The University of Texas at Arlington

JP Morgan Chase

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I. INTRODUCTION

JP Morgan Chase (JPMC) is a combination of over 1,200 institutions, some of which date back to 1799. These include The Chemical Bank, The Bank of the Manhattan Company, and the Chase National Bank. These institutions have been influential in the formation of U.S. industries, in funding the construction of the erie canal, the Brooklyn Bridge, and the Statue of Liberty. Pursuing ambitious goals and taking calculated risks are the fundamental motivators of JP Morgan Chase, which led it to become the first billion-dollar company. Its early market entry has enabled it to gain much needed experience in a free market economy, enabling it to understand risk, consumer behavior, and consumer banking.

To this day JP Morgan Chase has remained an influential force in the finance industry with its dedication to be the best. The company is motivated by its commitment to its business principles of "exceptional client service", "operational excellence", "integrity, fairness, and responsibility", and "a great team and winning culture."

JPMC operates in consumer and community banking, corporate and investment banking, commercial banking, and asset and wealth management. Its wide range of product offerings make it one of the largest banks in the world, which requires a leader well versed in the field of financial products.

JPMC is led by James Dimon who serves as Chairman and CEO. He has held executive roles in Citigroup Inc., the Travelers Group, Commercial Credit Company and American Express Company. His experience in the financial industry made him a prime candidate to lead JPMC.

II. EXTERNAL ENVIRONMENT (O/T)

General Environment

With Britain's attempt to exit the European Union, severe stress would be placed on the global financial system. JPMC is a multinational company with a presence in Great Britain. The fallout from Brexit would place stress on the company, to mitigate this, the company has decided to expand its offices in Dublin, Frankfurt, and Luxembourg.

Political/Legal Environment

<u>US - President's Economic Report</u>

According to the Presidential Economic Report, the implicit government support created after the financial crisis of 2008 has undermined market discipline. The financial industry economic agenda of the Trump administration aims to reduce inefficiencies in regulatory practice, address systemic risk, and tailor regulations to banks.

The Trump administration believes that by eliminating redundant regulations, overlap, and fragmentation the finance industry will be better equipped to compete at the global scale. This policy is aimed at helping small financial companies, but also reduces the cost of regulatory compliance for banks.

The administration also plans to reduce inefficiencies by consolidating regulators that have similar missions and at the minimum increase coordination between them. This would allow the U.S. government to reduce the costs of enforcement, while removing confusion that result from contradictory regulations. By reducing the cost of compliance, banks would have the opportunity to use the extra funds for investment in other opportunities.

An unintended consequence of the Dodd-Frank Act is an overreliance on regulatory discipline, rather than on market discipline. Title II of the Dodd-Frank Act requires companies to consider bankruptcy as the first method to resolve failing institutions, and established an oversight committee to determine when a company needs Federal Reserve Supervision.

Removing these regulations or modifying them, will shift the responsibility back to the financial industry. The aim is to make banks more responsible for their actions, as they would be the ones managing the consequences.

Lastly, the Trump Administration aims to tailor regulations based on the size of the bank. This is a direct result of the Dodd-Frank Act which promoted "consolidation among small and mid sized banks."(Peirce, Robinson, and Stratmann 2014) By tailoring regulations small banks become more competitive, because the cost of compliance would drop. This is a threat large banks because smaller banks would find it easier to follow regulations, greatly reducing one of the incentives to being acquired.

<u>EU - Basel Committee</u>

The EU Basel Committee is a supervision framework for banks composed of three pillars:

Pillar 1
Capital

All banks must adhere to a quality and level of capital according to differing needs. There are methods of raising minimum common equity, having a capital conversion buffer, and a countercyclical buffer.

Additionally, the committee has a method for capital loss absorption at the point of a bank's non-viability. It allows bank's capital instruments to be written off which reduces moral hazard by allowing the private sector to contribute to resolving banking crises.

Risk Coverage

The committee also standardized credit risk, market risk, credit valuation adjustment risk, and operational risk. It also reduces over reliance on external ratings of securities.

Containing Leverage

Uses a non-risk based leverage ratio to include off-balance sheet exposures to help mitigate some of the issues with risk-based capital requirement.

Pillar 2
Risk Management and Supervision

Interest Rate Risk in the Banking Book (IRRBB) has guidance for baking management process.

Pillar 3
Market Discipline

Introduces metrics used by banks to help keep them accountable and disciplined

These three pillars of the Basel supervision reforms present challenges for international banks because it means that they have to follow many regulations, which increases adherence costs.

Economic Environment

After the 2008 financial crisis, large banks were heavily criticised for their role in causing the recession. The criticism resulted in international banking regulatory changes. The EU imposed more strict and overarching regulations, this increased the costs of compliance for large European banks. Additionally, the U.S. imposed their own set of regulations on American banks. This has resulted in a lack of competitiveness at the international scale. This provides an opportunity for banks in economies like Japan, China, and India to grow.

Demographics

A rising middle class in countries like China, India, and other developing nations presents an opportunity for traditional banks that offer credit based systems. Credit cards, loans, and mortgages are becoming more accepted in these societies. In China, traditionally people save up for an item and then buy it, but younger generations are becoming more accepting of alternative methods of buying goods. The demand for credit to buy large items such as cars, houses, and appliances will only increase as new generations gain working class status and begin making these large purchases. This presents an opportunity for growth for traditional banks.

Socio Cultural Environment

As disposable incomes increase across the world, with developing economies' increasing middle class, the amount of money that can be invested, saved, and spent will increase. This means that spending habits of these consumers will change drastically over the next decades, this presents a very lucrative opportunity for banks to capitalize on this change.

Technology

The digital age has resulted in increased competition from non-banks, for example Facebook, Inc. founded and is spearheading a project called Libra. Libra is an association with the goal of transforming the global economy by creating a new currency that is not governed by governments, instead this currency would be governed by corporate partners. The currency is based off of blockchain technology, but unlike Bitcoin it is backed by real assets.

This is a considerable threat to banks because Libra targets emerging economies that are opportunities for the company. The aim for Libra is to build "more inclusive financial options for the world." Libra wants to replace current monetary systems that are timely, costly, and inefficient.

In response to the problem of timely, costly, and inefficient transfers of money the banking industry came together to create Zelle. Zelle is a system that allows users to send money from peer to peer by simply inputting the recipient's email address or phone number. The banking industry offers this is as an alternative to bank transfers which are often costly and take a long time to process.

Additionally, Zelle competes against companies like Venmo and CashApp which perform similar functions to Zelle. Zelle is an opportunity to solve some of the inefficiencies that have led consumers to find alternatives to managing small cash transfers, for example Venmo and

CashApp. It is also an attempt by banks to catch up to the ever changing technological environment.

Porter's Five Forces Industry Environment (O/T)

Threat of Buyers - Low

The threat a single consumer closing a bank account is essentially non-existent. The impact of closing a bank account is dependent on the net worth of the client. Corporate clients and high net worth (HNW) clients tend to have a higher bargaining power when compared to smaller clients. To accomodate corporate and HNW clients banks offer personalized services such as Private Client services, that give HNW clients access to advisors and other similar services.

For smaller clients, banks create stickiness by encouraging clients to open new accounts, which increase switching costs. Some of the methods of creating stickiness include offering mobile payments and cash back opportunities to credit card holders.

Threat of Suppliers - Low

The supply system for a bank are depositors and employees. Suppliers also have relatively small individual bargaining power. HNW depositors and Corporate depositors have a relatively higher bargaining power.

To address the threat of employees, banks must provide attractive compensation plans to attract the best talent. Executive employees would be the only ones with individual bargaining power. Lower level employees can exert some pressure to raise wages depending on their level of expertise.

Threat of New Entry - High

Banks in developing economies, like China, are an increasing threat to international banks. Chinese banks have grown relatively unfettered due to Chinese government subsidies. As these banks grow, they will begin to enter international markets and becomes an even bigger threat to other deep seated international banks.

Fintech is a considerable threat to large banks, as the rise of Robinhood, Bull, and Acorns have threatened the investment sector. These companies have disrupted the business model of many of the large financial institutions by lowering commissions on trades to zero, and offering the purchase of micro shares.

Investment companies like Tencent and Softbank are also increasingly controlling large percentages of financial institutions that have the potential of being a threat to large banks. Tencent owns WeChat which allows users to hail taxis, make online purchases, text friends, and pay for items at brick and mortar stores without leaving one single app. With that much consumer data and power, if this app where to grow internationally it would affect the power of large financial consumers. Consumers in developing countries are increasingly using mobile devices to handle their finances and don't mind the idea of using one single app to handle all of their finances.

Threat of Rivalry - Moderate

American banks faces competition from multinational firms like HSBC and Barclays. HSBC has invested heavily in many developing markets, allowing it to compete and grow fast. HSBC and Barclays use product offerings to attract clients, this is a threat because the traditional tactics of offering bonuses and perks can be easily replicated by competitors.

Large international holding companies have the capital to disrupt traditional banking methods. These pose a significant threat to large banks because they have new competitors with competing banking technologies, that also aim at making consumers purchasing habits easier to track and easier to manage.

Threat of Substitutes - High

Technological innovation has enabled payment processing services like Square, Paypal, Venmo, and CashApp to substitute traditional bank services. These services often offer lower costs for processing similar products because they are specialized, which allows them to cut costs considerably.

Peer to peer lending has also risen considerably through the introduction of Propser.com and LendingClub.com. In response to these technological substitutes, large banks have introduced products like Chase Pay, and started divisions focused on small businesses.

Libra is a blockchain technology that aims to take banks out of the equation by creating a decentralized system to process transactions between peers. Other alternatives like Bitcoin have been a relatively low threat to banks because of the lack of adoption my major sponsors, the reason being the instability in the price of the currency. To remedy this, Libra is pegged to a currency backed by real assets. This creates confidence in the users of the currency and has convinced major companies to support the association. A threat to entry for Libra has been the lack of confidence in the system by governments, due to the absence of government regulation in the model. This has resulted in major regulatory roadblocks for the meantime, and allows large banks time to adapt.

Overview of All Opportunities and Threats

Large banks are facing threats from competitors at the international level, non-banks technological services, and changes in the political system. As developing economies' financial institutions enter the international market, they have the potential to create fierce competition for established banks which would require it to find innovative ways to remain competitive.

Technological advances have enabled non-banks to offer similar services at lower costs, faster, and more efficiently. This is a threat to the traditional banking business model. Lastly, Brexit is a threat to international large banks as their access to the Eurozone market would be cut off.

Some opportunities include potential changes in regulations that could reduce the cost of compliance. Additionally, the regulations enacted after the 2008 financial crisis have stifled growth in the banking sector, the removal and simplification of these regulations gives large banks an opportunity to better compete at the global scale.

Other technology based non-banks are facing increasing challenges from governments, as governments are comfortable with the traditional banking system. Technology based non-banks aimed at replacing monetary systems, like Libra, are a threat to governments due to the lack of oversight. This is an opportunity for banks to adapt and use technology to stay competitive.

III. INTERNAL ENVIRONMENT (S/W)

Internal Analysis

Core Competence

The core competencies of JPMC include its robustness, deep knowledge specialization, and power to enter new market sectors.

JPMC has grown to become a robust system due in large part to its history of mergers and acquisitions. With its large buying power the company can rapidly remove growing threats by acquiring smaller banks. This technique has allowed the company to grow without needing the massive capital investments required of greenfield investments for new market entry.

Additionally, the shared activities of the business has allowed it to increase efficiency by reducing redundancies.

The corporate and investment banking sector of JPMC benefits from a deep specialization in knowledge of markets. This builds confidence in its corporate partners that they will provide a superior service to other new entrants. Additionally, the bank is well invested in the Middle Eastern and Asian markets which provide it a competitive advantage over other late entrants.

Another way in which it has an advantage over smaller competitors is its access to capital funds to fund promising fintech and other projects. For example, in response to the zero commission trades of fintech investment companies, JPMC announced in 2018 that it would lower its commissions on the JP Morgan Markets platform to zero. Eventually, the commissions rates for margin, options, and other investment capabilities where lowered to zero. Another example is JPMC investment in the fintech industry.

In response to the rise of promising new technologies that have the potential to disrupt the current dominant players, JPMC announced investments in fintech through a program called Financial Solutions Lab. The aim of this lab is to foster fintechs that offer financial inclusion solutions.

Large banks have often served a wide range of customers, but often leave out a portion of customers that are considered too risky or don't have easy access to their services. Many fintech solutions aim to close this gap by giving access to banking to the poorest in society, and this has proven to be a lucrative approach.

The goal of JPMC "is to be the best financial services company in the world." As one of the largest banks, it's strategy of making mergers and acquisitions has worked out well. Whether it be entering a new international market or expanding locally, JPMC uses the capabilities of the companies it is acquiring to easily enter the new market. The relationships that the local management have built with the governments in which they operate allow JPMC to have an easier entry.

VRIN

One of the ways the JPMC stays ahead of the curve is by investing heavily in new finance technologies. By investing heavily in technology they are able to test out capabilities before other competitors enabling them to adapt, competitors on the other hand have a learning curve which JPMC can use to their advantage.

Old technology systems were developed with C++ and Excel, but as technology has progressed, development options have also changed. Companies can now make apps at a lower cost, that are more efficient, and allow for plug-ins. This system allows employees to test new features with A/B testing to measure efficiency improvements in real time. Integrated information technologies for online banking are valuable to JPMC, because it reduces development costs and increases efficiency.

Another factor that adds value to JPMC is its multinational organizational scale. The scale of the bank gives it an advantage because it is hard for smaller banks to compete against a bank of that scale. With its large scale it also has access to global markets, which is rare for many smaller banks.

The deep specialized knowledge of JPMC makes it imperfectly imitable. Its global presence provides the business access to market information which it can use to provide guidance to its customers, and offer superior service to competitors.

Lastly, the Chase brand it unsubstitutable. The brand has a legacy of over 200 years of working with government and corporations to fund large projects, as well as developing community relationships.

JPMC has a sustainable competitive advantage due to its strong integration between business units, its value, its deep specialized knowledge, and its large scale.

Business Level

The consumer and community banking sector benefits from its history of banking, technology pioneering, and mergers and acquisitions.

JPMC has a history of banking in America which has allowed to build a strong reputation with American consumers. Additionally, its history of understanding markets makes it an expert at marketing and attracting new customers.

A weakness in this sector is its overreliance on the American market. Since it started in the American continent and it has grown to a massive scale, the company is very comfortable with the market. Unfortunately, it also means its more heavily invested there compared to the rest of the world. This means it is exposed to market risks such as fluctuating economic conditions.

JMPC is also known for pioneering technologies that help make banking easier for consumers. It merged with Bank One, a bank known for pioneering a national credit card system and ATM’s.

Lastly, by merging and acquiring other banks Chase has been able to grow at a much faster rate. Mergers and acquisitions allow it to take advantage of the relationships that have been built with customers over the year, while also growing its business.

Corporate Level

JPMC strategy is related diversification. It uses similar technologies and shares its knowledge across its different business units to help it make better business decisions. It has similar strategies across business units which allows it to share its knowledge across them. For example mergers and acquisitions in both consumer banking and investment banking is common. This allows it to standardize similar operations and reduce costs across all business units.

Other examples of synergies across its business units is the similar nature of all of its units, they are all in the financial sector and although each require specialized knowledge it also gives the company an opportunity for leaders in other business units to provide insights and advice when needed.

Overview of Strengths and Weaknesses

Some strengths of the company include robustness, deep knowledge specialization, and power to enter new market sectors. The company has had many years to gain expertise and deepen its knowledge of capital markets as well as consumer behavior. This gives it an edge over other new entrants into the field because they don’t have access to as much customer data and consumer trends.

Weaknesses include overreliance on American market and its lack of expansion into international markets. Since its beginning is in the US it only makes sense that it is heavily invested in this market, but unlike some of its rivals, HSBC, it has failed to expand internationally. Its growth has been limited and the company has not been willing to take some of the risks necessary for international growth. Although this can be seen as fiscally positive, the end result is that it is over reliant on the American market.

When the American financial sector is struggling, the company is severely hit, and to mitigate this risk it has successfully invested in a range of product offerings in the financial world.

IV. SWOT AND STAKEHOLDER ANALYSIS

Strengths - Opportunities

Deep knowledge of markets and the president's aim to remove regulations from the banking industry imposed by Dodd Frank Act results in a great opportunity for growth. As mentioned earlier, the President's Economic Report mentioned that one of the main goals of the Trump administration is to remove barriers on banks. This presents a domestic growth opportunity, as well as presents the opportunity for growth internationally. The money that would have been spent on policy adherence, can be reinvested into exploring projects.

Strengths - Threats

JPMC has a deep technology knowledge and history of experimenting with technologies that revolutionize the banking industry. The banking sector of developing economies present a threat to JMPC. By leveraging its knowledge of technology it can disrupt the entry of new banks, offering compelling technologies that make existing products stickier as well as more useful is a way to retain customers. Additionally, the brand image of JPMC is one of trust and expertise. Compared to new entrants which are fairly inexperienced in international markets.

Weaknesses - Opportunities

JPMC overreliance in the American financial sector can be countered by continuing its investment in fintech. Fintech aims to serve underserved communities like the poor. This community has been underserved due to its view as unprofitable or hard to target. Another benefit of fintech is that it provides the company with the opportunity to grow internationally. Technology is accessible throughout the world, and many places have access to reliable internet.

Weaknesses - Threats

JPMC is heavily invested in the American market and with this is mind the threat of new entry by international banks in developing countries is very large. This leaves international markets exposed and without first mover advantage in many of them it would be behind or have to play catch up.

V. VIABLE STRATEGIC ALTERNATIVES

Alternatives

Viable Alternative (1)

JPMC can capitalize on its experience innovating and using new technologies, considering the high entry barriers for non-bank fintech companies. This gives an opportunity to get ahead of the curve on some technologies that might be a threat in the future.

Viable Alternative (2)

Its deep expertise in understanding international marketing and its lack of diversification in international consumer and community banking gives it an opportunity to expand.

Viable Alternative (3)

Its strong global brand image and stiff competition from financial service providers gives it leverage for growth, although it lacks international investment.

Best Alternative

The best viable alternative for JPMC is capitalizing on its experience innovating and using new technologies. Non-bank fintech companies are currently receiving considerable pushback from government around the world due to government's distrust of their ability to properly regulate them. Banks have the opportunity to grow because they have more opportunities for growth.

Some examples of technologies that it could invest in are phone applications for managing finances. Mint is a non-bank fintech competitor that has recently been granted a ruling in its favor in Europe. Banks are now required to have API's to give third parties optional access to bank account holder's data. This helps bank account holders better control over their data, as well as gives companies access to sensitive data that can be used for marketing purposes. This is a detriment to banks because they usually make their money when customers go on to open more accounts or credit cards with them. By allowing third parties access to the same information they are losing potential customers. In order to mitigate this risk, the company could invest in its own version of the bank so as to provide customers with more functionality. This would ensure that customers stayed on their platform.

JPMC has considerable experience innovating, for example it has used Zelle in collaboration with other banks to allow customers to have easy payment alternatives. This helped mount an aggressive competition to existing companies Venmo and CashApp. In the same manner, the company can invest in advice technologies.

Another technological threat to traditional banks are mobile payment technologies, because now non banks have access to consumer data and can use this data to target consumers with advertising. Banks can invest in technology to safeguard this consumer data.

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