

Having Struggled with Recession, JP Morgan Chase Now Looks to Prosperous Future with Bank One

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On January 14, JP Morgan Chase and Company announced a merger with Bank One Corporation that will create the second largest financial services firm in the U.S. Bank One has 71,200 employees, \$290 billion in assets, and 1,800 branches in 14 states. The combined company will have “assets of \$1.1 trillion, a strong capital base, 2,300 branches in seventeen states and top tier positions in retail banking and lending, credit cards, investment banking, asset management, private banking, treasury and securities services, middle market, and private equity”(news release).

The Board of Directors of both companies agreed to a stock-for-stock merger in which 1.32 shares of JP

Morgan Chase common stock will be exchanged tax free for each share of Bank One common stock. The deal is valued at \$58 billion. Over the next three years, it is anticipated that the merger will provide cost savings of over \$ 2.2 billion. The merger reflects a consolidation trend in the financial world in which banks are combining investment banking with retail banking in order to achieve a balance between corporate and consumer customers. For JP Morgan, this means that they will now focus on selling “everything from checking accounts to credit cards and mortgages” (Financial Times).

JP Morgan Chase & Co. is a premier global financial services firm

which maintains dealings with roughly 99% of the Fortune 1000 companies. Chairman and CEO William B. Harrison, Jr., has helped JP Morgan Chase & Co grow into one of the largest banks in the world. JP Morgan Chase & Co. is headquartered in New York City and is divided into five major business divisions: Investment Banking, Treasury and Securities Services, Investment Management & Private Banking, JP Morgan Partners, and Chase Financial Services. JP Morgan Chase has offices in over 50 countries and serves over 30 million customers. JP Morgan's business includes: Investment Banking, Research, Private Equity, Treasury and Securities, Asset Management, and Private Banking. The Chase brand focuses on the individual consumer as well as small business and middle market financial services. JP Morgan & Co. would not have become as pervasive in the

financial industry if it hadn't merged with Chase Manhattan. (10k).

In September of 2000, JP Morgan & Co. merged with Chase Manhattan Corp. in what became a \$33 billion deal. The merger united the bank of wealthy investors with the bank for middle market clients. Some of the products and services the Chase brand provides for individuals include: auto loans, checking, credit cards, education loans, home equity, investments, mortgage, online services, savings, and insurance. The combined company has \$660 billion in assets, which kept it as the third-largest bank holding company in the country. JP Morgan and Chase Manhattan had "\$2.8 billion in merger-related expenses before taxes, and annual savings of \$1.5 billion, with about a third coming from real estate, a third from systems integration, and a third from reduced staffing" (The House

of Morgan, money.cnn.com). JP Morgan Chase and Co. also anticipates about \$400 million in incremental revenue growth over the next three to five years. (The House of Morgan, money.cnn.com). Now with the Bank One merger in sight, pretax cost savings of 2.2 billion dollars are also expected over a three year period.

JP Morgan Chase & Company has experienced diminishing net income and Return on Assets since 2001. The sharp decline in these numbers can be attributed to the technology stock bubble burst and the 9/11 disaster, which, combined, caused an economic recession, and its relations with Enron. In 2000 the firm posted a return on assets of 0.8%, which is very close to the 1% benchmark (ROA is the ratio of income to total assets and is used to evaluate how well the company is using its assets to generate profits); however,

in 2001 the firm reported an ROA of 0.24%, well below the benchmark. 2002's ROA was even lower at 0.22% (see figure 1). The steep reduction in ROA was due to a dramatic decline in net income while total assets increased along with an increase in total deposits (see figure 5). Net income for FY 2000 was \$5.73 billion, compared with \$1.69 and \$1.66 billion in 2001 and 2002, respectively; and total assets numbered \$715.35 billion for FY 2000, compared with \$693.58 and \$758.80 billion in 2001 and 2002, respectively (see figure 4). These negative results were affected by dragging capital markets, a sizeable \$1.3 billion charge connected with the settlement of its Enron-related surety litigation, and continuing integration expenses related to the JP Morgan merger with Chase (10k).

Although the slow economic recovery, diminished investor

confidence, and weak capital markets activity has caused lower returns in the firm's Investment Banking business, the national consumer credit business Chase Financial Services prospered because of low interest rates (10k). The firm's loan loss provision has steadily increased from \$3.67 billion in 2000 to \$4.52 and \$5.35 billion in 2001 and 2002, respectively (see figure 2). The increase in this provision was due to the troubled commercial credits in the telecommunications and cable sectors (10k). The firm's Tier 1 capital ratio, which is the shareholders' equity and retained earnings divided by total risk-weighted assets, has declined slowly

from 8.5% to 8.3% to 8.2% but remains well above the 4% benchmark (see figure 3). The Board of Directors intends to keep the quarterly dividend at \$0.34 per share on common stock, as long as the capital ratios remain strong (10k).

JP Morgan Chase predicted in its 2002 10k that the outlook for its investment banking and capital markets activities in 2003 remain cautious because of the uncertain economic conditions. It also predicts that Chase Financial Services will perform well due to the continued low interest rates and that the Bank One merger in 2004 will create an enterprise with a market capitalization of \$130 billion.

Sources:
JP Morgan Chase & Co.'s 2002 10K report
"The House of Morgan"
money.cnn.com
news release about the Bank One merger