Host
Ilene Fiszel Bieler, Head of Fixed Income Investor Relations

Speakers
John Gerspach, Citi Chief Financial Officer
Eric Aboaf, Citi Treasurer

PRESENTATION

OPERATOR: Hello and welcome to Citi’s Fixed Income Investor Review with Chief Financial Officer, John Gerspach, and Treasurer, Eric Aboaf. Today's call will be hosted by Ilene Fiszel Bieler, Head of Fixed Income Investor Relations. We ask that you please hold all questions until the completion of the formal remarks, at which time you will be given instructions for the question-and-answer session. Also, as a reminder, this conference is being recorded today. If you have any objections please disconnect at this time. Ms. Fiszel Bieler, you may begin.

ILENE FISZEL BIELER: Thank you, Operator. Good morning and thank you all for joining us. On our call today, our CFO, John Gerspach, will speak first. Then, Eric Aboaf, our Treasurer, will take you through the Fixed Income investor presentation, which is available for download on our website, www.citigroup.com. Afterwards, we will be happy to take questions.

Before we get started, I would like to remind you that today's presentation may contain forward-looking statements, which are based on management's current expectations and are subject to uncertainty and changes in circumstances. Actual results and capital and other financial condition may differ materially from these statements due to a variety of factors, including the precautionary statements referenced in our discussion today and those included in our SEC filings, including without limitation the Risk Factors section of our 2011 Form 10-K. With that said, let me turn it over to John.

JOHN GERSPACH: Thank you, Ilene and good morning everyone. We're very pleased to be hosting our Fixed Income Investor Review this quarter. Today we're going to update you on our continued execution and progress in several areas, including the strength of our liquidity and balance sheet, as well as our management of each. Eric Aboaf is going to take you through some specifics on our strong balance sheet; our strong liquidity profile and capital position, as well as review our recent issuance activity and current funding plans for the remainder of the year. Before I turn it over to Eric, however, there are some key points from our third quarter earnings we announced last Monday that I would like to highlight to start us off here on slide one.

We reported earnings of $468 million for the third quarter of 2012. Excluding non-operating items, such as the loss on MSSB, CVA, and a tax benefit, net income was $3.3 billion. Our businesses gained momentum during the quarter, while the impact of Citi Holdings lessened. Loans and deposits increased, and in all three of our operating businesses, we had positive operating leverage for the third straight quarter. We also had positive operating leverage in Citigroup as a whole. We also made progress winding down Citi Holdings. Last month's price agreement on Morgan Stanley Smith Barney has given us more certainty on our exit. Citi Holdings assets were reduced by $20 billion in the quarter, and now total $171 billion, or 9% of our balance sheet. Holdings assets are down 31% from the end of the third quarter of last year. Citi remains highly liquid, with roughly $400 billion in unencumbered assets, primarily cash and government securities. And our Basel III Tier 1 Common Ratio increased to an estimated 8.6%, and is among the highest in the industry.

In the US, it would appear that the prospects for stronger economic growth are somewhat dependent on the resolution of the fiscal cliff. We continue to watch the housing market carefully, and have taken note of some recent indications that the market may be stabilizing. In Europe, the actions by policy makers appear to have set a path for preserving the Euro, but more needs to be done to create deeper market confidence for a better GDP picture. In the emerging markets, policymakers have been quick to act, and
we expect growth there to substantially keep outpacing the developed markets. In light of these factors, we will continue to manage our risk carefully, using the deep knowledge we have of the markets where we do business.

Turning to slide two, I’d like to re-emphasize some of our key earnings results from the third quarter. Revenues of $19.4 billion were up 3% from last year, while the operating expenses of $12.2 billion declined 2%, resulting in positive operating leverage for Citigroup in total. Credit costs of $2.7 billion were down 20% versus last year. Net credit losses of $4 billion were 12% lower than the prior year, including incremental mortgage charge-offs of approximately $635 million in Citi Holdings in the third quarter of this year. These incremental charge-offs were related to new OCC guidance regarding the treatment of mortgage loans where the borrower has gone through Chapter 7 bankruptcy. The vast majority of these charge-offs were related to loans which were current.

Substantially all of the incremental $635 million of charge-offs were offset by a related reserve release of approximately $600 million this quarter, and so the net impact on earnings was minimal. Excluding these incremental charge-offs, net credit losses would have been down 26% from last year, and the net reserve release in the third quarter would have been roughly $900 million, down from the $1.4 billion in the prior year. We earned $3.3 billion of net income in the third quarter, driven by revenue growth and a decline in both expenses and credit costs. Citigroup end of period loans grew 3% year-over-year to $658 billion, as loan growth in Citicorp continued to outpace the wind-down of Citi Holdings, and deposits grew 11% to $945 billion. And now, let me turn it over to Eric

ERIC ABOAF: Thank you, John. To start us out, I’d like to discuss our credit trends and the quality of our consumer and corporate portfolios. Turning to slide three, we show net credit losses in the loss reserves. Overall, net credit losses of $3.3 billion were 26% lower than prior year, excluding the incremental mortgage charge-offs of approximately $635 million in Citi Holdings in the third quarter, due to the new OCC regulatory guidance, which John just described. A significant portion of the incremental $635 million of charge-offs was offset by related reserve release this quarter, and so the net impact on earnings was minimal, as he just said. Excluding this adjustment, the net reserve release in the third quarter was roughly $900 million, down from $1.4 billion in the prior year. Along the bottom of the slide, you can see that we ended the quarter with $25.9 billion of total loan loss reserves, or approximately 4% of loans. And on the right side, both corporate and consumer credit have continued to improve.

Turning to slide four, I’d like to take you through the credit trends in our consumer portfolios globally, so that you can see how our geographically diverse portfolios have performed over time, and how they are performing today. On the top, we show credit trends from their peak during the crisis through to today. You can see that the net credit losses peaked at different periods in each region, starting with Asia in the second quarter of 2009, and ending with the US in mid-2010. In the most recent quarter, our total consumer credit losses fell to 2.83% of the portfolio, which reflects the high quality of our loans. On the bottom of the page, you can see a similar trend in 90-day delinquencies, which tend to be a leading indicator of performance. 90-day delinquencies peaked in the first half of 2009 in our international markets, as well as in the U.S., and have been trending well since. Obviously, credit losses vary by portfolio and need to be thought of in the context of yield and spread in each geography, as well as the prevailing interest rates in each country. We show a comparison of that at the top right.

To give you some additional texture around our consumer portfolios, on slide five, we show loan balances and credit trends in a number of our key countries. In our consumer business, we operate 4,600 branches in 40 countries, and we are also the leading global cards issuer. You can see on the page that, with the exception of the United States, no country is more than 10% of the total, which exemplifies the geographic diversification of our portfolio. The credit quality in these international portfolios is not only good; in fact, in many of the countries where we do business, it’s even better that the U.S. Across this footprint, we are growing our consumer loans in a disciplined manner with a strategic focus on higher quality, multi-product households. We operate in markets which are expected to enjoy sustained higher GDP growth, even if some overall growth rates slow in the near term.
Moving to slide six, given our continued interest in mortgages by investors, I wanted to spend a moment reviewing our North America consumer mortgage portfolio. Starting on the top of the page, to be clear, we are including a summary of our North American Citicorp and Citi Holdings consumer mortgage portfolios together. You will recall that this portfolio is one-half to one-third smaller than that of major U.S. peers.

Credit trends remained favorable this quarter, with 90-day delinquencies declining from the last quarter. And we ended the quarter with $8.7 billion of loan loss reserves allocated to North America mortgage loans, which is almost double the amount of delinquencies that we had at the end of the quarter, which were $4.5 billion. You can see that we are well-reserved as compared to both NCLs and 90-day delinquencies on the page.

On slide seven, having covered consumer credit trends in some detail, let's take a look at our corporate loan portfolio. This slide shows you the trend in our corporate non-accrual loans as a percentage of corporate loans over time. As there is no industry standard for non-accrual loans, let me take a moment to define them for you here. Non-accrual loans are loans in which the borrower has fallen behind in interest payments or those loans for which Citi has determined that the payment of interest or principal is doubtful and therefore considered impaired. The amount of non-accrual loans as a percentage of corporate loans has decreased significantly from the peak in late 2009. And it is important to note that more than 40% of these non-accrual loans shown here are current, paying both principal and interest. Overall, this is a book that is well diversified by region and country, with no country outside the U.S. or U.K. greater than 5% of the overall loan portfolio. The vast majority of the book, or approximately three-quarters of the portfolio, is investment grade while the rest is largely BB and B credits.

Given the continued interest in GIIPS countries, we wanted to update you on our exposures on page eight. At the end of the third quarter, Citi’s gross funded credit exposures to GIIPS was $21.3 billion, up slightly from last quarter. Net of margin, collateral, and purchase credit protection, our net current funded exposure to GIIPS at the end of the third quarter was $9.5 billion, which was up slightly from the $8.4 billion last quarter. Unfunded commitments, which you can see in the appendix, are down $2.5 billion. While our net funded exposure was up slightly quarter-over-quarter, you can also see that the majority of our credit exposure in these countries is to corporates. These are our large, multinational clients, which are often rated higher than their host countries. Very importantly, since the end of the third quarter of 2011, we have decreased our net current funded credit exposure by approximately 40%, as we continue to carefully manage these exposures while serving our most important clients.

Turning to slide nine, looking at Citi Holdings, let me describe our progress in reducing the amount of these assets in general. Holdings total assets have declined by 79% from their peak in 2008 to $171 billion, and now stand at approximately 9% of our balance sheet. The $20 billion reduction in the third quarter included a $12 billion decline in assets related to Morgan Stanley Smith Barney, $4 billion of other asset sales, $3 billion of net paydowns, and roughly $1 billion of cost of credit. This slide shows you the key businesses within Citi Holdings where those reductions occurred. Importantly, the two largest components of Citi Holdings, the Special Asset Pool and Local Consumer Lending, are down 38% and 24% respectively from the third quarter of 2011. And as I just mentioned, our Local Consumer Lending U.S. mortgage business is a fraction of the size of that of large U.S. peers. Clearly, we are continuing to make significant progress executing on our Citi Holdings asset reduction strategy. However, as we have stated, the Holdings wind-down is likely to continue, though at a slower pace than the third quarter.

Now to slide 10, let me describe how we are managing the balance sheet for the current environment and investing to grow the Citicorp businesses. On the left, you see assets for Citicorp and Corp/Other, which are up 4% year-over-year, as we continue to expand our franchise and deploy our balance sheet to support our customers. For example, net loans, which is our largest asset category, is up approximately $57 billion year-over-year, and approximately $10 billion quarter-over-quarter, as we continue to lend to both consumer and corporate clients in a disciplined manner. And this quarter, trading assets are up slightly, largely in response to customer flows in our fixed income businesses around the world. As you
know, we had a strong quarter in rates and currencies, as well as higher revenues in credit-related and securitized products, and that was achieved without significant balance sheet expansion and without increases to VaR, as you can see in the appendix. On the right, you see Citi Holdings assets, which are down 31% year-over-year, as the wind-down continues to free up capital.

Turning to slide 11, given our strong balance sheet, we have been deploying capital in our Citicorp lending businesses in a disciplined manner, as I just mentioned. So let me describe what we are seeing in terms of loan volumes. In Citicorp, loans grew to $537 billion, or up 11% year-over-year and approximately 2% quarter-over-quarter. Lending in our institutional businesses was up 19% year-over-year, both on a reported basis and adjusted for FX. Lending increased 31% in Transaction Services from the prior year, driven by trade finance in Asia, Latin America, and EMEA. And we saw 15% growth in our Securities and Banking corporate loan book, which increased borrowing across most client segments in most regions. International Consumer Banking loan volumes increased 7% year-over-year, adjusted for FX, led by growth in Asia, EMEA, and Latin America. These trends reflect the varied economic growth in these regions. North America Consumer loan volumes remained flat year-over-year and quarter-over-quarter, as the cards market continues to reflect both consumer deleveraging as well as other regulatory changes.

Now to slide 12. Having just discussed the asset side of the balance sheet, and loans in particular, let's turn to liabilities and spend a moment looking at deposits which serve as our primary source of funding. This page shows our deposit growth by business on an average basis, with the end of period amounts along the bottom. Similar to our trends in loans, deposits also increased. Year-over-year, average deposits were up 7% or 10% adjusted for FX. Deposits grew across all three of our main businesses, with 13% growth in Transaction Services. While more and more clients are drawn by our transactional banking offering and see us as a flight-to-quality during an uncertain economic environment, we also experienced approximately $10 to $15 billion in episodic deposits at the end of the quarter, which is not unusual. We would not expect those deposits to remain, and would be fine either way. Further, in the fourth quarter, we expect approximately $4 billion in deposits to be transferred to Morgan Stanley as part of our agreement. Deposit funding costs continue to decline in sync with prevailing interest rates, bringing our average cost of deposits to a new low of 70 basis points. Our business model continues to deliver lower price points, notwithstanding that we are seeing competitors selectively bidding up deposit rates to secure funding.

On slide 13, I wanted to show you how some of the balance sheet activity that we just reviewed is impacting our net interest margin. This quarter we saw NIM increase. Let me give you some context. We and many other banks continue to see pressure on loan yields and investment portfolio yields, given the low rate environment. That said, in the third quarter, this was offset as we continue to pay down higher cost long-term debt, which is a positive impact on NIM, and this quarter we redeemed three of our outstanding trust preferred securities. And we have had the ability to continue to reduce deposit costs both in the U.S. and in high interest rate international markets, given our international reach. All of these factors were largely taken into account in our NIM guidance.

Looking forward, absent any other significant changes, our NIM will likely continue to reflect the pressure of a low interest rate environment. We'll likely see some offset to that by continued improvement in our cost of funds. As a result of all those factors, we are likely to see some reduction of our NIM in the fourth quarter, probably down a couple basis points from where we are this quarter.

Moving to slide 14, let's review Citi's liquidity and funding strategy, which has been a cornerstone of strength for some time. Our strategy is designed to provide ample, high quality liquidity to make sure that we are well-positioned to grow our core businesses and navigate various market conditions. In both the Bank and Non-Bank, we carry a healthy liquidity buffer, which is generally held in cash and highly liquid securities, such as Treasuries and Agencies and other G7 instruments. We execute on this funding strategy in both our Bank and Non-Bank businesses by accessing a spectrum of funding sources. In our Bank businesses, our funding is primarily in the form of stable, diversified deposits from around the world,
which I discussed earlier and will discuss more in a minute. In our Non-Bank businesses, we use a modest amount of short-term funding, such as repo, to finance liquid assets. We then use a range of long-term debt instruments to cover our broader business needs.

On slide 15, you can see the size of our liquidity buffer, which is defined as cash and highly liquid securities. It stood at approximately $404 billion at the end of the third quarter. This quarter, our high level Bank liquidity has increased due to increased deposit flows, which I just discussed. At the same time, our Non-Bank liquidity, which supports our Broker-Dealer, decreased as we consciously used cash to pay down long-term debt. As you know, we continue to focus on liability management and lowering our cost of funds. Our liquidity buffer in the Non-Bank was a healthy $78 billion at the end of the third quarter, as measured by our internal risk metrics and stress tests. We expect to manage our excess liquidity to somewhat below $400 billion as we continue to pay down our long-term debt. Obviously, we will take market conditions into account, as always.

Moving to slide 16, having discussed the size of our liquidity buffer, let me take a moment to talk to you about our conservative liquidity pool. As you can see on this page, the liquidity pool is conservatively invested primarily in cash; government securities, including U.S. Agency debt and U.S. Agency mortgage-backed securities; and a certain amount of highly rated investment-grade credit. Foreign government securities that we hold are largely in support of our local liquidity requirements and our local deposit franchises. At this time, we expect the portfolio may fluctuate some in size and expect only modest changes in asset allocation.

Our funding strategy has served us well over the last few years and has prepared us to meet the proposed Basel III liquidity requirements ahead of schedule, as we show on slide 17. The Basel III Liquidity Coverage Ratio, or LCR, is designed to ensure banks maintain an adequate level of unencumbered cash and liquid securities to meet liquidity needs under an acute 30-day stress scenario. The LCR calculation includes highly liquid unencumbered government and government-backed securities, as well as unencumbered cash in the numerator, and net outflows in the denominator. The net outflows are calculated by applying an assumed outflow factor, which is prescribed in regulatory guidance to various categories of liabilities such as deposits, unsecured and secured wholesale borrowings, as well as to unused commitments. As you are aware, the proposed minimum requirement for the LCR is 100%.

The Basel Committee recently disclosed results from its quantitative impact study exercise, which was conducted in the fourth quarter of last year. The weighted average LCR for the large Group 1 banks was 91%, while the European large bank average was 72%. However, within the large Group 1 banks, less than half of those institutions currently meet or exceed the LCR requirement. While we are still awaiting final guidance on the Basel III Liquidity Coverage Ratio, we believe that we are already comfortably in compliance, given the proposed rules as we understand them, with an estimated LCR ratio of approximately 116%. In keeping with our estimates regarding Citi’s excess liquidity, we currently expect that our LCR will decrease modestly as we manage to a level that is comfortably above the proposed 100% requirement.

Slide 18 shows the funding composition that we have for the Bank and Non-Bank. Citi has significantly shifted its funding mix over the last few years away from short-term sources, to deposits and long-term debt and equity. Most recently, in keeping with our liability management initiatives and continued focus on further reducing our cost of funds, we have shifted our funding profile to an even higher percentage of deposit funding. Within our Bank, we view our deposit base as our most stable and lowest cost funding source, and you can see that approximately 81% of our Bank is funded by deposits, compared to 76% as of the third quarter of 2011, and 72% at the third quarter of 2010. In the Non-Bank businesses, long-term debt represents the most significant component of our liability mix. The vast majority of this funding is comprised of senior term debt, along with subordinated instruments. While longer-term debt was lower over the course of the past year, so is the level of assets, especially illiquid assets it is meant to support. At the same time, equity has become a larger proportion of the balance sheet.
On slide 19, let me turn to long-term debt, which is the primary source of funding for our Broker-Dealer and parent. The top half of the page shows our long-term debt outstanding by category over time, including senior debt, remaining TLGP, and credit card securitizations. The bottom half of the page segments the amount of long-term debt in the Bank and Non-Bank entities. So the bottom is just another cut of the top to provide you with some further texture. As you can see here, our long-term debt outstanding has decreased year-over-year in most categories, as we have deleveraged the balance sheet and continued to lower our cost of funds. In the Bank, as I just mentioned, we have consciously reduced debt funding as we have grown our deposit base.

Looking at the Non-Bank at the bottom half of the page, long-term debt has decreased as we have let TLGP roll off while keeping a healthy amount of funding for our Broker-Dealer. As you can see here, we are revising down our long-term debt outstanding estimate for year-end 2012 to approximately $240 billion to $250 billion, as the last of the TLGP will mature.

Moving on to slide 20, this quarter we have updated this page to more clearly demonstrate our liability management initiatives in addition to our expected maturities and issuance activity. This chart clearly shows that the maturities peak in 2012 and come down in 2013. You can also see that we expect to execute approximately $17 billion in buybacks, tenders, and redemptions this year. In the first nine months of 2012, we had $13.5 billion of liability management actions, which consisted primarily of redemptions of trust preferred securities of $5.4 billion, as well as tenders and open market purchases of senior unsecured securities of $5.9 billion, and purchases of structured securities of $2.2 billion. Calling our trust preferred securities will benefit NIM by about $370 million per year, or approximately 2 basis points on a go-forward basis.

Year-to-date, we issued approximately $12.8 billion of long-term structural debt. We issued across multiple tenors in both benchmark and structured notes. We expect to issue approximately another $1 billion or $2 billion of long-term debt during 2012, given that we just issued $1.5 billion in preferred stock. You can also see that our liability management activities and lower issuance activity have resulted in net negative issuance in both 2011 and 2012, with net reductions in long-term debt of $36 billion and approximately $62 billion respectively.

On slide 21, I'd like to update you on our capital structure. Optimizing the components of capital, including stockholders' equity and other types of securities, continues to be important to us. You can see in the bar chart on the middle of the page how our qualifying regulatory capital breaks out by instruments. As of the end of the third quarter, we had qualifying Tier 1 Common of $124.2 billion, $10.4 billion of trust preferred securities, and approximately $300 million of preferred stock, as well as $18.8 billion of sub debt. In the third quarter, we redeemed three series of trust preferred securities, for a total of $5.4 billion. And as you can see on the right side of the page, just this week we priced $1.5 billion of preferreds, expected to close on October 29th, bringing our total outstanding preferred stock to $1.8 billion. It is generally expected that non-cumulative perpetual preferred stock will continue to qualify as Tier 1 Capital under the proposed U.S. Basel III capital rules. In general, we will consider various factors when evaluating whether and when to redeem each of our remaining trust preferred securities, including aspects such as coupon, currency, market conditions, and the call features of those securities. This is also true in terms of possibly issuing preferreds.

So, turning to slide 22, let me talk about capital, which continues to be an area of significant strength for us and supports the lending growth that I described. Our Basel I Tier 1 Common capital stands at $124 billion, and our Basel I total capital is $167 billion. At the end of the third quarter, our Basel 1 Tier 1 Common ratio was 12.7%, significantly up from a year ago and flat to the second quarter. Adjusting for the final market risk rules recently adopted by the U.S. regulators that will be effective in January 2013, our Basel I Tier 1 Common ratio would be approximately 11.5%. You can also see that under Basel III, our estimated Tier 1 Common ratio as of the third quarter was 8.6%, up from 7.9% in the second quarter. More than half the increase was driven by our operating earnings. Roughly 17 basis points came from the Morgan Stanley Smith Barney transaction. Roughly 7 basis points was due to lower risk-weighted assets,
and the remainder was driven by changes in other comprehensive income and other items. Our capital base is one of the strongest in the industry, both as compared to U.S. and international banking peers.

Moving to our last slide, let me summarize four major points. First, while the environment remains uncertain, we saw continued strength in our core lending and deposit-taking businesses and good performance in our markets businesses. Second, our capital base continues to be one of the strongest in the industry, and this is reflected across every one of our significant capital ratios, including Basel III. Third, we continue to have a highly liquid balance sheet and robust structural liquidity. Our estimated Liquidity Coverage Ratio is approximately 116%, which is comfortably above the estimated industry average and the proposed required minimum. Fourth, we will have a significantly lower proportion of wholesale funding going forward. We currently have modest long-term debt issuance plans and have been consistently executing on our liability management initiatives. Thus, we expect that our long-term debt outstanding will continue to decline. That concludes our fixed income review. John and I will be happy to take your questions.

OPERATOR: (Instructions). We'll hear first from Ryan O'Connell, Morgan Stanley Investment Management. Please go ahead.

RYAN O'CONNELL: I just wanted to clarify something because there was a fair amount of discussion on the earnings conference call and I've seen this in some equity reports, and this is really about the idea that given the recent management change that Citi might somehow accelerate the disposal of Citi Holdings assets. I think we all recognize that it's really the mortgages that would be the focus here. As you pointed out, you've got large reserves against that book so I assume that you could sell the mortgages without taking a large hit to the capital, so that's not the issue. But I think, John, what you said on the conference call is that there just aren't buyers for that sort of scale out there and I just want to make sure that my understanding is correct and that's a real obstacle, and 2) that therefore we really shouldn't expect a large reduction in the mortgage portfolio any time soon.

GERSPACH: Let's try to parse through what we have. We've been focused on winding down Holdings now for I guess going on four years and from the outset, we said we're going to do it in an economically rational fashion, and that has been our approach. And so as we look at every asset sale, we look at it not just on the face of is it a gain or a loss, but what's the impact from a capital point of view, and certainly in the last two years we've shifted over to looking at the impact on Basel III capital. So we're very focused on making sure that we measure very carefully every sale as far as its impact on our capital base.

Having said that, a lot of the discussion in the [earnings] call, and don't forget, the investor call was before we had the announcement of the change in CEOs, that really came about more as, okay, with the existing market, what are the prospects for advancing sales of the assets. And there, the issue is one of liquidity and funding. So let's separate those two things. There is a lot of liquidity in the market. There's no doubt about that. When you're going through, to think about doing large bulk sales of the mortgages, the whole loans that we have in Holdings, that is a matter of funding. How can someone put together enough funding to carry that portfolio for a period of time? So regardless of whether or not we have adequate reserves for that portfolio -- and let me assure you, we do have adequate reserves for that portfolio -- it's really a matter of what's the cost of our funding versus what the cost of someone else's funding would be and there we clearly have a funding advantage. And so it's -- I don't want to leave you with the impression that we could dispose of large pieces of that mortgage portfolio by merely saying well, I'll just take the $8.5 billion of reserves that I currently have, mark that against my carrying cost of the loans of $95 billion, and someone's going to appear out of the blue with a check for $86.5 billion, and we'll just walk away, you know, everybody happy. That's just not the way the economics work out. We can fund that portfolio through -- as Eric I think laid out -- a rather robust funding base including $945 billion of deposits. It's not likely that a third party purchaser would be able to produce that amount of funding. That's where a lot of the discussions would clearly lie.
Given all that, now that I've given you a rather long answer to your question, I don't anticipate that you're going to see a rush to push this portfolio out. The economics just don't seem to lead to that type of conclusion. So I apologize for the long-winded answer to your succinct question.

RYAN O'CONNELL: Okay, thanks. And I promise my second question will be short. That's very helpful. The recent issuance of the perpetual preferred, I understand that's part of Tier 1, but you've already got really robust Common Tier 1 ratios, so maybe you could walk us through your thought process as why you decide to do that?

JOHN GERSPACH: Yeah. Well, don't forget, at 8.6%, there's no doubt that we've got robust Basel III Tier 1 Common and certainly from a Basel I point of view, at 12.7% Tier 1 Common's not an issue under that either. However, we've got the reality that under both Basel III and specifically under Dodd-Frank – the Collins Amendment to Dodd-Frank – the trust preferreds begin to phase out over a period of time as counting towards Tier 1. And so you've got the calendar facing you that Collins Amendment is going to come in; that's going to knock out the trust preferreds from being counted as Tier 1 capital under Basel III. You've got Basel III that does require that above whatever you have as a Tier 1 Common requirement, there's some element of Non-Common that you're going to have to carry, maybe as much as 150 basis points, and so over a period of years we felt that we need to bridge that gap between where we are today with, in effect, zero of preferred, to where we need to get out by maybe 2015 or so. So given the extended time frame, given that set of facts, we felt that in the current market conditions, being able to do $1.5 billion issuance of preferred at a fairly attractive coupon was a nice first step.

RYAN O'CONNELL: That's very clear. Thanks very much.

JOHN GERSPACH: Not a problem.

OPERATOR: We'll take our next question from David Knutson with Legal and General. Please go ahead.

DAVID KNUTSON: Hi, good morning. With Pandit's departure, is there any change to what you've laid out in terms of your liquidity, capital, and funding needs? I know that you've detailed where you expect to be for at the end of next quarter, the fourth quarter, but what about some of the more longer-term strategic goals? Have there been any changes due to the departure?

JOHN GERSPACH: That's a good question there, David. As Corbat said on the investor call that we had – I guess it was last week now – I think he was fairly clear. I thought Michael basically said very strongly that there's not going to be any change in the strategic direction of Citi. And I think he further emphasized that he believed it was the right strategic direction. So, no change in the strategic direction. Now, Michael obviously comes in with his own way of conducting operations. He's going to, I think as he said, immerse himself in the businesses. He's going to obviously be heavily involved in the planning process as we build towards the 2013 budget, the 2013 CCAR process, etc. We'll see what changes there. But I don't anticipate any significant changes in any of the goals that we had previously set out.

DAVID KNUTSON: So S&P recently published an update on their estimates on the cost of Volcker. And what the they said in my mind, they seemed to indicate that this is going to be a process that will take time to implement. S&P right now has Citi at “A-/Negative”. Does this extend the time frame that they will maintain the negative outlook, or how did you interpret that, the article they published?

JOHN GERSPACH: I'm always fascinated by people that can put together estimates of what the cost of Volcker is going to be since we don't know what the Volcker rule is actually going to be. So how you put together an estimate based upon what you're estimating the final language to be – that's just a series of conjectures that I'm just not willing to participate in, to be honest with you. I think we're all looking to see where we come to final grips on the language in Volcker – how you define market-making versus proprietary trading. And that still is, I think, the biggest issue and I'm not quite sure that we're any closer to reaching a final decision on that.
ERIC ABOAF: David, it's Eric. We haven't gotten any indications one way or another from S&P after the piece and I think if you took a good read of it, they also indicated that there are others whose business models are more affected likely by Volcker than ours.

DAVID KNUTSON: Can you give us an idea of how much the cost of Volcker has already been incurred by Citi? Are you halfway through what you expect to ultimately be the cost of implementing a reduced proprietary trading, some of the other things that Volcker suggests?

JOHN GERSPACH: I think we were pretty clear on some of the earnings calls we had earlier this year and later last year. We don't have any proprietary trading businesses left.

DAVID KNUTSON: You mentioned, I can't remember which slide it is, but you talked about the total value of debt redemptions this year. You've done $13.5 billion. I think you mentioned that you were looking to do $17 billion total. Does that mean that we should expect around $3.5 billion that will occur during this fourth quarter?

ERIC ABOAF: David, it's Eric. Yeah, that math is pretty good. I think you've seen us do a series of liability management actions this year, the largest of which was the $5.5 billion of trust preferreds that we redeemed. I think putting those aside, we've been averaging $2 to $3.5 billion of buybacks of senior debt each quarter and so the calculation you're doing is about right. It's the $17 is kind of the rough full-year projection, give or take a bit, and we've done $13.5 so far.

DAVID KNUTSON: The change in the OCC's rule on provisioning, can you tell us how many second liens are current behind delinquent first liens?

JOHN GERSPACH: In the entire portfolio, David?

DAVID KNUTSON: Sure. I don't know….

JOHN GERSPACH: I'm trying to figure out. I don't have the entire mortgage portfolio broken out in front of me. What are you really trying to get to?

DAVID KNUTSON: What I'm trying to get to, we heard a lot since the crisis came out that people continue to pay on their second liens even if their first lien was in default, and now it seems to me that this rule change speaks to that and so I'm curious, of the second liens that are current, are there 20% of first liens in front of them that are delinquent, or is it 5%, or is it 80%, or something of that nature?

JOHN GERSPACH: I don't have those factors in front of me, but most of the impact of the OCC guidance was actually on our first mortgages, not on the seconds.

DAVID KNUTSON: Okay.

JOHN GERSPACH: I'm sorry. No, I'm sorry. It was on seconds. I don't have the figures in front of me, David, so I really can't answer your question. Maybe if you give Ilene a call in Investor Relations, she can help.

DAVID KNUTSON: Okay. Thanks very much, guys.

OPERATOR: Operator. We'll hear next from David Macgown with Morgan Stanley.

DAVID MACGOWN: Good morning, guys. I think it was Eric who mentioned that the balance sheet is growing and Corp is growing faster than holdings is running off. In light of that and some potential
changes in how regulation develops over the next couple years, could you comment on your ability to continue to reduce your long-term debt footprint? That's my first question.

ERIC ABOAF: David, it's Eric. I think you're seeing a number of different factors that are shaping the balance sheet over the last quarter, but it's also good to take a look and be familiar with the full balance sheet trend. Citicorp is up primarily because we had quite a bit of growth in deposits, and what we're effectively doing is putting that to work either in loans, which is a traditional place, or if they happen to be deposits which fluctuate at quarter end, they end up in cash or in securities. And that's really the immediate driver of the change. I think if you actually look back at page 10 and if you look at the broader data in the balance sheet in the supplement or in the appendix here, you'll see a modest growth in Citicorp and all that can be funded pretty easily. I think if you go one level down in your question, I think what you're effectively asking is how do you fund the various vehicles, the Bank versus the Non-Bank and if you actually turn to slide 18, what you're seeing is that more of the growth that we're seeing is on the Bank side of the balance sheet and that Bank balance sheet can be readily funded with deposits, whether it's Consumer deposits or Transaction Services deposits which are in abundance. Especially with the liquidity available in the marketplace and the offering that we have in our various businesses. In contrast, in the middle of the page on 18 you actually see some of the Non Bank activities actually trending down. Why? Because the core business is pretty stable. Holdings is coming down and so the net has been floating down over the last couple years and that's the piece that needs to be funded with a slug of long-term debt plus equity, plus some of the other financing sources. And so in effect, I think as the balance sheet continues to take shape and we don't expect material growth in the Non-Bank, there's probably some room for long-term debt to continue to trend downward.

DAVID MACGOWN: Appreciate it, Eric. John, I'm not going to ask you to comment on Volcker costs but as you guys have been thinking about preparing for whatever the rules are as they come out, do you have a sense for how much work you think you have to do on systems and infrastructure to get ready for that, and how long it might take you to get there?

JOHN GERSPACH: We've been working that for some time now and I think we're in relatively good shape. Again, until you see the final rule, you're never quite sure. I'm cautious by nature, so I don't want to tell you that we're almost all the way there because, again, I'm not quite sure what the final rule is going to require. Obviously, there's a lot of reporting elements that are out there and we expect to be able to meet the reporting requirements. So again, I think we're well on our way and we'll just have to see how the final rule ends up actually being drafted.

DAVID MACGOWN: Thanks, guys.

OPERATOR: We'll take our next question from Robert Smalley, UBS.

ROBERT SMALLEY: Hi. Good morning. Three questions. First on slide 21. In the bar 3Q'12, you also note Tier 2 capital of $31.2 billion, and in the footnote you talk about including a portion of credit losses, $12.4 billion, not shown on the chart. So your total loan loss reserves are about $25.9 billion, if I'm right. So close to half of this is allowed as Tier 2?

JOHN GERSPACH: I believe that's correct, yes.

ROBERT SMALLEY: Okay. So in designating it this way, does this in any way inhibit your ability to release more reserves down the road and could you talk about how this designation takes place, how you count it as one and the other?

JOHN GERSPACH: It's not that we choose a designation. This is a calculation. So it's not that we're designating a portion of the loan loss reserves as Tier 2. It's just the way the calculus works that it becomes Tier 2. You follow the regulatory rules and that leads you to a result.
ROBERT SMALLEY: Okay.

JOHN GERSPACH: But that calculation doesn't change in any way your ability, or your requirement then to assess the adequacy of your reserves and whether you need to either add to or allow the reserves to run off.

ROBERT SMALLEY: Okay. And I'm assuming this is all at the Bank level, the reserves are kept at the bank level and when I look over at the subordinated debt of $18.8, that's primarily Bank level as well?

ERIC ABOAF: It's Eric. The reserves for the loans typically are booked in the vehicle in which those loans exist, right, so those would typically be in the Bank. If you think about the sub debt that you have on page 21, as well as the TruPS and the preferreds, those are typically issued at the Holding Company from a vehicle perspective.

ROBERT SMALLEY: Okay. One of the places I'm trying to get at is if you would need subordinated debt in the next couple of quarters and would it be at the Holding Company or at the Bank?

ERIC ABOAF: At this point the binding constraint on us like many institutions around having the sub debt at the Holding Company. What we call the Non-Common Tier 1 capital at the Holding Company and kind of as we laid out here, and as John said, under Basel III there are needs for each one of those components of capital. There's 1.5 points that eventually will be needed for Non-Common Tier 1 capital under Basel III so that would be primarily made up of the preferreds over time and that's 2019. And there's 2 points that are specified as part of the Tier 2 capital under Basel III. Again, that has several components, both a sub debt and a portion of the reserves and we can go through that calculation in detail – Ilene can do that with you for us and how it generally works. And that again is 2 points and again in 2019.

ROBERT SMALLEY: Okay. Turning to slide 16. Your increase in cash up about $16 billion, decrease in foreign government outstandings here in the liquidity pool. So it looks like you sold them down. How much was that in European government debt, was it peripheral versus core? And could you give us an idea of the $120 billion, how much of that is necessary for lack of a better term for in-country liquidity, that you need assets against the deposits that you have in-country that you want to keep in-country, versus how much of that is discretionary buying of European government debt?

ERIC ABOAF: Rob, it's Eric. I think there are four or five questions in there so let me hit a couple of them and why don't you come back with clarification.

ROBERT SMALLEY: Sure.

ERIC ABOAF: On page 16 there's a number of different factors that influence what this liquidity pool looked like each quarter. The cash is higher largely because some of the deposits came in a little heavier at the end of the quarter, as I talked about. Those tend to be deposits in dollars and so the natural place for them is in the cash account from a kind of management standpoint. I think at the same time you saw some continued lending in select international geographies and so as we deploy our liquidity from cash and securities into loans, then the foreign government balances will float down and that's literally what you saw. And given how liquid we are in a number of these international geographies, that's exactly what happened. With regard to the mix of foreign government securities, we are almost rigid or religious in the kinds of assets we would consider as highly liquid, right. So in Europe, that's not a very large group. There's assets in Sterling, there are German government bonds and very little else, to be honest, and in fact we have for better part of at least a year, if not longer, I'd have to go back, we purposefully excluded any peripheral governments, not that we owned very many, as part of the liquidity pool as part of our disciplined approach to liquidity management.
ROBERT SMALLEY: Thanks for all of that. And can we assume of the $120 billion that is overwhelmingly the result of deposits in those countries that you’re looking to match up with an asset, while you’re looking for lending or other type of higher-yielding opportunities as opposed to a more Treasury-oriented operation where you’re just looking at buying sovereign debt?

ERIC ABOAF: Rob, absolutely. Those are literally the result of our local deposit franchises, net of the loans. So we operate in countries around the world, Singapore, Hong Kong, London – you can go all the way around the world. We've got more deposits than loans in just about every geography. That's how we have to run each of those countries or geographies. And the surplus sits in the local government bonds. So they are literally the result of the classic banking activity. We don't explicitly try to take foreign exchange risk of convert from one currency to the other. We have a natural match position in each of these geographies and countries, and we keep it that way.

ROBERT SMALLEY: Okay. Thanks, Eric. Thanks, John.

OPERATOR: Our next question comes from James Campbell with Calpers.

JOHN CAMPBELL: Thanks, John, thanks, Eric. My question actually had to do with the recent Orderly Liquidation Authority guidelines that the FDIC has been discussing, specifically for your U.S. banking subsidiary. My question was if that rule has had any impact on your decisions to issue debt out of your U.S. bank subsidiary? I understand that you said earlier, Eric, that there's going to be some long-term debt in that bank subsidiary just as a matter of course, but was just curious what if any impact there was as a result of this OLA authority being flushed out in more detail.

ERIC ABOAF: Yeah, it's Eric. We're at the early stages of understanding how the OLA authority and Title II will work. Obviously the agencies are exploring that. They've been talking with U.S. market participants and exploring that. But it's really early stages and it's pretty unknown what it's going to look like. The unknowns include some of what you touched upon – how much long-term debt, is it long-term debt plus equity as a percentage of assets, is it a ratio of long-term debt to equity? There's uncertainty there on kind of type and amount. There are big uncertainties as to in which vehicle; so far it seems like it's about long-term debt the Holding Company, but long-term debt at the Bank counts. We don't have very much in the bank; we typically issue out of the Holding Company. That's not any real indication there. So there is quite a bit of uncertainty. I think what we've been doing is keeping tabs on the development. We've been in touch obviously with all the regulators and we'll look for either rule-making or guidance but we don't expect any in the immediate future. But we'll see. I think what we have been conscious of is that we do want healthy amounts of long-term debt and equity to support our franchise. Right now, the total of long-term debt and equity is about 24% of the balance sheet, if you just go through the numbers and it's actually several percentage points above a number of our U.S. peers, and so we're also keeping tabs on what others do. But I think we'll learn more probably over some period of time.

JAMES CAMPBELL: Great. Thank you.

OPERATOR: Our next question comes from Samuel Crawford with Stone Harbor.

SAMUEL CRAWFORD: Two questions. One is on the selection of Mr. Corbat. If I understand his CV correctly there's a lot of corporate banking and even deeper core perhaps in areas that are thought of conventionally as investment banking. Is there much in his background that I'm not aware of that directly addresses retail banking? Is there any deep experience there that I'm not aware of?

JOHN GERSPACH: Samuel, this is John. If you look at -- I think we published Michael's CV. Obviously, the years that he spent running Holdings, certainly a large piece of what was in Holdings had to do with consumer businesses, both domestically as well as overseas. And so Michael, certainly, over those years developed quite a deep understanding of all the consumer businesses in which we operate, both retail as well as card products, mortgages. So I'd say that Michael has got a rather well-developed background in
both the consumer businesses that we run; he's got a well-developed background certainly in the institutional businesses that we have; he's got breadth of geography as well. So I think it's a CV that's particularly well-suited for his current role.

**SAMUEL CRAWFORD:** Okay. Different question. Some of the equity analysis that has come out over the last less than a week, I suppose, tends to arrive at the conclusion that Citigroup should be broken up because of the conglomerate discount, etc etc. It's the sort of reasoning that I imagine you all may not have a whole lot of patience for. The question I have is do you all find some of the parts sufficiently valuable that it is an exercise that management and the Board run through on a periodic basis to examine this question, regardless of whether you agree with the kind of analysis that's been put out in the public domain by the equity sell-side?

**JOHN GERSPACH:** Actually, Samuel, I'm not familiar with any of equity analysis that you're referring to. I've seen newspaper articles but I don't confuse newspaper articles with equity or any other type of in-depth analysis. But there certainly has been some re-hashing in the press about that. However, we look at strategic options broadly on a regular basis.

**SAMUEL CRAWFORD:** Not quite the same thing.

**JOHN GERSPACH:** Then perhaps I don't understand your question.

**SAMUEL CRAWFORD:** Do you all find some of the analysis useful in terms of arriving at an internal evaluation at Citigroup? And whether or not there is a conglomerate discount, or a conglomerate premium?

**JOHN GERSPACH:** I'm sorry, I thought I addressed that by saying that I haven't seen any of the analysis that you're referring to. All I've seen is articles in the newspaper or in other areas of the media. Those types of articles don't really have any analytical basis behind them. So I wouldn't find the media articles to necessarily be terribly informative.

**SAMUEL CRAWFORD:** Right, thank you.

**OPERATOR:** And our final question today will come from David Jiang with Prudential.

**DAVID JIANG:** Hi, guys. This question's for Eric. On slide 20 on the maturity and issuance page, the year-to-date issuance of $12.8 billion, is that all kind of vanilla long-term debt? Or does that include some of the structured issuance as well?

**ERIC ABOAF:** It's Eric. The $12.8 there is both of those together. We're trying to give you guys visibility into our primary unsecured issuances. It's a mix of the benchmark, kind of more plain vanilla as well as structured debt. It tends to be two-thirds, three-quarters of vanilla and secured but it varies. It varies based on market conditions. It varies based on demand. I think more broadly I've said in the past we end up also looking at different tenor points, currencies and so on and so forth in determining that issuance.

**DAVID JIANG:** Got you. The soft target is $16 billion for year-end? Is that assuming another 3 billion to come? I think you might have mentioned about potentially another $1 billion in the fourth quarter.

**ERIC ABOAF:** I said $16 billion for the full year. So we've already done the $12.8 that you see here. The preferred that we issued, the $1.5 billion preferred also has kind of debt characteristics. I can use that as long-term funding. So you've got to count that. And I think that leaves us after the $12.8 plus the $1.5 of preferred, it might leave us a billion or two, obviously depending on market conditions and how the picture looks outside.
DAVID JIANG: Got you. And then given kind of the state of your debt footprint, looking forward into next year, do we expect the same type of kind of negative net issuance in 2013 that we've seen the last few years?

ERIC ABOAF: I'm not ready to give detailed guidance for next year. We tend to do that annually in the January timeframe, and certainly we'll come back with that. I think if you just want to think about it broadly at this point, clearly looking at page 20 we've had two years of very large maturities that you can see on the page – $50 billion, $78 billion. Looking into next year, we go back to the more normal pattern of $25-$26 billion of scheduled maturities. So that will clearly be a different environment. I think at the same time we've also been pretty consistent over the last two years issuing $15-$20 billion. We usually give a range. We've ended up being at the low end of that range, both years, and I think in line with John's comments earlier, we're sticking to our strategy and I think you can expect consistency in how we manage the balance sheet and not big departures one way or the other.

DAVID JIANG: All right. On the following slide, on the capital structure slide, there's $1.8 billion of preferreds. I think you talked about getting to a point and-a-half of risk-weighted assets in the preferred bucket. That could be quite a large number and I know you have a runway to do that. How do you guys think about how to fill that bucket over time and given that the cost of preferreds are back to almost pre-crisis levels.

ERIC ABOAF: I think we think about it carefully, but there's a lot of judgment that's at stake and we also would know that pacing ourselves is probably a good general approach. I think as John mentioned earlier on, the trust preferreds come down in value based on the Collins Amendment that starts in 2013. Each year they trend down by about a third, and so there's roll-off there; that's one way to think about it. On the other hand, preferreds aren't inexpensive, so you don't want to rush in and do a bunch. And the other bookend is that Basel III requires preferreds at the 1% then eventually 1.5% level by 2019, right? So I've got five or six years to build up.

And so you have to look at it from the roll-off, the eventual need, we're going to pace ourselves, and obviously be opportunistic. We saw some good markets over the last week. Obviously, the last day or two have been a little clunky out there, but it was a good time to go. We thought we could print a good coupon. We're very pleased with the results. We think investor demand is, I think it was noted was we had a very, very large book. I think I was a book that was five times oversubscribed or something for a new security we haven't issued in a long time. We were very, very pleased. And obviously, we'll continue to think through and selectively tap the market. But we'll pace ourselves on this one.

DAVID JIANG: And that has to be all part of the CCAR submission, right, in terms of your preferred issuance?

ERIC ABOAF: Yes. Capital in general, right, whether it's issuances, whether its redemptions, whether its Tier 1, whether its Tier 2, whether its preferreds, whether its dividends or buybacks or issuances, all this is part of the annual CCAR process as well as whatever other processes occur mid-year. So it's all part of the ongoing management structure.

DAVID JIANG: Got you, and one last question. It's more of an operating question. Just on page 27, in the International consumer unit, you've had several quarters of operating leverage in EMEA, still negative operating leverage in Asia. Like what are you seeing in Europe? Are you seeing any signs of a slowdown?

JOHN GERSPACH: David, I hate to interrupt. But we've only had one consecutive quarter of positive operating leverage in EMEA.

DAVID JIANG: Okay.
JOHN GERSPACH: This is actually the first. I'm sorry, I just wanted to set the baseline right.

DAVID JIANG: Okay, so are you seeing any slow-down in Europe, just generically?

JOHN GERSPACH: Generically, Europe is not something that I would consider to be a strong region at this point in time. We're very happy with the decision that we made some years ago to exit most of the consumer businesses that we had in Western Europe. And so I think that trend continues. And as I said, we're very happy with the decision we made back then.

DAVID JIANG: Got you. And then in Asia, you talked about Korea and Japan as being, I guess, challenging. What is particularly going on there? I know there are some regulatory changes in Korea.

JOHN GERSPACH: I think throughout the region, you're seeing some level of slow-down. Again, we're slowing down from growth rates in the 7%-9% and now we're looking at growth rates in the 4% to perhaps 7%. So there still is growth, it's just at a lower pace than what it was. Combating that, you've had a whole series of countries that have taken proactive measures. In Korea, maybe it's the most proactive, but they're not alone. They've put in consumer credit caps, and almost every country has had — or a lot of countries anyway had some level of interest rate reductions where they've lowered interest rates. So you've had all of those policy decisions that have been implemented and they've had an effect. They've slowed the growth down. That is why we've said, though, that once we work through the repositioning in Korea that we talked about last week, from where we are today, we still think that looking out at Asia from our current base, we can grow our Asia consumer business revenues grow 4%-6% and get back to positive operating leverage in 2013.

DAVID JIANG: Great, thank you for your time.

OPERATOR: That concludes the question-and-answer session. Ms. Fiszel Bieler, do you have any closing remarks?

ILENE FISZEL BIELER: Thank you, everyone, for joining our call today. If you have any follow-up questions please don't hesitate to reach out to us in Fixed Income Investor Relations. We'll talk to you again soon.

OPERATOR: That will conclude today's conference. Thank you for joining. You may now disconnect.