Deutsche Bank
Research

Rating
Buy

North America
United States

Financial
Banks

Company
JPMorgan Chase

Reuters	Bloomberg	Exchange	Ticker
JPM.N	JPM US	NYS	JPM

Date
13 October 2021

Forecast Change

Price at 12 Oct 2021 (USD)	165.36
Price Target (USD)	175.00
52-week range (USD)	170.22 - 96.54

What's $200b Worth? Estimate Changes and 3Q Recap Post Conf Call

Valuation & Risks

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2021/22 Estimate changes

Our 2021 estimate goes to $15.32 (from $14.89) and our 2022 estimate goes to $11.59 (from $11.67).

- The increase in our FY21 is largely due to the 3Q beat.
- The decrease in our FY22 isn't material... but reflects a few moving pieces including weaker card fees, slightly higher expenses, the impact of a $2b preferred issuance in 3Q and net II benefit from deployment of some cash into securities (period-end securities were $30b higher than the 3Q average).

Potential to deploy $200b of excess liquidity into securities over time

Recall that JPM has deployed less cash into securities than some banks, preferring to wait for higher rates. Period-end securities rose by $24b this qtr and mgmt signaled additional purchases were possible. However, a material increase in the securities book still seems unlikely with rates at current levels as JPM views the long term return as being too low.

That said, JPM has a ton of dry powder to add securities over time if rates rise and/or they change their view on rates. On today's call, we asked how much this could be if rates rise to a level that mgmt felt comfortable would generate a good long term return. JPM noted it could "easily" deploy $200b of cash into securities. *Note that upside from potentially deploying this $200b is in addition to the rate leverage JPM discloses in the 10Q.*

- This $200b compares to nearly $600b of excess deposit growth since 4Q19 (ie before COVID and related central bank actions).
  - We define excess deposit growth as the change in deposits (of $840b vs. a combined $244b increase in loans + securities). Recall that mgmt has previously acknowledged that some of the deposit growth over this period is noncore/less sticky as system liquidity is reduced over time/rates rise.

$200b of liquidity deployment can add nearly 20% to EPS with rates at 3%

Deutsche Bank Securities Inc.

It all depends on the level of rates and whether JPM would deploy the full $200b. But assuming they would, we can run some earnings sensitivities shown below.

- If 10 year Treasuries hit 2% and JPM were to deploy the full $200b into 30 year agency backed RMBS pass throughs (what big banks typically buy), this would boost net income by 11%.
- Each 100bp rise in base rates would increase this 5%...**so the $200b could be worth 16% if 10 year rates hit 3%,** RMBS spreads remain around current levels (of 50bps) and JPM deploys the full $200b. These are a lot of ifs, but this helps illustrate the potential earnings upside from deploying excess liquidity.
  - As noted in the prior section, the earnings leverage outlined just above from deploying excess liquidity is in addition to the rate leverage disclosed in JPM's 10Q. Recall that as of 6/30, a 100bp rise in rates would boost JPM's (2022) net income by 15%.

Other tidbits from the call

- Mgmt noted expenses would increase in 2022 vs. 2021, even though capital markets related revenue (and related comp) would likely be lower. This is higher than the flattish costs assumed in consensus for 2022 prior to today, but also not a huge surprise given expense pressure at JPM and across the banking industry. On the call, JPM noted the likely higher costs in 2022 reflected continued inflationary pressures and investment spend. We previously assumed flat costs and now assume a 1-2% rise.
- Mgmt acknowledged that FY22 net II guidance implied a $300m-plus increase in 4Q21 vs. 3Q. However, JPM cautioned not to run rate the implied $13.5b given seasonal boosts from markets/trading and one time benefits from PPP. Looking out to 1Q, there's also day count adjustments to make. This caused some market concern that consensus FY22 net II expectations (of $55.1b) may be too high.
  - However, we'd point out that mgmt was also upbeat about card growth in 2022 and as discussed above has already started to deploy some liquidity into securities.
  - Accounting for all this, our 1Q22 net II estimate is $13.1b and our FY22 estimate is $55.8b.
- Card fees: In the Consumer Bank, card fees were $651m in 3Q vs. $1.2b in 2Q. Mgmt noted on the call that the sequential decline was primarily due to higher marketing/acquisition costs and due to a $180m adjustment to rewards liabilities. The adjustment is considered a one time event while marketing costs are expected to continue and be slightly higher in 4Q.
- On loan growth, mgmt noted it has seen some recovery across lending products including the following:
  - For card, mgmt noted faster spend down of excess deposits for customers who are generally inclined to revolve and believe card outstandings should grow in 2022.
  - In home lending, mgmt expects portfolio additions to outpace prepayments in 4Q (similar to 3Q trends).
  - For C&I, mgmt noted that utilization rates had a little bit of an uptick among smaller corporates.
  - In CRE, mgmt noted robust origination pipelines and have removed any pandemic-related pullbacks in credit and expect to see a little bit of net loan growth going forward.
  - Mgmt also noted expected loan growth in markets but noted it's

not part of the core lending portfolio.

- FICC trading: In the earnings materials, it was noted that the current qtr included an adjustment to liquidity assumptions in the derivatives portfolio. Mgmt noted that while FICC declined 20% yoy (on a reported basis), ex the adjustment, FICC declined 15%. This implies about $235m.
- Mgmt noted 4Q IB fees would be up yoy, but likely lower than the robust 3Q level.

Quick recap of 3Q results below and see full note from earlier today

What Mattered Most in 3Q21 Results

EPS of $3.74 vs. consensus of $2.96. It was a strong quarter overall. The biggest drivers of the EPS beat were a large loan loss reserve release (and lower than expected charge-offs) and a tax credit. However, even ex these items, results were better than expected--with net interest income, fees and costs all better.

- Net interest income upside was driven by slightly better loans with 4Q to benefit from modest deployment of cash into securities later in the qtr.
- Outside of net II, EQ trading, IB fees, and asset mgmt revenues were all better than DBe.

Recent research

- State of the Banks (Remain Positive); Six Banks to Watch; 3Q Preview
- Cheat Sheets: Potential Catalysts/What To Focus On For Each Bank in 3Q
- US Banks: Notes From the Road: 60 Meetings in 120 Days
- 3Q21 Earnings Tear Sheets

Appendix 1

Important Disclosures

*Other information available upon request

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Company	Ticker	Recent price*	Disclosure
JPMorgan Chase	JPM.N	165.36 (USD) 12 Oct 2021	1, 2, 7, 8, 14, 15

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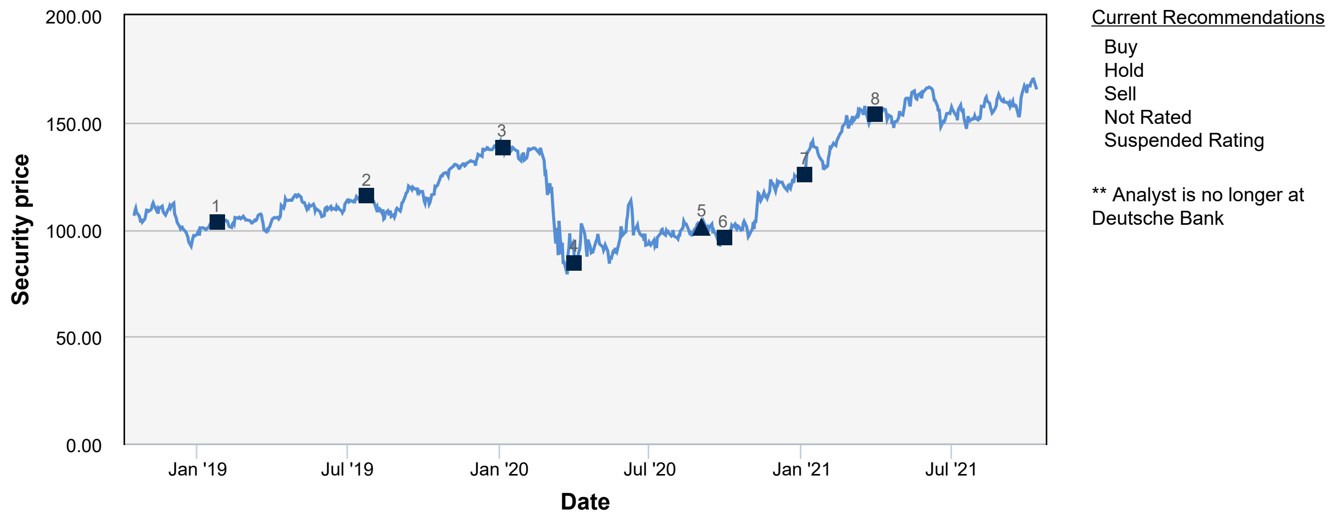
(as of 10/12/2021)



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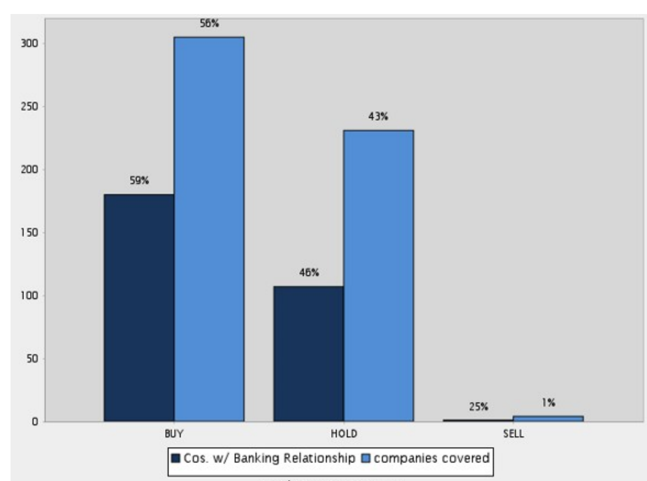

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