JP Morgan 2009 Q3 Results – Miracle or Mirage?

By Muhammad Rafeeq

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Once more, according to the financial press, the world's fiscal problems have finally turned the corner and it's all over, all over again. But the truth is far from the puff pieces being spread around the mainstream media. The financial press is beginning to give déjà vu a bad name.

Looking at a typical article on Bloomberg "***JPMorgan's Investment Bank Rescues Earnings From Loan Losses***" (October 14th 2009), we find a series of interesting claims. These include the claim that the bank has managed to produce record quarterly earnings year-on-year of US$3.59bn, whilst at the same time re-paying US$25bn of government bailout funding. A *big cheese* of Wall Street is then quoted in the article as saying that this is impressive stuff.

Indeed, it would be impressive stuff if there were any truth in it. So let's take a look a JP Morgan's own supplement to the Q3 financial report and see how many fiscal miracles have really been worked.

Firstly, there is a footnote on page 4 of the supplement which discusses the "AML Facility" started by the Fed to help out money market mutual funds (MMMFs). This facility was used to bailout MMMFs, and NOT banks, by allowing these funds to issue securities, which the Fed promised to buy. The bank participated in this scheme by purchasing the securities and then lodging them with the Fed on what is known as a "repo", or repurchase, basis. During the time that these were held by the banks the Fed allowed the banks a 0% capital allocation, meaning that these MMMF securities were "risk free" to the banks.

This scheme did not bailout the banks. In this scheme the banks were being encouraged to help bailout MMMFs. Therefore, the footnote that JP Morgan is no longer holding any AML securities (in this case ABCP) means that JP Morgan, as a bank, is no longer helping any Money Market Mutual Fund companies. JP Morgan has not paid back any money to the Fed under this scheme, since as a bank they were not a beneficiary institution of this particular Fed scheme.

In order to look at how much borrowing JP Morgan is doing from the Fed it is necessary to look at the bank's main "repo" (and "reverse repo") activity.

Before doing this however, there are some other very revealing figures in the current set of reports.

JPMORGAN CHASE & CO.
CONSOLIDATED BALANCE SHEETS
(in millions)

	Sep 30 2009	Jun 30 2009	Mar 31 2009	Dec 31 2008	Sep 30 2008
ASSETS					
Cash and due from banks	$ 21,068	$ 25,133	$ 26,681	$ 26,895	$ 54,350
Deposits with banks	59,623	61,882	89,865	138,139	34,372
Federal funds sold and securities purchased under resale agreements	171,007	159,170	157,237	203,115	233,668
LIABILITIES					
Deposits	$ 867,977	$ 866,477	$ 906,969	$ 1,009,277	$ 969,783
Federal funds purchased and securities loaned or sold under repurchase agreements	310,219	300,931	279,837	192,546	224,075

1) The deposits, the lifeblood of any bank are down by US$102bn (969bn – 867bn) from Q3 2008 to Q3 2009, representing a drop of 10%. Without deposits the bank simply can't lend or buy securities.

2) We can also see that the bank has had a drastic drop in the amount of available (non-tied up) cash, losing US$33bn or just over 60% of it. This is an important figure since cash is the primary form of Tier 1 capital for bank solvency. Where has the cash gone?

To understand the next part we need to look at the financial transactions called Repos and Reverse Repos. These are re-purchase contracts between two parties, one of whom is the owner of a security and the other is a temporary holder who "rents" the security from the owner for an agreed period and who collects the income from the security over the holding period. The owner receives the cash back equal to the value of the security and this temporarily improves the liquidity of the owner. For instance, if you had $1000 and invested it all in US treasury certificates that mature after 10 years, your money is locked up for the whole 10 years. But if someone agreed to buy them off you for one year, as long as you made a contract guaranteeing the re-purchase, you could free your money up for other purposes, until the re-purchase date.

3) From the section of the report above the "securities purchased under resale agreements" has decreased by approximate US$62bn between 2008 Q3 and 2009 Q3. What does this mean? Simply that JP Morgan are paying out US$62bn less than before to other parties, in order receive the income streams from their assets. Put in another way, JP Morgan is providing $US62bn less liquidity to the money market. These numbers contrast with "securities loaned under repurchase agreements" in the Liabilities section of the report. Here we see that JP Morgan has actually increased the number of Reverse Repo agreements, from US$224bn in 2008 Q3 to US$310bn in 2009 Q3, an increase of US$86bn.

What we see is that in total JP Morgan has tried to increase the amount of cash funds at its disposal by US$ (62 + 86) 148bn. Yet in spite of raising all this extra cash on the money markets by decreasing repos and increasing reverse repos, the bank has actually got 60% less cash on hand.

Where has all that extra money gone? And a profit of less than US$3.6bn for the last quarter 2009 is being celebrated by the financial media. A drop of more than US$100bn in deposits is being ignored, a reduction in Tier 1 cash by 60% is being ignored and US$148bn of missing repo market funding is being ignored.

At least this handsome profit (US$3.6bn) should take our minds of the huge amount of money being handed out as bonuses at JP Morgan right now.