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Host
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Speakers
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John Gerspach, Citigroup Chief Financial Officer

PRESENTATION

ERIKA NAJARIAN: For those of you in the webcast, it's Erika Najarian, the head of the U.S. banks team here at BofA. Our next company presenting is Citigroup. With a footprint that spans 160 countries and superior capital positioning, Citi is the very definition of a premier global franchise.

And according to your request, this is the presentation that you, the investor community, have the most interest in. So I'm going to go right ahead and see the stage to management. We are so very pleased to have co-President and CEO of Global Consumer Banking, Manuel Medina-Mora; and Chief Financial Officer, John Gerspach, with us today.

With that, I will hand it over to Manuel.

MANUEL MEDINA-MORA: Thank you, Erika, and thank you for the invitation to this conference. This is, I think, the third time that you have invited me to this conference. Good morning, everyone. What we would like to discuss with you today is our Global Consumer Bank; our strategy, our key execution priorities and our financial results.

Let me start with a brief review of our business. Over the last 12 months, Citi's Global Consumer Bank generated more than $38 billion of revenues and over $7 billion of net income. With more than $400 billion of assets, our business, our consumer business, ranks among the largest in the world. And it is a significant and growing contributor to Citicorp.

We serve roughly 62 million customers in 36 countries. Our retail bank operates nearly 3,800 branches with $330 billion in deposits. We are the number one credit card issuer globally. And in total, we have retail and card loans of over $290 billion, and have more than $160 billion in assets under management within the Global Consumer Bank.

We generate a strong return on assets, representing less than a quarter of Citicorp's total assets, but nearly half of net income. We are also well diversified, with nearly half of our revenues generated outside of North America.

The basic principles of our consumer strategy have been consistent for the last few years. They started being defined at the end of 2009, and we have consistently executed on the basis of those four principles.

First, we are executing a customer-centric business model. That means putting the customer at the heart of everything we do; delivering the best possible product, services and experience.

Second, we focus on markets and client segments where we have a competitive advantage; retail banking for the affluent and the emerging affluent segments in the world's top cities; a somewhat broader approach in credit cards with a focus on deepening our existing relationships; and local commercial banking for clients who value our global capabilities.

Third, we believe we are positioned for organic growth, with a unique presence in markets where both GDP and our target client segment, the most affluent, continue to expand.

And fourth, we are leveraging globality by sharing best practices across markets and capturing economies of scale.

This is our global footprint. While Citi serves institutional clients on the ground in roughly 100 countries around the world, in the consumer bank we focus our efforts in 36 of these countries. And more specifically, and this is a key part of our strategy, we think of our presence in the consumer banking business in terms of cities, not countries. The global trend of urbanization, particularly in emerging markets, continues to drive GDP and population growth in the major cities of the world.

We have identified 150 cities in the world that represent a third of total global GDP. Let me repeat that. Only 150 cities around the world concentrate one-third of the global GDP of the world. And we believe that it is in those cities where we will see significant growth for the foreseeable future. We have a retail banking presence in more than 120 of those cities, with nearly three-quarters of our branches in the emerging markets. With this footprint, we believe we can achieve scale by focusing on high credit quality, globally-minded customers with very similar needs in each city around the world.

Turning to credit cards, as I said before, we are the number one credit card issuer globally, with total card loans of about $145 billion as of the last September. In the U.S., credit card issuers continue to face slow economic growth and high payment rates, making loan growth elusive. But U.S. cards remain a very strong return business for us. However, we expect growth to remain muted until we see a stronger U.S. economic recovery.

By contrast, nearly a quarter of our card loans are outside of North America, and these portfolios continue to generate strong loan growth and purchase sales. Besides the U.S., our share of purchase sales is greater than 10% in 13 international markets, positioning us well as these markets grow and mature.

Our strategy is to leverage this global scale by driving to common products, common platforms and common processes, and delivering global benefits to our customers, such as worldwide rewards programs.

Here we show our penetration among our target segments - emerging affluent, affluent segment, high credit quality customers in top cities. We touch a significant portion of the emerging affluent and affluent segments, as well as global clients, which tends to be concentrated of course in urban areas in the top cities.

For global clients, those working, living or studying abroad or that travel internationally quite frequently, our platform and our capabilities are a natural fit for them. And while this only describes a portion of the consumer in any given market, it's a very profitable relationship where we provide a differentiated service.

Our diversified franchise gives us unique exposure to faster-growing regions of the world. Over the last 12 months, nearly half of our revenues were generated outside of North America, with the largest contributors being Mexico, Korea, Australia, Singapore, Brazil, Hong Kong, Taiwan. While emerging market GDP growth expectations have slowed somewhat over the last year, our major international markets are still expected to expand by 3.5% to 4% annually for the next five years.

Perhaps the most critical aspect of our strategy is leveraging our globality. This is the difference, as we say at Citi, between managing a loose confederation of local banks, 36, or operating a truly global consumer bank. And this is the transformation that we are immersed in.

In late 2011, we formed the Global Consumer Bank for the first time at Citi, placing all of our markets under one single global management team for the first time. While our institutional business had been managed globally for decades, this was a fundamental shift for the consumer bank. And we are still in the early stages of reaping the benefits of running it as a global consumer bank.

We have tremendous scale on a global basis, which allows us to better serve our clients while providing the consistent diversified earnings stream and a low-cost deposit base.

With this strategy as our guide, let me move to the second part and let us look at how we are executing our key execution priorities. First, we are deepening our client relationships. Through better engagement with our existing customers, we are growing revenues more consistently and with higher profitability.

Second, we are very focused on improving our operating efficiency. As you know, earlier this year our CEO, Mike Corbat, disclosed a target operating efficiency ratio for the Global Consumer Bank of 50% or lower, an improvement from the 54% over the last 12 months.

We believe this target is achievable through a combination of reallocating resources to better performing markets, driving our businesses to a common set of products, processes, platforms and sites; and optimizing the way in which we interact with our clients through the branch network and the digital channels.

Third, we are focused on risk management. In everything we do, our goal is to build a culture of execution and accountability, pursuing responsible growth while optimizing returns for our shareholders.

We serve our customers best when we leverage several touch points. Over the past year while we have continued to grow our customer base, we have meaningfully expanded, about 8% growth, the number of customers who have more than one Citi product, deepening relationships and building a full relationship.

On the right, you can see how the marginal contribution increases dramatically as we build on the number of products per customer. The data that I'm showing is from North America, but the relationship holds true around the world. So the contribution multiplies as we add products because the cost of acquisition goes down quite significantly.

To improve our operating efficiency, we are exiting or restructuring underperforming businesses, and reallocating resources to our core markets. Over the last year we announced five market exits - in Turkey, Romania, Pakistan, Uruguay and Paraguay, and even the non-Citi branded cards operations in Brazil, the Credicard - because they were not a fit with our strategy or they were not performing up to our standards.

We have also identified the structure markets where we believe we can improve results while maintaining our presence. In our core international markets, as you can see from the slide, operating efficiency has improved over the last two years, from 59% in the first nine months of 2011, to 55% in 2013.

However, this improvement has been offset by North America, where declining mortgage revenues caused the efficiency ratio to increase to 48% this year from 46% last year. We have taken actions to resize our U.S. mortgage business, but only a portion of the expected savings have been realized to date.

In our restructure and exit markets, the efficiency ratios are much higher, but have improved this year. While we do not currently anticipate any additional market exits, we are highly focused on underperforming businesses. And if there is no clear path to acceptable returns, we will significantly scale back or exit certain markets.

Our next lever is the “drive to common” - what we call at Citi the “drive to common” - which will not only assist in reducing expenses but also in providing better customer experiences. Over the years, the proliferation of products, policies, platforms, and sites have been developed in our 36 markets.

In cards, as an example, we are in the process of reducing our product offerings and moving to five common chassis around the world. We are also simplifying our processes, covering every aspect of the customer lifecycle. These common processes will be matched by common technology platforms, a project I had discussed with you previously.

We are in the process of migrating legacy systems to a common card and retail platform. Implementation is well underway in Asia and in EMEA. We have the front-end customer-facing implementation done in our North American branches, and we are preparing for Latin America.

This is a multi-year process. However, we don't need to be fully implemented to begin to see a positive impact on the business.

And finally on this stage, we are addressing the places in which we operate, particularly in operations and technology where we are reducing the sites and moving to lower cost locations. So, several important opportunities to continue to improve our efficiency ratio from the drive to common.

We are also optimizing the ways in which we interact with our clients. We have repositioned in certain markets, further concentrating our presence in major cities. While we have reduced the number of branches by about 10% by now, both the number of Citigold bankers and our productivity per square foot have increased substantially.

As consumer behaviors have changed, we are adapting in multiple ways. We view the branch just as one touch point in an ecosystem which includes flagship branches, traditional branches, kiosks, multifunctional ATMs, and more important, digital channels. As we keep saying to all our people around the world, we want less branches, more touch points, and more bankers.

In digital we are increasing our engagement with clients to improve the customer experience and drive lower costs. You can see that over the last year and a half, we have made a substantial improvement, substantial in North America. And e-statements are also growing quite nicely.

The U.S. is not at the top of our countries in terms of digital usage and acceptance by our clients. There are certain countries in Asia which are even higher than the U.S. while some other countries, especially Latin America, still lag. And we have an opportunity there to improve our digital experience.

So while we have made progress, we still have more work to do and will benefit from a common technology platform to drive digital around the world.

We have weathered spread compression and grown volume while maintaining one of the best operating efficiency ratios in our industry, at 54% over the last 12 months. If you look back in this decade, most of the consumer banks around the world have seen their efficiency ratio deteriorate quite significantly because of the lack of revenue growth -- actually, the drop of revenue growth.

Not the case in Citi. We have kept our efficiency ratio, and so we have now one of the best. But as I mentioned earlier, we have set a target operating efficiency ratio of 50% or lower by 2015, with the top end, 50%, of that range assuming a flat revenue environment.

Of course, revenues are down so far in 2013, given the decline in North America mortgages, refinancings and general originations. But we believe we can make up for that pressure by growing other parts of our businesses. We view this efficiency target as achievable, given the many opportunities I just described to streamline our operation.

Turning now to risk management, our third execution priority. We look, in Citi, at risk through three lenses, and this is consistent throughout the whole house. By business, by product and by geographies, and how we define our risk appetite in each market, in each product, in each line. Over the past few years, this has resulted in stable to improving credit trends, even as we have continued to grow our loan books.

Of course, risk management does not just apply to credit risk but to all the various operating and regulatory responsibilities we face around the world. We want to be known as a strong and stable institution in every market in which we operate.

Let me go to third and final part. Let's review our financial results briefly. We have made significant progress in generating consistent, high-quality earnings for Citi. Citicorp pretax earnings, excluding loan-loss reserve releases, have increased by 55% over the past two years. So this is pre-provision, pre-tax earnings, the highest quality, no releases; 55% over the past two years, with Global Consumer Bank contributing over half of this growth.

Since I first spoke at this conference in late 2010, I was reporting at the time last 12 months to third quarter 2010 results, for the Global Consumer Bank, of $3.7 billion. Today they are in excess of $10 billion. In three years, much more than double those high-quality earnings.

Our recent performance reflects a combination of modest revenue growth, expense discipline and improving credit trends. Let's start with revenue growth and take a deeper look at it. While we face a low interest rate environment globally and a slowdown in U.S. mortgage revenues, the Global Consumer Bank has been able to grow volumes to more than offset the impact of spread compression.

So on a trailing 12-month basis, we have grown revenues on average by 2% annually since the third quarter of 2011, for the last two years as you can see on the left-hand side of the slide, reflecting 4% annual growth internationally and flat revenues in North America.

The performance was driven by strong growth across many of our key drivers. And if you look at what has happened this year, we have grown international loans by 5%, even as we have absorbed headwinds from our repositioning in Korea. Assets under management are up 10% from a year ago. Deposits are up 2%, but if you look at operating balances, checking accounts - the highest quality of deposits, they are up 10%. And international card purchase sales also increased by 10% from last year. So our international drivers are there, quite strong, helping us drive revenues overall.

We have grown our business while maintaining strong credit standards. Over the past two years, net credit losses in our international portfolio have remained broadly stable as a percentage of loans while North America has continued to recover, driving the loss rate from Global Consumer Banking overall from 3.6% to 2.4% in the last two years.

Dollar losses have also improved, as declining losses in North America were partially offset by volume-driven increases in the rest of the portfolio. So as credit has stabilized globally, our loan loss reserve releases have slowed, contributing only a modest amount to our earnings over the past four quarters. We are not making our earnings by very big loan loss reserve releases. We have not.

The Global Consumer Bank generates attractive returns on both GAAP assets and regulatory capital. We generate the return on assets of 1.9% over the last 12 months. And our return on Basel III regulatory capital at 10% of risk weighted assets was over 25%.

These returns reflect, of course, some of the higher mortgage refinancing volumes we saw at the end of 2012 and early this year, as well as a modest benefit from loan loss reserve releases. But they have also been dampened by the current low rate environment.

As we continue to grow the business and improve our operating efficiency, we believe the Global Consumer Bank can be a powerful driver for reaching our Citigroup level targets.

While we have covered many topics here today, I want to leave you with a few thoughts, some of the key thoughts. The world around us is changing, and it continues to change. Globalization, organization, digitization are transforming the way we live and the way we do business.

As the pace of change increases, our business model becomes even more unique, as our CEO Mike Corbat keeps telling people. To seize the opportunity ahead, we must operate as one team and one business. And this is exactly what we are doing by transforming into one global consumer bank, doing the same things in every country across every segment. This is the bank that we are building.

We believe this is the right path to create higher returns for our shareholders and sustained value creation. With that, John Gerspach, our CFO, and I are happy to address any of your questions. Thank you.

ERIKA NAJARIAN: Thank you, Manuel. Before we turn it over to Q&A, I just wanted to ask one quick polling question of the group before we get started. So if we could bring the polling question up, I thought it would be interesting to get your feedback on the stock with shares trading below tangible book.

With the stock, again, now trading below tangible book value, what would make you more bullish on Citi? One, achieving its profitability targets ahead of schedule. Two, and given, Manuel, your very compelling presentation, this seems to be more of a sentiment question - improvement in the sentiment outlook for emerging markets. Three, acceleration in the wind-down of Citi Holdings. Four, improve top-line outlook for capital markets. And five, increase capital return coming out of next year's CCAR.

So I believe we are giving you five seconds to register your vote. So the results are coming up. Thirty-two percent of you, for those on the webcast, said that achieving the profitability targets ahead of schedule would be the most compelling reason. The next most popular answer, 27%, is increase capital return coming out of CCAR.

And before we open the floor to you guys, any comments from Manuel and John on the responses?

JOHN GERSPACH: No, actually, I'm actually surprised that the achieving profitability targets didn't score higher, to be honest with you. I think it still shows that in a lot of people's minds, we still remain a capital return story. And that's okay, we understand that.

ERIKA NAJARIAN: Questions from the audience? We have one right here if you don't mind waiting for the mic.

SPEAKER 1: Speaking of emerging markets, when you sit with your top lieutenants in East Asia particularly, given the slowdown earlier this year there was quite a bit of trepidation about where things we're going. What's the body language in your internal meetings? Are they confident about acceleration? What kind of acceleration is it? Is it like 2009? What is it on a scale of 1 to 10?

MANUEL MEDINA-MORA: I think that clearly there is confidence that the growth will actually improve as we go into the next two or three years. On China, for example, we are expecting growth to be above 7%, of course, this year and above 7%, 7.2% next year.

We are expecting India to do much better next year than what they did this year. And we are expecting - and this is particularly important for us - Southeast Asia to do fairly well, quite consistent and quite stable, between 4.5% and 5%, depending on the country that you are talking about.

Remember that Citi has quite significant operations in Southeast Asia, and that is a region that has been very stable for us. So we still have the challenge of the repositioning that we are doing in Korea. We still know that Korea is going to impact somehow our results next year. But we believe that after a year, we will be basically where we want to be in Korea, which by that time the franchise will resemble more the type of franchises that we have around the world, caring for the top segments in top cities. So in general, we are quite positive and constructive about Asia.

ERIKA NAJARIAN: Questions from the audience? Right here, Bill.

SPEAKER 2: In Mexico, wondering whether you are seeing any signs of real estate or consumer financial bubbles, any credit quality deterioration? I can understand given the growth there, you need to raise reserves, but is there any deterioration going on under the surface?

MANUEL MEDINA-MORA: I will separate the two partly, real state from consumer. What you saw in Mexico this year was, of course, the impact of a new administration coming into office, and they changed some of the rules. They are trying to actually get approved significant reforms.

One of the impacts, one of the few negative impacts of this administration has been on the construction side, as you see. And that is basically concentrated in the three top homebuilders, so it is very concentrated there. I think we have seen the worst of that. And I think we feel very good, very well provisioned for. That is not something that concerns us quite significantly going forward. Of course, we will continue to be very attentive to the situation.

On the consumer front, we feel good about it. The economic slowdown as the new administration came into power, everyone was a little bit surprised, because everyone was expecting Mexico to expand to about 3% this year. And the economic growth will be probably be between 1%, 1.2%.

Going into next year, we see that the administration is now going into full public spending mode within the budget. We see that the U.S. economy is helping Mexico a lot because that has a lot of relevance for the Mexican economy. And so we see the consumer sector actually expanding at a good pace and with no significant credit quality problems, except in the lower segments of the market, which is exactly where we are not.

Remember that our franchise in Mexico is fairly well-positioned in the middle-class top, I would say top middle-class, emerging affluent and affluent. And that we lend basically to our customer base. That, of course, has a much better, higher quality in terms of credit, credit risk.

SPEAKER 3: Hello. Separately, multi-product customers at 8% seems low. What's the prognosis for the next couple years?

MANUEL MEDINA-MORA: That's the growth rate, year on year. That's the growth rate year on year. So our multi-product clients, of course, are probably close to 60% of our customer base around the world.

One of the great things that we are seeing is that Citi has penetrated and is penetrating very well our target segments. So you can think of Citi as being in three key segments - affluent, including high net worth, because above that, ultrahigh net worth is handled by the private bank on ICG; emerging affluent and the, let's say, the top half of the mass market where cards and lending are so important, what we call Citiblue.

So from Citiblue to Citigold, we have probably the best segments that we can have everywhere in the world. And those are the segments that are expanding the fastest, and those are the segments in which the deepening of relationship is taking place. I can tell you 60% of the base now is multiproduct, growing at 8% every year. So that's a very powerful engine.

ERIKA NAJARIAN: Actually, we are out of time, so Citi will be hosting a breakout across the way on this floor. Thank you, guys, for coming.

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