TRANSCRIPT

Citi Second Quarter 2013 Earnings Review
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Host
Susan Kendall, Head of Investor Relations

Speakers
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John Gerspach, Citi Chief Financial Officer

PRESENTATION

OPERATOR: Hello and welcome to Citi's second quarter 2013 earnings review, with Chief Executive Officer, Mike Corbat, and Chief Financial Officer, John Gerspach. Today's call will be hosted by Susan Kendall, Head of Citi 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. Kendall, you may begin.

SUSAN KENDALL: Thank you, Regina. Good morning and thank you all for joining us. On our call today, our CEO, Mike Corbat, will speak first. Then, John Gerspach, our CFO, will take you through the earnings presentation, which is available for download on our website, 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 2012 Form 10-K. With that said, let me turn it over to Mike.

MIKE CORBAT: Thank you, Susan, and good morning everyone. Earlier today, we reported earnings of $4.2 billion for the second quarter of 2013. Excluding CVA and DVA, net income was $3.9 billion, or $1.25 per share. Overall, we had strong high-quality earnings, which were well balanced across our products and geographies. As you know, generating such results consistently is one of my top priorities.

Although volatility did increase in June, we had good performance across our Securities and Banking businesses during the quarter. Our Transaction Service business continues to be impacted by spread compression, as does our Global Consumer Bank. However, we did grow our loans in our core businesses in a disciplined manner, particularly in the emerging markets, and we did so while maintaining a high-quality portfolio. Our capital position strengthened, and our Tier 1 common ratio increased to an estimated 10% on a Basel III basis, and we believe our firm is well-positioned for the regulatory requirements regarding capital and leverage ratios, although they've not yet been finalized.

We continue to make progress in two critical areas: reducing the drag on earnings caused by Citi Holdings; and the utilization of our deferred tax asset. We reduced our assets in Citi Holdings by $18 billion and Holdings assets now total just under $131 billion, and are less than 7% of our GAAP balance sheet. This was the largest percentage reduction in assets since 2010, and it was driven not only by Morgan Stanley's purchase of the remaining 35% stake of the MSSB joint venture, but also by continued opportunistic sales, including over $3 billion of U.S. mortgages, bringing the total year-to-date to nearly $6 billion.

More significantly, the loss in Holdings was reduced to less than $600 million for the quarter. In fact, Holdings actually made a small profit, when you exclude the impact of legal, rep, and warranty costs. Associated legal costs will likely remain elevated in the near term, but we took another significant step to get passed legacy issues, with our rep and warranty agreement with Fannie Mae.

Regarding DTA, we again consumed a modest amount during the second quarter. $600 million of DTA was utilized, bringing the total to $1.3 billion for the first half of the year. We also made good progress executing the repositioning plans we announced at the end of last year. Among other actions, just after the end of the quarter, we closed the sale of our consumer businesses in Turkey and Romania, and reached an agreement to sell our consumer business in Uruguay. We're on track to realize about $900 million of expense savings this year, and $1.2 billion next year, due to these and our other repositioning actions.

Looking to the second half of the year, it's unclear whether the market volatility that emerged in the second quarter will continue, and if so, to what degree. Low short-term rates continue to be a headwind against our deposit taking and accrual businesses, such as Consumer Banking and Transaction Services. And in the U.S., although the housing market is gaining strength, the lower volume of mortgage refinancing will impact our consumer business. We're already taking steps to make sure the mortgage business is sized correctly.

While still outpacing developed markets, emerging market growth slowed, but we remain very disciplined about to whom we'll offer credit, in light of our targeted segments. As the Brazil Credicard transaction indicates, we've managed our risk profile carefully in every country we do business, and our target clients are stable, whether they be multinational corporates or high-credit-quality consumers.

John Gerspach will now go through the deck, and then we'll be happy to take your questions. So with that, over to you, John.

JOHN GERSPACH: Thanks, Mike, and good morning, everyone. To start, I'd like to highlight some significant items affecting our results this quarter. First, CVA and DVA were positive $477 million pre-tax, and $293 million after tax in the second quarter, for a positive impact on EPS of $0.09. For comparison purposes, in the second quarter of 2012, CVA and DVA were positive $219 million pre-tax, or $140 million after tax, for a positive impact of $0.05 per share. In addition, in the second quarter of 2012, we recorded a pre-tax loss of $424 million, related to the sale of minority investments, which had a negative impact on EPS of $0.09 per share in that quarter. Adjusting for these items, we earned $3.9 billion in the second quarter of 2013, or $1.25 per share, as compared to $1 per share on an adjusted basis in the second quarter of 2012. Throughout today's earnings presentation, I will be discussing our results excluding CVA and DVA, and gains or losses on the sale of minority investments, to provide comparability to prior periods.

In addition, as we show on slide 4, there are a few other items which are included in our results. First, operating expenses in the second quarter included legal and related costs of over $800 million, compared to roughly $700 million last quarter, and nearly $500 million in the prior year. Legal and related costs from Citicorp were roughly $130 million in the second quarter, mostly in Corporate Other, while Citi Holdings legal expenses remained elevated at roughly $700 million, primarily reflected in the Special Asset Pool. Legal and related costs will likely continue to be elevated and somewhat volatile, as we continue to put our legacy issues behind us.

Second, repositioning costs were $75 million in the second quarter, compared to $148 million in the first quarter of 2013, and $186 million in the second quarter of last year. We expect to have some level of repositioning charges each quarter, but we are working to incorporate these actions into the daily management of our business. So, going forward, we would not expect to take large episodic charges as we did in the fourth quarter of last year. And finally, the loan loss reserve release in the second quarter was $784 million, including a release of roughly $525 million related to the North America mortgage portfolio in Citi Holdings. The net reserve release was $650 million in the prior quarter, and $1 billion in the second quarter of last year.

On slide 5, we show total Citigroup results for the quarter. Revenues of $20 billion grew 8% from last year, driven by Securities and Banking, while operating expenses of $12.1 billion increased 1%, reflecting the higher legal and related costs in Citi Holdings. Credit costs of $2 billion declined 25% year-over-year. Net credit losses of $2.6 billion were down 25%, and as I noted earlier, the loan loss reserve release was also lower versus last year. We earned $3.9 billion of net income in the second quarter, or $1.25 per share, up from $1.00 per share last year on a comparable basis, driven by revenue growth and lower net credit losses, partially offset by higher legal and related expenses, and a lower net loan loss reserve release.

Our effective tax rate was also higher in the second quarter at 33% versus 20% last year, reflecting higher earnings in North America, a higher effective tax rate on international operations due to the previously disclosed change in our assertion surrounding the permanent reinvestment of earnings in certain international entities, and the resolution of certain tax issues in the second quarter. We expect our effective tax rate for the remainder of the year to be approximately 30%. Citigroup end-of-period loans declined 1% year-over-year to $644 billion in the second quarter, as growth in Citicorp was more than offset by the wind down of Citi Holdings, and deposits grew 3% to $938 billion.

Turning to Citigroup expenses on slide 6, in addition to the legal and related, and the repositioning costs I discussed earlier, in the second quarter, we recorded a $60 million charge for the estimated impact of the Fed's proposed supervisory assessment on large banks. This fee is expected to be retroactive to the beginning of 2012, so the $60 million charge represents the cumulative impact of six quarters of assessments. Excluding this fee, core operating expenses declined roughly 1% in constant dollars, both year-over-year and sequentially. Year-over-year, the expense decline reflects approximately $200 million of repositioning savings, partially offset by higher performance-based compensation expense. And sequentially, the expense decline reflects approximately $100 million of incremental repositioning savings, as well as lower performance-based compensation expense compared to the first quarter, partially offset by higher marketing and transaction-related costs. We remain on track to achieve approximately $900 million of repositioning savings full-year 2013, with a run rate of approximately $1.2 billion beginning in 2014.

On slide 7, we show the split between Citicorp and Citi Holdings. Citicorp generated second quarter revenues of $18.9 billion and net income of $4.5 billion. Year-over-year, revenues grew 7% and expenses declined by 2%, driven by lower legal and related expenses. Credit costs in Citicorp increased modestly year-over-year, as the decline in net credit losses was more than offset by lower reserve releases. Citicorp loans increased by 4% year-over-year. Consumer loans grew 1%, as growth in international loans, mostly offset by a decline in North America, and corporate loans were up 7%, including the impact of adding approximately $7 billion of previously unconsolidated assets. Excluding this item, corporate loans would have increased 4% year-over-year.

Turning to Citi Holdings, revenues were $1.1 billion and the net loss was $579 million in the second quarter, an improvement from prior periods, driven by a continued decline in credit costs. Citi Holdings ended the quarter with $131 billion of assets, down $60 billion or 31% year-over-year. At quarter end, Citi Holdings accounted for just under 7% of total Citigroup assets.

Turning now to Citicorp. Our growth in the second quarter was broad-based across the region, as shown here on slide 8. In North America, revenues grew 7% year-over-year to $8.2 billion, driven mostly by improved Securities and Banking performance, while expenses and net credit losses declined, offset by a lower reserve release as credit continued to normalize. In Asia, revenues grew 7% to $4 billion, mostly reflecting Securities and Banking, although we also grew consumer revenues, while reducing expenses. In Latin America, our business is weighted more to consumer, which drove 8% growth in revenues to $3.5 billion. Expenses grew on higher volumes, and credit costs were also up year-over-year, primarily reflecting portfolio growth and seasoning. However, we still grew earnings in the region. And in EMEA, our business is weighted more to the institutional franchise, which continued to perform well, driving 8% revenue growth to $3.1 billion. We generated solid revenue growth across each geography, with overall expense discipline and stable-to-improving credit quality, resulting in pre-tax earnings of over $1 billion in each region.

Turning to slide 9, we show the composition of Citicorp revenues in pre-tax earnings by region, before the impact of loan loss reserves. These results also exclude Corp Other. For the first half of 2013, 43% of Citicorp's revenues, and nearly half of pre-tax earnings, were generated in the emerging markets. The higher relative profitability in the emerging markets reflects a lower cost base, as well as the predominantly flow-driven nature of our institutional franchise in these markets.

Slide 10 shows the historical trend for Citicorp revenues on a trailing 12-month basis, with emerging markets contributing over two-thirds of Citicorp's total revenue growth over the past two years. In the last 12 months, Citicorp generated $32 billion of revenues in emerging markets. Over half of these revenues were generated in the consumer business, where we target a high quality consumer segment, largely based in the major cities. And the remainder was institutional, predominantly serving our large multi-national clients as they fund their local operations, manage currency needs, and move payments around the world.

Turning to slide 11, we show results for international Consumer Banking in constant dollars, including the impact of moving our Credicard business in Brazil to discontinued operations in each period. On this basis, revenues grew 5% year-over-year, while expenses grew 1%. In Latin America, revenues grew 8%, and expenses were up 4% from last year. In Asia, revenues returned to growth, up 2% year-over-year, while expenses were down 2%. And in EMEA, revenues grew 2%, with a 1% decline in expenses.

While international consumer revenues continued to reflect spread compression in certain markets, as well as the impact of regulatory changes, particularly in Asia, most underlying drivers showed sustained momentum in the second quarter. Total average loans grew 5% from last year. Card purchase sales were up 9%, and investment sales grew 36% year-over-year. Both Latin America and Asia returned to positive operating leverage for the first half of 2013, and we expect to maintain this performance for the rest of the year. Credit costs of $751 million in the second quarter were up 19% from last year on higher net credit losses, due mostly to loan growth and portfolio seasoning. The loan loss reserve build was also higher this quarter at $123 million, driven by portfolio growth, as well as builds for specific credits in our commercial market businesses. Despite higher credit costs, positive operating leverage drove a 7% increase in earnings before tax to $1.2 billion.

Slide 12 shows the results for North America Consumer Banking. Total revenues of $5.1 billion in the second quarter were down 1% year-over-year. Retail banking revenues of $1.6 billion declined by 4%, reflecting lower mortgage origination and servicing revenues, as well as continued spread compression, partially offset by a gain of roughly $180 million on the sale of an on-balance sheet mortgage portfolio. This sale of approximately $2.5 billion of conforming loans was opportunistic, given the favorable market environment earlier in the quarter. Cards revenues of $3.5 billion were flat versus last year, as lower average loan balances were largely offset by an improvement in net interest spreads.

On a sequential basis, net interest spreads were up slightly in Citi branded cards, while spreads were lower in Retail Services, driven by a higher percentage of deferred interest promotional balances. Total operating expenses of $2.4 billion were down both year-over-year and sequentially, reflecting lower legal and related costs versus the prior year, and lower repositioning costs versus last quarter. Credit costs of roughly $850 million increased 19% year-over-year. Net credit losses declined by 21% to $1.2 billion, driven by an improvement in cards. However, the net loan loss reserve release was significantly lower at $351 million this quarter, compared to $814 million last year.

Overall, while we faced mortgage and spread related headwinds in North America this quarter that are likely to continue, we also saw some progress in our core franchise. Average deposits continued to grow, up 9% year-over-year, including 16% growth in checking account balances. Commercial market loans were up 17%. Card purchase sales grew year-over-year in both portfolios, and in branded cards, accounts also continued to grow up 3% from last year.

Slide 13 shows our Global Consumer credit trends in more detail. Credit quality in North America continued to improve in the second quarter, with declining net credit losses and delinquencies. And in our international portfolios, we also saw stable to improving credit trends on a sequential basis. In Asia, the NCL improvements in the second quarter reflects higher recoveries, but even excluding this benefit, the rate would have remained under 1%, with 90-plus day delinquencies stable at under 50 basis points. In

EMEA, we saw net credit recovery in the second quarter, while delinquencies continued to improve. And in Latin America, the NCL rate improved to roughly 4%, while delinquencies were fairly stable.

We currently expect the NCL rate in Latin America to remain in the range of 4% for the remainder of 2013. However, the rate could be higher if we incur any material losses on our exposures to home builders in Mexico, which are included in commercial market loans. Our loans outstanding to the top three builders totaled roughly $300 million at the end of the second quarter, with nearly 100% collateral. While we currently believe that we are adequately reserved for any potential losses related to the homebuilding industry in Mexico, we continue to monitor the performance of our clients, as well as the value of our collateral.

Slide 14 shows our consumer loans by major countries. Roughly 80% of our loans are in six markets - North America, which is roughly 50% of our portfolio, followed by Mexico, Korea, Australia, Singapore, and Hong Kong. While in certain markets, including North America, Korea and Australia, loan growth has been hampered by the economic or regulatory environment, in other countries, we continue to expand, reflecting the quality of our franchise, and the growing population of high-quality borrowers in these markets. Importantly, we are growing our loans with a disciplined focus on credit quality. In Mexico, while the NCL rate ticked up at the end of 2012, reflecting portfolio seasoning, the loss rate of under 4% remains low on a historical basis, driven by more stringent underwriting criteria, and the repositioning of our cards portfolio over the past five years. And in Singapore and Hong Kong, we have consistently maintained our focus on higher-quality borrowers, resulting in low delinquency and loss rates.

Slide 15 shows our Securities and Banking business. Revenues of $6.4 billion grew 21% from last year, and declined 12% from the prior quarter. Investment banking revenues of $1 billion were up 21% from the prior year, with higher revenues in all major products, and declined 2% sequentially, driven by lower debt underwriting activity. Overall investment banking wallet share continued to improve in the first half of the year. Equity market revenues of $942 million were up 68% from last year, reflecting improved derivatives performance, as well as higher cash equity volumes. Sequentially, equity market revenues increased 14%, driven by derivatives.

Fixed income market revenues of $3.4 billion increased 18% from last year, with strength across all major products, and were down 27% sequentially from a strong first quarter. Private bank revenues of $645 million grew 9% from last year, with growth across all regions, primarily driven by investment products, and were up 3% sequentially, driven by North America and EMEA. Lending revenues, excluding the impact of gains and losses on hedges related to accrual loans, were $401 million in the second quarter, down 3% from last year on lower volumes, partially offset by slightly higher spreads. Lending revenues were up 21% sequentially, due mostly to the absence of losses on loan sale activity in the first quarter, and slightly higher spreads. Total operating expenses of $3.5 billion were down 2% both year-over-year and sequentially, reflecting the impact of repositioning versus the prior year, and lower compensation versus last quarter. Earnings before tax of $3 billion grew 80% from last year, and declined 19% sequentially.

Moving to Transaction Services on slide 16, revenues of $2.7 billion were down 1% from last year. Treasury and Trade Solutions were down 3%, as loan and deposit growth was more than offset by the impact of spread compression globally, and Securities and Fund Services revenues grew 5%, as higher settlement volumes and fees more than offset lower spreads. Spread compression continued to dampen revenues this quarter. However, the volume drivers for Transaction Services showed sustained momentum.

Average trade loans grew 16% year-over-year. Average deposits were up 7%. Assets under custody grew by 10%, and SFS settlement volumes grew 13%. Expenses of $1.4 billion grew 2% year-over-year, driven mainly by higher volumes, partially offset by efficiency savings. While spread compression is likely to impact revenues in the near term, we continue to believe we can achieve revenue growth and a return to positive operating leverage in the second half of 2013.

Slide 17 shows the results for Corporate Other. Revenues were down versus the prior year, driven by hedging activities, while expenses of $525 million declined as well on lower legal and related expenses. Assets of $290 billion included approximately $95 billion of cash and cash equivalents, and $141 billion of liquid available-for-sale securities.

Slide 18 shows Citi Holdings assets. We ended the quarter with assets of $131 billion in Citi Holdings, or roughly 7% of total Citigroup assets. The $18 billion reduction in the second quarter reflected $8 billion of assets related to the sale of our remaining stake in the Morgan Stanley Smith Barney JV, $4 billion of other asset sales, and $6 billion of net pay downs.

On slide 19, we show Citi Holdings' financial results for the quarter. Total revenues of $1.1 billion were up 17% year-over-year, as lower funding costs drove higher revenues in both the Special Asset Pool and Local Consumer Lending, despite the continued decline in loan balances. And we also saw improved asset marks in the Special Asset Pool. Citi Holdings expenses increased 25% year-over-year to $1.5 billion, driven by higher legal and related costs in the Special Asset Pool. Excluding these legal costs, core operating expenses declined 18% year-over-year, to roughly $845 million. Credit costs declined 63% year-over-year, to $451 million. Net credit losses declined significantly to $770 million, and the net loan loss reserve release was over $470 million, including a release of roughly $525 million, related to North America mortgages.

Looking at the past five quarters of Citi Holdings results on slide 20, rep and warranty reserve bills and legal and related costs continued to weigh on Citi Holdings in the second quarter. Excluding these items, Citi Holdings was breakeven on a pre-tax basis. The earnings improvement over the past two quarters has been driven by credit, as net credit losses continued to decline, and we began utilizing our mortgage loan loss reserves. North America mortgage NCLs declined to $553 million in the second quarter, roughly 95% of which were charged to the reserve. We ended the quarter with $6.4 billion of loan loss reserves allocated to North America mortgage loans in Citi Holdings, or 35 months of coverage.

Going forward, assuming the U.S. economic environment remains favorable, we currently expect to continue to utilize reserves to offset nearly all of our mortgage net credit losses. Legal costs are expected to remain elevated in the near term. However, we put a significant piece of our rep and warranty issues behind us with the recent Fannie Mae agreement, which covers substantially all potential future repurchase claims from Fannie Mae, on loan originations from 2000 through 2012. While we continue to work through our remaining rep and warranty issues, we believe we are currently well reserved for potential whole loan claims.

On slide 21, we show mortgage loan and adjusted net credit loss trends over the past two years. Since the second quarter of 2011, we have reduced the North America mortgage loans in Citi Holdings by 31%, driven by $17 billion of pay downs, $11 billion of asset sales, and $9 billion of net losses. In the second quarter of 2013, we sold $3.1 billion of loans, including $700 million of delinquent mortgages, and $2.4 billion of current reperforming loans. We have also significantly reduced the quarterly net credit losses on the portfolio, down 49% since the second quarter of 2011, to $553 million.

On slide 22, we show delinquency trends, including both residential first mortgages and home equity loans. Thirty-plus day delinquencies improved by 10% sequentially to $5.5 billion, with improvement in each bucket across both portfolios.

On slide 23, we show Citigroup's net interest revenue and margin trends, which as a reminder, includes the impact of moving our Credicard business to discontinued operations. Net interest revenue of $11.7 billion in the second quarter grew 3% year-over-year, and was up slightly from last quarter. As we discussed at the end of the first quarter, our net interest margin in the second quarter decreased by 3 basis points to 285 basis points. This decline was driven by lower loan and investment yields, partially offset by an improvement in funding costs. Looking to the second half of 2013, we expect our net interest margin to stay roughly flat to perhaps a few basis points lower than the second quarter, so on a full year basis, we expect to be slightly above the net interest margin of 282 basis points we achieved last year.

On slide 24, we show our key capital metrics through the second quarter. Under Basel III, our estimated Tier 1 common ratio increased to 10% versus 9.3% last quarter, driven by retained earnings, DTA utilization, and the sale of our remaining stake in the Morgan Stanley Smith Barney joint venture, partially offset by losses on available for-sale-securities in OCI.

Turning to the leverage ratio, Citigroup's supplementary leverage ratio as calculated using the U.S. Basel III NPR was an estimated 4.9% for the second quarter. Unlike the Tier 1 common ratio, which is a period-end calculation, the supplementary leverage ratio is the average of three month-end ratios calculated in the quarter. While our average for the three months was 4.9% for the second quarter, this leverage ratio improved sequentially during the period, with an exit rate of just above 5% for the month of June.

We are still reviewing the final U.S. Basel III rules, but do not believe the final rules will have a significant impact on the estimated ratios. Our supplementary leverage ratio estimate does not incorporate differences in the definition of leveraged assets, as recently proposed by the International Basel Committee. As you are all aware, there has been quite a bit of activity and pronouncements relating to the capital requirements of large financial institutions over the past several weeks, and so our estimates are necessarily subject to our continued review and understanding of these recent developments.

In summary, our results for the second quarter reflected a continued challenging operating environment with spread compression, slowing global growth, and elevated legal and related costs remaining as headwinds. However, even with these challenges, we have continued to grow our core business, while significantly reducing the earnings drag from Citi Holdings. In Securities and Banking, we had a strong second quarter, even as market conditions became more volatile late in the quarter. In Transaction Services, we continued to grow loan and deposit volumes to mostly offset the impact of global spread compression, and in Consumer Banking, we also grew our loans in many markets year-over-year, overcoming spread compression to generate revenue growth and positive operating leverage in every region outside North America.

In North America Consumer, the environment remains challenging, with a combination of spread compression, consumer deleveraging, and a slowdown in mortgage refinancing activity expected to continue to put pressure on revenues for the remainder of the year. In the mortgage business, we are beginning to take actions to reduce our expense base with a decline in activity, but we would expect there to be some lag as we continue to fulfill our backlog through the third quarter. We may face additional pressure if not only volumes but also margins decline further, as we look to the back half of the year.

Turning to Citi Holdings, assets are now roughly 7% of total Citigroup, and the net loss was less than $600 million this quarter, even as we continue to face elevated legacy costs. While legal and related costs are expected to remain elevated in Citi Holdings in the near term, we put a significant piece of our rep and warranty issues behind us, with the recently announced Fannie Mae agreement. And finally, our liquidity and capital positions remain strong, with estimated aggregate liquidity resources in excess of $380 billion, and an estimated Basel III Tier 1 common ratio of 10% at quarter end.

Finally, we remain on track to achieve the expense savings from our fourth-quarter repositioning actions, even as some of our year-over-year savings were offset by higher performance-related compensation, given our strong revenues in the first half of the year. And with that, Mike and I will be happy to take any questions.

OPERATOR: *(Operator Instructions)* Our first question will come from the line of John McDonald with Sanford Bernstein.

JOHN MCDONALD: Hi. Good morning. John, a question on expenses. I recall, in terms of the repositioning saves, you're shooting for $900 million this year. In the first quarter, you said you didn't get much of that. How much of that did you get in the second quarter? So where do we stand right now on realizing the $900 million you're shooting for this year?

JOHN GERSPACH: You've probably seen about $200 million of the repositioning savings reflected in the second quarter results.

JOHN MCDONALD: Okay, and that $900 million, we should think of that as a year-over-year savings: 2013 versus 2012? Is that how we should look at it?

JOHN GERSPACH: Yes, I guess the way I would think of it, John, is if you go back to the fourth quarter, when we first talked about the $900 million and the whole repositioning action, I think we had core operating expenses in that quarter of about $11.5 billion. Now, since then, we've taken out Credicard, we've moved that to discontinued operations, and we certainly had some impact of FX, and so if you adjust for those two items, that would probably adjust that $11.5 billion to just a little bit north of $11.3 billion. So the fourth quarter repositioning actions, we've said would yield full year saves of $1.2 billion, which means that $300 million of that save should be visible in our fourth quarter numbers. So if you start with $11.3 billion in the fourth quarter of last year, and you look at $300 million of saves that should be embedded in our fourth quarter numbers, you should expect a fourth quarter core operating expense number somewhere around $11 billion. Again, depending upon how performance-related IC could flow, for the balance of the year.

JOHN MCDONALD: Okay, and that was around $11.2 billion, the $11.173 billion this quarter, is that the right comparable number?

JOHN GERSPACH: Yes, so this quarter we're at $11.173 billion and I'd say, that includes the higher performance related IC that we've had this quarter, and I'd say that we're on target to deliver the annual savings by the end of the year.

JOHN MCDONALD: Okay, and in terms of the legal expenses remaining high, $800 million this quarter, it seems like you're on track to be similar to last year, when you did about $2.8 billion for the total. It's hard to predict that. Any color you can give us on the outlook there, or what's driving that to remain high? Is this kind of private label litigation stuff or any color you could offer there?

JOHN GERSPACH: Certainly private label litigation is one of the legacy issues that we're dealing with, and you're quite right. We had $2.8 billion of legal and related expenses last year. We had $700 million or so in the first quarter of this year, so I would expect legal and related costs to, as we said, remain high and somewhat volatile.

JOHN MCDONALD: Okay, and in terms of the DTA utilization, $1.3 billion for the first half, are we on a steady pace here? Can we think of $600 million to $700 million per quarter as a reasonably sustainable pace in this kind of environment, John, or are there funny factors we need to think about that might drive this to be volatile over the next couple of quarters?

JOHN GERSPACH: Well John, it's actually going to depend upon the level and component pieces of our earnings stream. In looking at this quarter, Citicorp earnings actually utilized $1.3 billion of DTA. That would have been partially offset by $300 million of DTA that was created by Holdings. Then you had CVA, that actually utilized, because CVA was a revenue item this quarter, CVA utilized $200 million of DTA this quarter, and then OCI created DTA, so there's a lot of moving pieces that go into that $600 million.

JOHN MCDONALD: Okay, that's helpful, but the gradual trend of smaller drag of Holdings is the key thing that will get this higher over time, I guess?

JOHN GERSPACH: I'd say the two key things would be continued strong earnings out of Citicorp, especially then the gradual decline hopefully in Citi Holdings losses, yes.

JOHN MCDONALD: Final thing for me, John. In terms of that new supplemental leverage ratio, any thoughts on where you would look in terms of the bank level, that will ultimately need to be into the 6% standard?

JOHN GERSPACH: We did not have enough time to run the bank ratios for the second quarter. As we mentioned, you're going to run each month, and then the average of three months, and it's just a little bit more involved in running the bank. We had run the bank for the month of March, and at least as we ran the bank for the month of March, we were right around 6% for the month of March.

JOHN MCDONALD: Okay that's helpful. Thanks very much.

OPERATOR: Your next question comes from the line of Matt O'Connor with Deutsche Bank.

MATT O'CONNOR: Just been getting some questions in terms of why we didn't see maybe more negative impact from the volatility in emerging markets, either within your capital or some of the fixed income businesses. I realize it's two different things, but just the volatility we saw in FX and some of the spread widening and the credit problems, it didn't really seem to go all that material in the grand scheme of things.

JOHN GERSPACH: As a matter of fact, I think that we managed our emerging markets business quite well in the quarter. In the fixed income numbers, one of our real strong performers was our local market FX business. That business, if I recall, it generated revenue growth 25% year-over-year and 7% sequentially, so we actually performed quite well this quarter.

MATT O'CONNOR: Okay, and then just somewhat related on the fixed income trading, any meaningful impact from the OTC clearing of the swaps, or do you think we'll have one going forward?

JOHN GERSPACH: We still have to see how everything settles out. I still haven't seen the final guidance and everything that's coming out of all of the debates from last week, and I think that is still something yet to be developed.

MATT O'CONNOR: Okay, and then just lastly, you gave some net interest margin guidance, what about for net interest income dollars overall? Do you think we'll see them trend up from here?

JOHN GERSPACH: That's a little bit difficult. If you look over the last couple of quarters, we've been relatively stable in our daily net interest revenue. I think our daily net interest revenue this quarter was $130 million a day. Last quarter it was $131 million a day. I wouldn't, so it's going to be somewhat dependent on day counts and a few other things. I really wouldn't want to go out on a limb and start predicting big increases in net interest revenue at this point.

MATT O'CONNOR: Okay, thank you.

OPERATOR: Your next question comes from the line of Betsy Graseck with Morgan Stanley.

BETSY GRASECK: A couple questions on the capital ratios you indicated earlier. So the bank sub level first pass 6% March, but the Hold Co 4.9%. Could you just give us a sense as to what the big deltas are there, and I just want to make sure the bank level 6% first pass is based on the estimated, the proposed, the NPR, not the final rule, is that right?

JOHN GERSPACH: It's based on the -- you've actually confused me with that question, Betsy. It's based upon the rules that we've got outstanding right now.

BETSY GRASECK: Got it. And the difference between -- what makes the bank in such better position relative to the Hold Co?

JOHN GERSPACH: It would be capital level and component of the balance sheet as far as how the leveraged assets are calculated.

BETSY GRASECK: Okay, I'm just thinking about it from the perspective where your derivatives business is held, a portion of it in the bank, but a portion of it as a Hold Co, so I'm just wondering if that has a disproportionate impact on the bank or not.

JOHN GERSPACH: Everything has an impact. It's just the way -- all we do is just run the rules. Don't forget the bank also has intercompany relationships, that's why the bank is a little bit more complicated to think through.

BETSY GRASECK: Got it. I know you downstream some equity to the bank as well, and that helps, I would assume. Why just doing the ratios on the NPR, as opposed to the final rule for the Basel ratio?

JOHN GERSPACH: Which final rule? We're running them off of the U.S. final rule.

BETSY GRASECK: Okay I'm just thinking there's the slide 2, you had the note that all references to Basel III capital ratios are based on the proposed Basel III, the Basel III NPR?

JOHN GERSPACH: Well it's based upon the final rule, as we best understand it right now. We have not finished going through every detail of the 900-plus pages in the final rule, so as we have looked at the final rule, we don't believe that for us, there is any significant difference between the final rule and the NPR, at least we haven't been able to find anything as yet.

BETSY GRASECK: Okay, got it. I just want to understand why you put that footnote in there. Okay, so two other quick things. One is on the $50 million, $60 million that you called out, which is obviously a pretty small number, and not really that material, especially on a quarterly basis. I'm just wondering what it is exactly in the regulatory assessment, that you called out?

JOHN GERSPACH: Well the Fed last quarter, actually I believe they are allowed to do this under Dodd-Frank. Dodd-Frank permits the Fed to assess large banks with a special assessment for higher cost of regulation. And so the Fed put out last quarter an assessment proposal on all banks. I think that the total assessment was $440 million, and when we ran through the calculations for us, it comes out to be roughly $10 million a quarter. Now that was put out, subject to a comment period, and all the comments are in, and we expect the Fed will do something in the third quarter, and we thought it was prudent then to begin to accrue what we would estimate the impact of the fee to be. And since it's retroactive, all the way back to the beginning of 2012, for this quarter then, we would have recorded six quarters of the estimated $10 million assessment.

BETSY GRASECK: Got it, okay. That's clear. And then just lastly, on the litigation cost that you called out, you had obviously, as you indicated, several settlements this quarter, as well. So I'm just wondering how much of the settlements were already reserved for how much of the litigation costs this quarter were to true-up those settlements, or how much is building reserve for future litigation?

JOHN GERSPACH: Yes, I think that you'll see more detail when we publish the Q. Clearly, if any of those settlements had involved significant charges in the quarter, we would have called that out.

BETSY GRASECK: Okay, thank you.

OPERATOR: Your next question will come from the line of Guy Moszkowski with Autonomous Research.

GUY MOSZKOWSKI: Good morning gentlemen. So you referred to the Basel proposal for add-ons to the leverage ratio denominator, and I guess you were talking about the sold credit protection and match book and derivatives collateral disallowed. I think that's probably what you were referring to. Do you have any estimate for what the increase in your denominator would be in dollar terms for those things?

JOHN GERSPACH: Well Guy, we have -- again, all of this stuff has just come out so we did a very, very preliminary look at what the impact would be, and we would currently roughly estimate that the combination of all those things could cost us as much as 40 basis points in the supplementary leverage ratio. But again, it's early, and we still have to take a look as to exactly what the details are, and what else we might be able to do to offset some of that.

GUY MOSZKOWSKI: Fair enough, but that's really helpful that you gave that number, I appreciate that. On emerging markets, obviously what's happened over the last several months in some markets like China and Brazil would make you think that maybe we're looking at some weakness in macro growth. Any revisiting of the plans that you had talked about a few months ago, to rationalize emerging markets investment, in light of all that?

MIKE CORBAT: Guy, it's Mike. The simple answer to that is no. You saw us as we laid out, take some actions in the first quarter in terms of continuing to refine in particular parts of our consumer portfolio but again I think as we looked at the world, and described coming into the year what we saw was going to be a challenging uneven environment, we obviously saw the numbers come out of China early this morning in terms of a slight slowdown, the 7.5 versus 7.6, a bit slower Mexico, but I don't think those things have caused us to rethink where we are.

GUY MOSZKOWSKI: Okay, that's also helpful, thanks. The AOCI hit was obviously reasonably meaningful in light of a pretty bad increase in long rates, and yet it seems like looking at your AFS portfolio, it could have been worse. Did you take actions to reduce the impact by repositioning risk or something, in mid quarter ahead of the potential for rates to rise, or was there something else there?

JOHN GERSPACH: No, Guy. It's just the way we manage the business on an ongoing basis. Nothing special.

GUY MOSZKOWSKI: Okay, and then I guess the final question I'll ask is, I think you alluded to trade finance growth and looking at CTS, it looks like loans grew sequentially by about $13 billion - if I'm reading this right - and that was about the same growth year-over-year, as well as sequentially. So it basically all happened this quarter. It's pretty sizeable. Anything in particular going on, in terms of market share initiatives or something that would have taken those loan balances up so fast?

JOHN GERSPACH: Guy, one of the things that we tried to footnote for you, and maybe we didn't get it on every schedule, but I tried to mention it in some of my comments is that this quarter we also consolidated a previously off balance sheet vehicle that added about $7 billion of trade loans. So we decided that this was a conduit that we had, that housed really high-quality government-guaranteed export trade loans, and just looking at the vehicle and the spread we were getting, we felt that we could actually more efficiently fund these loans by bringing them back on to our balance sheet. So that $7 billion of loans that got added in this quarter, and that certainly is impacting the number that you see.

GUY MOSZKOWSKI: So all of that $7 billion went to CTS?

JOHN GERSPACH: Correct.

GUY MOSZKOWSKI: That wasn't clear. Okay great, thanks very much.

OPERATOR: Your next question comes from the line of Jim Mitchell with Buckingham Research.

JIM MITCHELL: Hey good morning guys. Couple quick questions. One on the mortgage NCLs. They came down 12% sequentially in Citi Holdings, which was great, but if we look at your peers they were down much more than that. Is this just a function of you being more conservative on home price assumptions, or how should we think about the pace of recovery and loss rates in mortgage?

JOHN GERSPACH: Well I don't want to say that we're more conservative in taking losses than anybody else. I think what you're starting to see now is that as that mortgage legacy mortgage portfolio shrinks, and it's down to $80 billion, what you have now is a bit more of an influence on the loss rates from the mortgage loans that we would have had, as part of our Citi finance business. Those mortgages carry a slightly, well, carry a significantly higher loss rate than what the home mortgages would. So, I hate to use the word mix, but you're getting something of a mix impact on the NCL rate.

JIM MITCHELL: And you're suggesting that those might be a little lagged in terms of the recovery because of the quality of them?

JOHN GERSPACH: Yes, those mortgages have an inherent larger loss rate. They didn't necessarily peak to the same extent, peak as high as some of the other aspects of the book, but they pretty much consistently run a loss rate of say 5%. You've got an element of our book that is running a 5% loss rate, and that's also an element of our book that we're really not able to do much in the way of asset sales on. So those Citi finance mortgages become an increasingly larger percentage of the overall $80 billion. And therefore, they are going to be a somewhat mitigating factor, as far as our ability to bring the overall loss rate for the portfolio down.

JIM MITCHELL: Okay, that's helpful, thanks. Maybe just on the rate sensitivity you in your Q have talked about a steepening curve, I think a benefit of a little over $100 million, not very much. I'm just trying to get versus your peers, that's it's on the low end, is it a function of you being shorter in duration in your AFS book, and if you have that number, that would be great. Or is it just a factor of geographic mix on the balance sheet, that you're just less exposed to the U.S. rate curve?

JOHN GERSPACH: I can't tell you how other people are positioned, but I think you're right as focusing on that scenario six that we've got in the 10-Q, and but there's also a whole series of assumptions that go behind that analysis, including the assumption that in that type of environment, we would just match our investments and our funding book. In other words, the duration of the investment book would remain static. We wouldn't look to extend the duration of the book to capture higher yields. And I think you're right in assuming we are somewhat shorter duration right now, at least in what we would normally be.

JIM MITCHELL: Do you have that number, or you don't disclose it?

JOHN GERSPACH: I'm not going to give you the overall duration, but it is fairly short.

JIM MITCHELL: Okay, great, thank you.

OPERATOR: Your next question comes from the line of Brennan Hawken with UBS.

BRENNAN HAWKEN: So thanks for the color of the emerging market book. I was just kind of curious of the trends that you saw in the 30-day delinquency rates were any different than the 90-day rates that you gave us?

JOHN GERSPACH: In the mortgage book?

BRENNAN HAWKEN: No, in the emerging market credit books?

JOHN GERSPACH: I'm sorry, in the emerging market, in the consumer book that we've given you the detail?

BRENNAN HAWKEN: Exactly.

JOHN GERSPACH: We have actually got a lot of that back in the supplement. I don't think there's anything terribly telling as far as the 30-day delinquency statistics. You get some noise in some of the statistics. I think we've talked in past calls about how the 30-to-90 day bucket in Latin America tends to move from quarter to quarter, because we've got a mortgage portfolio in there, that actually we collect payments on every 60 days. So you would have seen 30-to-90 day delinquencies in Latin America consumer spike up in the first quarter, and now you've seen them drop in the second quarter. But outside of some individual portfolio quirks, there's nothing in the credit statistics in the early bucket delinquencies that gives us any extraordinary cause for concern.

BRENNAN HAWKEN: Cool, okay, that helps. You also said that you were, you had seen the slowing growth in emerging markets, but the revenues have hung in there. So should we continue to expect that revenue and credit would track roughly similar to what you've recently seen this quarter, if we continue to see the slowing growth play out in emerging markets?

JOHN GERSPACH: Well that's somewhat easier to talk about in the consumer businesses than it is in the institutional businesses. But on the consumer businesses, I think that's exactly the guidance that we were trying to provide you with, in some of the closing commentary, where we feel that the consumer businesses in both Latin America and Asia should produce positive operating leverage in the second half of the year, as we are able to grow revenues faster than growing expenses. On the institutional side, it's somewhat going to be dependent on overall market conditions.

BRENNAN HAWKEN: Sure, great. That's helpful, thanks. And then in the equities business, another encouraging step here this quarter, and I also notice it seemed as though, at least in the press, you guys recently hired someone out of PB. Is that a side of the business that you are looking to grow? What are your thoughts on the equities business at this point? Is it going to remain, is it going to continue to be a focus to try and grow that further, or are you guys happy where it is now?

MIKE CORBAT: Well, I think, Brennan, what you saw is when we over the past several years, we've been going at the expense side of that business trying to get it really in line with what we saw as future revenue opportunities. I think that what you've seen us also do is while we've shrunk our overall headcount and expense base, we've also selectively made investments in terms of people and trading platforms in that business and so, early times, the results are improving. We're focused on continuing to want to take market share. We've seen that. We've seen good sequential growth quarter-over-quarter, but we've got more work to do.

BRENNAN HAWKEN: Terrific, and then last one for me. You highlighted decline in funding costs in Holdings. Should we assume that decline is sustainable, and can you give further color on what drove that decline?

JOHN GERSPACH: Well as the assets roll off, we obviously have some slightly higher-cost debt associated with those Holdings assets, so as those Holdings assets roll off, the debt levels will reduce, and that should serve then, to provide a funding cause benefit to that business. But it really is more in line with the assets continuing to come down.

BRENNAN HAWKEN: Terrific. Thanks a lot.

OPERATOR: Your next question comes from the line of Gerard Cassidy with RBC Capital markets.

GERARD CASSIDY: Thank you. Good morning. Can you give us a guide, you're doing quite well on your Basel Tier 1 common ratio, it's 10% now. Where do you think we're going to manage to, when you know all of the ins and outs of what's required, which may take another 12 months, but where do you think you ultimately manage to on that ratio, as well as the new supplemental leverage ratio?

MIKE CORBAT: I think, Gerard, you touched on the challenges, but I don't think we yet know all of the ins or outs. As we've spoken about in the past, we don't really know yet around the rules really what buffer in either metric we need to run the institution to. So, one of our objectives we stated to was within reason trying to get to at or around these leverage ratios within a reasonable time. And as these rules continue to clarify themselves, we'll continue to adjust to that. But again, I think there's a lot more work we've got to do to see how these things finalize themselves and what that buffer is.

GERARD CASSIDY: Okay, and I may have missed it. Did you give us the LCR ratio for this quarter?

JOHN GERSPACH: No, I didn't, but would you care to ask about it?

GERARD CASSIDY: Sure. Could you tell me what it is, please?

JOHN GERSPACH: I mentioned the fact that we had over $380 billion worth of high-quality liquid assets, and at least the early estimate of the LCR ratio says that it's coming in exactly where we targeted at, which is about, as we said last quarter, around 110%.

GERARD CASSIDY: Good. Could you also share with us, you mentioned Mexico, those three largest builders. Are those still accruing loans, or are any of them in default? And then just some color on what you're seeing down in Mexico right now.

JOHN GERSPACH: I don't know the answer to your first question, so I'm going to have to ask you to call Susan or somebody in IR, and by the time that happens, they will figure out the answer to your first question.

GERARD CASSIDY: Sure.

JOHN GERSPACH: They are 100% collateralized, those loans. Nearly 100% collateralized.

GERARD CASSIDY: And just color in general, what are your guys telling you about what's going -- because Mexico has been so strong and now this housing situation, seems kind of odd, considering the economy down there is pretty good.

JOHN GERSPACH: Yes, I think what you have there is just market forces at work, supply and demand, and as usual, with real estate, the most important consideration is location, location, location. Some of the home builders got a little overextended in putting supply where people don't necessarily don't want to live anymore.

GERARD CASSIDY: I see, and then just finally in Citi Holdings, the decline in the SAP assets to $14.9 billion from $18.5 billion, were there any bulk sales, because you had some impressive declines in some of the categories.

JOHN GERSPACH: I can't recall any large bulk sales off the top of my head, so again, it's just continuing to chip away at everything that is in Holdings.

GERARD CASSIDY: And has pricing for these assets, has it improved, or does it continue to improve from what you've seen in the last six months?

JOHN GERSPACH: I'd say in general, the pricing has held up. Obviously, with mortgages now, given the change in the 10-year rate, that certainly has had an impact on the pricing that we see for reperforming loans. We mentioned the fact that we did about $3 billion of loan sales this quarter and roughly $2.4 billion was reperforming loans. Those types of loan sales are more sensitive to changes in interest rates, because they are very yield sensitive. So that clearly is a portion of the market that we've seen prices decline in. In contrast, non-performing loans, non-performing mortgage loans seem to be more sensitive to changes in HPI, so pricing there has held up pretty well.

GERARD CASSIDY: Thank you.

OPERATOR: Your next question comes from the line of Mike Mayo with CLSA.

MIKE MAYO: Good morning. What's the capital markets backlog at the end of the quarter, compared to the end of last quarter?

JOHN GERSPACH: I don't have that, Mike, sorry.

MIKE MAYO: Okay, you made the comment that you expect to use reserves in Citi Holdings to offset nearly all of the mortgage losses. If you could elaborate on what that means, and does that mean if I look at slide 20, the bottom right hand corner, where you have adjusted pre-tax earnings for Citi Holdings, that's zero this quarter. Does that statement that you'll use the reserves to offset the mortgage losses imply that adjusted pre-tax earning figure of zero in the second quarter of 2013 should stay at zero or go higher, or you aren't willing to make a statement that this is an inflection point?

JOHN GERSPACH: I think it's a little early to make a prediction as far as an inflection point and a statement as far as using the reserves, it's really nothing more, Mike, than basically continuing to do what we've done here in the second quarter, where we use the reserves to cover basically 95% of the mortgage NCLs. Don't forget that the Holdings portfolio is pretty much a closed book, right? It's not that we're adding new loans into that portfolio. So that's a little different than you'd think about in a normal mortgage business, so we've established reserves for what we believe to be the losses that are inherent in that portfolio. Based upon the way that the markets are moving, and the way that we would look at our need for reserves right now, we felt this quarter, and we think that certainly in the next two quarters, you can look out about six months, we don't see any reason why we shouldn't be using the reserves that we've already established then, to almost fully cover the losses that we set them up to cover.

MIKE MAYO: What about blowing out some more of the problem mortgages from Citi Holdings? You said that it's more a function of home prices, so why not get more aggressive with sales?

JOHN GERSPACH: Well again, you've got two different components to the book, Mike. From a non-performing loan point of view, you're quite right. Those non-performing loans are really very price sensitive to HPI, and we were able to do about $700 million of non-performing loan sales this quarter. But we've been doing non-performing loan sales, go back to the last 15 quarters, and so our non-performing loan book is fairly well picked over at this point in time. With delinquencies performing the way they are we aren't necessarily creating a bunch of new inventory, which we think is good.

The other side of the book, as we continue to modify loans and those loans then perform, that gives us a different set of inventory to deal with, and you've noticed in the last two quarters, we've actually taken advantage of that. We sold $2.4 billion of reperforming loans this quarter, and a similar number last quarter. The trouble with reperforming loans is that the pricing on those loans is really yield sensitive, and so now that -- with interest rates spiking the way they are, the pricing is not quite as favorable in that market at this point in time.

MIKE MAYO: And then a completely separate question, I think this is for Mike. Going back to your March 5th presentation, slide 12, you had a couple categories, optimize and grow, and optimize restructure. So I was wondering with a benefit with a few more months to evaluate the franchise, if there's any incremental information on that, and also, as you said on the call, you expect to have your $1.2 billion run rate expense savings going into 2014. What's after that? So really, what's next for expenses and restructuring, and what else have you learned in the past few months?

MIKE CORBAT: Well, I think as we laid out in March, Mike, what we said is that those slides are going to continue to evolve, our four buckets. And so we have, as part of the restructuring and as part of the things we've announced as normal course of business, in terms of refinements of our institutional clients and our consumer strategies, continued to work against that. I think importantly, as John spoke about from a repositioning charge perspective, we're not planning, signaling, talking about, some big repositioning, but want to continue to push our businesses to work and optimize over time. So, I think what you've seen in the first half of the year, and it is just the first half of the year, from an efficiency ratio perspective, we're making progress, and we're pushing our leaders and managers around the concept of thinking about running their businesses that way. So there's nothing we've got planned that's a big monumental move in terms of an overall restructuring or change of direction of the Company, it's just a focus on being in a challenging operating environment, and making sure we're managing ourselves in an appropriate way.

MIKE MAYO: I think before, you said the optimize restructure bucket might be about 10% of the firm. Is that correct, and has that changed, and any more color on what that bucket might include?

MIKE CORBAT: I don't have that slide in front of me. That number actually sounds a bit low to me, as you describe it, at that percentage. Again, I think this work continues to evolve, and I would say at this point, nothing new to report. As we get to year-end or into the fourth quarter and go through budgets, we'll be continuing to assess how we're thinking about our products and our countries, and we'll continue to align and realign those buckets accordingly.

MIKE MAYO: All right, thank you.

OPERATOR: Your next question comes from the line of Chris Kotowski with Oppenheimer & Company.

CHRIS KOTOWSKI: Yes, my first question is, assuming the change in leverage ratio rules stay, does that impact any of your major significant businesses? I mean, that is, do you have to run them differently? Then I'm thinking custody and transaction processing, maybe government bond dealing? Anything that's heavy and leverage asset ratio but not RWAs. Are there any businesses you'll have to run differently?

JOHN GERSPACH: All good questions, Chris, and all way too early in the process to really address. Certainly what we've seen so far are proposals. I don't think we've actually had a chance to read through every aspect of it, and I would expect that, as usual, we'll engage in a robust and a healthy dialogue, constructive dialogue with the various regulators on these topics.

CHRIS KOTOWSKI: And then secondly, just to follow-up on the questions about emerging markets, a lot of the damage to the whole commodities complex, all that has happened very recently, in the second half of May and June. Just was wondering if Mike's comments earlier, should we read that if commodity prices roughly stay at this level, that we should not expect any significant fall out in terms of your businesses in the emerging markets?

MIKE CORBAT: Well, I think again, as John described, there's two components to our business. One is the consumer piece and we've signaled how we think about the second half of the year there. I think it's difficult right now to be able to judge where we are in terms of a trading environment. June was certainly choppier than the first four or five months of the year, and it's hard to predict what the trading environment is going to be like in the second half.

CHRIS KOTOWSKI: I didn't mean so much the trading environment. I meant gold and all other commodities that you can look at basically, have come down fairly significantly in May and June, and does that impact, does that significantly impact the economy?

MIKE CORBAT: Well Chris, I think that's exactly what you have to see, is how does it impact -- It's not so much the commodity price in and of itself. It's what's the ongoing impact on the economy. And as we've said before, we still anticipate that the emerging market economies are going to grow at a much faster rate than the developed economies, and so we would still expect to get more growth out of the emerging markets in general than the developed markets. And we continue to run our business in each of those geographies with a very disciplined focus on credit.

CHRIS KOTOWSKI: Okay, thank you.

OPERATOR: Your next question comes from the line of Erika Penala with Bank of America.

ERIKA PENALA: Just a quick follow-up question. I appreciate the guidance on NCLs for GCB Latin America. Should we expect the same stability in dollar provision, or should we continue to increase it as we've seen over the past two quarters?

JOHN GERPACH: That's a good question. I would say that when we say that the rate should stabilize, that would mean that you would likely see some small increments in the NCL, nominal dollars themselves. Again, subject to currency fluctuation.

ERIKA PENALA: Okay, and so the dollar NCLs are going up, but the dollar provision will go up in tune with growth and the dollar increase in NCLs?

JOHN GERSPACH: The NCLs will, the nominal, on a constant dollar basis, with growing portfolios and a stable NCL rate, you would expect the nominal dollar NCL to increase slightly, and right along with the growth in the portfolios. As those portfolios grow, it's likely then that we would have to provide some level of additional loan loss reserve against those portfolios.

ERIKA PENALA: Okay that's clear. And just one more question, just to go for a different topic. Mike, could you update us on what your thoughts are in terms of potentially doing large card transactions in the U.S., and whether the top parameters you're considering, whether thinking about putting a bid in or formulating a bid in, if a large card transaction were to become available?

MIKE CORBAT: Yes, so a couple of things we can point to or speak about. One is that you saw us in the first quarter announce our Best Buy transaction, roughly a $7 billion card portfolio that we thought fit in well against our retail partner services business. And so, in that business, we would continue to look at portfolios that we think fit in and have adjacencies, either from a sector or from a geography perspective in there. Obviously, we're going to be mindful of returns of capital, of absolute risk profiles that are there, so things that make sense from that perspective, we're happy to consider. I think in the branded space, there's probably less opportunities to acquire portfolios in that segment of the market, in the areas where we are, but if those presented themselves, and economically they made since, they were the right client set that fit against our targeted set of clients, and they were the right risk profiles, we would certainly consider them.

ERIKA PENALA: Okay, thank you for answering my questions.

OPERATOR: Your next question comes from the line of Fred Cannon with KBW.

FRED CANNON: Great, thanks. I just had a couple follow-up questions on the DTA. I was wondering about the reduction in the DTA this quarter, if you were able to reduce the foreign tax credit carry forward portion of the DTA as a result of that reduction.

JOHN GERSPACH: Great question, and it's resting the component pieces of the DTA as far as how much of it relates to foreign tax credits and everything else, and that's something that you can really only answer as you close out the year and you finalize your overall tax provision. Trying to provide detailed guidance as far as how much of the $1.3 billion of DTA that we've utilized in the first half of the year, how much comes off of FTC's -- I can't reliably do that at this point in time.

FRED CANNON: That's why it's in the K and not the Q's I imagine?

JOHN GERSPACH: That's exactly why.

FRED CANNON: In terms of the last question, in terms of the Best Buy card deal, any update on the timing of the closing of that, and also, can we -- is there any way we can estimate how much positive impact that would have on the DTA once it does close?

JOHN GERSPACH: It's a little hard to isolate a specific portfolio, but as far as I know, we're still on track to close that deal in September, so that we won't get much benefit if any in the third quarter out of that portfolio. But it's a $7 billion portfolio then that we should get a full quarter benefit from in the fourth quarter.

FRED CANNON: And then a tax rate taken against that, at least I know it's hard to isolate, but just from our standpoint, a tax rate taken against that should help directly reduce the DTA?

JOHN GERSPACH: All things being equal, yes.

FRED CANNON: Okay, great. Thanks so much.

OPERATOR: Your next question comes from the line of Matt Burnell with Wells Fargo Securities.

MATT BURNELL: Good morning. Thanks for taking my questions. There will be a couple of quick follow-ups. John you mentioned Treasury Services, you expect operating leverage gains in the second half. Just specifically, is that expected in fourth quarter, or are you suggesting that could be the case for the full second-half results within TS?

JOHN GERSPACH: I want to make sure that was for Transaction Services.

MATT BURNELL: You're right, I'm sorry.

JOHN GERSPACH: I wasn't being specific to part of a part of TTS, that was really expansive for TTS. And I actually think you might be able to see positive operating leverage as early as the third quarter.

MATT BURNELL: Okay. Then you mentioned that there was still some regulatory headwinds in the Asian business. I guess you've mentioned in the past some of the regulatory challenges that you faced in Korea. Guess I'm curious maybe to get a sense as to how far along on that path, specific to Korea, you think you are. Since it sounds like you're expecting somewhat better operating leverage trends within the Asian business overall.

JOHN GERSPACH: Yes, I would say that Korea is still going through some issues. I don't think that we're going to be completely out of the regulatory headwinds in Korea. In other words, have completely worked through the repositioning of the book until some time next year, maybe even to the end of next year. So that's going to continue to be a drag on us. That's why when we look at Asia, Korea certainly is a weight on us, but Asia overall, we still have some good loan growth. If you look in the back of the presentation material that we gave you, on slide 33, if you take a look at Asia, excluding Korea and Japan, year-on-year, we're getting 10% loan growth coming out of Asia, so Korea is an anchor, but it's not the only thing that is propelling our business forward.

MATT BURNELL: Okay, fair enough, and then just finally back home, any thoughts as to a potential settlement with Freddie? I know that Fannie was a bigger buyer of your mortgages over time, but any thoughts about potentially settling with the other side of the GSEs?

MIKE CORBAT: Yes, what I would say is that we won't comment on Freddie specifically, other than to just reaffirm that continuing to work through these things and get them behind us is a top priority.

MATT BURNELL: Okay, thank you very much.

OPERATOR: Your next question comes from the line of David Hilder with Drexel Hamilton.

DAVID HILDER: Good morning. Thanks very much. A couple of numbers questions and then a policy question. Can you update us on what the Basel III risk-weighted assets in Citi Holdings are?

JOHN GERSPACH: I don't have that number off the top of my head, but if you get a hold of IR, they will be able to supply you with that. But I believe that it's now down to 21% of our total risk weighted assets, but I don't have the math of that in my head.

DAVID HILDER: Right, well, that's helpful. Then in the reconciliation on page 43 where you list deductions from Basel III Tier 1 of $45 billion for DTAs and other items, is it fair to assume that most of that $45.3 billion is DTAs of one sort of another, at this point?

JOHN GERSPACH: Yes, David.

DAVID HILDER: Okay, and then finally, you talked about being engaged with the regulators on the leverage proposal. Could you be more specific about that, or are you actually going to object to either the percentage or the way the denominator is calculated, for example?

JOHN GERSPACH: Well, I don't want to specify where we might object or anything like that, because when you look at whether you're dealing with risk weighted assets, leveraged assets, liquidity rules, each one of these broad concepts is valid in its own right, and serves a purpose in ensuring the safety and soundness of the financial system. In almost every case, it's really a matter of degree, and how well the various elements work together. I think those are areas worthy of discussion.

DAVID HILDER: Thanks very much.

OPERATOR: Your next question comes from the line of Andrew Marquardt with Evercore.

ANDREW MARQUARDT: Good morning guys. Couple of questions. First, in terms of the run-off portfolio in North America mortgages, can you help us think about the pace of the run-off going forward? What has the appetite been like recently, you've talked about that in the past. Any change in terms of -- given the macro back drop potentially shifting again?

JOHN GERSPACH: Well as you've seen, Andrew, over the course of the last two quarters, we've been able to sell about $6 billion of those mortgage loans, roughly I think a little bit shy of $3 billion in the first quarter, and then $3.1 billion or so in the second quarter, as we took advantage of some favorable market conditions. With a large portion of what we were able to sell in the first half of the year, were these reperforming loans that I talked about earlier. The reperforming loans are -- the pricing on those loans is really sensitive to yield, and so with the recent rise in interest rates, the market has changed for those reperforming loans. We'll have to reassess to see whether or not we can continue the pace of sale that we've got for those types of assets.

MIKE CORBAT: Andrew, I think as part of that, as we've said historically, the focuses are a couple things. One is that we want to obviously continue to reduce the size and drag of the portfolio but that drag comes from a couple perspectives. It not only comes from the cost of credit, it comes from the operating expenses associated with the portfolio, and when we can go in particular at the delinquent part of the portfolio, and continue to sell that part of the mix down, it allows us to go back, and get out a lot of high costs, so we're focused in the aggregate, derisking, getting smaller, reducing the drag, and so as the market affords opportunities, we'll continue to try and take advantage of them.

ANDREW MARQUARDT: Got it that's helpful. In terms of accelerating the pace of that, you previously talked about that the buyer of liquidity has been a hurdle, just given the size of the portfolio that you need to reduce. But then also, you brought up how there's been a difference in lifetime loss estimates, more recently. Can you expand on that point a little bit more, in terms of what you mean, in terms of maybe just the buyer/seller perspective?

MIKE CORBAT: Sure. So historically when we've looked at or thought about different larger, in particular, bulk sales, there's at least three components to go into the pricing that comes in. One is what's the buyer's cost of money. Second is what is their expectations around loss rates, and the third is, what's the capital they need to hold against it, and what's the cost of capital. I would say, in most every instance when we see that from a bulk perspective, the numbers or the math associated with each of those three things, from our perspective makes it a sale that's not worthwhile. So again, we pretty simply look at our own view towards those three things, and if somebody is willing to pay us what we think the value of those assets or of those securities are, we're happy to sell them. To date, in bulk form we haven't seen that. If and when that opportunity presents itself, we would love to act on it. But we don't, we haven't seen that to date and we're not running the portfolio with the belief that in the near term that's going to be out there.

ANDREW MARQUARDT: Okay, that's helpful. And separately, you had mentioned the LCR currently at about 110%. Is that comparable to last quarter, if I have it correctly, 116%?

JOHN GERSPACH: Yes, that's perfectly comparable.

ANDREW MARQUARDT: Okay and did I understand also that 110% is about the right level that you feel comfortable running at in terms of kind of a buffer on top of the current minimums?

JOHN GERSPACH: That's the target that we established last quarter.

ANDREW MARQUARDT: Okay, great. And then just lastly, kind of stepping back, can you help just frame out in terms of your near-term, long-term, maybe medium term goals of 10% ROE and 91/10 ROA, how the recent global slowdown that you've mentioned, as well as the U.S. mortgage market maybe shifting here, how much does that affect if at all those growth or those goals? Thanks.

MIKE CORBAT: We're not changing those goals. We said that those goals were constructed in what we believe to be a slower growth challenging environment. We said that we would hope to be able to achieve those goals, and we hadn't built in interest rate rises into those pieces, and I think that as global growth presents a headwind, or the market presents a headwind, we've got to take those in stride within the numbers that we've put out there.

ANDREW MARQUARDT: Great, thank you.

OPERATOR: At this time, there are no further questions.

SUSAN KENDALL: Thank you all for joining us here today. If you have any follow-up questions, please reach out to Investor Relations, thanks.

OPERATOR: Ladies and gentlemen, this does conclude today's conference. Thank you all for joining, and you may now disconnect.

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