Company Name: JPMorgan
Company Ticker: JPM US
Date: 2018-10-12
Event Description: Q3 2018 Earnings Call

Market Cap: 363,567.15
Current PX: 109.33
YTD Change($): +2.39
YTD Change(%): +2.235

Bloomberg Estimates - EPS
Current Quarter: 2.276
Current Year: 9.209
Bloomberg Estimates - Sales
Current Quarter: 27485.529
Current Year: 110861.087

Q3 2018 Earnings Call

Company Participants

- Marianne Lake
- Jamie Dimon

Other Participants

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

MANAGEMENT DISCUSSION SECTION

Marianne Lake

Financial Highlights

Net Income, EPS and Revenue

- Starting on page 1
- The firm reported net income of $8.4B and EPS of $2.34 on revenue of $27.8B, with a return on tangible common equity of 17%
- The results this quarter were strong
- Record net income for our third quarter, even excluding the impact of tax reform, with key drivers being higher net interest income across businesses, reflecting continued rate normalization and solid growth in both loans and deposits, as well as very strong credit performance across all portfolios

Core Loan Growth

- Highlights include: average core loan growth, excluding the CIB, of 6% year-on-year; card and debit sales as well as client investment assets and merchant processing volumes in Consumer were all up double-digits

- We gained share in global IB Fees and across all regions YTD
- And in Asset & Wealth Management, AUM and client assets were both up 7%

Q3 Results

Revenue and Net Interest Income

- Turning to page 2 and some more detail about our third quarter results
- Revenue of $27.8B was up $1.4B or 5% year-on-year
- Net interest income was up $945mm or 7%, reflecting the impact of higher rates, net of lower Markets NII, as well as loan and deposit growth

Noninterest Revenue

- Noninterest revenue was up $425mm, driven by Markets NIR and higher auto lease income, partially offset by markdowns on certain legacy private equity investments
- Expense of $15.6B was up 7% year-on-year
- More than half of the increase relates to investments we're making in technology, marketing, bankers broadly defined, and real estate

Credit Trends

- And the remainder is driven by revenue-related costs, principally higher auto lease depreciation and transaction expenses on higher volumes
- Credit trends remain favorable across both Consumer and Wholesale
- For the quarter, credit costs of $950mm were down $500mm year-on-year, driven by changes in Consumer reserves

Balance Sheet and Capital

- Briefly on page 3, turning to balance sheet and capital
- There's little to say here, other than as you can see, capital and risk-weighted assets remain basically flat quarter-on-quarter with a CET1 ratio of 12%

Consumer & Community Banking

- Moving on to page 4 and Consumer & Community Banking
- CCB generated $4.1B of net income and an ROE of 31%
- Core loans were up 6% year-on-year, driven by Home Lending up 10%, Business Banking up 5%; Card up 4%, and Auto loans and leases up 3%

Deposit Growth

- Deposits grew 4% year-on-year, continuing to outpace the industry, although slower than a year ago
- According to the recently released FDIC annual survey, we grew at nearly two times the average and we were the fastest-growing bank in 9 of our top 10 markets
- Chase also earned the number one spot in customer satisfaction in the J.D. Power U.S. National Banking Satisfaction Study

Client Investment Assets

- Client investment assets were up 14% as we saw clear record net new money flows, more than doubling year-on-year, with flows accounting for more than half of the growth
- Card sales volume was up 12%, with strength across our portfolio and we also saw very strong debit sales performance, up 13%
- Revenue of $13.3B was up 10%; Consumer & Business Banking revenue up 18% on higher NII, driven by continued margin expansion and deposit growth

Revenue Growth

- Home Lending revenue was down 16%, as higher rates drive loan spread compression and a smaller market, pressuring production margins
- In addition, net servicing revenue was down including the MSR
- Card, Merchant Services & Auto revenue was up 10%, driven by higher Card NII on margin expansion and loan growth, higher net Card fees on lower acquisition costs, substantially offset by lower net interchange and also on higher Auto lease volumes
- Expense of $7B was up 7%, driven by continued investments in technology and by Auto lease depreciation
- The overhead ratio was 53%

Reserves

- Finally on credit, starting with reserves
- This quarter, we built reserves in Card of $150mm, largely driven by growth and we released reserves in the Home Lending purchase credit-impaired portfolio of $250mm, reflecting improvement in home prices and delinquencies
- On charge-offs, there are a few moving pieces
- Year-on-year charge-offs were down $137mm, driven by a recovery from a reperforming loan sale in Home Lending this quarter of about $80mm, together with an approximately $50mm charge-off adjustment in Auto this period last year
- Excluding those charge-offs, we’re about flat, but we are seeing improvement across all portfolios, except for Card
- And in Card, while charge-offs are up as newer vintages season, they are up less than expected, as credit performance remains very strong
- At this point, we expect Card charge-off rate for the year to be below our guidance at about 310BPS

Corporate & Investment Bank

- Now turning to page 5 and the Corporate & Investment Bank
- CIB reported net income of $2.6B and an ROE of 14% on revenue of $8.8B, up 2%
- In Banking, we maintained our number one ranking YTD in global IB fees as well as in North America and EMEA and gained share across regions
- For the quarter, IB revenue of $1.7B was flat to a strong prior year and we outperformed in the market that was down meaningfully as we saw robust activity, particularly in ECM.

Equity Underwriting Fees

- Equity underwriting fees were up 40%, gaining share across all products, with continued strength in IPOs, particularly in technology and healthcare
- Advisory fees were down 6% compared to a third quarter record last year, outperforming the market and gaining share YTD
- And debt underwriting fees were down 11%, although better than the market, as our strong lead left positions drove share gains
- Looking forward, the overall pipeline remains strong, up solidly from the prior year across products

Market Conditions

- Moving to Markets
- Total revenue was $4.4B, down 2% or up 1% when adjusting for the impact of tax reform
- So, another good performance

Fixed Income Markets

- Fixed Income Markets revenue was down 6% adjusted, with no single predominant driver
- We saw mild weakness in Rates, Financing, Credit Trading and Securitized Products as a result of compressed margins and tighter financing spreads in range-bound and competitive markets
  - This was partially offset by higher activity levels in Emerging Markets on volatility and Commodities returning to more normal levels relative to a weaker prior year

Equities Revenue

- Equities continued the momentum from previous quarters and was up across all segments on the back of strong client activity
- Equities revenue was up 17%, reflecting continued share gains in cash and prime and strong performance in corporate derivatives
- Treasury Services and Securities Services revenues were $1.2B and $1.1B, up 12% and 5% year-on-year, respectively, driven by higher rates and balances
- And Securities Services also benefited from higher asset-based fees on new client activity

- Quarter-on-quarter, Securities Services revenue was down, principally on seasonality and the impact of a business exit
- Finally, expense of $5.2B was up 8%, driven by higher legal expense, higher compensation expense as we invest in technology and bankers, and volume-related transaction costs

Commercial Banking

- Moving to Commercial Banking on page 6
- Another strong quarter for this business, with net income of $1.1B and an ROE of 21%
- Revenue of $2.3B was up 6% year-on-year, driven by higher deposit NII.

Gross IB Revenue

- Gross IB revenue of $581mm was flat, although we saw a strong underlying flow of business and pipelines remain robust and active
- On deposits, while we continue to benefit from the normalizing rate environment, as expected, the balances are down year-on-year and bases are trending higher, as we are seeing some migration at the top end to higher-yielding investments
- Expense of $853mm was up 7% as we continue to invest in the business in banker coverage and technology initiatives
- Loan balances were up 4% year-on-year and 1% sequentially

C&I

- In C&I, demand remains muted in the wake of tax reform, as well as client confidence is high, balance sheets are strong and liquid, and the environment is competitive
- For us, C&I loans were up 4% year-on-year and flat sequentially, in line with the industry
- But if you decompose it, we’re growing strongly in our expansion markets and specialized industries, growing solidly in our core markets, but are seeing notable offset in tax-exempt activity given the mix of our business
- CRE loans were up 3% year-on-year, a little less than the industry as we are seeing increased competition and continue to be very selective
- Finally, credit performance remains strong with net recoveries of 3BPS

Asset & Wealth Management

- Moving on to Asset & Wealth Management on page 7
- Asset & Wealth Management reported net income of $724mm, with a pre-tax margin of 27% and an ROE of 31%
- Revenue of $3.6B was up 3% year-on-year, driven by higher management fees, net of fee compression, on higher market levels and continued growth in long-term products
  - These were partially offset by lower mark-to-market gains including on seed capital investments
- Additionally, Banking results were strong

- Expense of $2.6B was up 7%, driven by continued investment in advisors and technology, as well as higher external fees on revenue growth

AUM

- For the quarter, we saw net long-term inflows of $8B, with positive flows across all asset classes
- In addition, we saw net liquidity inflows of $14B.
- AUM of $2.1 trillion and overall client assets of $2.9 trillion were both up 7%, with more than half of the increase being driven by flows and the remainder on higher markets
- Deposits were down 8% year-on-year, reflecting migration into investments with us and down 5% sequentially, including seasonality
- Finally, we had loan balances up 12%, with strength in global wholesale and mortgage lending

Corporate

- Moving to page 8 and Corporate
- Corporate reported a net loss of $145mm
- Treasury and CIO net income was up year-on-year, primarily driven by higher rates
- Other Corporate was a net loss of $241mm, including markdowns on certain legacy private equity investments of $220mm pre-tax
- For the whole company, legal costs were a modest negative, with the benefit here in Other Corporate being more than offset in the CIB

Outlook

FDIC Surcharge

- Moving to page 9 and outlook
- We recently gave you updated outlook, so unsurprisingly, that still holds and it's here on the page
- Only two things of note, our expense outlook assumes that the FDIC surcharge ended this quarter
- So clearly an extension would pose a risk
- And on tax, there are a number of questions in the rules which we expect to be clarified by the end of the year
  - We will have to work through them, but would not expect any changes to be material

Market Share Gain and Strategy

- So to close, we are growing across most of our businesses
- We're investing heavily in all of them
- We're investing in technology, bankers and beyond
- Credit is in great shape and the earnings power of the company is evident

- We are particularly proud of the strength and improvement in customer satisfaction broadly and our continued investments, which drive leadership positions and market share gains
  - This quarter, we announced Sapphire Banking and our digital investing platform, You Invest
- We opened our first branch as part of our expansion strategy in Washington D.C., announced additional expansion into Philadelphia and Boston and also announced our Advancing Cities Initiative, as we invest for growth in the clients and communities that we serve

QUESTION AND ANSWER SECTION

<Q - Glenn Schorr>: So at the Investor Day, I remember asking you the same question. So I apologize, but you had a slide that talked about Consumer and Corporate balance sheets being in great shape and having a low debt service burden. The 10 years' up a modest 35BPS since then and the world's freaking out that it's the end of the cycle and that's going to choke off the recovery. Your results are your results, but they're, some will say, backward-looking. Are you seeing any impact, A, at the modest increase in the curve now? And B, I'll ask again, is there a level of rates where you would start to see an impact of slowdown in what you're willing to lend, rising in credit costs, things like that? Thank you.

<A - Marianne Lake>: Yes. So I would say – I would sort of pick up on the tone that you had in your question, which is the level of rates is not surprisingly high. And so from our vantage point, we're not seeing anything in terms of looking at our client dialogue or, for that matter, at the credit trends that would suggest that this is problematic.

With higher rates – and we do this all the time, we obviously look at all of our portfolios and stress them for shocks of up 100BPS, even up 200 although, clearly where we are now, risks are more symmetric, but there doesn't seem to be any extraordinary stress that becomes evident even if you – obviously the margin you're going to get more, but it doesn't seem to be overwhelming. And it speaks I think to the fact that low rates have been around for a long time. People have had a chance to get prepared.

There is a lot of liquidity. And in the corporate space in particular, people have been able to hedge. So is there an absolute level of rates where things will be problematic? At some point, but we don't think we're anywhere near there. So I'm not saying that there couldn't be select downgrades. I'm not saying that at the margin, there may not be some incremental stress if rates continue to go much higher, but that's not where we are right now.

<Q - Steven Chubak>: I wanted to start with a question on the You Invest launch. As we think about the strategy for the business, I want to understand is the goal to compete with the incumbents to win new clients? Or are you simply trying to augment the existing offering for JPMorgan clients? And it's really just our effort to understand the long-term strategy given that the pricing is quite competitive, but at the same time, the marketing effort has been fairly minimal so far?

<A - Marianne Lake>: Yes. I mean remember, You Invest, it's early. Jamie just said, I don't know if you heard it, yes and yes. Clearly, we are trying to add products and capabilities and value to our existing clients in an effort to continue to drive loyalty and engagement and also earn more share of their wallet.

But we do think that the proposition is compelling and that the pricing is disruptive and we should also expect over time to be able to attract new accounts. So yes and yes. But it's early days. We're going to continue to develop You Invest, its capabilities to iterate it and improve it. So far, it's early, but good.

<Q - Steven Chubak>: Got it. Thanks for that, Marianne. And just one follow-up for me relating to the commentary on the deposit side. You spoke of some of the headwinds to deposit growth and these are more industry trends, including yield-seeking behavior on both the Commercial and Asset Management side. I know you've given some helpful guidance in terms of the impact of Fed QE unwind as well in the past. I'm just wondering is the yield-seeking behavior you've seen so far consistent with your expectation? Do you still expect to grow deposits as we look out for the next couple of years?

<A - Marianne Lake>: Yes. So the answer is generically yes, as we would've expected. Obviously, we have no crystal ball as to the sort of timing and path of these things, but it is playing out arguably a little slower than we thought, but like we thought. And I would say that our outlook for deposit growth is for it to be slower, but still positive.

<Q - Betsy L. Graseck>: So first question, just on the rate question that you got earlier, but I wanted to understand how you're thinking about the impact on the outlook for your asset yields, in particular of the securities portfolio. I know you've given guidance on that before. But given the sharp backup that we got over the last couple of weeks, how's that impacting your forward look on that?

<A - Marianne Lake>: Yeah. So I mean – on the asset side of the balance sheet, just a big rule of thumb is that a little less than half of our loans are variable, indexed to prime and LIBOR. So what we've been seeing – in any one quarter, there can be noise on onetime items or mix or whatever else. But largely speaking, for every rate hike we've been seeing on the front end, we're seeing our assets reprice about half of that and that – or our loans reprice about half of that and that's what we'd expect. Similarly, if we see sustained increases in the long end of the curve, then we would see that play through into our investment securities yield. Obviously, this quarter, while there was a meaningful increase on a spot basis, on an average basis, that wasn't the case and particularly not for mortgages. So it had a modest impact on investment security yields this quarter. But again, if it was sustained and more sizable, we would see that pass through, yes. We would rotate the assets into higher book yields over time.

<Q - Betsy L. Graseck>: Okay. And then my follow-up question has to do with a blockchain that you launched this quarter. I think it was on September 25, you launched a blockchain for international payments. And I know at Investor Day, you talked a lot about the investments you were making on that side. Should we be viewing this as a competitor to SWIFT? Is that how the vision is for this blockchain?

<A - Marianne Lake>: So, this is the Interbank Information Network which we talked about at Investor Day. And now we have, I think, 75 banks and growing signed up to it. I wouldn't necessarily look at it exactly like that. I would say this use case, at least for now, is very much around reducing the friction in the wholesale payments space in terms of inquiry and information sharing and not at this point about processing payments. So we are still exploring use cases across the board on blockchain. I'm very excited about this and the uptake, it will be, I think, meaningful, but I wouldn't think of it that way. Not yet.

<Q - Erika Najarian>: My first question expands on what Glenn had asked. So clearly, the bank stocks have been hit along with the broad market. And I guess, they're telling us one of two things, one, either the economy is slowing down or the relationship between bank revenue growth and solid economic growth in the U.S. is broken, or not somehow as correlated as expected. And I'm wondering, given your fairly strong results across the board, where is the market wrong in terms of how they're thinking about either the economy or bank revenues related to a strong economy?

<A - Marianne Lake>: Yeah. I need to start by saying, I mean, there's a lot of sort of macro uncertainty noise and overhang that have been affecting the markets over the last few days. So overthinking any one driver or sort of confusion I think might be challenging. I would say that as we look at the economy, we don't see it slowing down. It seems to be continuing to grow pretty solidly. There is divergence around the world. So it's led by U.S. strength, but still expecting there to be more convergence going forward. So I actually think that our outlook is still quite optimistic on the global economy. Not to say, to Jamie's point, that there aren't some risks out there.

And also, just to talk about monetary policy for a second, everything – given that growth outlook is really sort of lining up for a December rate hike and for more hikes into 2019 and the continuation hopefully of a steeper yield curve and that all should be constructive for bank stocks.

It is definitely the case that as we've been talking about for years now, as the Fed is shrinking its balance sheet and liquidity is coming out of the system, yes, we are seeing deposit growth slow and there's a natural feedback loop as you reprice liabilities, you'll have a natural asset-based response. And so, you might have slower growth on the asset side relative to the past, but it should be at higher spreads and that should be how it plays out. So there's really no change, I don't think, in our expectation of the drivers.

<Q - Erika Najarian>: That's helpful. And just as a follow-up. I picked up in part of your response to an earlier question, Marianne, as we think about your Wholesale loan trends y-over-y, which continue to outpace the banking industry, could you tell us a little bit more about the dynamics in terms of competition from non-banks, particularly in private middle-market lending?

And I guess we're really wondering what you're observing in terms of competition more on structure rather than rate and whether or not some of the liquidity that you noted could be drained out of the system would change those competitive dynamics near term. And sort of what is JPMorgan's indirect exposure that remains on balance sheet on the sponsor-backed transactions? Sorry, I know that's a lot.

<A - Marianne Lake>: Yes. I'll try to remember all that. First of all, I would just clarify that when you say Wholesale loan growth has been outpacing the industry, I would say that from my recollection over the course of the last several quarters, we've basically been saying in line with, if not, maybe even slightly less than in line with the industry. But it is nuanced. You need to get beneath it.

There are areas where we would fully expect to be growing more strongly than the industry and those are in our newer expansion markets where we've been investing. We're reaping the benefits of those investments and we're going from a smaller base and deepening into the market.

In our core markets, the mature markets, in line to maybe not even quite as we are being cautious given where we are in the cycle. So I just want to clarify that.

<A - Jamie Dimon>: We haven't changed our standards.

<A - Marianne Lake>: We haven't materially changed our underwriting standards, no. And if anything, I would say we're just being cautious of the margin. And with respect to competition outside of banks, it's definitely true that non-banks are gaining share. And it's also true that they are structure-wise going to be willing to do and are willing to do things that we are not. And so, for our best clients, we aren't largely going to lose on price. We would be willing to work on price, but we would walk away on structure.

<A - Jamie Dimon>: And we don't have a lot of residual exposure to sponsors who are doing that kind of lending.

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

<A - Jamie Dimon>: Right.

<Q - Mike Mayo>: So Marianne, look, I mean ROTCE is 17%. You seem to have some deposit market share gains, but y-over-y for Q3, expenses were up more than revenues. So can you highlight the dollar amount of investment spending and how that's changed and where you are in that progression?

<A - Marianne Lake>: Yeah. Actually, just before we get into expense, for a second, if you step back, just a couple of things. I wouldn't look at any one quarter when I'm thinking about like operating leverage, not to overplay seasonality or anything else, but I would look at the whole year.

And tax reform's an important part of that. So if you look at YTD on a reported basis rather than a managed basis, y-over-y, YTD, we have about 200BPS of positive leverage. So tax reform is a big factor.

And then obviously, we have some private equity losses, which are episodic in this quarter's revenue print. So I think that there's strong growth across the businesses. The expense number and investments, our expenses are up over $1B year-on-year, outside of FDIC and revenue-related costs, in line with the guidance we gave at Investor Day.

So think about that sort of $2.7B of y-over-y investment and we're working through it. So we're on track. It's different from revenues insofar as, it's more linear, and so expenses are in line and leverage is – positive leverage is, I think, pretty strong.

<Q - Mike Mayo>: All right. And just one separate question for you, Jamie. Your CEO letter highlights the expectation that interest rates would go a lot higher. So I guess, we're along the track that you laid out, but doesn't seem like the market's digesting it maybe as well as you might have thought the market would digest. So basically what you expected, so what's different between your expectations and how the recent market's been reacting?

<A - Jamie Dimon>: Well, I think I noted that the market may not take it that well if rates go up, because it'll surprise people, but then people shouldn't be surprised. And of course, so many things have changed since we've been through this before like monetary policy, liquidity ratios, capital ratios, et cetera.

So I was also pointing out that - just about probabilities that rates can go higher. People should be prepared for that. They should not be surprised about it. So I'm always surprised when people are surprised. And the why is more important. Are you still growing? The economy is strong. Rates are going up. Most of us consider it a healthy normalization and going back to more of a free market when it comes to asset pricing and interest rates, et cetera. And we need that.

So to me, overall, it's a good thing, particularly because the economy is strong. And so I do expect rates will continue to go up. We don't bet the company on that. That's just my own expectation. I'd put much higher odds at it being at 4% than most other people. But again, the economy is strong. So as long as it's a normalized and strong economy, it's a good thing.

And the economy could be strong for a while. I mean, Marianne pointed out wages are going up. Participation's going up. Credit that's been written is pristine. Housing's in short supply. Confidence, both small business, consumers is extraordinarily high. And that could drive a lot of growth for a while in spite of some of the headwinds out there.

<A - Marianne Lake>: I also think – I mean not exactly, but if you went back and looked a couple of years ago what the 2-year forward, 10-year rate would look like, it would look much like this. And so it's just that it's been – because the curve was having a hard time pushing up that people are now focused on it, but this is what we would've expected, should expect and higher.

<Q - James Mitchell>: Maybe just a quick question on deposits. We're starting to see some slowing of growth, if not outflows in some areas as rates rise, but you guys still have a loan-to-deposit ratio that's in sort of the mid-60s and you've been gaining share on the Retail side. What's your sense of, I guess, competition for deposit and pricing, particularly in the core Retail Bank?

<A - Marianne Lake>: Yeah. So when we think about this as we...

<Q - James Mitchell>: Yeah.

<A - Marianne Lake>: Well, it's not really about competition particularly. When we think about the deposit base and the Retail/Consumer relationship, deposit and rate paid is a important part of it, but it's increasingly less important, not that it's not significant. And so, when you think about the value that we give to our customers, it's not just that, but it's also all of the customer experience initiatives that we've had. It's about convenience. It's about digital/mobile capabilities. It's about launching new products, new services, simplifying the environment for them. So, there's a lot of different investments and things to play, which might make this kind of normalization cycle look a little different.

And so, the way we think about it is we look carefully across the spectrum of deposits, Retail and Wholesale, at what we are seeing in terms of flows and balances and elasticity for our customers on our balance sheet. And that's how we think about our strategy for deposit reprice and it's, sort of, largely behaving as we would have expected.

<A - Jamie Dimon>: Can I just make a macro point too. As the Fed reduces balance sheet, just say by $1 trillion over the next 18 months or whatever, which is what they indicate they're going to do, that's $1 trillion out of deposits. That will have an effect, kind of macro competition and stuff like that. And we try to estimate the big point is it coming out of Wholesale here, you're coming out of Retail, and it's kind of hard to know. But that will change the competition a little bit for deposits.

<Q - James Mitchell>: Okay. Fair enough. And maybe a follow-up on that investment spend. I mean, obviously, it went up with the tax cut helping to accelerate some investments. Do we think of it, going forward, stabilizing at these high levels? Or is this sort of a one-off sort of increase and we might see that come down, or do we keep increasing?

How do we think about the investment spend needs going forward a little further out?

<A - Marianne Lake>: Yeah. So I would say – and first of all, obviously, we'll give you more thoughts on forward-looking guidance today. But just generically, I wouldn't really put tax reform as being a primary reason for what we're doing on the investments. I would say that we have identified the opportunity to accelerate capabilities that are consistent with our clients' strategic long-term goals. And so we've been leaning into that this year.

And so it was a pretty sizable step-up this year. Acknowledging that, we wouldn't necessarily expect to see that continue. But we're going to carry on investing in technology, adding bankers, opening branches, launching new products, so that we're sort of defending the long-term growth and profitability of the company.

And in the absence of giving you guidance, I would just point you to the fact that we're still targeting – not targeting, but we're still expecting an overhead ratio to be around about the mid-50s over the medium term, which on revenue growth implies we'll continue to invest and there's also volume-related costs associated with that.

<Q - John Eamon McDonald>: I was wondering on the regulatory front, do you have any visibility yet into the future interaction of CCAR process with the new loan-loss accounting rules, CECL, particularly in the context of the Stress Capital Buffer potentially being implemented? Because it seems like we could have some overlapping procyclicality and then the potential to freeze that into the run rate capital. So I'm just kind of wondering, is there any visibility yet on that and is that a big area of uncertainty for you?

<A - Marianne Lake>: So you hit the nail on the head with both your question and what that could imply. It is a big area of uncertainty. We do not have clarity on capital broadly, as it relates to CECL, including whether there will be permanent capital release and/or how that will play into CCAR. It is one of the most open questions we have. So right now, what we know is as far as I know anyway that we don't have to put the CECL impact in until CCAR 2020. So it's not a sort of imminent question, but it's an important one and we don't know the answer.

<A - Jamie Dimon>: It seems to me that every single time there's a chance to make things more procyclical or less, we make it more procyclical.

<A - Marianne Lake>: That's a danger for sure. So we would encourage the dialogue on clarifying capital treatment writ large to be at the forefront of standard-setters' minds and regulator minds.

<A - Jamie Dimon>: But it also won't change our strategy. That's just accounting.

<Q - John Eamon McDonald>: Got it. And then just as a follow-up, I was wondering how rising rates are affecting competition and capacity in the mortgage business and whether the regulations in mortgage have made you open to reconsidering getting back into some areas that you exited after the crisis?

<A - Marianne Lake>: Well, yes. So mortgage being a cyclical business as it is, we are on higher rates expecting the overall market to be down about 10% year-on-year. We are down in line maybe even a little more than that, but for us, it's a tale of two channels. We are flat year-on-year in the Consumer channel. So, decent consumer engagement and purchase market share and we're down meaningfully in Correspondent because we are pricing for the risk and higher rates. With respect to would we be willing to reconsider our position on mortgage, the narrative, the dialogue is constructive, but there hasn't actually been any resolution to the bigger challenges. So if we can get that resolution, then I think the answer would be largely, yes. Jamie?

<A - Jamie Dimon>: Yes. I would say the mortgage; the mortgage company is earning money. It's doing quite well.

<A - Marianne Lake>: Yes.

<A - Jamie Dimon>: Delinquencies are way down, we're competitive. We started Chase – what's it called?

<A - Marianne Lake>: Chase myHome.

<A - Jamie Dimon>: Chase myHome, so you can digitally track your mortgage process and there's a lot of good stuff coming. And so – and the big picture is pretty good. Obviously, refis and new home sales will probably be down because of rates a little bit.

<A - Marianne Lake>: Right. And you're right, there's excess capacity in the market right now and that will clear – it will clear itself out over the course of the coming months and we're in this for relationships, not volumes. And margins are under pressure as a result, but they will stabilize.

<A - Jamie Dimon>: And that is an area, by the way, where all the riskier lending has gone to the non-banks pretty much.

<Q - Alevizos Alevizakos>: I would like to ask a question on the CIB. Especially, I would like to focus more about the outlook that you gave that the spreads are getting tighter. And I would like to know regarding the credit and securitization business where we've seen issuance being quite slow during the summer and then continuing like that in September. Do you see that there is a risk-off mode in the market? And how would you believe that the revenues would actually move going in Q4 and then in the new year? Do you think that generally fixed income wallet would actually be going down? Thank you.

<A - Marianne Lake>: A risk-off what, sorry?

<Q - Alevizos Alevizakos>: The what – sorry?

<A - Marianne Lake>: No, no. Okay. So...

<A - Jamie Dimon>: The risk that wallet would go down.

<A - Marianne Lake>: Yes. So I would just say on the margin point, it's been the case that for, particularly in the sort of more liquid space, you've seen margins coming down consistently over the years. And we've – so it's not necessarily that this is some sort of step change or a new phenomenon, but it's competitive and so that's what we're seeing. On the SPG side, pipelines aren't strong at this point. So we expect Q4 to feel much like the third.

<A - Jamie Dimon>: Maybe I'd just make a long-term point here too. In the next 20 years or so, the total fixed income markets around the world are going to double. And that is just an important thing to keep back in mind, so when you run the business, you're running the business to capture your share of that doubling. But, of course, margins over time will come down and the way you do it will be transformed by electronics, et cetera, but it's a pretty good future outlook.

<Q - Ken Usdin>: Marianne, on the Consumer credit side, I should say, you made the point about Card losses remaining low and towards the low end of what you had thought for the year. I also noticed that you also added to the Card reserve and noted higher losses. So, can you just give us the to and fro about just what you're seeing in the underlying on Card and losses and trajectories? Thanks.

<A - Marianne Lake>: Sure. Okay. So as you know, we've been talking for a couple of years now about the fact that we did some targeted credit expansion in the Card space a few years back. And naturally, as that seasons, and our risk-adjusted returns are healthy, but underwriting loans at higher loss rates, which means as that seasons that the overall portfolio loss rate will naturally increase.

So, the higher the percentage of newer vintages are, the higher the loss rate will be in accordance with our underwriting standards, and that's good risk-adjusted return. So, that's something we've been tracking and guiding to and expecting.

The build this quarter was more about loan growth than it was about the seasoning of the charge-off rate, but it was a bit of both. My comment about the performance though is if we had looked at the 2018 Card loss rate, as we did at the beginning of the year, we said we would have expected it to be closer to 3.25%. But there are three things driving it to be slightly better.

The first is the pre-expansion vintages are holding up very well. So, the sort of pre-2015 vintages continue to hold up very well. The second is that as we have continued to observe the newer vintages, we've been rigorous in terms of, at the margin, doing risk pullbacks and ensuring we're managing the performance really well. And the third is that we've been improving our collection strategy. So a combination of factors have allowed us to deliver apples-to-apples a charge-off rate for the portfolio that's a little better than we would've expected coming into the year.

<Q - Ken Usdin>: Yeah. Great color. Thank you. Can I...

<A - Jamie Dimon>: Still perceived better than through the cycle number.

<A - Marianne Lake>: Yes.

<A - Jamie Dimon>: So you should explain that to him too.

<A - Marianne Lake>: Yeah. And obviously, in this portfolio, as we go through the cycle, we would expect charge-off rates to continue to rise and that's one of the reasons why I emphasize that the pre-expansion vintages continue to be that kind of – you'll remember we hit that 2.5% charge-off rate, which is extraordinarily low for this kind of portfolio. And we're still there for those pre-expansion vintages. So naturally as the cycle matures, we will see that rise, but we aren't seeing it yet.

<Q - Ken Usdin>: Yeah. Makes sense. And can I ask you just on the other side, can you talk a little bit of Auto in the same context too, where the losses have been flat as a pancake? Can you talk about that? And also just that leasing side of the book, which we more see in the other income? Are you still seeing the same potential for growth in both the on-balance sheet and the leases?

<A - Marianne Lake>: Okay. So on the loan side in Auto, I would say that we have – we are losing share as we see competition from credit unions and captives that may have economic frameworks that are different from ours. We are not going to chase volume. We're going to get the appropriate returns for the risk.

So, our credit reflects our discipline on pricing and underwriting standards. And so it is continuing to be flat to a little better. On the leasing side, we do leasing with our manufacturing partners. We are seeing very strong growth. We're very careful about how we think about residual risks and reserving on that portfolio, but it's very high-quality growth, and that looks set to continue.

<Q - Saul Martinez>: Just wanted to follow up on the question on operating leverage. How should we think about the outlook for positive operating leverage, which is more philosophically because your efficiency ratio is currently not materially above the 55% through the cycle expectation? So I mean, should we be thinking of positive operating leverage as part of the investment narrative? Or is the goal really to invest in favourable business outcomes, operating leverage does what it does and really doesn't drive business decision?

<A - Marianne Lake>: Yes, more the latter than the former. So obviously, we have a view of what we think the right return profile for these businesses should look like. And we're investing to deliver those returns through the cycle and over the long term. So we don't have an operating leverage target in mind when we set our investment strategy, nor do we, for that matter, have an expense target in mind either. So again, we saw a reasonable step up year-on-year this year because we saw the opportunity to do that well. I wouldn't necessarily expect to see that kind of growth. But again, operating leverage is more of an outcome, not entirely, but more of an outcome than an input.

<A - Jamie Dimon>: And mix.

<A - Marianne Lake>: Yes, and mix.

<Q - Saul Martinez>: Got it. Okay. Fair enough. And then if I could just ask a quick follow-up on CECL, I know you don't manage the accounting outcomes and I think, Marianne, you mentioned a number of areas last quarter where CECL could have an impact. But any update just on CECL preparations and when you think you might have an estimate of what the effects could be?

<A - Marianne Lake>: Yes. So I appreciate that you guys have been asking about this now for a while and I hate to tell you that the modeling, the data, the methodologies are complicated. So operationally, we are working through that across all of our businesses. We continue to expect to be running in parallel through some parts of 2019 across some of our portfolio so that we can make sure that we fully understand the potential implications.

We don't have a number for you, but I will tell you this, and same as I said I think last time, the biggest driver is likely to be Card because of the size of the portfolio and the 12 months incurred loss model today. So the weighted average life of the portfolio driven by revolvers would be longer than that most likely.

There'll be some other impacts, pluses and minuses. Research reports have been written. They, I think, on average for those that have been written have suggested that not just for us, but across others that the reserve increase could be 20% to 30%. And while I don't have a number for you, it's not implausible.

<Q - Matthew O'Connor>: I want to follow up on the discussion about increased competition in FICC and just the language in the release kind of implied there was some increase in competition. Your comments on the call here kind of says been competitive for some time, and I guess I was just trying to square the two. And I would just add, coming to this year, you had the number one FICC share and incredibly, you've been the biggest FICC share gainer I think YTD when we look on a global basis. So you've been building on top of that share. And I'm just trying to gauge if there's been kind of a change among competition trying to get some of that share back and maybe if that's just started to accelerate.

<A - Marianne Lake>: Yes. I mean I think if you go back a number and number of years when we were all having those like deeper meaningful debates about whether we should be changing our sort of FICC operating model and we were committed to the sort of full spectrum complete platform, you roll forward to 2016, there was outperformance in Fixed Income and people had made changes to their operating model and operations and the competition came back pretty fiercely, I would say, into 2017.

And then in 2017, the market didn't play nicely, particularly the volatility and volumes were less robust than they had been in 2016. But we haven't seen the competition let up. So people are back and wanting to enjoy – Jamie just talked about it, the Fixed Income wallet will double and pretty much everyone everywhere wants to enjoy some of that.

And so the competition – it's a combination of it's been very competitive for a while and it continues to be so. So I don't think it's a step change, but it does obviously feel, particularly when volatility has been reasonably contained outside of specific Emerging Market kind of areas, that everybody is competing for these same margins.

<Q - Matthew O'Connor>: And then just broadly speaking, I mean if we look at both FICC and equity trading, obviously, you've had the leadership position in FICC. You've been gaining a lot of share in equity including this year. And what do you think the biggest driver of that is? Like it doesn't feel like it's the capital or liquidity advantage? Is it all the technology spend that you've been doing? What are some of the reasons you had just chalked it up to high level?

<A - Marianne Lake>: Yes. So I mean, if you think about we're sort of gaining share most notably in cash and prime. And if you go back a number of years ago, we were pretty open and honest about the fact that we weren't where we needed to be in either of those two scenarios and we have been consistently investing in the platform.

And it is technology, think about prime with – building out of the prime platform, particularly internationally has been a game changer and we had a best-in-class competitive offering over the course of the last couple of years. And now we're getting the momentum of being able to deliver that to clients. And similarly we've been investing in the cash side. So it's across the complex, but we're getting the benefits of the investments we've been making.

I also think that the sort of relationship effect of having our Equities business with our Private Bank and with the Commercial Bank, the sort of feedback loop is also quite powerful. So it is a little bit to do with our operating model, our platform as a company.

<A - Jamie Dimon>: And really great research.

<A - Marianne Lake>: Yes, great research.

<Q - Brian Kleinhanzl>: Yes. I had a quick follow-up question on the Securities Services. You mentioned that there was a decline sequentially based on seasonality and the exit of the business. But is there any way to size that to kind of get to what the underlying growth trends were in that segment?

<A - Marianne Lake>: Yes. I mean – so from an underlying growth trend perspective, I would look y-over-y rather than sequentially. I sort of point out the sequential point because of seasonality, we also exited U.S. broker-dealer business, so that obviously has an impact.

It is also the case, so if you think about the year-on-year growth of 5%, we had been growing more than that, led by very strong growth in NII. For this business, this is a Wholesale business where deposit bases are high. So we would expect that growth to level off.

And in this quarter in particular, just the specifics of our internal transfer pricing is that LIBOR/OIS narrowed and it just had an impact. Y-over-y, continue to expect us to grow asset, asset-based fees, NII solidly, but not as strongly, and transactions. So I don't know whether it's going to be high-single digits or mid-single digits growth year-on-year.

<Q - Brian Kleinhanzl>: Okay. Thanks. And then just one separate question on the non-interest-bearing deposits, I mean, it came down, I think a quarter. Was that mostly just on the Corporate side, or was there also some pickup in the deposit gammas on the Retail side as well?

<A - Marianne Lake>: Yeah. Not on the Retail side, not yet. I mean there's not a sufficiently compelling rate differential to be driving intra-product migration on the Retail side yet, but we are seeing it on the Wholesale side.

<Q - Gerard Cassidy>: I apologize if you've already addressed this, but can you give us the outlook for the pipeline for Commercial loan growth or Commercial loans and Investment Banking? And I know, it's very early in the quarter, but with the trading volatility we've seen, any color that you can share with us on that as well.

<A - Marianne Lake>: Okay. So Commercial loans, we're 4% up year-on-year, flat to 1% up sequentially. At this point, as we look forward over the near term, it feels like that kind of steady growth, GDP plus GDP is what we're going to get. And remember, everybody has a different mix. But one of the things that happened quickly with tax reform is that the sort of government healthcare, hospital not-for-profit space was less compelling from a loan sense and now they'll be more compelling in the capital markets. So we're seeing that impact our growth down. So I would say that kind of not quite mid-single-digit growth feels like a decent outlook, all other things being equal.

In terms of the capital markets, well, I would say that Q3 pipelines coming out into fourth quarter and momentum sets us up for a decent fourth quarter, honestly, across products. Clearly, volatility, depending upon how long it stays around and what the drivers are can impact business confidence. We're not necessarily expecting that. So I would still say the outlook across products is good with ECM obviously being the one that would be most likely impacted. But even there, I think it might be more of a sort of temporary set of porters or people see how everything is digested.

And honestly, on Markets, no good ever comes of trying to predict what a quarter will look like after a couple of weeks. And volatility is not necessarily a bad thing. It can be constructive in some ways and less in others. So yeah, there's no good coming of a prediction at this point. I will say one thing about Markets, just to give you guys a tiny view, which I know you know. But just because of tax reform and another one-off item in Q4, flat year-on-year comparably would be up.

<Q - Gerard Cassidy>: Very good. I appreciate that. The second question is when we look at the weekly H8 data on Friday's, the smaller banks in this country are growing their loan books much faster than the larger banks. You obviously had good loan growth this quarter, but it doesn't match up to what the smaller banks are producing. So the question is what impact do you think the CCAR process has had on you when you compare your underwriting pre-financial crisis? I know you're not changing your underwriting standards. But do you think the larger banks are more conservative as a general statement? And it's reflected in these very strong credit quality numbers you and your peers are posting today.

<A - Marianne Lake>: I mean, so – it's difficult to generalize. And obviously, everybody has a sort of different risk appetite. It might be fine, if you're getting properly paid, to grow more quickly. We are sticking with our guns in terms of our underwriting and risk appetite on credit.

The other thing I think you have to bear in mind; and again, it depends on the particular situation of any competitor is that we are materially and increasingly bound by standardized risk-weighted assets. And so, while we don't overthink that and we do honestly think about economic capital, at some level, we have to generate a positive return for shareholders and shareholder value and it's on these very high-credit quality loans that we're producing, it's expensive.

<Q - Marty Mosby>: I wanted to take a little bit different slant on deposit betas. Just kind of ask a three-part question. One, is the increase in deposit betas that we've seen over the last couple of Fed moves surprising at all or abnormal, in your opinion, to normal historical trends?

<A - Marianne Lake>: Okay. So I would say, if you look at the first four hikes, it was relatively muted deposit reprice across the context. It accelerated for the last three hikes. I'm excluding September, given, obviously when it happened.

So, we are seeing an acceleration in betas. And it started at the top end of Wholesale and it will migrate through the complex over time. I would say it's in line to arguably better than we would have modeled. But remember that this cycle did start at a very different place.

So while, if we looked at history, we might have been repriced in totality having been higher at this point, we started at 100BPS of rate not 25. So I think that that plays into it too. So generally, in line with expectations is what I would say.

<Q - Marty Mosby>: Okay. That's what I would say. So let's go to the next questions. Given the rates have been low for so long, going up until we started increasing rates, we've repriced almost every security and loan we had on the books. So the actual upward potential to reprice portfolio yields to current market rates has got to be larger than what we would typically have seen historically. Do you agree or disagree with that idea?

<A - Marianne Lake>: I would say, yes. Obviously, it depends on how you position the company over that period. But we talked about it before, we were and have consistently been relatively short of the market. We've been keeping dry powder, so we could invest as the long end of rates goes up and we still are looking at that. But obviously, there's complexity in the portfolio too. So we're paying attention to that. Yes I agree.

<Q - Marty Mosby>: Yes. So the stretch between just portfolio yields, so asset yields can actually reprice faster than what we've seen historically. So the combination of those two things, in our estimation, gives us a threshold. So if we solve backwards for deposit betas, it gives us a threshold, if we estimate for JPMorgan, of somewhere between 80% to 90% deposit betas before you actually kind of break through and start eroding net interest margin. Currently you had about a 40% deposit beta this quarter. So you have a lot of headroom still to go before margins start to really erode given deposit pricing. So just wanted to kind of get a feel for that estimate of 80% to 90% given where you're at today.

<A - Marianne Lake>: Okay. So obviously, I don't know exactly your sort of mental model, but let me tell you this. I think you're right. I don't know about the 80% to 90% specifically, but you're right about net interest margin, if you look through any short-term noise. So we would expect the trend for our Firmwide and Core NIM to trend or grind higher over time, but it does depend on the path and pace of reprice.

So if we continue to see deposit betas stay low or lower than potentially a linear kind of move, you'll see margins increase. And then as they accelerate back to target, you might even see it compressed. But if you see through that over the long run, yes, net interest margins will be higher, and that will be driven mainly by balance sheet growth mix and long end of rates.

At Investor Day, you might remember we told you that beyond 2018, net-net, there was little rate left to go and it was going to be more about balance sheet mix and growth and long end of rates a little compounding. But the path does matter. So you can see Core NIM in particular will be very vulnerable to the pace of reprice. Why would you look through that? Sorry, operator.