxes to changes in

Basel capital. These ideas are all in varying

stages of development and are too undefined

to comment on here. What we would urge our

regulators and legislators to do is proceed with

clarity and purpose and avoid broadly penalizing

all firms alike – regardless of whether

they were reckless or prudent. As we grapple with the enormity of the issues

facing the nation, we must not lose sight

of our strengths. America has successfully

brought these strengths to bear on crises in

the past – some much bigger than the current

one – and I am optimistic about our ability to

do so again.

America’s success as a nation requires a strong

and growing economy. A strong and growing

economy requires the right kind of government

policies and a private sector that is

innovative as well as responsible. Responsible

businesses can be both small and large – and,

in a global economy, it behooves America to

have large multinational companies that are

operating on a global stage. Creating a culture

that ties it all together requires a greater sense

of shared responsibility.

America’s success is not a God-given right –

it is something we always must work hard

to achieve.

The need for a strong economy and good

government

America’s success depends upon many

things, including good government (and the

strength of our exceptional military). But it

cannot succeed without a healthy and vibrant

economy. That is what allows us to share the

rewards of success, defend our nation, educate

our children and build a better future.

A strong U.S. economy, one with the ability to

continually improve and reform itself, depends

on good government. Bureaucracy is lethal,

and we cannot let it drain the energy, talent,

creativity, drive and goodwill of our citizens –

or those we encourage through our example,

many of whom come to work and innovate

in America. To thrive, our country and our

economy need:

• Legal clarity and consistency.

• The fair application and steadfast enforcement

of the rule of law.

• Trade policies conducive to growing the

American economy and the global competitiveness

of U.S. companies.

• Immigration policies that allow America to

attract the world’s best and brightest – an

essential ingredient of our success as a nation.

• Sensible and effective regulation that

protects investors and the public.

• A strong and efficient infrastructure (from

highways and bridges to electrical grids, etc.).

• The proactive promotion of economic

growth and rules that foster U.S. capital

accumulation.

• Policies facilitating job growth, as opposed to

those that inadvertently make it harder to hire.

Countries can have different social values

and objectives (though I believe most countries

and most citizens would like to reduce

poverty and suffering). But countries should

not confuse values and objectives with maintaining

a strong economy.

Healthy and growing countries can do

wonderful things for their people. And countries

that fail to create healthy economies

frequently relegate their people to increasing

levels of pain and suffering. Many countries

have professed wanting to help their people

but, instead, have damaged their countries and

hurt their people. Maybe the intentions were

real, but, even if they were, the road to hell is

often paved with good intentions.

Brazil is an example of a country that seems

to be successfully using pro-growth policies

to expand its economy while using the

wealth from that economic growth to finance

important social programs. Over the last 20

years, Brazil has adopted many policies that

dramatically strengthened its economy. It

also bolstered its institutions, privatized its

businesses, improved the rule of law, left the

bulk of capital allocation to the private capital

markets and developed world-class companies. Eight years ago, Brazil elected a left-leaning

president, but he continued policies to

strengthen the economy. He also used some

of the wealth to start a program called Bolsa

Familia that gave Brazil’s poorest citizens vaccinations,

education and $80 a month for food.

The lesson is clear: Good policies and

economic growth are not the enemy of social

progress – they are the fuel for progress.

Businesses need to be responsible — and

healthy and vibrant

At JPMorgan Chase, we feel a deep responsibility

to build a company that benefits our

customers, our employees, our shareholders and

the communities in which we operate around

the world. The best companies don’t make decisions

for short-term profits. Contrary to public

opinion, corporations are not in business solely

to maximize quarterly earnings but rather to

serve clients and earn their trust over a long

period of time and, in so doing, earn a fair profit.

Profits in any one year, in effect, are a reflection

of decisions that may go back decades.

We always have been deeply committed to

being good corporate citizens and adhering to

the following practices:

• Treating our customers and employees with

the respect they deserve.

• Building safe and useful products.

• Maintaining ethical and responsible business

practices.

• Meeting our fiduciary responsibilities and

creating real value for shareholders.

• Developing a company for the long run –

one that stands the test of time.

• Making a meaningful difference through

philanthropic endeavors in supporting

our communities.

• Acknowledging our mistakes (which are a

natural part of doing business), fixing them

and learning from them.

• Supporting the economies in which we

work through job creation and appropriate

tax payments. JPMorgan Chase, on average,

pays more than $12 billion a year in taxes to

governments around the world.

Building a great company allows investment in

the future, provides opportunities to employees,

builds better products for customers and serves

communities. Companies that are not healthy

and vibrant cannot do these things.

Businesses — small to large — are one of

America’s key strengths

A healthy business sector is fundamental to

our economic strength: Of the 130 million

people who go to work every day in the United

States, nearly 110 million are employed by

private businesses. These private businesses

are and always have been the nation’s primary

drivers of job creation and innovation.

The strength of the business sector is rooted

in its diversity, from the smallest start-up or

family-owned firm to the largest multinational

corporation.

Indeed, the relationship between larger and

smaller businesses is symbiotic. Studies show

that for every one job created at a larger business,

five jobs are created at smaller businesses

that provide supporting goods and services. At

JPMorgan Chase, in particular, we spend more

than $15 billion per year with approximately

40,000 vendors, who provide jobs to millions

of employees.

We need global flagship companies —

including banks

In the current political environment, size in

the business community has been demonized,

but the fact is that some businesses require

size in order to make necessary investments,

take extraordinary risks and provide vital

support globally. America’s largest companies

operate around the world and employ millions

of people. This includes companies that can

make huge investments – as much as $10

billion to $20 billion a year – and compete in

as many as 50 to 100 countries to assure America’s long-term success. Combined, big and

small businesses spend $1.5 trillion per year

on capital expenditures and $300 billion on

research and development. It is estimated that

more than 70% of the capital expenditures are

made by large companies.

The productivity of our workers and the huge

economies of scale of our corporations (generated

from years of investing and innovating)

are what ultimately drive our economy and

income growth. Employees at large companies

share in that productivity: Compensation and

benefits for employees at large companies are

substantially higher than at small firms.\*

It is estimated that large enterprises and large

foreign multinationals active in the United

States have accounted for the majority of U.S.

productivity growth since 1995.

Companies such as Ford, Boeing, Pfizer, Caterpillar,

Apple, Microsoft and Google are exemplars

of initiative and innovation worldwide.

Cutting-edge companies like Hewlett-Packard

underpin vibrant networks of small and midsize

suppliers and vendors. Academic research

shows that these investments abroad actually

create more jobs in the United States.

Large companies such as the ones mentioned

above need banking partners with large

enough balance sheets to finance transactions

around the world. And it’s not just multinational

corporations that rely on such scale:

States and municipalities also depend on

the capital that a firm like JPMorgan Chase

can provide. To be sure, smaller banks play a

vital role in our nation’s economy but cannot

always provide the type of service, capital,

breadth of products and speed of execution

that clients need. Only large banks have the

scale and resources to connect markets around

the globe, in places like China, India, Brazil,

South Africa and Russia; to execute diverse

and large-scale transactions; to offer a range of

products and services, from loan underwriting

and risk management to local lines of credit;

to process terabytes of financial data; and to

provide financing in the billions.

U.S. banks actually are less consolidated than

those in the rest of the world, and our financial

system is less dominated by large banks than

that of almost any other nation. For example, in

2007, the three largest U.S. banks held 34% of

total U.S. bank assets – the second-lowest figure

among Organisation for Economic Co-operation

and Development (OECD) nations, just ahead

of Luxembourg; the average for the rest of the

OECD nations was more than double, at 69%.

Not only is our banking system not particularly

concentrated, but our large banks are not

relatively large compared with the size of the

U.S. economy. The arguments that “big is bad”

and that “too consolidated is bad” are refuted by

many examples of countries with large, consolidated

banking systems that did not have problems

at all (e.g., Canada).

Capping the size of America’s largest banks

won’t change the needs of big business. Instead,

it will force these companies to turn to foreign

banks that won’t face the same restrictions.

JPMorgan Chase’s capabilities, size and diversity

were essential to withstanding the financial

crisis in 2008 and emerging as a stronger firm.

Everyone needs to be responsible

America was built on the principles of rugged

individualism and self-responsibility. We need

to continue to foster a sense of responsibility in

all participants in the economy. Bad outcomes

are not always someone else’s fault – we need

to cultivate an environment where consumers,

lenders, borrowers, businesses and investors all

take responsibility for their actions and don’t

look for someone else to blame. We have to stop

slipping into a cacophony of finger-pointing

and blame. And while bad actors always should

be punished, we also should note that not all

who got into trouble were irresponsible. We

fully acknowledge, for example, that many individuals

found themselves in a difficult position

that was caused by a medical condition or loss

of employment beyond their control, and they

should be treated fairly and respectfully.

The crisis of the past couple of years has had

far-reaching consequences, among them the

declining public image of banks and bankers. While JPMorgan Chase certainly made its

share of mistakes in this tumultuous time,

our firm always has remained focused on the

fundamentals of banking and the part we can

play to support our clients and communities.

Our 220,000 people go to work every day to do

a great job serving clients, whose trust we have

to earn over many years. The vast majority of

our people, customers, operations and shareholders

are far from Wall Street – they actually

are part of the everyday life of Main Street, in

virtually every part of the country. And they

are active and contributing members of society

in communities around the world.

Very often, when the public or politicians

take punitive efforts against banks like ours,

they think they are punishing only the senior

management team, when, in fact, they are

punishing ordinary shareholders as well.

Contrary to popular perception, Main Street

owns our biggest banks and corporations

through savings and retirement funds. Our

shareholders represent a true cross section of

America, including teachers, retirees and public

employees. When we reduce the debate over

responsibility and regulation to simplistic and

inaccurate notions, such as Main Street vs. Wall

Street, big business vs. small business or big

banks vs. small banks, we are indiscriminately

blaming the good and the bad – this is simply

another form of ignorance and prejudice.

By extension, when we vilify whole industries

or all of the business community, we are denigrating

ourselves and much of what made this

country successful. We also should refrain from

indiscriminate blame of any whole group of

people, including politicians or the media. We

need to focus a bit less on daily media and polls

and more on the books that will be written after

this crisis subsides. We all should ask ourselves

whether we, in a time of stress, did the right

things the right way for the right reasons.

Conclusion

The United States faces many challenges. In

the short run, overcoming this economic crisis

and getting our unemployed back to work

are most important. In the long run, we must

confront our health and education systems;

develop a real, substantive energy policy;

and build the infrastructure for the future.

We also must confront the large U.S. deficit,

being honest about the facts and being fiscally

responsible for ourselves – it is dangerous to

wait for the global markets to pressure us into

that discipline. These are all serious challenges,

but, if we work together, we can fix them.

Your company continues to do everything it

can, in every community in which we work, to

help the world recover as quickly as possible.

In 2009, as they have so many times before,

our people rose to the challenge, working amid

tremendous uncertainty in a fragile economic

and political environment. They also have

coped with the anger directed toward the

financial services industry. Through it all, they

did not lose focus on why we are all here: to

serve clients and, therefore, our communities

around the world. On behalf of JPMorgan

Chase and its management and shareholders,

I express my deepest gratitude to our people.

I am proud to be their partner.

Jamie Dimon

Chairman and Chief Executive Officer

March 26, 2010