Company Name: JPMorgan
Company Ticker: JPM US
Date: 2019-01-15
Event Description: Q4 2018 Earnings Call

Market Cap: 344,811.84
Current PX: 103.69
YTD Change($): +6.07
YTD Change(%): +6.218

Bloomberg Estimates - EPS
Current Quarter: 2.457
Current Year: 9.888
Bloomberg Estimates - Sales
Current Quarter: 28955.222
Current Year: 114262.259

Q4 2018 Earnings Call

Company Participants

- Marianne Lake
- Jamie Dimon

Other Participants

- Erika Najarian
- James Mitchell
- John Eamon McDonald
- Alevizos Alevizakos
- Mike Mayo
- Glenn Schorr
- Andrew Lim
- Matthew Derek O'Connor
- Saul Martinez
- Betsy L. Graseck
- Brian Kleinhanzl
- Steven Chubak
- Marty Mosby
- Gerard Cassidy
- Ken Usdin

MANAGEMENT DISCUSSION SECTION

Marianne Lake

Earnings Highlights

Q4 2018

- The firm reported fourth quarter:
  - Net income of $7.1 billion
  - An EPS of $1.98
  - Revenue of nearly $27 billion
  - With a return on tangible common equity of 14%

Business Drivers

- Market impact aside, underlying business drivers remained solid, including:
  - Core loan and deposit growth

- Consumer sentiment and spending in a robust holiday season
- Capital market activity
- And with credit performance continuing to be very strong across businesses

FY2018

- For the full year of 2018, the firm reported revenue of $111.5 billion and net income was $32.5 billion
  - Both clear records, even adjusting for the impact of tax reform
- As we said, we're entering 2019 with good momentum across our businesses

Q4 Financial Results

Revenues

- Turning to page two and some more detail about our fourth quarter results
- Revenue of $26.8 billion was up $1.1 billion or 4% year-on-year
  - Driven by net interest income
- NII was up $1.2 billion or 9% on higher rates and on loan and deposit growth
- Non-interest revenue was down slightly with lower market levels impacting Asset & Wealth Management fees and private equity losses, being offset by higher Card fees, and Auto lease growth in CCB

Expenses

- Expense of $15.7 billion was up 6% year-on-year
- The increase relates to investments we are making in technology, marketing, real estate and front office, as well as revenue related costs including growth in Auto
  - This was partially offset by a reduction in FDIC fees
- As we had hoped, the incremental surcharge was eliminated effective the end of the third quarter
  - And this is a benefit of a little over $200 million for the quarter across our businesses

Credit Trends

- Credit trends remain favorable across both Consumer and Wholesale
- Credit costs of $1.5 billion were up $240 million year-on-year, driven by changes in reserves
- In Consumer, we built reserves of $150 million in Card on loan growth
- In Wholesale, over the last several quarters, we have seen net reserve releases and recoveries
  - However, this quarter, we had about $200 million of credit costs, again, largely reserve builds on select C&I client downgrades, driven by a handful of names across multiple sectors
- While we are constantly looking, at a granular level, for shadows, these downgrades, are idiosyncratic and do not reflect signs of deterioration in our portfolios. The outlook for Credit, as we see it, remains positive

FY2018 Financial Results

Net income and EPS

- Shifting to the full year results on page 3, we reported:
  - Net income for the year of $32.5 billion
  - A return on tangible common equity of 17%
  - And EPS of $9.00 a share
- Net income was a record for the firm as well as for each of our businesses, even excluding tax reform

Revenue

- Revenue of $111.5 billion was also a record and was up nearly $7 billion or 7% year-on-year, $4.3 billion of which was higher net interest income on higher rates with growth and Card margin expansion being offset by lower Markets NII
- Non-interest revenue was up $2.5 billion or 5%, driven by CIB Markets and growth in Consumer, being offset by Private Equity losses, and the impact of spread widening on FVA

Adjusted Expense

- We ended the year with adjusted expense of $63.3 billion, up 6%, which brings our overhead ratio to 57% for the year, even as we continue to make very significant investments across the franchise
- And although we are showing modest positive operating leverage on a managed basis, remember our revenues were impacted by lower gross-ups, given tax reform
  - Adjusted for this, or looking on a GAAP basis, we delivered nearly 200 basis points of positive operating leverage for the year, and well over 100 basis points for the fourth quarter

Credit Environment

- On Credit, the environment remained favorable throughout 2018
- Credit costs were $4.9 billion, down 8%, driven by lower net reserve builds in Consumer as well as the impact in 2017 of the student loan sale

Balance Sheet and Capital Highlights

- Moving on to page 4 and balance sheet and capital
- We ended the quarter with a CET1 ratio of 12%, flat to last quarter
- Risk-weighted assets decreased, with loan growth more than offset by derivatives counterparty and trading RWA, given a combination of seasonality, market conditions and model enhancements
- Our net payout ratio for the quarter exceeded 100%, and we repurchased $5.7 billion of shares

Segment Business Results

Consumer & Community Banking

- Moving to Consumer & Community Banking on page 5
- CCB generated net income of $4 billion and an ROE of 30% for the fourth quarter; and for the year, nearly $15 billion of net income and an ROE of 28%
- Customer satisfaction remains near all-time highs across our businesses

Loans

- For the quarter, core loans were up 5% year-on-year, driven by:
  - Home Lending, up 8%
  - Card, up 6%
  - And Business Banking, up 5%

Deposits

- Deposits grew 3%
- Growth continues to slow, given the rising rate environment
  - But importantly, we believe we continue to outpace the industry

Market Expansion

- Of note this quarter, we opened the first 10 branches in our expansion markets, including:
  - D.C
  - Boston
  - And Philadelphia
- And although it’s clearly early, reception in the market and the performance of the new branches have been strong

Client Investment Assets

- Despite volatile markets, client investment assets were still up 3%
- And we saw record net new money flows for the year
- Card sales were up 10%, debit sales up 11% and merchant processing volumes up 17%, reflecting a strong and confident consumer during the holiday season

Active Mobile Customers

- And in keeping with our focus on digital everything, of note, active mobile customers were up 3 million users or 11% year-on-year

- Revenue of $13.7 billion was up 13%

Consumer & Business Banking Revenue

- Consumer & Business Banking revenue was up 18% on higher deposit NII, driven by margin expansion
- Home Lending revenue was down 8%, driven by lower net production revenue in a low volume, highly competitive environment
  - And of note, while not a material driver of overall expense, revenue headwinds here were offset by lower net production expense

Card, Merchant Services & Auto Revenue

- And Card, Merchant Services & Auto revenue was up 14%, driven by:
  - Higher Card NII on both loan growth and margin expansion
  - Lower Card net acquisition costs principally Sapphire Reserve
  - And higher auto lease volumes
- Card revenue rate was 11.6% for the quarter and 11.27% for the year, as expected

Expenses

- Expense at $7.1 billion was up 6%, driven by investments in technology and marketing, and auto lease depreciation, partially offset by lower FDIC charges and other expense efficiencies
- On credit, net charge-offs were down $18 million, as modestly higher charge-offs in Card were more than offset by lower charge-offs in Auto and Home Lending
- Charge-off rates were down year-on-year across all portfolios. Economic indicators remain upbeat, and given the breadth and depth of our franchise, we have a pretty good barometer
- From everything we see, the U.S. consumer remains very healthy

Corporate & Investment Bank

Net Income and ROE

- Now, turning to page 6 and the Corporate & Investment Bank, CIB reported net income of $2 billion and an ROE of 10% on revenue of $7.2 billion for the fourth quarter
- And for the year, net income is nearly $12 billion and an ROE of 16%
- In Banking, it was a record year for both total fees and advisory fees

Business Ranking

- We ranked number one in Global IB fees for the 10th consecutive year, gaining share across all regions
- For the quarter, IB revenue of $1.7 billion was up 3%

- We saw continued momentum in advisory with fees up 38%, driven by the closing of several large transactions
- For the year, we ranked number two in wallet, gaining share
- Equity underwriting fees were down 4%, but significantly outperforming the market
- We ranked number one for the year and the quarter and saw leadership positions across all products globally with particular strength in IPOs as well in the technology and healthcare sectors
    - And debt underwriting fees were down 19% versus a strong prior year and better than the market
- We maintained our number one rank for the year and continued to hold strong lead-left positions in high yield bonds and leveraged loans

Markets Revenue

- Moving to Markets, total revenue was $3.2 billion, down 6% reported and down 11% adjusted for the impact of tax reform and the Steinhoff margin loan loss last year
- A confluence of factors throughout the quarter, including trade, concerns around global growth and corporate earnings, fears of a more hawkish Fed
    - As well as other negative headlines, caused spikes in volatility, which were amplified by markets that lacked depth and liquidity
- And although we saw a decent client flow, rates rallied, spreads widened and energy prices fell significantly, all against general market conviction that was anticipating a stronger end to the year
    - As a result, Fixed Income Markets, in particular, were challenging with revenue down 18% adjusted
- Weaker performance across Rates, Credit Trading and Commodities was partially offset by good momentum in Emerging Markets

Equities Revenue

- Equities revenue was up 2% adjusted, a solid end to a record year
- Prime continued to do well, but we saw client deleveraging over the course of the quarter and cash and derivatives were solid in a tougher environment

Treasury Services and Securities Services Revenue

- Treasury Services revenue was $1.2 billion, up 13%, driven by growth in operating deposits as well as higher rates, but also benefiting from fee growth on higher volumes
- Securities Services revenues was $1 billion, up 1%
    - Underlying this was strong fee growth and a modest benefit from higher rates, together being substantially offset by the impact of lower market levels and a business exit
- Credit Adjustments & Other was a loss of $243 million, reflecting higher funding spreads on our derivatives

Expenses

- Finally, expense of $4.7 billion was up slightly with continued investments in technology and bankers, and volume-related transaction costs, partially offset by lower FDIC charges and lower performance-based compensation
- The comp-to-revenue ratio for the quarter and for the year was 28%

Commercial Banking

Net Income and ROE

- Moving to Commercial Banking on page 7, the Commercial Bank reported net income of $1 billion and an ROE of 20% for the fourth quarter, and for the year, $4 billion of net income and an ROE of 20%

Revenues

- Revenue of $2.3 billion for the quarter was down 2%, as the prior year included a tax reform-related benefit
  - Excluding this, revenue was up 3%, driven by higher deposit NII
- Gross IB revenue of $600 million was down 1% year-on-year, but up 4% sequentially on a strong underlying flow of activity, particularly in M&A
- Full-year IB revenue was a record $2.5 billion, up 4% on strong activity across segments, in particular Middle Market Banking, which was up 8%

Deposit Balances

- Deposit balances were up 1% sequentially, as client cash positions are seasonally highest towards year-end, although down 7% year-on-year, as we continue to see migration of non-operating deposits to higher yielding alternatives
- We believe we are retaining a significant portion of these flows

Expenses and Loans

- Expense of $845 million was down 7% year-on-year, as the prior year included $100 million of impairment on leased assets
  - Excluding this, expense was up 5%, driven by a continued investments in the business, in banker coverage as well as in technology and product initiatives
- Loans were up 2% year-on-year and flat sequentially
- C&I loans were up 1%, reflecting a decline in our tax-exempt portfolio, given tax reform
  - Adjusting for this, we would have been up 4%, which is still below the industry as we focus on client selection, pricing and credit discipline
  - But keep in mind in areas where we have chosen to grow such as in our expansion markets, we are growing at or above industry benchmarks
- CRE loans were up 2%, also below the industry as we proactively slowed our growth due to where we are in the cycle through continued structural and pricing discipline and targeted selection of new deals

- Underlying credit performance remains strong with credit costs of $106 million, including higher loan loss reserves largely due to select client downgrades

Asset & Wealth Management

Net Income and ROE

- Moving on to Asset & Wealth Management on page 8
- Asset & Wealth Management reported net income of $604 million with a pre-tax margin of 23% and an ROE of 26% for the fourth quarter
- And for the year, net income was nearly $3 billion, pre-tax margin of 26% and an ROE of 31%

Revenue

- Revenue of $3.4 billion for the quarter was down 5% year-on-year, with the impact of current market levels driving lower investment valuations and management fees as well as, to a lesser extent, lower performance fees
  - These were partially offset by strong banking results and the cumulative impact of net inflows

Expenses

- Expense of $2.6 billion was flat as continued investments in advisors and in technology were offset by lower performance-based compensation and lower revenue-driven external fees
- For the quarter, we saw net long-term outflows of $3 billion, with strength in Fixed Income more than offset by outflows from Equity and Multi-Asset products

Net Liquidity Inflows

- Additionally, we had net liquidity inflows of $21 billion
- For the 10th consecutive year, we saw net long-term inflows of $25 billion this year
  - Driven predominantly by Multi-Asset and in addition saw $31 billion of net liquidity inflow this year
- Assets under management of $2 trillion and overall client assets of $2.7 trillion were both down 2% as the impact of market levels more than offset the benefit of net inflows

Deposits and Loan Balances

- Deposits were flat sequentially and down 7% year-on-year, reflecting migration into investments and we continue to capture the vast majority of these flows
- Finally, we had record loan balances up 13% with strength in global wholesale and mortgage lending

Corporate Business

- Moving to page 9 and Corporate
- Corporate reported a net loss of $577 million

- Treasury and CIO net income of $175 million was up year-on-year, primarily driven by higher rates
- Other Corporate saw a net loss of $752 million, including on a pre-tax basis funding our Foundation For Corporate Philanthropy $200 million this quarter flat year-on-year and including $150 million of markdowns on certain legacy Private Equity investments market related
  - The remainder is driven by tax-related items, totaling a little over $300 million
- And within this are two notable components:
  - The first is regular-way tax reserves
  - And the second represents small differences between the effective tax rate for each of our businesses and that for the overall company as we close the year
- So therefore, there is an offset across our businesses
- Our full-year effective tax rate was just a little over 20% in line with guidance

Q1 2019 Financial Outlook

Moving to page 10 and outlook, we will give you more full-year outlook and sensitivity information at Investor Day as always

However, for now, I do want to provide some color and reminders about the first quarter

Net Interest Income

- Net interest income will continue to benefit from the impact of higher rates and growth, but quarter-over-quarter will be negatively impacted by daycount and we expect the first quarter NII to be relatively flat sequentially

Revenues

- While it's too early clearly to give guidance on fee revenues, it's also fair to say that this quarter markets feel calmer and more positive and capital market pipelines are strong
  - So if the environment remains supportive, we would expect normal seasonal strength in the first quarter
  - But I will remind you that the first quarter 2018 included $500 million accounting write-up as well as broad strength in performance

Expenses

- Expect expense to be up mid-single-digits year-on-year obviously market-dependent, primarily annualization effects
- And finally, as I said, we expect credit to remain favorable across products

Closing Remarks

So to close, while the markets in the fourth quarter were more challenging, we should not lose sight of the fact that 2018 was a strong year, indeed a record full revenue, net income and EPS both reported and adjusted for tax reform

Fundamental economic data remains supportive of continued growth and we're generally constructive on the outlook for 2019

We have good momentum coming into the year and the company and each of our businesses are very well-positioned

QUESTION AND ANSWER SECTION

<Q - Erika Najarian>: So the way bank stocks have performed, clearly, the investors are starting to worry about revenue trends near term, and of course, credit which you addressed. I am wondering if the revenue trends continue to be weaker than expected, if the overhead ratio of 57% that you posted in 2017 and 2018 is something that you could continue to level off to? Or will the investment horizon be more of a dominant factor when we're thinking about the overhead ratio?

<A - Marianne Lake>: Yeah. So I would say, a couple of things. The first is just to remind you that 2017 and 2018, I would look at a GAAP rather than a managed basis because of the adjustments to our revenues from tax reform. But that said, while we don't set expense targets nor do we set overhead ratio targets, we have given you some outlook that would suggest that we continue to believe that a combination of revenue growth and expense discipline notwithstanding the investments that we've been making, we should see our overhead ratio continue to be stable to trending down to the kind of mid-50s, so 55-ish-percent. Obviously, the timing of that will depend on rates and markets and everything else.

So we would expect to continue to deliver positive operating leverage, on higher NII, on growth if nothing else and continued solid growth in fees. Clearly, in any one quarter you can have pluses and minuses that can be market-dependent, but generally, over time we would search for those trends.

<Q - Erika Najarian>: Thank you for that. And just as a follow-up question, the market is also thinking that the last rate hike from the Fed was December. And I'm wondering how we should think about the dynamics of net interest income and more specifically net interest margin and deposit pricing if December was indeed the last rate hike for some time?

<A - Marianne Lake>: So I would say, first of all, just to say that the question mark about whether that's a pause or a stop, is it the end of a cycle, we don't think so. We think the outlook for growth in the economy is still strong. The consumers still strong and healthy and we're expecting to still see maybe slower but still global growth going forward.

Having said that, just as a general matter, you've seen through our earnings at risk, as we have put more and more of the benefit of past rate hikes in our run rate, each incremental hike from here has while still positive significantly lower sort of incremental NII drive, and that the front-end skew is a lower percentage.

So it's not nothing, so clearly lower front-end rates, or lower long end of the curve, or a flatter curve, all other things would be net modestly negative. But against that, you pointed out the potential for this to lead to lower or slower re-price.

And so as the Fed pauses, it is fair to say there could be an offset from lower re-price as people digest the data and understand whether this is a pause or more. We would still look at – we delivered $4.3 billion of NII growth in 2018. We'll still benefit in 2019 from the annualization effects of the higher rates we've already had as well as solid growth. So while you can't expect 2019 over 2018 to be at that level, it would still be strong NII growth year-on-year.

<A - Jamie Dimon>: I would say the why is equally if not more important than the what. So if it is a pause because you're going to go into a recession, they're going to reduce rates. That obviously is very different than if it's a pause, the economy is strong, and they raise rates.

<A - Marianne Lake>: Right.

<A - Jamie Dimon>: You know which one you would choose.

<A - Marianne Lake>: Right. And if this were the end of a cycle, it's no cycle we've ever seen before. So in that scenario, if the terminal Fed fund rates were at 2.5% not – 4.5%, 5%-plus, I think we've never seen that movie before. But that's not our central case. And by the way, the house view, the research view would still be to see incremental hikes this year. If not in the first half, in the second.

<Q - James Mitchell>: Maybe a question on the Card business. There's been chatter about pulling back on rewards to focus more on profitability. I guess, how do you think about the strategy in Cards right now? And I think the revenue yield in the Card business was up 7 bps to 11.57%. Can that go higher from here as you maybe pull back on rewards?

<A - Marianne Lake>: Yeah. I would say that when we think about the product continuum we have in the constructs, rewards is a very important part of driving engaged relationships with our customers. Customers are very attuned to it, and we're looking for value in the product – value and simplicity and ease of use, are the three things in the products that we deliver.

And so for us, engaged relationships, drive profitability, this is still a very profitable business. And so while we'll always make adjustments to our offerings, it's not the case that we are looking at a meaningful pullback in rewards. And if you think about things like Sapphire banking where we're looking to bring the impact of our products together, we're continuing to offer rewards-based incentives to drive engagement with our customers.

So we think it's a solid strategy, a business that already has good returns. It's fair to say that we've seen a lot of competitive response and competitive products in the marketplace that are driving high rewards offerings too, and we've not seen that lower our ability to net acquire new accounts. So we feel great about the value proposition, the simplicity, and the compelling products that we have.

<Q - James Mitchell>: Okay. So we think about...

<A - Marianne Lake>: That's very profitable business.

<Q - James Mitchell>: Right. And so we think about still seeing decent growth, how do we think about card losses specifically this year? You seem pretty optimistic on credit. Should we still expect some seasoning? Or do you think the macro trends are that positive that we hold steady? How do you think about credit and cards?

<A - Marianne Lake>: So I think the macro trends are definitely positive. They are creating tailwinds. But it's also true, we talked about the fact that if you go back to 2014, 2015 that we had expanded our credit box, we'd expanded it intentionally at higher risk-adjusted margins. But over the course of the last couple of years, as we've experienced outperformance, we've done surgical risk pullbacks and we've amended our collection strategy, all of which have led to a charge-off rate for the fourth quarter in 2018 that's down slightly year-on-year. And for the year, that's at 310 basis points, which is reasonably meaningfully below our expectations even at the end of last year.

So we feel great that that kind of loss trends at that 310 basis points, maybe a little bit higher is something we look at forward to at least into 2019. And it will be helped by a supported macro environment. And we are seeing – if you unpick all of our trends, you see the phenomenon of three vintages, you see the mature vintages that continue to be stable to grinding lower in terms of delinquencies and loss rates you see the older expansion vintages that have passed their peak, delinquencies that are trending to a more stable lower level. And then you do have obviously with new acquisitions a cohort that are still seasoning, that will continue. But net-net, we're expecting relatively stable loss rates at levels similar to 2018.

<Q - John Eamon McDonald>: Just wondering on the markets commentary, obviously, it's super early in the quarter, but you mentioned things feeling better. Can you just talk about seasonality there, but also just what feels better so far? And then, also, in the fourth quarter, what you saw on leverage lending market? How much did you have to take in terms of maybe marks and leverage loans and hung deals? A little bit of color there would be helpful.

<A - Marianne Lake>: Sure. Okay. So I would say that, obviously, the fourth quarter was challenging and there was a lot of market moves – a big sort of broad sell-off. And at that point, there were elevated concerns around trade, global growth data, was causing concerns. There were concerns that the Fed was going to continue to be hawkish and not necessarily as responsive to some of the things the market was worried about. So there were a lot of negativity. We think too much negativity priced into the fourth quarter. And it started to change a bit when we saw the first really strong unemployment print, which reminded people that there's a very long distance between 3% growth and a contraction.

So yes, we could see slower growth but still growth in the U.S. and across the globe. A slightly more constructive narrative on trade and that continues to broadly progress we hope and believe in a positive direction. A more dovish outlook from the Fed, the potential for there to be pauses in rates, all being relatively supportive, and the fact that a lot of people were on the sidelines through the fourth quarter, and in fact, their appetite is out there for good value where it can be found.

So I would say, just early days in the first quarter, there are still obviously risks to the outlook. And any of those things could go in a worse direction. But so far things just feel a little bit more positive and that's constructive, and therefore, you would hope to see normal seasonal strength in January.

On leverage loans, look, diving into sort of the potential for there to be hung bridges, it's true that there was a significant market correction with both widening across high-yield bond and leverage loans in the fourth quarter. Clearly, stepping back, while the industry – leverage finance commitments are up, they are materially down from before the crisis and very different. So credit fundamentals look pretty good.

Having said that, and by the way, we passed on a lot of deals in the fourth quarter. We've maintained our protection in terms of flex pricing and flex protection. And as a result, the vast majority of our bridge book has still got decent cushion. And that's not to say that there is no deal that has the potential for there to be net losses after fees, but nothing that we would consider to be significant and nothing in the fourth quarter.

I would also say that coming back to the first quarter, that actually the market could be quite constructive for fixed income into the first quarter, given a more dovish Fed, supporting corporate margins, the corporate default rate is going to stay pretty low and we do have time. So none of the deals that we have need to be brought to market in a hurry and the market is moving in a positive direction.

<Q - Alevizos Alevizakos>: I again want to focus a bit on the Markets performance. You pretty much mentioned like weakness across the board in credit, in FX, in rates, which I assume like it's the case. First of all, I want a bit of an outlook on how you think rates will perform now that volatility has picked up? And more importantly, you mentioned strength in Emerging Markets. Can I ask whether that was primarily in Asia or LatAm? Thank you very much.

<A - Marianne Lake>: So it's nothing ever comes of talking about how we think things would have panned out in the first quarter other than just the general comments I've already made, which is the environment should be more constructive and we are expecting decent volatility and client activity, and we'll see how that pans out. And with respect to Emerging Markets, Latin America was big piece but Asia too.

<Q - Mike Mayo>: I guess I'm a little torn between the year and the quarter, so just ask it to Jamie. Jamie, seems like you guys are very happy with the year with all the record revenues and earnings. But the fourth quarter, are you happy with the fourth quarter given expenses, credit, fees?

<A - Jamie Dimon>: I am fully happy with it. The franchise is strong....

<A - Marianne Lake>: Yes.

<A - Jamie Dimon>: ...we're investing in new products and services, but we're not immune from the weather, volumes and volatility. We're not immune from market prices and assets going up or down. And I like the loans up 6%, assets up sub-10%, long-term flows up. I like the fact the credit card spend is up 10%, merchant process is up 17%. Shares in almost every business, market shares have gone up. That's what I look at.

<A - Marianne Lake>: Yeah.

<A - Jamie Dimon>: I really don't pay that much attention to speed bumps a little but in the fact that volumes are low in the last three weeks of December. I honestly could care less. And I look at more like in Equities, we've gained share and we're now bumping up to number one. Those folks have done a great number, of course, Cash, Derivatives, Prime Broker, et cetera. And Fixed Income, we've maintained our share and we're adding products and services around the world. And you don't know...

<A - Marianne Lake>: Gained share.

<A - Jamie Dimon>: You don't know what's going to happen next quarter and I don't care.

<A - Marianne Lake>: And we take the same position – like we had strong first half of the year and we said long may it continue, but it may not. And one quarter doesn't make a trend. And so we don't really react to the micro even though it was driven by the macro. The real underlying business drivers continue to be strong. And even in those businesses we are holding leadership positions and gaining share. And so this too will pass and things will continue to move forward in a constructive manner.

<Q - Mike Mayo>: Well, as a follow-up, let's talk about the weather. So the weather was lousy at the end of the year. And, Jamie, you were just appointed to your third year as Chairman of the Business Roundtable. So in that role what are you doing to help JPMorgan and I guess the other banks in terms of China, the government shutdown, immigration, some of these headline issues that Marianne talked about having hurt the CIB in the fourth quarter?

<A - Jamie Dimon>: Yeah. December is terrible, but if you look at January, you have half of it back generally in spreads and markets and stuff like that. And as BRT, I don't do anything to benefit JPMorgan. That's about public policy, that's good for the growth of America in total. I very specifically stayed away from doing anything about banks there. But the BRT does take up trade, and we are supportive of the fact that there are serious issues with China. We'd like to see the trade deal get done. And it looks to us like they're marching along at least to this March 1 deadline date that they will have enough to be done to get an extension and hopefully complete the deal.

We would like to see immigration reform. So proper border security, allowing people who have advanced degrees to stay here, having the DACAs to stay here, having more merit-based immigration and having some path to citizenship. That is the BRT position. We want more innovation. We'd like to reduce regulations at the local and federal level to stop small business formation. So you look at the BRT, there are 10 verticals around it, and we try to do things that are good for the growth of America. And bad policy can slow down the growth of America.

As I've pointed out over and over, it takes 12 years to get the permits to build a bridge, and it took eight years to put a man on the moon. It is time that we reform ourselves and not blame anybody else for our own lack of that we don't have kids getting out of school with educations, whether you get jobs that – whether innovations slow down, the government R&D spending is down, I always think you have to look at yourself and what can you do better and there's plenty in this country to do better self-growth over the long run. It's not about helping it next quarter.

<Q - Glenn Schorr>: Good morning. A follow-up on John's question earlier on leverage lending. On slide 24, you see the balance and loans held for sale go from like $6.5 billion to $15 billion. I heard your comments on marks. I'm assuming that that is just a disruption and you go back towards your normal level that's in the pipes and progress, but I just want to make sure that I'm not making that wrong assumption.

<A - Marianne Lake>: Yeah. We're not expecting anything to be elevated.

<Q - Glenn Schorr>: Okay. Cool.

<A - Jamie Dimon>: And that number goes up or down over time just based on episodic what gets cleared out of the books. There's nothing in that number we're afraid of.

<A - Marianne Lake>: No.

<Q - Glenn Schorr>: Understood. Curious on the credit – on the couple of marks in C&I, I'm just curious on how much of that is internal versus external rating agency. And I guess, it's a feel for the underlying fundamentals. So how do you know we should treat that as idiosyncratic as you go?

<**A - Marianne Lake**>: Yeah. So it's internal and it's like five names, four sectors. We know the specifics. It is situationally specific. Remember, just to give you some context, while those can drive the dollar value, regular way in any quarter given the size of our portfolio, we might downgrade and upgrade hundreds of individual names based upon the circumstances.

And so when we say that we're looking at this and saying that things are idiosyncratic, it's not just looking at the five situations that drive the biggest dollar value. It's also looking at the hundreds of downgrades and the hundreds of upgrades and seeing if there's any trends or net worrying finds there, and honestly not now. And so if anything, marginally, we had more upgrades, but it's just – there's nothing to see right now in our portfolios and we're looking.

<**Q - Glenn Schorr**>: Okay.

<**A - Jamie Dimon**>: We look for reasons to put up reserves.

<**A - Marianne Lake**>: Yes.

<**A - Jamie Dimon**>: Not to take them down.

<**A - Marianne Lake**>: Only the paranoid survive, we're more paranoid than you are.

<**A - Jamie Dimon**>: Right.

<**Q - Glenn Schorr**>: Last one. Obviously, markets all went down in the fourth quarter. And we had some freeze-ups, if you will, in high-yield first time in 10 years. But I'm curious, how you all think the markets functioned in general. In other words, things went down, spreads widened out, there was lots of fear, but it felt like the plumbing was working, but I don't want to put words in your mouth.

<**A - Marianne Lake**>: Yes.

<**A - Jamie Dimon**>: And half the people weren't even here the last two weeks in December.

<**A - Marianne Lake**>: That's right. The plumbing was working. We didn't see any algo or technology issues. We didn't see any volumes that couldn't be coped with. While I said that there was a little bit of a lack of depth to markets and liquidity, that's typically the case when you'd have one-way trends in the market and a lot of people similarly situated. So, I would say that it relatively functioned well, but challenging.

<**Q - Andrew Lim**>: I just had a follow-on question from the LevFin high yield marks question. You seem to be getting an impression that there weren't really much in the way of marks. Is that because you've got very strong hedging strategies in place and that the decline in FICC revenues mainly was due to lower volumes?

<**A - Jamie Dimon**>: There were no marks.

<**A - Marianne Lake**>: There were no marks. In our bridge book right now, we have – for the vast majority, we have good cushion and we expect to be able to clear and price through the market. And for anything that's even borderline, it's completely not material.

<**A - Jamie Dimon**>: And I think some or a few did have a few marks.

<**A - Marianne Lake**>: Yes.

<**A - Jamie Dimon**>: If you look at what happened to flex pricing like mid-December when things were at their worst. Yeah, some of these things are very close to the end of their flex pricing, and that means they're very close to having some kind of mark. Of course, since then, those spreads have kind of come back 40%.

<**A - Marianne Lake**>: Right.

<**Q - Andrew Lim**>: Interesting. Thanks. And then, my follow-up question is that also the debt capital markets had a tough time. But your wholesale lending growth accelerated quite nicely. Do you get the impression that corporates had a general shift there to seek borrowing from banks such as yourselves because they were shut out of the market?

<A - Marianne Lake>: There was an uptick at the end of the year. You saw it in the industry data. We saw it in our spot data. For us, in fact, it was largely driven by one investment-grade loan that we extended at the end of the quarter. But there was a little bit of an uptick, a little bit more in terms of acquisition financing on the balance sheet, but nothing I would call...

<A - Jamie Dimon>: I wouldn't say it was because they couldn't get funding.

<A - Marianne Lake>: No. There's nothing that I would call unusual or a trend. We didn't have to take down things that would have otherwise not clear the market.

<Q - Matthew Derek O'Connor>: I want to circle back on the expense flexibility. I think in your base case, you're pretty clear that you're targeting positive operating leverage and moving down the efficiency ratio to the mid-50s.

<A - Marianne Lake>: Yeah.

<Q - Matthew Derek O'Connor>: But what is some of the expense flexibility and where would it come from, if the revenue is light? I think in 2018, you accelerated some of the technology spend, given tax reform, you've been opening branches. Some of that stuff obviously can't be pulled back. But you always talk about some areas of flexibility. So, maybe what are those? And if you could kind of size or help quantify some of the flexibility you have, that would be helpful. Thank you.

<A - Marianne Lake>: Yeah. So, I would say first of all that you saw that from 2013 through 2016, we had a pretty structural expense reduction program associated with simplifying our businesses. So, in terms of the low-hanging fruit and things like that, we would say largely that's been harvested. We are always looking to generate core operating efficiency, so that we can absorb growth. And when we are investing in technology data, one of the reasons to do it, customer satisfaction, product innovation aside, is for efficiency. So, we are seeing some of that come through. We'll continue to drive that down.

<A - Jamie Dimon>: That's all – but the efficiencies and the investments are all in the number that Marianne gives...

<A - Marianne Lake>: Yeah.

<A - Jamie Dimon>: When she says up 5%.

<A - Marianne Lake>: That's right.

<A - Jamie Dimon>: Roughly up mid-single-digits.

<A - Marianne Lake>: And so, the way I would say it is that we continue to drive for expense discipline. But as long as you feel, as we do, that the decision criteria that we use to determine the investments we're making, which we think are strategically important to the long-term growth of the company and the profitability of the company supporting our clients, if those are good decisions for long-term growth, while we could obviously make changes, we would not look to do that.

And so, marketing expense, for example, is one area where you would say, there's pretty sizable and immediate flexibility. Nevertheless, when we invest in marketing, we're driving new accounts and engaged customers that drive long-term growth. So, we invest it through the cycle. We think it sort of differentiates our long-term performance, and we'd like to continue to do that. 2019 over 2018, you wouldn't expect to see necessarily the same slip-up that you saw last year. We did accelerate investments in 2018. So, more of the growth will be revenue-related, but still decent investments and the opportunity is still good to do that.

<Q - Matthew Derek O'Connor>: Okay, that's helpful. And then, just on a sidebar here on the reserve build as we think about credit quality, are we just in the period now where we should assume kind of some reserve build consistent with loan growth each quarter? Or was this just a quarter where you had a couple of "the lumpies" that really drove it? I guess what I'm getting at is last quarter, you had...

<A - Jamie Dimon>: What do you put in your model?

<A - Marianne Lake>: Sorry, keep going.

<Q - Matthew Derek O'Connor>: I guess what I'm getting at is like it's – are we at the point where like just a couple of lumpy loans is going to drive a few hundred million reserve build or is it just – maybe this is a bit unusual still?

<A - Marianne Lake>: So, first of all, I just want to sort of point out that in the Card space, we hope we continue to grow at healthy mid single-digits. There's seasonality to Card balances and losses. So, you typically see reserve builds in the second half of the year. That's what we saw this year and actually a little bit lower year-on-year than last. And in the Wholesale space, you're going to see some things will be a bit lumpier and episodic given the nature of the loans that we have. I wouldn't necessarily say that we expect to see a trend of significant reserves. But we've been flattered by recoveries and releases over the course of the last couple of years, partly – or a large part at least earlier releasing reserves we took on energy when the energy went through the downturn. And so, we'll have some downgrades. We might have some releases. I would, net-net, think that as we grow, we would build, but not disproportionately.

<A - Marianne Lake>: And we're arguably at the best point in the cycle. So, Jamie mentioned it earlier. To the degree that we have the flexibility, we're making sure that we're reserved accordingly.

<Q - Saul Martinez>: Well, no comment there. A lot of talk on macroeconomics and the policy backdrop and volatile markets. But as you mentioned earlier, you guys are in a pretty unique position, in that you have pretty consistent dialogue with a lot of economic agents, whether it's corporates, governments, institutional investors and whatnot. But just a sense of what your clients are saying, what are they concerned about? Is there any concern on your part that some of these issues have sort of a self-fulfilling effect, in that it does end up leading to actions that precipitate a downturn or a recession?

<A - Marianne Lake>: So, I think that we would look to the sort of macroeconomic data, which is still generally supportive and say things should be good. But for sure sentiment is not immune to external factors. And so, manufacturing data has been a little weaker. I would say CapEx is sluggish on fears around global growth. Government shut down and trade are not particularly helpful. Uncertainty is not good for anyone.

So, there's no doubt that as things continue, if there's a level of anxiety and uncertainty, it's just not constructive for confidence, and confidence begets a strong or a less strong market. So, I wouldn't say that I think it's clear and present danger, but I think we should be extremely careful because sentiment, particularly consumer sentiment, will be incredibly important. And right now...

<A - Jamie Dimon>: It's pretty good.

<A - Marianne Lake>: It's good, right, sentiment in consumer...

<Q - Saul Martinez>: Yeah.

<A - Marianne Lake>: And we just got back some sentiment from a whole bunch of our middle market companies that while neither are at their highest, they're still very high.

<Q - Saul Martinez>: Right. Okay, that's helpful. If I could just ask about loan growth and just a more broad question about your ability to continue to outpace the industry, and I suspect we'll get more color at Investor Day, but just want to get your sense of the sustainability of growth. And you mentioned on the Commercial side, maybe you scaled back a little bit, maybe we're late cycle. But where do you feel like you can continue to outgrow the industry? Where do you feel like maybe it's time to scale back on risk a little bit?

<A - Marianne Lake>: Okay. So, I think it's – and it's an incredibly nuanced question, because in general, Home Lending is – has a challenging market backdrop. For us, it's a tale of two cities. We're doing quite well and gaining a bit of share in the kind of retail purchase market and we are holding our sort of pricing discipline in correspondent and losing share there. So, there's a challenging market backdrop. Card was – we're doing well at and it's a factor of all the things we talked about, our investments in digital, product, rewards, all of the above. So, we would like to believe that we'll continue to hold our own there. Auto is extremely competitive. We play in prime, super-prime space, and we're seeing competition from people who have different economic drivers than us like, credit unions and captives. And so, we're willing to lose share to maintain returns there.

You bifurcate C&I, we're growing in line or better than the industry in our expansion markets, where we've been making the investments, where we've been adding specialized industry coverage, and we like to see that because of the investments we're making. But in mature markets, we're again being pretty prudent – I wouldn't call it tightening, but being very selective. Commercial Real Estate, particularly construction lending, yeah, we are tightening. We are being very cautious about new deals and selective about those. So, it isn't the case anymore that we would say we are seeking to grow or that we ever were. Loan growth is an outcome of a number of factors, mainly the strategic dialogue with other companies, but also the environment we're in, and it's extremely nuanced. And in many of our businesses, we're going to protect profitability and credit discipline over growth at this point.

<A - Jamie Dimon>: So, I let me just reemphasize that. We tell our management that we have no problem seeing loan books shrink.

<A - Marianne Lake>: Correct.

<A - Jamie Dimon>: We are not going to be sitting here ever in our lives and say, you got to grow the loan book, you got to show loan growth. Remember, Warren Buffett used to say, in the insurance business, sometimes it's true in the loan business, you're better off if your sales force go play golf than they are to make new loans. We're not going to be stupid. And the other thing you have to always keep in mind, it's not the loan – it's the relationship you're looking at in total.

<A - Marianne Lake>: Yeah.

<A - Jamie Dimon>: And so, when it comes to middle market or all these other things, there are reasons that we stay in a business knowing there's going to be a cycle and we're not going to be children when there's a cycle. We know that losses are going to go up.

<Q - Betsy L. Graseck>: Are we playing golf all day yet or is that still far away?

<A - Jamie Dimon>: No, it's – credit is pristine. Mortgage credit is pristine. Middle market is pristine. Underwriting standards have been pretty good, other than a few little pockets that Marianne's mentioned and – but we saw people stretching in Auto. We saw some stretching. And we're not in the subprime credit card, but a little bit of stretching in that and leveraged lending, we're not worried about our loan book. I think you can have a logical conversation, but there's...

<A - Marianne Lake>: Yeah.

<A - Jamie Dimon>: Kind of the non-bank loan book. But that's not our concern and it is what it is at the time, so...

<A - Marianne Lake>: And I think where businesses are notably a little bit less relationship-driven, so think about kind of loan-only relationships, Commercial Term Lending, Real Estate Banking, mortgage, to a lesser degree also, we are seeing – we are losing or ceding share where it makes sense to do it.

<A - Jamie Dimon>: Yeah. And competition, we've been in this before is back everywhere, and that's a good thing for America. That means the pricing is a little tough and that you have to compete and...

<Q - Betsy L. Graseck>: Yeah. So – and we're still off the golf course. All right, that's good. Just wanted to understand a little bit more on the expense side. I know it was a – even with the weather, you guys put out a 14% ROTCE, which is obviously best-in-class. The question is on the expenses, there's flexibility there, but yet I know you've guided to up single-digits in 1Q 2019. Based on the prior conversation, it seems like 1Q might be an aberration of mid single-digits or should I take that that's kind of the run rate you're expecting for the full-year? Or why would 1Q be...

<A - Marianne Lake>: No, I wouldn't annualize...

<Q - Betsy L. Graseck>: Why would 1Q be a little bit different, I guess, is really the question?

<A - Marianne Lake>: Yes. So, I wouldn't fully annualize the first quarter, but think about we've added bankers and advisers across our businesses. So, you're going to get some annualization impact, particularly first quarter over first quarter. We had added more and more as the year progressed. Similarly, something like auto lease, where we grew our auto lease business revenues and expenses strongly in 2018, and that will be in our run rate in the first quarter. So, front-office, auto lease, some of the technology investments we've been making, the annualization of those will be more pronounced first quarter to first quarter than fourth quarter to fourth quarter, because many of them are in our run rate in the fourth quarter.

And then, outside of that, there's a bit more in real estate, as we sort of execute on our head office strategy. And then, marketing, Foundation contribution, those things – there's going to be timing. So, the first quarter will be higher. I wouldn't annualize it. We are going to see likely growth year-over-year, much more because of revenue growth than because of investments, but both year-on-year not the same level as last year. And we'll obviously give you a lot more detail and insights and thoughts on ranges and everything at Investor Day clearly.

<Q - Brian Kleinhanzl>: Just a quick question on the balance sheet, sorry if you gave this already. But can you kind of walk through the idea of lowering down the deposit with banks and kind of moving into repo, what you saw in the quarter and then kind of is that just something that was temporary that's expected to reverse in the first quarter? Thanks.

<A - Marianne Lake>: Yeah. So, it's fair to say that money market rates traded above IOER throughout the fourth quarter and more pronounced at the end of the quarter. And so, through the quarter and at year-end, we were able to take advantage of the market opportunity to move out of cash into cash alternatives, think reverse repos and short duration assets. And so, for us, it was a yield-enhancing opportunity to redeploy cash and a mix change rather than adding duration. And that continues to be the case into the first quarter. It contributed to our NIM expansion in the fourth quarter. We continue to have a bit of that mix shift in the first quarter, and it's the market opportunity.

<Q - Brian Kleinhanzl>: Okay. And then, a separate question on – I know it's not a big revenue driver anymore, but within the Mortgage Banking, you had a negative gain on sale in the quarter. Can you just give us some color there, what drove the negative gain on sale?

<A - Marianne Lake>: Yeah. So, in the quarter, as we were looking at optimizing our balance sheet, we actually did a sale of conforming loans to the GSEs of about $5 billion. The impact of that was to have a loss on the sale of the portfolio, given that they've been originated at lower rates. So, as rates are higher, the fair value of the loans is lower. Against that, if you were to look at the rest of the P&L, you'll see a benefit in net interest income, because the interest rate risk of that has been transferred to the Treasury Department. So, it's geography. It's a loss on the sale of a portfolio, against which there's funding breakage in NII. Just so that you know, when we – a mortgage loan with RWA at 50% versus a security at 20% with better liquidity value, we did reinvest some of those proceeds in mortgage-backed securities in Treasury. So, we'll earn that back over time net for the company.

<Q - Steven Chubak>: So, I wanted to start with just a bigger picture question on credit and the impact of normalization. Certainly, the near-term guidance sounds quite encouraging. Jamie, you did make a comment recently at an investor conference, talking about how the banking industry is over-earning on credit, not particularly a controversial remark. But in the past, you guided to a medium-term loss rate on a blended basis of roughly 65 bps. That does contemplate continued low losses in Commercial. And just given that we're late-cycle, I was hoping you could maybe speak to your expectation for what a normalized credit loss rate is for JPMorgan, given your current mix, and where that might differ from your medium-term loss guidance?

<A - Jamie Dimon>: So, we're not talking quarter-over-quarter. You're just talking in general trends.

<Q - Steven Chubak>: I'm talking bigger picture.

<A - Jamie Dimon>: Right. So, Marianne has showed year-to-year, we've considered normalized losses. And for years, we've been doing better than that in credit card, middle market, large corporate. Mortgage has come back down to a very low number. And at one point, it's going to go up, and so I'm not – we're not telling you what's going to happen next quarter. Right now, it looks like it's kind of steady-state. But at one point, we will not be surprised to see it go up. I don't know if it'll be the second quarter or the third quarter or the fourth quarter, and I don't know if we're late-cycle. We don't exactly know where we're in the cycle. And so, we just won't be surprised to see it go up and the number – we look at it by product, we don't look at it in a total, so I can't actually – maybe Marianne can raise the total…

<A - Marianne Lake>: No, no, and I think – I hate to say this, because I know that you don't want to wait a few weeks, but we'll have a more complete conversation about, kind of, range of total outcomes on credit at Investor Day. But when we gave our medium-term simulation, we said, listen, we did a 17% return on tangible common equity in 2018 and our medium term guidance is 17%. We've under earned against our guidance in other parts of the cycle, maybe we will or won't over earn against it, but NII and reprice lags are higher and credit is benign. And at some point, we would expect both of those things to normalize, but we would continue to see solid growth in all of our drivers.

So, we don't know when it will be, and actually we don't see anything that – I know you say is it second, third or fourth quarter. There's no indication that in any of those quarters, but we'll have a more comprehensive discussion at Investor Day about range of total outcomes.

<Q - Steven Chubak>: All right. Looking forward to that. And just one follow-up for me on the IB outlook. Marianne, I was hoping I could unpack just some of your comments around the IB backlog. You cited that as being quite strong, but just looking at the individual businesses for M&A, ECM, DCM, especially given some of the economic pressures outside the U.S., what informs your outlook across each of those?

<A - Marianne Lake>: Yeah. So, I would say that, first of all, we did see, given the conditions in the fourth quarter, a number of deals were – got pushed from the fourth quarter into the first quarter, particularly in ECM and DCM. In M&A, there was a little bit more balance. So, for every deal there that got pushed or dropped, there were more that came to take its place. But as a result, as we go into the first quarter, pipelines across the board are – elevated relative to last year and pretty strong.

And at the end of the day, we talked about it earlier, confidence is still high, companies are still motivated to drive growth. And so, the environment should be constructive for continued M&A. The technology, healthcare, the biotech innovation, technology innovation momentum in ECM that we've been benefiting from and the IPO pipeline should continue market-dependent. And, notwithstanding December, actually, sort of, lower outlook for rates in the U.S. should broadly be a tailwind for fixed income in the first quarter and the first half.

So, the second half of the year, I think is going to be determined by how things shape up over the next several months, but walking into January, again, if the market remains generally constructive, we should see tailwinds across the businesses.

<A - Jamie Dimon>: Yeah, at least in terms of backlogs, generally, we want them high, because that's good. But it's like an accordion too, they come and go. So, that's not a forecast for the future that you definitely get those revenues, things get delayed particularly things like IPOs that you've already seen.

The other thing I just want to point out as well is shout out to the folks in the Investment Bank, our market share went up in Europe, Asia, Latin America and the United States last year. That's what we really look at, when look at the business.

<A - Marianne Lake>: 60 basis points whole year.

<A - Jamie Dimon>: Yeah, 60 basis points whole year. And first time ever, it went up in all four major markets.

<Q - Marty Mosby>: Jamie, I was glad that you mentioned that we don't know that we're at the end of the cycle, because that's kind of – just assume because of the lapse of time, but not really the economic factors. And then, the other piece of this is when you look at losses, they tend to be good until they go into recession, then they're bad. There is no just, kind of, normalization. So, the question about a normal rate of loss that we really have two dichotomis answers. We have a good answer, which is when we're expanding and the economy's stable, and we have a bad answer when we're in a recession. It's kind of one or the other. Just wanted to see what you thought about that.

<A - Jamie Dimon>: Yeah. You're exactly right. At one point, you're going to over earn, at one point you're going to under earn. And we try to – when we look at the business, we kind of try to price through that. So, we're trying to earn fair returns through the cycle. And I totally agree with you. We know it's got to – they're going to change at one point. And we try to do a better job underwriting too, by the way. And we do look hard to make sure we underwrite other people as best we can.

<Q - Marty Mosby>: Which then limits the volatility when you go into that bad period, which is what you want to do. You underwrite, you make sure you're defending against that cycle?

<A - Jamie Dimon>: Exactly. And the other one you have is the reserves. You put them up, you take them down. So, our total reserves are what, $14 billion? Yeah. But at one point, they were at $30 billion. And also, we went from – in the Great Recession, we went from $7 billion to $30 billion, back to $14 billion. And I call that ink on paper.

<A - Marianne Lake>: Right.

<A - Jamie Dimon>: Because it doesn't mean anything. It's just – so when you go into a recession, your losses go up and your reserves have to go up, and we're completely aware of that.

<A - Marianne Lake>: Although, I think, we would say for obvious reasons that we wouldn't expect any near-term recession, if there is one, to look anything like it did before. And even if it did, given the credit quality of the portfolio, performance would be not only absolutely better, but we think strong on a relative basis.

<A - Jamie Dimon>: So, other than – if you look at the Consumer, the $13 trillion that's outstanding, other than student, which is fundamentally owned by the government, the mortgage stuff that's been written is prime. So it's back to $10 trillion, but it's much better than what it was in 2007, but I think Credit Card, I've got the exact numbers, much more prime than it was in 2007. I think Auto is about the same, but Auto actually outperformed in the...

<A - Marianne Lake>: More prime.

<A - Jamie Dimon>: More prime and outperformed in the Great Recession. I think people in general have done a better job underwriting middle market and leverage stuff than they did last time. So, I think if you start a recession soon, going into it, the credit portfolio is much stronger than last time.

<Q - Marty Mosby>: And the follow-up question to that is, we talked about Auto and some of those other places, where you saw some of the deterioration. What our model is showing is that actually the discipline and the reaction time to that deterioration is much quicker than when we saw the one-to-four family cycle the last time, where you saw deterioration, but growth just kept going. We've had so many banks jump in and say, look we've already pulled back on auto lending, or we pulled back on multifamily. There's already been places where you've seen that discipline, so that discipline in itself puts the Governor on economic growth, which is why we're having less growth or slower growth, but yet it also creates, like you said, a stronger portfolio for that eventual downturn.

<A - Jamie Dimon>: And I agree with that, the lack of discipline we see is in student and a little bit in small commercial real estate.

<Q - Gerard Cassidy>: Can you guys – there's been a lot of talk about leveraged loans and how this time around everything seems to be underwritten better. Are there any tangible statistics that you can share with us or maybe on Investor Day you might, to show us that, yes, the leveraged loan portfolio, for you guys in particular, is much healthier than maybe 2006, 2007?

And then, second, on this leveraged loan issue, outside the banking industry, what are some of the indirect hits that you and maybe some of your peers may experience, none from the direct hit of the leveraged loan, but for some of the craziness that's going on outside the banking industry?

<A - Jamie Dimon>: Yeah. So, can I just give a big picture of this? I think $1.7 trillion of leveraged loans, okay? So, Term A is about half of that. These are very rough numbers, okay, most of which are with banks, and obviously, safer than Term B. A big chunk over I think 60% or 70% of the Term B is with non-banks. And so, if you look at the banking system, if you look at the leveraged lending bridge book in 2007, it was over $400 billion. Today, it's a number like $80 billion. In 2007, there were commitments and no flex. Almost everyone has plenty of flex now. So, when you look at covenants, there is kind of covenants, but there's flex and there's a whole bunch of other stuff in there. So, it is far, far, far sounder today. Even these CLOs, as we look to underwrite into these CLOs, they are far better underwritten with more equity, more sub debt, and more mezzanine, stuff like that.

And now, go to the shadow banks, they do things slightly differently. A lot of those folks are – they're quite bright, they kind of know what they're doing. Someone's going to get hurt there. And the issue there is in the next recession isn't going to be what the losses are – and remember, most of the major banks don't fund a lot of debt. We aren't taking huge indirect exposure debt by funding some of the non-banks. And I think the issue there is – for the marketplace, is going to be when we have a real recession, the lender will not be there. So, a lot of these borrowers will be stranded. And so that – and that's not – that's an opportunity or a risk or something like that, but it's not – I wouldn't put it in the systemic category.

<Q - Gerard Cassidy>: And do you think...

<A - Jamie Dimon>: And by the way, again, if you go back to 2007, we – it emerged in 2007, there was $1 trillion of bad mortgages that were kind of all over the place in CLOs, SIVs, there are no SIVs. The CLOs are much smaller, the leverage lending book is a much smaller book, capital liquidity is much higher. So, it is nothing like 2007. You will have a recession; it just won't be like you had the last time in the bank – affecting banking system. Well, it will affect the banking system. We're a little like canaries in a coal mine. We're not immune to what goes on in the economy, but it won't be anything like you saw last time for most of the large banks.

<Q - Gerard Cassidy>: No, I would agree with that. And do you think Janet Yellen and other Federal Reserve officials' comments about leveraged lending is more directed to the exposure outside of the banking industry than inside the banking industry?

<A - Jamie Dimon>: Yes, I do.

<A - Marianne Lake>: Yes.

<A - Jamie Dimon>: Yeah.

<Q - Gerard Cassidy>: Very good.

<A - Jamie Dimon>: Again, I don't think they were saying it's huge or systemic. They're saying it's something that you should keep an eye on, and I think that the regulators do keep an eye on that.

<Q - Gerard Cassidy>: Right. And then just to pivot on a deposit question, obviously, non-interest-bearing deposits are tough to keep as rates are going higher. Can you guys give us some color on the non-interest-bearing deposits? There was, I would say, a small decline. What parts of the business you're seeing that? And the Fed's unwind of its balance sheet, how much of an impact do you think that might be having on the non-interest-bearing deposits?

<A - Marianne Lake>: So, the migration intraproduct from non-interest to interest-bearing is predominantly or largely exclusively a wholesale thing. At this point, there's not enough rate benefit in the interest-bearing savings to drive intraproduct migrations. Definitely, some growth outlook in CDs, given pricing, but it's wholesale right now, and it's mainly rate related and not balance sheet related in terms of the Fed unwind.

<A - Jamie Dimon>: Could I just make a comment about interest rates and the balance sheet of Fed, so, interest rates is one thing, but the balance sheet of the Fed obviously is causing changes in the flow of funds. It's causing changes and the banks now have options other than reserves at the Central Bank, because the two-year and three-year bond yields per corporate or government bond is much higher. Some people are preferring to own that, because they think they'd be paid better, no corporate risk. So, it changes a whole bunch of fund flows that concerns people, but I'd say its part of the process of normalization.

<Q - Ken Usdin>: There were a couple of Fed or regulatory documents out in late December, one codifying the three-year burn in of stated CECL impacts and another one where they're pushing out till 2022 on their own implementation of CECL accounting and the supervisory stress test. Just wondering, just any takeaways you had from reading that and any hopes you might have for just as we get towards some finalization of which way CECL goes and how it looks, aspirations around that and how that interacts with CCAR and such?

<A - Jamie Dimon>: Before Marianne answers that question, I just want to do a shout-out to Jefferies, because we actually look at what everyone does in every investment banking group, but you guys did a hell of a good job in healthcare this year.

<Q - Ken Usdin>: I'll pass that along, Jamie.

<A - Marianne Lake>: And following that – it's hard to follow. I would say, look, we've been pretty clear about the fact that our biggest concern around CECL was like properly understanding not just for us, but for regulators probably to understand the implications for capital, not only in benign but in stressed scenarios, and what the implications of the outcome there could have on the willingness for people to extend credit particularly as cycles age, and with the outlooks for a lot of them to increase. So, having a transition is obviously helpful. You should imagine that we would likely avail ourselves of that opportunity, if that is what it is.

For me, the question that needs to be clarified is, if we are to include the impact of CECL in company-run stress tests, but the Federal Reserve is not going to include it in their stress tests, we need to kind of understand the interplay between those two things, particularly if that might coincide with a turn in the cycle in actual fact. So, I think we're looking for continued clarity from the regulators about what exactly that means. If we're embedding these assumptions into our stress tests and our results sooner than they are, how do we think about the implications of that on our distribution plans and capital outlooks. And importantly, if it really is the case, that we have to up-front significant amounts of capital for longer tenure, lower credit quality loans. I do really believe even though the cash flows and economics conceptually don't change, that you might find people less willing to lean into growth for longer duration assets, if there are concerns around potential volatility and we should worry about that.

<A - Jamie Dimon>: And it will be a big number for Credit Card.

<A - Marianne Lake>: Yes.

<A - Jamie Dimon>: If you put a 3% now, when you build a loan book by $100, the number would be 6% or 7% -- some number in the future be much higher. So, I do think particularly smaller banks will react fully dramatically in how they run their loan books to do that.

<A - Marianne Lake>: So, our view is that more analysis needs to be done in the industry about what this looks like. I hope that what was meant by we should include it in company-run stress tests is for us to collectively learn, and for the regulators to have the time to respond to that. But remember, 2022, considering all the discussion we've had on this call about the cycle, how long the cycle is, when is the turn in the cycle, we could actually face a stress before that. And so, it's great that they are waiting a bit, but it might all be a bit of an academic point, depending on what happens actually.

<Q - Ken Usdin>: Yeah. That's a fair point. And, Jamie, you've also said in the past that you guys lend on accounting, right – don't lend on accounting and lend on economic, right, but there's this kind of challenge to that that Marianne just mentioned about the unintended consequences. And so, it would be interesting to see that, if there is in fact a point where banks don't lean in as you just mentioned, Marianne.

<A - Marianne Lake>: Yes.

<A - Jamie Dimon>: They will change.

<A - Marianne Lake>: And we have the luxury or the flexibility of being able to say that we can continue to lend based upon the underlying economics. But someone who has a differently situated balance sheet and return profile may not be able to do that.

<Q - Mike Mayo>: Hi. A follow-up on the net interest margin. Two sides to the question. One is commercial loan pricing, I guess, it's been kind of brutal. You've had the BDCs, private equity firms, loan funds, all competing. Has there been any let up with some of the dislocation in the capital markets late in the year? And the other side, retail deposit betas, Marianne, you thought they would get a lot worse. I don't think it's been as bad as you thought. What was your retail deposit beta and what do you still expect?

<A - Jamie Dimon>: Before Marianne answers that, can I just go back to the cyclical stuff? One of the issues, it's not just CECL. A lot of things that have been built since the crisis were really good, but there is more pro-cyclicality built into it. And so, you're going to see the next downturn that we have a far more procyclical accounting, liquidity and rules, capital rules and stuff like that, which we don't know the full effect of that. But if I was a regulator, I'd be very cautious about constantly building procyclicality to the system. And I gave you the example of our loan losses going from $7 billion to $30 billion or whatever they went to back to $14 billion. It will affect how people respond in a downturn, and they will – it will cause people to pull back much quicker than maybe in the past in total.

<A - Marianne Lake>: Okay. So, just on your question, so corporate loan spreads, I would say, we did see sort of pretty brutal grinding down in corporate loan spreads, but over the last actually couple of quarters, we saw them find a bit of an equilibrium and stabilize at level. So, while I would say it's still true to say that there is a lot of competition, at least in the space in which we're operating, we're seeing spreads at relatively stable levels in the corporate space.

And honestly, I don't remember saying that I thought we would see an acceleration that was dramatic in retail betas in the short term. I mean obviously, at some point, when the absolute level of rates and the spread between market rates and rates paid gets to a certain level and if normalization continues, we would expect to see reprice lags sort of catch up, but we have not seen that yet outside of CDs in the retail space right now.

<Q - Mike Mayo>: And the way you calculated it, what was your retail deposit beta this quarter? And how does that compare to the past?

<A - Marianne Lake>: So, in checking and savings, at least savings, it's nothing. In CDs, it's something, but it rounds to a very small number.

<Q - Gerard Cassidy>: Thank you. Just a quick follow-up, Marianne. Have your investment bankers on the front lines passed on any concerns about the government shutdown? There's been reports that the SEC is not open and is that slowing down the investment banking business and your thoughts on that, please?

<A - Marianne Lake>: Yes.

<A - Jamie Dimon>: Of course.

<A - Marianne Lake>: So, I would say that we've been – we benefited from the fact that year-end and into the early part of January and the holiday season have a light calendar, typically in January, for IPOs in particular. But for sure, if we don't see the ability to get approvals from the SEC on IPOs, and to a lesser extent, some of the M&A deals that need approvals from government agencies, it will be problematic in the ability to see those activity levels play out and fees be realized. So, I mean, it's one of many things that would behoove us to end this sooner rather than later.