

Dear fellow shareholder,

As of year-end 2005, I stepped down as CEO of JPMorgan Chase – turning the leadership of the firm over to my partner, Jamie Dimon, who I believe will prove to be one of the outstanding CEOs the financial services industry has had in a long time.

As Chairman, I look forward to contributing to our growth by leveraging my global relationships and contacts and by helping to further develop strategy.

As I look back on my 38 years in the industry, all with the same organization, I realize how fortunate I have been and what an exciting journey I have been on. When I left a small town in North Carolina to join Chemical Bank in 1967, my goal was to spend two years in New York and then return to North Carolina. Little did I know I would be part of an industry and a career that were as challenging and rewarding as these have been.

I step down as CEO believing that:

- JPMorgan Chase is very well positioned strategically to be one of the great financial institutions in the world.
 - Size does matter in our industry – provided that size translates into operating and scale efficiencies, increased profit margins, stronger earnings and leadership positions. And the benefits of size can only be realized within a culture that values teamwork, partnership and execution.
 - One should be a leader – not a follower – as our industry irreversibly consolidates in a globalizing world.
 - A diversified model will prove to have competitive advantage in terms of creating shareholder value over time.
 - Managements and boards have to manage with a longer-term outlook and resist the pressures of the quarter-to-quarter mindset of the market.
 - Building the best performance culture in the industry will ensure that all of the inherent potential of size is harvested and maximized.
- Relationships matter – with clients and with each other internally – and without them, a firm will never reach its potential and be its best.
 - Companies with the highest ethical values, which start at the top and cascade all the way down, will be the great companies – and we must keep raising the bar on how we achieve this in a large, complex corporation.
 - Surrounding yourself with people who are smarter and better than you are is critical because your talent pool will be a key determinant of success.
 - I have been one of the most fortunate people in the world to have had the experience and the success I have had, and there is not one day that goes by that I don't think about this.

So from a small town to a big city – from a small bank to a big bank, I learned much along the way – that you, in fact, never stop learning. You should always commit to be the best you can be, you should think big and dream big, and you should think about how you can win and what your strategic platform should be to create sustainable shareholder value. And you should do this by always, always having the right set of values and living by them.

You learn that the peaks and valleys, the successes and failures of your job and life need to be viewed with the proper perspective and balance, and only with that balance and perspective can you find true north.

You learn how important your family and friends are in enabling you to maintain the passion and commitment to be the CEO of a firm like JPMorgan Chase and how privileged you've been to have been the leader.

Thus, while my JPMorgan Chase career is nearing an end, a new chapter in our company's long history is beginning. It is time to pass the baton to a new group of leaders, led by Jamie Dimon, who will take this firm to the next level of performance, harvesting its vast potential and maximizing shareholder value through great execution.

Dear fellow shareholder,



William B. Harrison, Jr., *Chairman*

James Dimon, *Chief Executive Officer*

Let me close with a profound thanks to our shareholders who have had the faith to believe in the potential of this firm. Thanks to our outstanding Board of Directors for their support and wisdom, and I want to express my special gratitude to retiring directors Larry Bossidy and Hans Becherer whose advice and counsel over many years have been invaluable. Thanks to all of our clients and customers around the world for the opportunity to serve them.

And thanks – 168,000 thanks – to our talented and dedicated employees around the world for what they stand for and for what they contribute every day.

I could not be more excited and confident about our future.

Sincerely,

William B. Harrison, Jr.
Chairman

March 8, 2006

This is my first letter to you as the CEO of JPMorgan Chase. From a personal standpoint, I want to share with you some feelings and thoughts. I feel a tremendous mix of emotions: excitement about our potential, and a great sense of obligation and responsibility both to you, our shareholder, and to those who have built our company over the years. They have given us an exceptional opportunity – and we owe them not only our gratitude, but also our commitment to deliver on our company's potential and make them proud of what they have helped to build.

We have accomplished a great deal over the last year, and we are excited about our progress in 2005 and our plans for 2006. The foundation for everything we are doing rests on a set of business principles that we believe, when executed properly, create great companies. These principles are described on our Web site: www.jpmorganchase.com. In essence, we strive to:

- Share with you the truth and offer honest assessments of our businesses and our prospects.
- Act with integrity and honor.
- Do the right thing, not necessarily the easy or expedient thing.
- Work hard and with fierce resolve to make this a company of which our shareholders, employees, customers and communities can be proud.
- Focus relentlessly on the execution of our business principles.

There are some specific issues that are integral to the success of our company. I would like to address them by answering the following questions:

- I. [Are we in the right businesses?](#)
- II. [Can we achieve outstanding performance?](#)
- III. [Are we properly managing our risks?](#)
- IV. [Do we have the right people and the right compensation strategy?](#)
- V. [Are we a good corporate citizen?](#)

I. Are we in the right businesses?

Let me unequivocally answer this question with a resounding “yes,” for three reasons: each business is already well positioned – in terms of size and scope – within its specific industry; there is exceptional value in the linkages among our businesses; and the company’s size, scale and brands are a competitive strength.

Each business is already well positioned within its specific industry

Our six major lines of business – Investment Banking, Commercial Banking, Retail Financial Services, Card Services, Asset & Wealth Management, and Treasury & Securities Services – all compete in consolidating industries. Businesses consolidate when the vast economies of scale that can be achieved (in systems, operations, distribution, brand and R&D, to name a few) will benefit the customer.

We cannot underestimate the power of these economic forces. Nor can we ignore the inevitable impact they have on our businesses. But change is hard – and many who attempt it fail. The winners will be those who can provide their customers with more access to better financial products and services at a lower price. In this environment, size, scale and staying power matter, and all of our core businesses *already have* what it takes to succeed; but as I discuss later, we must continue to improve our execution skills to distinguish our company in the marketplace. Our businesses do not and will not want for capital or investment. They are well equipped to survive in good and bad times, and our customers will continually benefit from their stability and efficiency, as well as the investments we are able to make in technology and innovation.

Our businesses belong together, and there is exceptional value in the linkages among them

As separate entities, our businesses are currently well positioned; together they are even stronger. Putting our businesses together makes sense only if doing so creates value for customers and, ultimately, shareholders. It does not work because we want it to – it only works because it gives the customer more for less, sooner rather than later. We have no interest in selling our customers products that they do not want or need.

In this context, the term “cross-sell” can be misleading. “Cross-selling” often carries negative connotations – as if it is a forced and unnatural act. In fact, it should be described more appropriately as “natural product-line extensions,” which businesses have been doing successfully for hundreds of years. Wal-Mart has continually expanded the types of products it sells. Twenty years ago, who would have thought that it would sell lettuce and tomatoes? These product-line extensions are true also for Home Depot, commercial banks, investment banks, stockbrokers and even manufacturers. GE Aircraft Engines now finances and services what it manufactures. The essence of what makes this successful is that the customer is the winner.

By extending our product lines, we are able to leverage the substantial investments we have made to build our distribution system (e.g., branches, technology and sales people), strengthen our brand and earn the trust of our customers. For example, today our branches, which are our retail stores, not only accept deposits and provide access to cash, but also sell investments, mortgages, home equity loans, debit and credit cards, and online bill paying services, as well as small business loans, international funds transfers, payroll services, annuities, etc.

Our clear “natural product” set is financial services, which is what individuals and businesses want and expect from us. Where the products are “manufactured” is of little interest to them. What is important to them and to us is our ability to provide a better product, or package of products, at a lower cost. Our challenge is to view this from their perspective and ensure that our collective resources are focused accordingly.

In addition to providing substantial potential for growth, our mix of businesses presents us with fertile ground for innovation. Here are a few examples of how our businesses are working together:

Retail and Card Services. The competitive advantage is formidable when our retail bank – which serves almost 10 million households – joins forces with our credit card company, with its 110 million cardholders. This collaboration should result in excellent new products that address specific consumer needs. For example, we may be able to

make life much simpler for our customers by linking credit and debit cards and by offering them other products. The results of recent efforts are promising: credit card sales in our retail branches are up nearly 100% from two years ago.

Commercial Banking and Retail. A strong connection already exists between our Commercial Bank and our retail branches. In fact, there are few successful commercial banks in America that do not have a retail bank – and for good reason. A large share of retail business comes from small businesses and mid-sized companies. Many use branches as their financial back offices for cash, payroll processing and wire transfer services. This interdependency is cost effective for us and beneficial to our customers. In addition, business accounts often lead to new personal accounts and vice versa.

Investment Banking and Commercial Banking. A natural connection exists between an investment bank, which essentially serves large public companies, and a commercial bank, which essentially serves mid-sized to small public and non-public companies. Our Commercial Bank already generates hundreds of millions of dollars in revenues from offering its clients traditional investment banking services (e.g., advisory, debt and equity underwriting). Over the next few years, we believe that we can double Commercial Banking’s revenues from these activities. In cities like Indianapolis, Austin, Denver and Tucson – where our Investment Bank does not have a physical presence – local businesses have strong relationships with our commercial bankers. These bankers know when their clients are contemplating transactions and need access to investment banking expertise. The connection is valuable for clients and beneficial to us. It enables our Investment Bank to generate revenues from its product expertise that it could not have previously produced without the client relationship. And it enables the Commercial Bank to better serve its clients by providing them with the additional products that they need.

Treasury & Securities Services; Asset & Wealth Management. Another important connection exists between Treasury & Securities Services and our other businesses. Many of our major customers (institutional, middle market, small business and retail) use TSS for activities such as cash, checks,

ACH payments, wire transfer and custody. TSS generates approximately \$9 billion of annual revenue by serving these customers. Asset & Wealth Management also benefits from working with other businesses, including managing assets for corporate clients, helping them meet their complex pension and investment needs, and offering products from across the company to individual clients.

Plenty of other examples exist, but the critical point remains: while each business should do well on its own, it should also be able to capitalize on our company’s extensive and unique set of products and services to more fully and profitably meet customer needs. There is certainly no reason why they should do worse because they are part of this institution. The key, of course, is that the customers must be the winners.

The size and scale of the company are a competitive strength

The size, scale and scope of JPMorgan Chase also offer huge advantages: economies of scale in operations and systems; diversification of capital, risk and earnings; a great global brand; and the capability to make large investments at a lower cost of capital. In particular, the benefits of size and scale in operations and systems are vast, and they are real. Our diversified earning streams lower our risk, increase our credit ratings and reduce the cost of our capital. And since one of our major costs is the cost of money, the ability to raise funds cheaper, better, faster and more effectively around the world than other companies is a major advantage.

But size alone is not enough to win. In fact, if not properly managed, it can bring many negatives. Huge companies operating in complex, consolidating and fiercely competitive industries like ours can only achieve and sustain their success by competing where the “rubber hits the road” – at the level of the store, the product and the banker – not at corporate headquarters. We must equip those employees on the front lines to be responsive and responsible. The way we manage our size will reflect how much we recognize and respect this imperative. Bureaucracy and waste are lethal. To remain healthy and vibrant, we must constantly and consistently minimize bureaucracy, eliminate waste and insist upon excellent execution.

II. Can we achieve outstanding performance?

“Yes,” but we are not there yet. Good positioning does not assure great performance. Creating great performance is not mystical; it takes consistent effort, focus, hard work and discipline.

The starting point for us is to admit where we are. Any way one analyzes our businesses, for the most part our costs are too high, our returns on capital are too low and our growth is not what it could be.

We are underperforming financially in many areas. We need to understand the reasons and focus our energy on making improvements, not excuses. We cannot afford to waste time justifying mediocrity. Each line of business now assesses its performance in a rigorous and very detailed way. Each compares results to targets in a variety of areas, including sales force productivity, customer service and systems development.

It is not enough for the overall business to make its profit targets. It would be unacceptable to achieve good financial returns by reducing expenses that are critical investments for the future or by compromising the *quality* of business that we do. The best way to reach and sustain a higher level of performance is to get every part of the business to step up its game. For example, we have some businesses that, in general, achieve adequate returns. These results are often produced when a few exceptional business segments do the heavy lifting for the rest. We cannot use our strengths in one part of our business to subsidize our weaknesses in another part.

We spend a lot of time on capital and return on capital. How we allocate capital should reflect our understanding of how changes in the economy – and the likely length and intensity of the cycles they cause – will affect specific parts of our business. Where will the risks and growth opportunities be? For example, there *will* be another recession; we just do not know when. What we do know, however, is that when it happens, our annual credit costs will increase substantially. Therefore, when we talk about return on capital, we must look at it through the cycle, not just during the best parts of the cycle.

Many companies that compete in our businesses have been well managed and able to produce excellent results for decades. We have every reason to be among them. Time will tell if we are. We have made progress, but not enough. To get outstanding performance, we must instill the following disciplines deep into the fiber of our company.

Become lean and efficient

This is an imperative. One cannot achieve great performance in fiercely competitive industries without being lean and efficient. It is irresponsible to waste our critical resources on expenditures that have nothing to do with better serving our clients and building a great company. We need to use our resources to grow, innovate, market, hire productive people and build systems. It is not just about cutting costs. A company cannot become great just by cutting costs. It is about building better systems to better serve our customers. It is about paying our people not only fairly, but effectively, to help create the right behavior. It is about how we run meetings. It is about designing the right products that are also profitable. (Many companies design products that lose money, and they do not even know it.) It is about constantly improving productivity.

We must continually ask ourselves: Can the same investment in the same area be better spent? Does every business strive to get the most out of its resources? The Investment Bank, for example, has many businesses, depending upon how you measure it. Does each business spend its money efficiently and wisely? Are we spending the right amount in the right way and expecting the right results? Last year, we spent over \$1 billion in marketing to get 11 million new credit card accounts. Can we spend more and get even better results? We probably can. This year, we want to both spend more and get more from every dollar we spend. When we determine that we can and are spending money wisely, we will want to spend *more, not less*.

Since the merger, we have realized \$1.9 billion in merger savings. However, much more is needed to achieve what we would consider to be *real* efficiency. This past year, we launched and completed major projects aimed at increasing our efficiency and improving our customer service over the long run. They include:

- Completing the largest credit card conversion in history. This effort combined over 30 million heritage Chase and Bank One accounts onto a single platform and provided us with a single best-in-class system to better serve our customers (and at a lower cost).
- Integrating and upgrading all of our businesses in Texas – in terms of products, brand, systems and operations – where we have 20,000 employees serving 2 million customers.
- Converting all U.S. dollar clearing to one platform globally, an operation that processes an average of \$3.2 trillion daily for 200,000 clients worldwide.
- Executing the largest merger of mutual fund families in U.S. history, affecting 1.1 million fund shareholders.
- Completing the first and second construction phases of our new Global Services Center in Bangalore, India, and hiring 8,700 employees to meet increased demand and deliver more services from India.
- Migrating much of the company's production, disaster recovery, and development and test systems into a new data center. The move increases our data storage capability, enhances our resiliency, reduces infrastructure points of failure and lowers overall cost to the firm.

Over this next year, we will continue to massively upgrade and streamline our systems and operations. Highlights include:

- Converting and upgrading all of our operations in the New York tri-state market, beginning in the second quarter. This will be one of the most visible bank conversions in our industry and will have an impact on all of our businesses – specifically, 4.8 million deposit accounts representing over \$190 billion, and involves more than 400 heritage Chase branches and over 3,000 teller workstations.
- Providing our retail and wholesale customers with uniform Internet platforms, upgrading loan origination systems and implementing a new mortgage servicing system.

- Substantially improving infrastructure, including data centers, networks and financial management systems.

We cannot build a great company unless we are unrelenting in our efforts to be a lean and efficient company. This must become a permanent part of our mindset.

Remove barriers to success

As I mentioned before, excessive bureaucracy is lethal. It slows us down, distracts us from our clients and demoralizes good employees. We must act with more openness, passion and urgency. The process of busting bureaucracy never ends, but what is different now is that our employees are engaged in challenging the system and solving the problems.

We continue to attack bureaucracy and improve all aspects of our management practices, including:

- *Accountability and decision making:* Central to the changes we have undertaken is the realignment of corporate staff. Now embedded in the businesses are many of the staff functions – like finance and systems – that used to be concentrated at the corporate level. The realignment gives our businesses greater ability to manage their support functions. For staff, better access to the businesses they support provides them with more knowledge and control. The restructuring will lead to better accountability, transparency and reporting, which in turn will *improve* execution and overall corporate risk management.
- *Management information and discipline:* It is hard to act on the truth if you do not know what it is. We want managers to have the tools and information to run their businesses as if they owned them. With this goal in mind, we now produce thousands of increasingly accurate reports that provide managers with specific information on their performance. In addition, we give them tools to proactively eliminate waste and manage their resources. Better reporting has dramatically improved the effectiveness of our business review meetings. Without this information, these meetings are often a waste of time. They now are convened at many levels of the company and focus on where we are and need to be, relative to our own benchmarks and the best performers

in each business. As a result of these discussions, we are able to establish real targets for our businesses in terms of growth, margins, returns, market share, etc.

- *People practices:* We have rationalized human resource processes by eliminating several unnecessary procedures and personnel to place accountability for managing people squarely where it belongs – with line managers. For example, performance reviews have been revamped and simplified, training has been streamlined and executive coaches have been eliminated. (We think coaching is the manager's job.) Performance reviews should facilitate, not prevent, meaningful, honest and comprehensive results-oriented exchanges between managers and their direct reports. Yet over time, the process grew to take on a life of its own and became a hindrance. Now the barriers are being removed. In addition, we have created a forum for discussion of our talent and made people management generally, and diversity in particular, part of the agenda of senior manager meetings across the company. We remain devoted to our people and their development, but we will use management accountability, not bureaucratic processes, to prove it. We want our people to communicate openly, easily and constructively.

Focus resources where we can succeed and win

We have sold or liquidated several businesses that either did not fit our strategy or did not contribute significantly to our long-term success. For these reasons, we sold BrownCo, and businesses in manufactured housing and recreational vehicles. We also announced the sale of our insurance business and have dramatically reduced the size of our auto leasing business.

By discontinuing or reducing our commitment to ancillary businesses, we availed ourselves of billions of dollars in capital. We redeployed this capital in businesses where we can win. For example, we invested in JPMorgan Cazenove, an investment banking joint venture in the United Kingdom (which already shows promising results); expanded our global trade management operations with the purchase of Vastera; and acquired the Sears Canada private-label credit card portfolio. In addition, we have recently completed

the purchase of a consumer educational loan business, Collegiate Funding Services, that both processes and underwrites loans. These are all transactions that position us for real growth.

We have also freed up and redirected our capital to support innovation. We want to make innovation part of our DNA. This does not mean spending hundreds of millions of dollars on failed ideas. It does mean, however, that we will take calculated risks, knowing that some will fail. Progressive thinking should be reflected in every conversation, every analysis, and every product and service we provide. We have many new products coming out this year that we think will fill this bill.

The ultimate goal: create organic growth

Profitable, sustainable, properly underwritten growth is not a vision. It is the result of excellent management discipline, an unrelenting focus on execution, consistent management of risk, a competitive product set and outstanding customer service.

The level of effort and expense associated with merger activities and systems consolidation has been predictably huge. So the fact that we were able to absorb the impact – and still cut costs *and materially increase* investment spending – is a source of pride to all of us. What is even more gratifying, however, is to see evidence of real growth in most businesses, something that is often a casualty in merger consolidations.

In 2005, real growth – albeit not always great growth – took place across the board. Retail increased its deposits, checking accounts and credit cards. Commercial Banking achieved growth in leasing, middle market lending and liability balances. Treasury & Securities Services produced more custody business and had growth in liability balances. Asset & Wealth Management increased the level of assets under management. Card Services had growth in new customers, partners, card receivables and spending. Revenues in the Investment Bank increased in M&A, asset-backed securities, high-yield bonds and energy trading.

Equally important, we materially increased investment in areas that will drive *future* growth. Specifics include: spending hundreds of millions of dollars to open 150 new branches (this will drive growth in 2007 and beyond); adding more retail loan officers; hiring additional private bankers; funding the build-out of our energy and mortgage trading capabilities in the Investment Bank; and investing in state-of-the-art “blink” credit card technology (which enables customers to use credit cards for small payments without having to sign anything). Now being piloted in six cities, blink is an investment that has put us at the forefront of changes in payment systems and card innovation.

In addition to making across-the-board investments to build our businesses, we are making investments in our infrastructure that anticipate growth and prepare us to successfully manage it for years to come. In 2005, we invested over \$1 billion in platform conversions, including those for Texas and Card Services.

By consolidating and improving platforms, we are eliminating the inefficiencies and competitive disadvantages associated with multiple operating platforms. In the process, we will create best-in-class platforms in many areas, such as global cash clearing, credit card, retail branches and some of our trading business. We believe that long-term success is not possible without great systems and operations. They will drive efficiency, innovation and speed to market. Much of this will be accomplished by the end of 2006.

III. Are we properly managing our risks?

Almost all of our businesses are risk-taking businesses – and we spend a great deal of time thinking about all aspects and types of risk inherent in them, including:

- Consumer and wholesale credit risk
- Market and trading risk
- Interest rate and liquidity risk
- Reputation and legal risk
- Operational and catastrophic risk

The notable fact about the first three risk areas is that they are cyclical, and all of them have elements of unpredictability. This requires us to be prepared for inevitable cycles. A company that properly manages itself in bad times is often the winner. For us, sustaining our strength is a strategic imperative. If we are strong during tough times – when others are weak – then the opportunities can be limitless. Protecting the company is paramount. I will highlight the types of risks we focus on to give you a sense of the threat they pose and how we plan for it.

Consumer and wholesale credit risk

Over the years, our company has substantially reduced its wholesale credit exposure by using a disciplined process for extending credit and maximizing return on shareholder capital. In the consumer market, we have controlled our risk by limiting the amount of low-prime and sub-prime credit we issue in our card and other consumer businesses. In addition, we have decided, at the expense of losing some volume, not to offer higher-risk, less-tested loan products, such as negatively amortizing Option ARMs.

While we are taking the right steps, we estimate that in a recession, consumer and wholesale credit costs could possibly get worse by more than \$5 billion. This daunting reality requires us to be prepared and well protected. Protection #1 is having larger and more durable profits to absorb the losses. We are accomplishing this by increasing our margins virtually across the board. Protection #2 is maintaining a fortress balance sheet. We try to understand and manage every asset and every liability and make sure that someone is accountable for each one. It also means maintaining, as much as possible, strong loan loss reserves.

Finally, having a well-capitalized firm is critical. With Tier 1 capital at 8.5% and total capital at 12%, we believe we are there. The important point is that we need to manage the business, the balance sheet and the investments to earn adequate returns through the cycles and to be prepared for surprises. We do not want to realize high returns at the top, only to give them all back at the worst part of the cycle.

Market and trading risk, and interest rate and liquidity risk

We need to manage our risk–return payoff better in 2006. In 2005, our trading volatilities were unacceptably high. The \$6 billion in trading revenues (not a bad result on its own) was the result of two great quarters and two quarters where we underperformed. We think that is too much volatility, and reducing it is one of our priorities. I believe we can accomplish this by continuing to diversify our trading business, by being more disciplined and precise in the execution of our risk management practices, and by hiring and retaining the best talent. We intend to deliver better, more consistent results over time, while maintaining our aggregate risk-taking appetite.

The good news is that we *have aggressively invested* to generate more diversified and consistent returns. For example, we have added energy trading, and increased our activities in mortgage- and asset-backed securities, and principal investing. We have leadership positions in credit markets and in our derivatives franchises, and we will continue to invest in order to sustain them. And while in the short run, some of this has actually increased volatility, we are convinced that our efforts – consistently applied – will succeed. However, we caution our shareholders not to expect immediate results.

Interest rate exposure is another area in which financial services companies can assume excess risk – often at great peril. As with underwriting credit, good analysis of interest rate exposure is rooted in facts and evaluations that are based upon a variety of realistic assumptions and scenarios. We devote substantial resources to understanding how interest rate changes will affect our performance. This analysis should be – and will be – an ongoing process. We believe that our company has carefully managed its interest rate risk so that even dramatic moves in rates of several percentage points cannot alone damage the company.

A healthy liquidity profile is essential to the ongoing viability of any company, financial or otherwise. We use a variety of tools to maintain a strong liquidity position at the parent and subsidiary companies, including stress scenarios, collateral management and a conservative debt structure for

the company overall. We engage in a continual dialogue with major rating agencies, and we are focused on maintaining and improving our strong credit ratings.

Reputation and legal risk

The litigation costs in business are well known. We are intensely focused on ways to safeguard the firm's reputation and exposure. They include:

- Senior management endorsement of a code of conduct that all employees must sign and adhere to, as well as a commitment to provide appropriate training.
- A strong and independent compliance program that encourages employees to assist in surfacing compliance and ethical issues, and identifying money laundering and terrorist financing activities.
- A more robust due diligence process focused on securities underwriting transactions, where we have established centralized oversight of our processes and standards.
- A disciplined governance process to address conflicts and review transactions that may present conflicts that could harm the firm now or in the future.
- A productive and open dialogue with our regulators and an ongoing emphasis on staying alert to changes in regulatory standards.

We believe that these actions will mitigate our exposure, but we recognize, unfortunately, that they will not eliminate it. We have also implemented a disciplined process to continually review our liabilities and establish appropriate litigation reserves. While we make every effort to properly manage the company to reduce litigation and legal costs, we believe that our shareholders should assume that high legal costs will continue for the foreseeable future. They should be viewed, unfortunately, as simply a higher, permanent cost of doing business than in the past.

Operational and catastrophic risk

This year, we also made progress in strengthening our operational risk management programs. We have a consistent approach across all businesses for defining and aggregating

our exposure to potential operational loss. This approach helps us determine whether we will be adequately capitalized in the event of such a loss. In addition to carefully managing operational risk, we need to be prepared for unforeseen disasters. Catastrophic risk can take a variety of forms and significantly impair the performance and the operations of the company. We have formal disaster recovery and contingency plans in place. They worked well during Hurricane Katrina and the bombings in London, but we must continue to refine them as new risks appear.

Whatever the type of risk, the key point is that we try to have a comprehensive approach to managing it. This requires that the right people be in the right jobs and that there be clear accountability in each business for managing risk in addition to rigorous corporate oversight.

IV. Do we have the right people and the right compensation strategy?

At the end of the day, it all comes down to people. We have great people in this company. As I travel across the United States and around the world, I have become increasingly impressed with the talent and potential of our employees. Rarely can a company assemble this level of creative firepower and professional competence.

To maximize the collective strength of our people, we will need to work better as a team. Great teams are not great because they have star athletes. Great teams are great because the players have learned how to work together and focus their collective energy and talent on winning. We are in the early stages of building a great team.

The compensation cycle was difficult but productive this year. We are getting better at relating pay to performance. But there is still room for improvement. Increasingly, we also must orient ourselves to *absolute performance* against best-in-class targets, not simply improvement in performance. We want to be clear and truthful when we rate ourselves, and fair as well as effective when evaluating performance. Good performance goes beyond individual productivity to

include group, unit and company performance. Compensation is not an entitlement; it should reflect an individual's and a team's contribution to helping make this a great company. We want to be one of the best-paying companies – but only when we are one of the best-performing companies.

We also want our employees to feel and act like owners, which is why stock is an important part of our compensation plans. Today more than 120,000 employees own, or have an option to own, approximately 14% of shares in the company. Executive Committee members are required to retain 75% of their stock awards as long as they are with the company. And in general, stock options are awarded on a limited basis.

We continually review our benefits programs to assure that they are of value to employees and cost effective. For example, the company has excellent medical benefits programs, but we subsidize them more for lower-paid employees than we do for higher-paid employees. (I hope that this instills a sense of pride in our managers.)

In addition, we no longer match highly paid employees in their 401(k); they have adequate pensions. We do not offer perks to executives like club memberships, financial planning and leased cars. We are reducing excessive executive severance plans. But more importantly, we are paying our employees more. Our thinking is simple – less compensation through entitlements, more from performance. We *want* to pay more and let our employees spend what they earn as they see fit.

We need to constantly remind ourselves that the most important thing we can do for employees is to build a healthy, vibrant company that treats people with respect and creates opportunity. Morale is not based upon perks; morale builds from respect, growth, innovation and success; from establishing a true meritocracy; from the stock performing well; from customers liking to do business with us. A great company will provide people with competitive compensation, the opportunity to benefit as the company grows and a rewarding career path.

V. Are we a good corporate citizen?

JPMorgan Chase has been – and will continue to be – a good corporate citizen. It is vitally important and enormously gratifying to all of us. Our commitment to our communities is deep, broad and multifaceted. We strive to be a great place to work and do business, and our success allows us to give back to the neighborhoods and cities we serve.

In one sense, we view ourselves as a small business. If we were the neighborhood store, we would give kids summer jobs, sponsor local sports teams and support community-based organizations. We operate this way in many of our communities around the world, striving to be as supportive as we can in all the communities we serve.

We add value by focusing on issues that are universally important, including education and community development. We dedicate resources to develop signature programs that help communities overcome the challenges they face in these areas. We are morally, programmatically and institutionally committed to inclusiveness and diversity.

JPMorgan Chase contributes more than \$100 million annually to support local, national and international initiatives. Examples include:

- **Chase Early Emergent Leaders** in Arizona, where we are funding a leadership and training program, and providing technological assistance and training in literacy skills.
- **Corporation for Supportive Housing** in Ohio, where we are helping the homeless as well as individuals recovering from drug and alcohol addiction by giving them access to 300 units of affordable housing and providing them with the support they need to live independent, responsible and healthy lives.
- **South Bank Centre** in London, where we are supporting music and technology education that will help bring artistic programs to thousands of young people.
- **DonorsChoose** in Chicago, where we are participating in an effort that uses the Internet to connect donors nationwide with underserved classrooms. We are helping to expand this program for public schools in states affected by Hurricane Katrina.
- **StreetSquash** in New York City's Harlem neighborhood, where we are funding a community youth facility that will serve over 1,000 students through academic and athletic programs.
- **Wilmington Housing Partnership** in Delaware, where our support is helping develop over 300 affordable housing units in our local communities.

Our commitment to community involvement goes well beyond philanthropy. Across the country and around the world, we bring this commitment to life through a broad range of initiatives:

- **Community reinvestment.** We have received outstanding ratings under the Community Reinvestment Act. In the past two years, we have fulfilled \$140 billion of an \$800 billion, 10-year commitment in the United States to provide community-development loans and investments, small business loans and consumer mortgages for lower-income and minority households.
- **Community schools.** We support community schools, which cost-effectively provide students in low-income communities with access to a broad range of services, including academic, health and extracurricular activities. In Chicago, we are partnering with the civic community, nonprofit groups and the Chicago Public School system to bring this model to scale. To date, 120 schools (20%) have been converted into community schools.
- **Youth opportunity.** We provide scholarships and internships to the underprivileged through our Smart Start program in New York City, and intend to expand the program to Louisiana in 2006. In both the United States and the United Kingdom, we work to place outstanding students of color in summer intern positions through Sponsors for Educational Opportunity. We are also a significant contributor to UNCF.

- **Volunteerism.** Around the globe, employees build homes for people in need, work with children living in homeless shelters, collect food and gifts at holiday time, offer companionship to seniors, maintain our parks and provide relief to victims of disasters.
- **Workforce development.** We help homeless people, welfare recipients, individuals with disabilities, and low-wage workers move toward economic and family stability by supporting organizations like Project Match and the hiring of individuals through the Chicago-based Cara program.
- **Hurricane relief.** When Katrina struck the U.S. Gulf Coast, we tracked down our employees, guaranteed their jobs and provided funds to help them rebuild their lives. We offered programs and services to customers and communities, and let our competitors operate out of our branches.
- **Supporting employees serving in the military.** We recognize the hardships employees face when called to active duty. We are doing whatever we can to support them by providing paid military leave, continuing most benefits and ensuring their jobs are waiting for them when they come home. We do not want to add financial hardship to their great sacrifice.
- **Protecting the environment.** We have adopted a comprehensive policy that makes environmental awareness part of our business model. We have tackled environmental risk management and taken a leadership role to reduce greenhouse gas emissions. We are looking for ways to make our facilities more energy efficient and reduce the amount of paper we use.

Of all these worthwhile efforts, the ones I find most personally inspiring come from our employees. All over the world, JPMorgan Chase employees of every nationality, race and socioeconomic background give their time and put their resources where their hearts are. They consistently stand ready to support disaster relief around the world, whether for victims of hurricanes in Louisiana, earthquakes in Pakistan, floods in Mumbai or bombings in London. We take our role as global corporate citizen seriously and personally, and I hope that all of our employees are proud of the work we collectively do around the world.

In closing, our progress would not have been possible without tremendous dedication and talent at every level. Firstly, I want to thank Bill Harrison for his vision, leadership and great partnership. It has been an honor to work with him throughout this complex merger. The experience has been a rewarding one for me personally. Bill's openness, honesty, maturity and experience are a great inspiration to me. I look forward to his counsel and support in the future.

In addition, I thank our Board. Like this merger, our Board has come together in a very effective way, and has provided great advice and guidance to me and the management team.

Finally, I thank the employees of JPMorgan Chase for their amazing efforts in 2005. We have come a long way and are well on the road to realizing the vast potential of this company. An enormous amount of work remains, but I am confident that by working together, we will build the best financial services company in the world.



James Dimon
Chief Executive Officer

March 8, 2006