

## Equity Research

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Rating Change — January 14, 2022

## Large-Cap Banks

## J.P. Morgan Chase &amp; Co. (JPM)

## JPM: Downgrade Rating and Lower Ests. Due to Expenses Post 4Q21

## Our Call

We downgrade our rating from Overweight to Equal Weight, our ests. by about 15% for each 2022-2025, and our price target from \$210 to \$180 (~15x 2023E EPS roughly in line with 20-yr avg). This issue is certain to us: front-loaded spending for less certain back-ended benefits. JPM continues to reflect our "Goliath is Winning" theme, but the cost and time frame for doing so is greater and longer than expected. Indeed, there was zero assurance that this historic increase in expenses will level off after this year. Moreover, we believe JPM is more expensive than the average bank at a time when other banks are more pure plays on our 2022 theme, "NII to the Sky". We continue to favor the banks featured in our new report, "[2022 Outlook: Stay Aboard the Bank Train](#)."

**Expenses are the issue.** To us, JPM is spending the benefits of rate increases, which should keep its ROTCE below its target of 17% for the next few years. JPM guides for 8% higher expenses in 2022 due to inflation/comp/T&E normalization (40%) and deliberate increases in investments (60%), implying a second year in a row of negative operating leverage. While JPM indicated that it intended to gain market share in each business, it gave few other concrete metrics around future expectations even though investments (targeted \$15bn in 2022) are set to increase by 30% YoY and by 57% since 2019.

**Big reduction to estimates given company-specific moves.** The degree of downside to our estimates is a surprise to us after reviewing our earnings model. We est. ROTCE declining to 15% and not getting to 17% over the next 3 years due to higher expenses, lower fee revenue in CIB and Consumer, and less buybacks; that's even while the company should show the best NII growth in its history (guided 12% higher core in 2022). The decline in our PT follows our est. revision downward.

We don't see how the math works otherwise with the increase in expenses this year, especially since JPM gave no assurance that expenses would not continue to increase after 2022. Specifically, JPM is projecting expenses to increase \$6bn while core NII is projected to increase \$5bn and the company is coming off record revenue in CIB. Net-net, we est. 2022E revenue to be up 1% while expenses are up 8% (core). As a result, we lower our estimates for 2022 to \$11.25 (from \$12.65), 2023 to \$12.30 (from \$14.35), 2024 to \$14.00 (from \$16.25), and 2025 to \$15.50 (from \$18.05).

Good long-term company, but perhaps too long of a horizon for bank stock investors, especially without more detail. This is not to say the wheels are coming off. On the contrary, JPM continues to gain market share along with progress, like the industry, in NII, loans, and mergers. Indeed, a mid-teens ROTCE is still decent. Nonetheless, at a time when most banks should show improving pre-tax profit margins, JPM is likely to go in the opposite direction over the next 1-2 years. In the end, we feel that the burden is on JPM to give more specifics about its expected benefits since they are incurring certain expenses for uncertain benefits.

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Rating/Prior	Equal Weight/Overweight
<b>Ticker</b>	<b>JPM</b>
<b>Price Target/Prior:</b>	<b>\$180.00/\$210.00</b>
<b>Upside/(Downside) to Target</b>	<b>7.0%</b>
<b>Price (01/13/2022)</b>	<b>\$168.23</b>
52 Week Range	\$127.35 - 172.96
Shares Outstanding	2,955,266,061
Market Cap (MM)	\$497,164
Enterprise Value (MM)	\$798,169
Average Daily Volume	11,296,218
Average Daily Value (MM)	\$1,900
Dividend (NTM)	\$4.20
Dividend Yield	2.5%
Net Debt (MM) - last reported	\$301,005
ROIC - Current year est.	12%
3 Yr EPS CAGR from current year (unless otherwise noted)	(3)%

\$	2021A	2022E	2022E	2023E	2023E
EPS		Curr.	Prior	Curr.	Prior
Q1 (Mar)	4.50 A	3.00 E	3.25E	3.04 E	3.52E
Q2 (Jun)	3.78 A	2.81 E	3.14E	3.04 E	3.55E
Q3 (Sep)	3.74 A	2.73 E	3.12E	3.08 E	3.60E
Q4 (Dec)	3.33 A	2.71 E	3.15E	3.14 E	3.68E
FY	15.36 A	11.25 E	12.65E	12.30 E	14.35E
P/E	11.0x	15.0x		13.7x	

Source: Company Data, Wells Fargo Securities estimates, and Refinitiv.  
NA = Not Available, Volatility = Historical trading volatility

All estimates/forecasts are as of 1/14/2022 unless otherwise stated. 1/14/2022 14:09:46EST. Please see page 5 for rating definitions, important disclosures and required analyst certifications.

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## Wells Fargo Express Takeaways

### Investment Thesis

JPMorgan Chase (rated Equal Weight) has excelled at both offense and defense over the past decade in which it has been gaining market share in all major business lines while optimizing its businesses, showing consistent earnings relative to other global banks and creating a fortress balance sheet (as defined by its CEO). Playing defense has carried more importance over the past few years; however, greater offense is expected to play a role as JPM continues to invest long term. This issue is certain to us: front-loaded spending in the near term for less certain back-ended benefits. JPM continues to reflect our “Goliath is Winning” theme, but the cost and time frame for doing so is greater and longer than expected. Moreover, JPM is more expensive than the average bank at a time when other banks are more pure plays on our 2022 theme (“NII to the Sky”).

### Upcoming Catalysts

JPM is not holding an investor day this year (the same as 2021) resulting in less interaction with the company and management than in pre-COVID years. Upcoming company-specific events include its 10-K release in February (incl. updated interest rate sensitivity information) and 1Q22 results in April. The Fed's FOMC meeting in March can act as a catalyst for the industry along with intra-meeting commentary by FOMC members and any change to the outlook for Fed Funds rate hikes.

### Risk v. Reward – Upside/Downside Scenarios

#### Base Case

We arrive at a price target of \$180, which implies 14.6x our 2023E EPS, based on the simple average of six valuation techniques (PE, price-to-book, discount dividend model, PEG ratio analysis and sum of the parts for both PE and PB). The 20-year forward PE for JPM has been 14x, and we assume a slightly higher level given its higher-quality balance sheet and earnings consistency overall.

Macro downside risk factors include a slowdown in global economic activity, greater-than-expected increases in unemployment and bankruptcies (in the US and abroad), and adverse changes in US and foreign laws and regulations. Company-specific downside risks include higher-than-projected credit losses (especially in credit cards and home equity but also other consumer areas and commercial lending), market and interest-rate risks (which can affect JPMorgan's businesses and portfolios in a variety of ways, especially MSRs and investment securities), and operational risks (primarily associated with regulatory compliance across the firm's domestic consumer and global wholesale businesses). Risks to the upside include higher rates with a steeper yield (helps traditional banking revenue), with no commensurate negative impact on capital markets activities (advisory, underwriting, trading) and a stronger than expected recovery (resulting in stronger than expected loan growth).

#### Upside Scenario

Risks to the upside include higher and steeper yield curve without adverse impacts on capital markets and trading. For example, if our NIM projection for JPM were 15bps higher than projected in 2022E and if capital markets in 2022 were at 2020 levels, we est. that our 2022E EPS would be 15% higher and our target would be up roughly the same (est. \$205).

#### Downside Scenario

Risks to the downside include a lower and flatter yield curve than projected, resulting in a flattish NIM (2022E vs. 2021), and if 2022E capital markets revenue were at 2019 levels, then we est. our 2022E EPS would 10% lower and our target would be down roughly the same (est. \$155).

## Financials

Exhibit 1 - JPMorgan Chase Summary Income Statement and Key Operating Metrics

Per share information (\$)	2020A	2021A	2022E	2023E	2024E	2025E	'21-'25 CAGR
EPS	8.88	15.36	11.25	12.30	14.00	15.50	0.2
Dividend per share	3.60	3.80	4.20	4.44	4.54	4.66	5.2
Book value	81.75	88.07	93.37	99.61	107.39	116.56	7.3
Tangible book value	66.11	71.53	76.25	81.87	89.04	97.60	8.1
Avg diluted shares O/S (MM)	3,087.4	3,026.9	2,920.5	2,820.2	2,725.8	2,637.5	(3.4)
EOP common shares O/S (MM)	3,049.4	2,944.1	2,844.5	2,745.6	2,653.8	2,567.8	(3.4)
Key operating metrics (%)	2020A	2021E	2022E	2023E	2024E	2025E	
Revenue growth	3.6	1.9	1.3	5.4	5.3	4.6	
Expense growth	1.8	7.0	7.4	2.8	2.2	3.1	
Core revenue growth	3.1	2.9	0.9	5.3	5.2	4.5	
Core expense growth	1.8	6.2	8.2	2.8	2.2	3.1	
Reported efficiency ratio	56.1	58.5	62.6	61.0	59.1	58.2	
Core efficiency ratio	54.6	56.3	60.4	59.0	57.2	56.5	
Net interest margin	1.98	1.64	1.72	1.84	1.91	1.93	
Net charge-off ratio	0.53	0.28	0.35	0.49	0.52	0.53	
Tier 1 common	13.1	13.0	12.7	12.6	12.6	12.7	
ROTCE	14.4	22.9	15.3	15.7	16.5	16.8	
ROA	0.91	1.30	0.91	0.94	1.00	1.04	
Income statement (US\$MM)	2020A	2021E	2022E	2023E	2024E	2025E	'20-'25 CAGR
Net interest income (FTE)	54,981	52,741	58,358	62,288	66,125	69,295	7.1
Fee revenues	67,153	72,908	68,465	71,307	74,451	77,659	1.6
Non-core revenues (incl. sec gains)	795	(345)	125	145	257	389	NM
Total revenues	122,929	125,304	126,948	133,741	140,833	147,343	4.1
Operating expenses	(66,656)	(71,343)	(76,603)	(78,777)	(80,471)	(82,980)	3.8
Non-core expenses	-	-	-	-	-	-	NM
Total expenses	(66,656)	(71,343)	(76,603)	(78,777)	(80,471)	(82,980)	3.8
Pre-provision net revenues	56,273	53,961	50,344	54,965	60,361	64,363	4.5
Net charge-offs	(5,324)	(2,945)	(3,848)	(5,698)	(6,338)	(6,752)	23.1
Reserve releases & other	(12,156)	12,201	(180)	(620)	(800)	(860)	NM
Net provisions	(17,480)	9,256	(4,028)	(6,318)	(7,138)	(7,612)	NM
Pretax net income	38,793	63,217	46,316	48,647	53,224	56,751	(2.7)
Taxes	(9,662)	(14,883)	(11,598)	(12,085)	(13,198)	(14,019)	(1.5)
Minority interest	-	-	-	-	-	-	NM
Net income	29,131	48,334	34,718	36,561	40,026	42,732	(3.0)
Preferred dividends & other	(1,721)	(1,831)	(1,860)	(1,860)	(1,860)	(1,860)	0.4
Net income available for common	27,410	46,503	32,858	34,701	38,166	40,872	(3.2)

Source: Company reports, Wells Fargo Securities LLC estimates

## Price Target Basis and Risk

### Price Target for JPM: \$180.00 from \$210.00

We arrive at a price target of \$180, which implies 14.6x our 2023E EPS, based on the simple average of six valuation techniques (PE, price-to-book, discount dividend model, PEG ratio analysis and sum of the parts for both PE and PB). The 20-year forward PE for JPM has been 14x, and we assume a slightly higher level given its higher-quality balance sheet and earnings consistency overall.

### Risk for JPM

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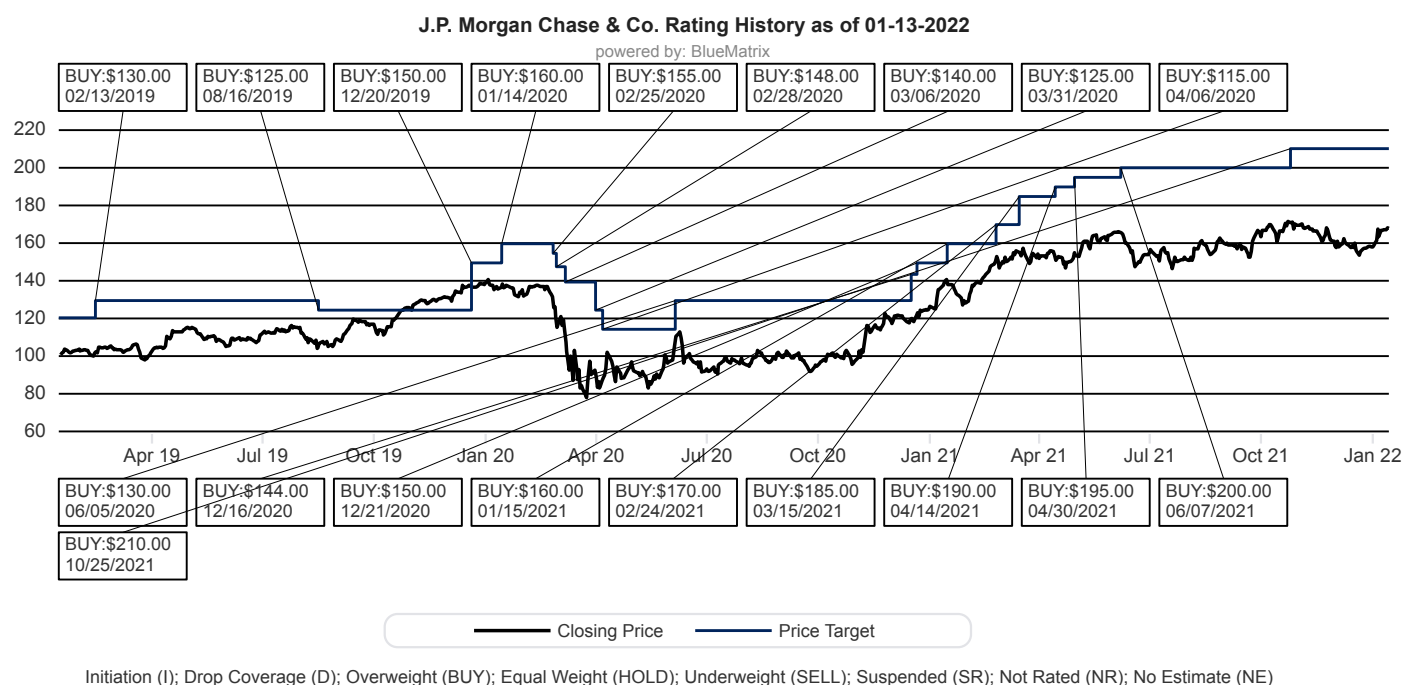
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