

J.P. Morgan Chase (NYSE: JPM)

Update Report - Price \$46.55

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Company description: J.P. Morgan is headquartered in New York City. It is one of the world's largest financial institutions providing a full array of banking, investment and related financial services.

Investment Rating Market Perform

	<u>Current</u>	<u>Prior</u>
Target Price	\$44.00	
Price (March 24, 2008)		\$46.55
52 Week Range	\$36.01 - \$53.25	
Shares Outstanding	3,472 MM	
Market Capitalization	\$161,622 MM	
Assets	\$1,561,147 MM	

	<u>Rev/Share</u>		<u>P/R</u>
	<u>Current</u>	<u>Prior</u>	
2010E	\$25.47		1.83x
2009E	\$23.35		1.99x
2008E	\$21.47		2.17x
2007	\$20.35		2.29x

	<u>EPS</u>		<u>P/E</u>
	<u>Current</u>	<u>Prior</u>	
2010E	\$4.50		10.3x
2009E	\$3.88		12.0x
2008E	\$3.30		14.1x
2007	\$4.37		10.7x

	<u>Book Value</u>		<u>P/B</u>
	<u>Current</u>		
Reported	\$35.49		1.31x
Tangible	\$20.70		2.25x

	<u>Current</u>	<u>Yield</u>
Annualized	\$1.52	3.3%

<u>Ratios</u>	
December, 2007	
	<u>Income</u>
Trading/Rev	0.9%
Inv Banking/Rev	9.6%
Net Int. Inc/Rev	41.5%
Operating Cost Ratio	61.7%
Provision/Loans	1.96%

	<u>Equity</u>
Reserves/Loans	1.78%
Common Equity/Assets	7.89%
Tangible CE/Assets	4.60%

	<u>Annual</u>
Past 3-Year RPS Growth	9.6%
Past 3-Year EPS Growth	17.9%
P.E./Past EPS Growth	0.79x
Proj. 3-Year EPS Growth	2.0%

	<u>Returns</u>
ROE	9.6%
ROA	0.76%

High Risk Transaction

- J.P. Morgan Chase increased its bid for Bear Stearns (BSC/\$11.25/Market Perform) on Monday. The bank will offer 0.21753 of its shares for each share of Bear Stearns. At J.P. Morgan's close on Monday, the value of the deal was \$1.47 billion or \$10.13 per Bear Stearns share. This was a four-fold increase from J.P. Morgan's original offer of .05473 of its shares for every share of Bear Stearns, made a week earlier.
- In addition J.P. Morgan will purchase 39.5 million shares of Bear Stearns by April 8 at the same price offered all shareholders or \$10.13 per share. The total cost of these shares will be just under \$1.0 billion. Finally, J.P. Morgan has agreed to absorb the first \$1 billion in first losses on Bear Stearns portfolio. The Federal Reserve will absorb the next \$29 billion (down from \$30 billion) a week ago.
- The total cost of the transaction to J.P. Morgan could be \$3.44 billion. Based on Bear Stearns original number of shares (assume the 95 million shares were not issued), the cost works out to be about \$23.75 per share. Additionally, J.P. Morgan will report a 12 month loss of \$6.0 billion to combine the two companies. Add this to the purchase price and J.P. Morgan is paying about \$65 per original Bear Stearns share. This is approximately the same as Bear Stearns opening price on March 12 (\$65.50).
- Investors believe that J.P. Morgan is underbidding for Bear Stearns and getting it at a bargain price. I do not. Bear Stearns is a deeply troubled company which would have no value if the Federal Reserve had not stepped in to bail it out. It is basically a fully integrated mortgage company with a number of other businesses. J.P. Morgan certainly does not need the mortgage operation.
- It may not need the other businesses either. J.P. Morgan has a stronger investment banking business than Bear Stearns. It has a much stronger investment banking business and it is better in transaction processing. Bear Stearns building is just another piece of Manhattan real estate that it must rid itself of..
- The key jewel, which Morgan needs from Bear that Morgan does not have, is its prime brokerage business. However, it is my understanding that this business' best customers have long since decamped to Goldman Sachs (GS/\$178.88/Market Perform). J.P. Morgan is going to have to work hard to get these people back.
- What is most disturbing about this deal is that it uses a great deal of Morgan capital to buy a company that is losing market share, in a series of businesses that are declining in size, with a top management team that is best described as sclerotic.
- These same funds could have been used to buy a bank with top management, a solid balance sheet, which was gaining market share, in what is now a sector that is gaining in market share.
- From my perspective the greatest benefit that could accrue to J.P. Morgan here is that it may take advantage of accounting techniques that can be used to revalue Bear Stearns assets at par value.
- Finally, expect every aspect of this transaction is likely to be tested in the courts with J.P. Morgan paying the bill all the way. This is not a "lay-up" at all.

Estimated Earnings Per Share

	<u>March</u>	<u>June</u>	<u>September</u>	<u>December</u>	<u>Year</u>
2010	\$1.06	\$1.12	\$1.11	\$1.21	\$4.50
2009	\$0.90	\$0.96	\$0.98	\$1.06	\$3.88
2008	\$0.75	\$0.85	\$0.82	\$0.88	\$3.30
2007	\$1.34	\$1.20	\$0.97	\$0.86	\$4.37

Notes: Reported/Operating Profits

Analyst Certification and important disclosures can be found on the last page of this report.

Important Disclosures

Risk Factors

Companies in the financial industry do not control the macro economic factors that have the greatest impact on their earnings performances and their stock prices. These include changes in the level of interest rates and the shape of the yield curve, as well as changes in economic direction which may slow or accelerate unit growth and loan losses

These companies do not provide adequate data concerning their holdings of loans and securities. In this sense they are blind pools and investors only become aware of problems after they have occurred. Managements are also prone to errors in decision making in positioning their balance sheets and in the general operation of their businesses which may impact the profits of the company.

The analyst preparing this report may also make incorrect judgments concerning interest rates and economic direction and this could cause his estimates to deviate meaningfully from actual results. Further, his assumptions concerning PE multiples may be faulty leading to faulty price targets.

Rating Definitions and Coverage Percentages

Rating	Definition	% of companies under coverage with this rating	% within rating category for which investment banking services have been provided in the last 12 months
Buy	Common stock is expected to outperform the market by 15 or more percentage points	60.00%	16.67%
Accumulate	Common stock is expected to outperform the market by five to 15 percentage points	1.67%	0.00%
Market Perform	Common stock is expected to perform with the market plus or minus five percentage points	35.00%	4.76%
Sell	Common stock is expected to under perform the market by 15 or more percentage points	3.33%	0.00%

The rating system is a guide to expected total return (price plus dividend) relative to the total return of the market on which the stock trades over the next 12 months.

Analyst Certification:

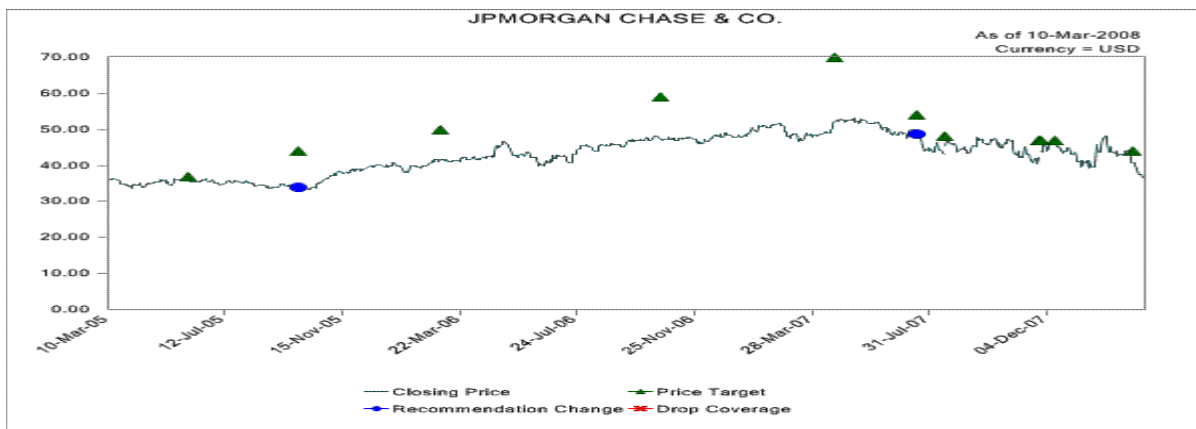
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Currency = USD		JPMORGAN CHASE & CO.			
Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
18-Jul-2007	48.88	MARKET PERFORM	29-Feb-2008	40.55	44.00
27-Sep-2005	35.38	BUY	11-Dec-2007	45.94	47.00
			27-Nov-2007	42.35	46.52
			27-Nov-2007	42.35	47.00
			15-Aug-2007	43.00	49.00
			19-Jul-2007	48.62	54.00
			18-Apr-2007	52.07	70.00
			18-Oct-2006	47.21	59.00
			01-Mar-2006	41.63	50.00
			27-Sep-2005	33.98	44.00
			01-Jun-2005	35.76	37.00