Citi First Quarter 2014 Fixed Income Investor Review
TRANSCRIPT
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Host
Peter Kapp, Head of Fixed Income Investor Relations

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

PRESENTATION

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

PETER KAPP: Thank you, Brent. Good morning and thank you all for joining us. On our call today, our CFO, John Gerspach will speak first, then Eric Aboaf, our Treasurer, will take you through the fixed income investor presentation, which is available for download on our website, 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 2013 Form 10-K. With that said, let me turn it over to John.

JOHN GERSPACH: Thank you, Peter, and good morning, everyone. We're very pleased to be hosting our Fixed Income investor review this quarter. Eric Aboaf, our Treasurer, will review some specifics on our balance sheet, liquidity profile and capital position as well as an update on our funding plans for 2014. Before I turn it over to Eric, however, there are some key points from our first quarter results that I would like to highlight on slide 2.

Earlier this week we reported earnings of $4.1 billion on an adjusted basis, a 4% increase over last year. Overall, we grew both loans and deposits while focusing on improving our operational and balance sheet efficiency. During the first quarter our institutional business performance performed well across our products and geographies. Our Consumer Bank again posted growth internationally generating positive operating leverage year-over-year. Assets in Citi Holdings declined to $114 billion in the first quarter and we brought the portfolio closer to breakeven.

We also resolved another significant legacy issue last week with the $1.1 billion settlement regarding certain private-label mortgage securitization, and we reduced the DTA by an additional $1.1 billion during the first quarter following a $2.5 billion reduction for the full year 2013. We ended the quarter with an estimated Basel III Tier 1 Common ratio of 10.4% and at 5.6%, we already surpassed the Basel III Supplementary Leverage ratio requirements.

Regarding the Fed's objection to our capital plan, as Mike mentioned on our earnings call, and based on what we've learned so far, we don't believe that this is an issue with our business model or strategy. It also isn't an issue with our levels of capital or our capability to generate capital. As you saw last month on a quantitative basis, we passed with 150 basis points of capital above the Fed's threshold levels. We believe we can fix what needs to be fixed in our CCAR process so we can pass the qualitative components. We will devote whatever resources and make whatever changes are necessary to accomplish this critical goal. We are engaged with the Fed so we can fully understand their concern, and we are committed to bringing our capital planning process in line with the highest standards befitting an institution of our global reach.

Regarding the fraud in Mexico, as we discussed earlier this week, we have completed our rapid review of $14 billion of global financing relationships, and have not identified similar issues with any other accounts receivable program other than with the Pemex supplier program. Our efforts to recover misappropriated funds continue as does our review of our controls and processes in Mexico.

Turning to slide 3, we summarized Citigroup's financial results for the quarter. As I noted earlier, we earned $4.1 billion or $1.30 per diluted share in the first quarter versus $1.29 in the prior-year period, as lower operating expenses and lower credit costs were partially offset by a decline in revenue. Citigroup end-of-period loans grew 3% year-over-year to $664 billion, as 7% growth in Citicorp was partially offset by the continued decline in Citi Holdings, and deposits also grew 3% to $966 billion. Disciplined balance sheet management drove increased net interest revenue year-over-year and our return on assets increased by three basis points year-over-year to 89 basis points. And with that, let me turn it over to Eric.

ERIC ABOAF: Thank you, John. Let me start on slide 4 with a review of how we're managing our balance sheet to achieve several business objectives. Since 2011 we deliberately held our balance sheet flat at around $1.9 trillion while expanding our client activity. Managing a compact balance sheet helps us achieve our ROA and leverage ratio goals.

On the asset side of our balance sheet, net loans grew 4% year-over-year as loan growth in Citicorp outpaced the continued wind-down of Citi Holdings. Cash and investments were 27% of our assets, up slightly from the recent quarters as we maintained a liquid balance sheet.

Our investment portfolio has grown and remains well-diversified and high quality, as we saw attractive opportunities to invest at slightly higher interest rates during the quarter. Trading assets and reverses by contrast were down 6% year-over-year, as we held less inventory in our markets business given more muted market activity.

On the liability side, we maintain a diversified, stable and low-cost funding profile. Deposits were roughly half of our balance sheet, up 3% year-over-year as we maintained deposit pricing discipline and continued to improve deposit quality. Total long-term debt has remained flat since mid-2013, consistent with our previous guidance even as we continue to optimize the composition of our debt, and our equity base grew primarily due to retained earnings and preferred stock issuance.

On slide 5 you can see how our active balance sheet management has helped us maintain a stable net interest margin during an extended low rate environment, and grow our net interest revenue at the same time. Net interest revenues were $11.8 billion in the first quarter, up from last year due to slightly higher interest-earning assets and an improvement in net interest margin.

Towards the bottom of the slide you can see that our net interest revenue per day, shown in constant dollars, has generally trended upward. Net interest margin itself increased by two basis points sequentially and year-over-year to 290 basis points this quarter. Long-term debt costs declined by 12 basis points sequentially and approximately 50 basis points year-over-year. The combination of debt maturities, targeted buybacks and redemptions allowed us to replace higher cost debt with new issuance at lower rates, reflecting both improvements in our credit spreads and our increased use of the securitization market. Over time our deposit costs have trended down steadily and were flattish sequentially. As we look to the second quarter, we expect our net interest margin to decline by several basis points likely followed by a modest increase in the back half of the year.

Turning to slide 6 let me summarize how we have positioned our balance sheet to create further opportunities for net interest revenue improvements in a rising rate environment. We evaluate our overall interest rate position under a range of scenarios considering the effects of interest rate changes on net interest revenues and on our capital position. On the left side of the page, you can see that as economic conditions have improved, we have adjusted our interest rate position progressively, with the goal of meaningful net interest revenue growth as rates rise.

As of March 31 we estimate that 100 basis points parallel rate shock would increase our net interest revenue by $1.8 billion in the first year of which $1.2 billion relates to the U.S. dollar interest rates. This would increase our net interest margin by 11 basis points. In this rate shock which is labeled Scenario 1 on the right side of the page, we estimate that our AOCI would decline by approximately $3.4 billion after-tax reflecting a decline in the value of our securities portfolio. The net effect of this change in our AOCI equates to a decline of approximately 38 basis points in our Basel III Tier 1 Common ratio.

While rising rates can reduce our Basel III regulatory capital ratios through AOCI, we would expect to recover the AOCI through both increased net interest revenue and accretion of our investment portfolio as the bonds mature at par. We estimate that these effects should allow us to recover the AOCI at risk within approximately 18 months.

In Scenarios 2 and 3 on the right side of the page, we demonstrate that our net interest revenues benefit much more from increases in short rates than from long rates. However, all these rising rate scenarios only capture part of the benefit to net interest revenue. In many cases, we would expect to see a bigger impact in later years as we reinvest our cash out the curve at higher rates. And of course any changes in our interest rate position would be based on our refreshed view of rate outlook and governed by our overall investment policy including risk limits.

Now turning to slide 7, let me discuss our year-over-year loan growth excluding the impact of FX which has contributed to our net interest revenue growth. Citicorp loans increased 9% with growth in both our consumer and corporate loan portfolios. Consumer loans grew 5%. International consumer loan volumes increased 6% led by growth in markets such as Mexico, China, Singapore and Hong Kong. North America loans grew 4%, primarily reflecting the $7 billion Best Buy portfolio acquisition in the third quarter of 2013.

Corporate loans grew 12% with 12% growth in Asia, 11% growth in LatAm and 17% growth in North America including the consolidation of the $7 billion trade loan portfolio in the second quarter of 2013. Within our corporate segment, traditional corporate lending balances increased 8% as we funded previously expended commitments and generated new loans for our target clients. Going forward we expect demand for new loan commitments may remain episodic as many of our target corporate clients remain highly liquid.

Treasury and trade loans grew 14% with growth in each of our regions reflecting strong originations in trade finance throughout the year, and Private Bank loans grew 16% led by growth in Asia and North America.

Citi Holdings loans decreased 17% year-over-year due to expected runoff and asset sales. North America mortgages represent 80% of total Holdings loans. Net credit losses in this portfolio have decreased by almost 50% year-over-year and the loss rate has improved by nearly 100 basis points to 1.9%.

On slide 8, I'd like to review the credit trends in our Citicorp consumer and corporate loan portfolios so that you can see how our geographically diversified portfolios have performed over time. The top half of the page illustrates Citicorp's consumer credit trends across our four regions. In the first quarter, total consumer net credit losses declined year-on-year to 2.45%. We have approximately $11 billion of reserves against this portfolio representing roughly 18 months of coincident NCL coverage.

In North America credit remains favorable in the first quarter and we continue to anticipate the full year NCL rate to be in the range of 3%. In Asia, the NCL rate was also broadly stable at 91 basis points in the first quarter. In LatAm, we saw an uptick in both NCL and delinquency rates. The higher NCL rate in the first quarter was primarily driven by Mexico cards as that portfolio continues to season.

We have seen a greater than anticipated impact on consumer behavior from the fiscal reforms enacted in Mexico last year, which include higher income and other taxes. This appears to have dampened card purchase activity and is resulting in increased card delinquencies across the industry. As we stated on Monday, given these changes in combination with the generally slower pace of economic recovery in Mexico we expect the full-year NCL rate in LatAm to be roughly in line with the 4.6% we experienced in the first quarter. Any losses related to our homebuilders exposure in Mexico may also increase our NCL rate in the coming quarter. However, we would expect these losses to be charged against previously established reserves.

The bottom half of the page highlights the quality of our corporate portfolio. Non-accrual loans as a percentage of corporate loans continued to improve, and as of the end of the first quarter were approximately 55 basis points for the entire portfolio. Current loan loss reserves allocated to our corporate loan portfolio provide non-accrual loan coverage of approximately 1.5 times.

On slide 9 I'd like to provide some additional texture around our emerging markets exposures in our loan portfolio. At the top of the page you can see the geographic diversification of our consumer loans. 43% of our consumer loans are in the emerging markets with the five largest of these representing 29% of all consumer loans. Mexico remains our largest emerging market consumer loan portfolio. As I just described, while we have recently seen net credit losses increase in Mexico, we remain constructive on the long-term economic and political outlook. We continue to reposition our Korean franchise. Loans were broadly flat year-over-year after a period of declining balances, and we believe our revenues there have largely stabilized, while credit has remained favorable. The credit trends in Singapore, Hong Kong and Taiwan remain stable with each market having loss rates at or below 30 basis points.

On the bottom half of the page you can see the geographic diversification of our corporate loan portfolio. Our target clients are the world's largest corporations and investors, whom we can serve in many countries and across our business segments. To a significant degree, our loan portfolio reflects their geographic presence and banking needs. 47% of our corporate loans are in the emerging markets. However, no single emerging market country accounts for more than 6% of our total exposure.
Our emerging market corporate loan portfolio is approximately 40% treasury and trade, 40% traditional corporate loans and 20% to private banking and markets clients. The higher proportion of trade loans in the emerging markets as compared with the developed markets reflects the types of client activity served in these markets. Within both TTS (Treasury and Trade Solutions) and traditional corporate lending, a significant portion of our emerging markets loans support subsidiaries of multinational companies headquartered in the developed markets.

While the GDP growth outlook for many EM economies has slowed, we continue to believe that the growth in the EM will exceed growth rates in the developed markets. In addition, our country markets should be less vulnerable to economic instability than in past cycles, with more flexible currency regimes, more sustainable levels of public debt and generally healthy current account positions.

Turning to slide 10, let's discuss our funding strategy, beginning with deposits, which continue to serve as the primary source of funding for our bank. Our overall deposits have grown significantly over the past year, in part reflecting elevated levels of market liquidity and strong corporate balance sheets. Deposit costs continue to stay low and the share of operating accounts remains high, reflecting our focus on high quality deposits.

Average deposits grew $37 billion or 5% year-over-year in constant dollar terms despite continued transfers of deposits to Morgan Stanley following our sale of the joint venture. Consumer deposits increased 2% ex-FX as growth in LatAm and North America was offset by a modest decline in Asia. We continue to shift the mix of our consumer deposits with 4% year-over-year growth in operating accounts offset by a deliberate reduction in higher cost time deposits.

Corporate deposits increased 12% year-over-year ex-FX, as continued strong deposit flows led to 15% growth in LatAm and 27% growth in North America. Our total cost of average deposits decreased 12 basis points year-over-year to 49 basis points for the quarter.

On slide 11, let me cover our long-term debt, which is a primary source of funding for our parent company and our broker-dealers, and is a valuable liquidity management and funding tool for our banking subsidiaries. During 2013, our long-term debt balances stabilized just above $220 billion, reaching $223 billion at the end of this quarter. We expect to maintain our long-term debt at approximately these levels throughout the remainder of this year, though likely with some modest reductions in parent company debt, offset by moderate growth in bank securitizations as we continue to optimize our long-term debt footprint. We manage our parent company debt to a weighted average maturity of around seven years. This term structure enables us to meet the needs of our businesses and maintain adequate liquidity to satisfy our requirements.

We continue to expect the regulators to propose minimum debt requirements in connection with their implementation of the Orderly Liquidation Authority, or OLA. While potential regulatory debt requirements have been widely discussed, we don't yet have clarity around the exact form of the requirements. We continue to believe we are well-positioned to adapt to the proposals being discussed. As of March 31, we had holding company debt, preferred stock and Basel III Tier 1 Common equity equal to 22% of our estimated Basel III risk-weighted assets, consistent with prior periods as we detail on slide 21 of the Appendix.

Slide 12 provides context for our debt issuance and redemption activity at our parent company throughout 2014. For the full year 2014, we continue to expect to issue approximately $20 billion of benchmark long-term debt, consistent with both our previous guidance and our 2013 issuance levels. We also expect to issue another $10 billion of customer-related and local country debt.

During the first quarter, we issued approximately $5 billion of debt, including $2 billion of senior unsecured benchmark debt. We also issued another $2 billion of benchmark debt early in April, which is not included in our first quarter progress update on this slide. While our issuance pace in the first quarter was somewhat below our quarterly run rate, we expect to make up some, though perhaps not all, of the difference over the remainder of the year.

We have scheduled maturities of $23 billion in 2014, approximately $6 billion of which occurred in the first quarter, and we expect to buy back or redeem approximately $10 billion of our debt throughout the year, as opportunities arise to replace high coupon securities at more attractive levels. We bought back $2 billion of debt in the first quarter and we announced redemptions of $2 billion of trust preferreds for settlement at the end of this month which will further reduce the cost of our long-term debt. When combined, our expected maturities, planned issuances and redemptions will result in approximately $3 billion of expected net redemptions at our parent company during 2014.

In terms of preferred stock issuance, in 2013 we issued $4 billion of preferred stock, followed by $480 million in the first quarter of 2014. Our Basel III additional Tier 1 capital now totals approximately 70 basis points of risk-weighted assets. We expect to issue preferred stock as market opportunities allow as we build our additional Tier 1 capital between now and when the Basel III rules are fully implemented in 2019. The time remaining until the rules are fully in effect allows us to take a more measured approach to issuance. We have previously indicated that our preferred stock issuance across 2014 will be below 2013 levels. Market development, the evolution of our balance sheet and further clarity around minimum debt requirements or other regulatory developments could alter our outlook for expected issuance and redemptions for this year.

On slide 13, we continue our recent securitization activity and our current expectations for 2014. During 2013 we issued $11 billion of securitizations backed by Citi-branded card receivables as we re-established our issuance program and worked to build a benchmark curve. This program diversified the funding sources available to Citibank in a cost-effective manner. Throughout 2014 we continue to expect to issue a total of $10-$12 billion of securitization, primarily backed by Citi-branded credit cards. Factoring in $9 billion of securitization maturities and redemptions, we anticipate net new issuance for the year of $1 billion to $3 billion. During the first quarter, we issued over $4 billion of securitization debt out of

CCCIT [Citibank Credit Card Issuance Trust] as market conditions were very attractive, allowing us to accelerate our issuance plans for the year.

Separately, last week OneMain Financial, which we own as part of Citi Holdings, priced its inaugural securitization issuance raising $760 million in a very successful offering. We had previously noted our desire to establish third-party funding sources for OneMain which will expand our options for exiting that business. OneMain's securitized debt resides outside our banks so it is not included in our expected issuance guidance on this page.

On slide 14 I'd like to update you on our liquidity profile. We size our liquidity portfolio to meet our operating needs and to withstand a variety of internal and regulatory defined stress scenarios. As of the end of the first quarter, we have $425 billion of High Quality Liquid Assets [HQLA] based on the Basel III rules, roughly flat to last quarter and above our average of approximately $400 billion over the past two years.

Over 80% of our HQLA is held in the form of Level I assets – cash, U.S. government securities, and high-quality foreign sovereigns. Just less than 20% is held in Level II assets – U.S. agency securities, U.S. agency MBS and investment-grade debt – leaving us significant flexibility to optimize our investments for liquidity and yield.

Under the Basel III LCR rules, as of quarter end our LCR was 120%, up from 117% in the fourth quarter and representing a $70 billion liquidity cushion above the 100% proposed minimum fully phased-in requirement. We continue to evaluate the U.S. LCR Notice of Proposed Rulemaking from October. Based in our current interpretation of the U.S. LCR proposal, we believe we are above the proposed minimum requirement. Certain details, however, regarding how we calculate the LCR under the U.S. rules remain under discussion, so as we clarify our understanding of the proposal, we expect there could be further refinement to our estimates.

Beyond the LCR, we are also assessing the impact of the Basel Committee's updated standards regarding the Net Stable Funding Ratio, known as the NSFR, which measures our liquidity under a 12-month stress scenario. Based on the Basel Committee's standards, we currently estimate that our NSFR is approximately 100%. We are continuing to develop our implementation plans based on the proposed rules and expect further clarity from the Basel Committee later this year as well as an NPR from the U.S. regulators in 2015.

Turning to Slide 15, let me summarize our capital position which remains among the strongest in the industry. Citi's estimated Basel III Tier 1 common ratio under the advanced approaches for the first quarter was 10.4%. In February we announced we would be required to add roughly $56 billion of operational risk RWA to our total risk-weighted assets, related to our transition to Basel III advanced approaches. The increase in RWA reduced our pro forma Basel III Tier 1 Common ratio to 10.1% at year-end. Our Basel III Tier 1 Common capital increased by $6.3 billion during the first quarter of 2014 driven by growth in retained earnings and the $1.1 billion reduction of DTA. Our estimated SLR under the July 2013 final U.S. Basel III rules was unaffected by the change in operational RWA, and increased to 5.6%. Citibank's SLR remains in excess of 6%.

Across the bottom of the slide you can see our leverage exposure under the July 2013 Basel III rules. We have held our supplementary leverage exposures fairly steady at slightly less than $2.5 trillion. As you know, the Fed released the Notice of Proposed Rulemaking last week that broadly aligned the U.S. supplementary leverage rules with the Basel Committee's final rules. While we're still analyzing potential impact of these rules, our current estimate is that our SLR would be flat to slightly higher under the proposed rules.

Moving to our last slide let me summarize four major points. First, during the quarter we saw continued progress on a number of our business priorities. Our consumer and institutional businesses performed well and we maintained our expense discipline, contributing to $4.1 billion of earnings and over $6 billion of regulatory capital generation for the quarter. We continued to make progress on legacy issues as we reduced the drag from Citi Holdings and reduced our deferred tax asset by $1.1 billion. We also announced the agreement to settle rep and warranty claims related to a significant portion of our private-label securitizations, and we took further actions to simplify our business and bring it in line with our overall strategy, including, for example, the continued repositioning of our consumer franchise in Korea, and the announced sale of our consumer bank in Honduras.

Second, we have managed our balance sheet towards achieving our overall financial targets, maintaining total assets around $1.9 trillion and optimizing our balance sheet structure to support stable net interest margin and earnings. Overall, credit trends remain favorable across both our consumer and corporate portfolios.

Third, our deposit base remains a key strength as we continue to grow high quality deposits. Our funding plans for 2014 reflect a continuation of the programs we executed in 2013 geared towards supporting the operating needs of the bank and the parent company. And lastly, our capital and liquidity position remains among the strongest in the industry. That concludes our fixed income review. John and I will be happy to take your questions.

Question and Answer

OPERATOR: Your first question comes from the line of Ryan O'Connell with Morgan Stanley. Please go ahead with your question.

RYAN O'CONNELL: Thanks very much. Two questions if I could. On CCAR, I know that the Fed has not exactly been a model of blinding transparency on this, but John when you said that based on what you know so far, it's not a question of business model. Is it fair for us to take away from that that the Fed has not raised as an issue, let's say, with the scale and the scope of the international network?

JOHN GERSPACH: You can certainly take that away Ryan, as I said, it's not a question – again based upon our interaction so far, what we're hearing, it would not be associated with either our business model or our strategy.

RYAN O'CONNELL: Okay, great. The other thing is just to clarify something that you all discussed on the earnings call, so you said that mortgage revenues are stabilizing and actually I've got really sort of two questions on that: one, originations obviously were down a lot year-over-year and also sequentially, so I guess the question is, what sort of offset that? Maybe it was servicing? Maybe you can walk us through that but also just more fundamentally, what's your outlook for your mortgage business in the U.S. going forward?

JOHN GERSPACH: The outlook going forward, we're certainly not looking for a return to where we were in years past. So I'd say that we're looking for revenues to basically stabilize at the current levels, perhaps some upside but certainly stability at this point in time would be, I think, the best way to describe it.

As far as how revenues have stabilized, we did have some uptick in mortgage servicing revenues. We had some positives that came through the mortgage servicing rights asset but also gain on sale spreads actually increased sequentially this quarter. There's a certain mix element to that as we've discussed, we've changed the mix of our origination efforts to be much more branch-focused than from third-party sources, so we see both of those elements in the stabilization of revenues this quarter.

RYAN O'CONNELL: Great, okay. Thanks, that's very helpful.

JOHN GERSPACH: Thank you, Ryan.

OPERATOR: Your next question comes from the line of Robert Smalley with UBS. Please go ahead with your question.

ROBERT SMALLEY: Hi. Good morning. Thanks. Three quick questions; first one for John, following up on your comments the other day on drivers of the loan loss reserve after TDRs you mentioned the reset of home equity loans in 2015 to 2017. Could you give us a little bit more color on that?

JOHN GERSPACH: If you take a look at the disclosures that we've put into certainly our 10-K and the 10-Q before that, we've given you a sense as to the reset of profile of our second portfolio, and we've got a rather large amount of the portfolio that is resetting in both 2015, 2016 and 2017. And that is where we see the risk. We also give you in that disclosure what we would consider to be the potential payment shock value that's in there, and so those are – that's what we are focused on.

Again, I don't think that our risk with home equity lines of credit is any different than anyone else, but it's clearly something that we want to be very careful of. You know, when you've got, I think it's roughly $14 billion, $14.5 billion, $15 billion worth of your home equity book that is resetting over a three-year period, you want to be thoughtful about how you're reserving against that.

ROBERT SMALLEY: And are you going out now to these clients and trying to get them to reset and lock in at lower rates now?

JOHN GERSPACH: We continue to work with our borrowers within the construct of a whole series of programs.

ROBERT SMALLEY: Second question, shifting gears a little bit: now that we see that cash is included in the SLR and Citigroup has always been a very liquid and big holder of cash, are you looking at that any differently? I know when we look at balance sheet and look at your liquid assets, we get a point in time I know we're going to go to an average daily balance. So maybe you could talk about how that varies and how you look at cash going forward?

ERIC ABOAF: Rob, it's Eric here. For the last year or two as the SLR was in development we have certainly kept an eye on cash and cash and AFS securities as kind of the underpinnings of our liquid asset buffer, and I don't think we were particularly surprised by the inclusion, because in truth, the SLR is about a full balance sheet and it makes some sense for full inclusion.

That said, we generally think about cash and the securities, the available-for-sale securities typically that comprise our HQLA, as a collective group of investments. Cash earns returns at the Fed at the front-end of the curve. Securities can be either held short-term, one month, three months bills, or further out on the curve. And then obviously there's a mix of treasuries, agency, MBS and so forth that we can hold with some tenor. And we generally think about the composition together of those, of the cash and those securities, as a way to properly position and minimize rate risk in our accrual books and then turn a reasonable return.

So I think I'd summarize, we don't take cash out as a very specific item, it's part of a broader set of instruments that we keep for our liquidity buffer on one hand and our investment needs and returns on the other.

ROBERT SMALLEY: That's helpful. And then my last question, and it's a more general one; as we look at the Institutional Clients Group, that has grown in size probably as a percentage of revenues for the company beyond what you thought it would be a couple of years ago, certainly. And, John, I know you made some comments on the fixed income side about shrinking pie in that business, so overall could you talk about how you calibrate the size of that business for the market going forward and the opportunities out there, and then within the company itself? And where do you feel comfortable as an overall percentage of revenues? Or how else would you measure that?

JOHN GERSPACH: Yeah, good question. I don't want to give you the – I don't want you to think that ICG is in any way outsized. We think that it's sized appropriately. If you look at the consumer and the ICG, I'd say the revenues at least in the first quarter are roughly equivalent. I'd say that we would expect in the future to see more growth coming from the consumer side, but that's consistent with what we've said back in 2009, 2010 when we first really launched the strategy.

So I'd say that the continuing low interest rate environment has probably had more of an impact on our ability to grow the Consumer business at this point in time than it necessarily has had on the totality of the ICG business. It certainly has had impacts on elements of the ICG business, like Treasury and Trade Solutions, certainly in the private bank, but not on the other elements of it. So I'd say that each is sized kind of where you would expect it to be given the economic environment, the low interest rate cycle that we just seem to be continuing to live in, and the strategy that we put forward almost five years ago now.

ROBERT SMALLEY: That's great. Thanks very much.

JOHN GERSPACH: Not a problem, Rob.

OPERATOR: Your next question comes from the line of Dave MacGown with Morgan Stanley. Please go ahead with your question.

DAVE MACGOWN: Thank you. Good morning, guys. Just a couple of topics to drill into this morning. First, looking at the good slide you have in the Appendix on the regulatory landscape, teasing out something in there. The short-term wholesale funding, I wonder if you might give us some feel for what you're expecting on that front? And related to that, if you have any plans to start giving us a little bit more disclosure around where you stack up with respect to what's a pretty good-sized secured – short-term – well, I shouldn't call it short-term without the knowledge – a repo book around $200 billion or so I think from the latest disclosures, and the disclosures on, pointing to or some of the things that your peers have been putting out around weighted average term or maturity, some detail around the type of assets, its funds, the liquidity of those assets and then investor concentration?

ERIC ABOAF: David, it's Eric. Let me give you some general perspective on short-term wholesale funding and then we can certainly talk about some of the disclosures we've made in the past and happy to reemphasize now.

Clearly, a lot of discussion with, at the Fed, appropriately, on short-term wholesale funding which is primarily around repo books, and that's been going on for the better part of a year. And we expect some sort of rules over the coming maybe a few months, few quarters, hard to gauge, on repo books in particular.

The question really, and the form of those rules is the underlying, I think, area to consider, which is are they going to be focused on the volume of short-term wholesale funding, or the quality? And quality can be further subdivided into quality of underlying collateral short-term wholesale funding where you might have more run risk in illiquid collateral than high grade collateral. Or the tenor is another measure of quality of a short-term wholesale funding book. Or the diversification of counterparties, as we've talked about that in the last few years, of how we manage to make sure that it is a robust counterparty structure.

So I think over the coming period of time we're going to learn more about what those rules may look like, volume or quality or a mix of both, and then I think we as an industry, I don't think it's specific to us, obviously have to react and have to roll that into our decisions on how much and what size repo books to run and what the quality is.

What I could tell you is, it gets to your disclosure question, is we are very focused on maintaining a high quality set of repo books. Why? Because we need to. We need to for liquidity reasons, we need to for funding reasons, and that's a critical responsibility that we have.

I think we've said in the past that our funding, our repo funding for less liquid collateral, which is the place people have some concerns around from time to time is around three months. It moves around a bit, a couple weeks here, a couple weeks there. But we've been clear about that and we have every intention to keep it at around that level, at least for the foreseeable future, and you can rest assured we have a deep and thorough set of risk limits around tenor structure of the repo book, the counterparty concentrations, the counterparty mix and so forth, across our various entities.

DAVE MACGOWN: That's some helpful color there, Eric. Is the message, stay tuned on additional disclosures there?

ERIC ABOAF: I think as the industry evolves, yeah, absolutely, we're happy to disclose what will be helpful. And clearly, off-line, if there's some specific items you'd like to see, feel free to reach out to the Investor Relations team.

DAVE MACGOWN: Absolutely. I'll do that. Changing gears a little bit, both on the last call and then today, John, you and Mike have both stated clearly that the CCAR failure was not around business model or strategy. But I wonder if you could give us a little color around whether you are seeing more sensitivity on business model or strategy in any of the other things you are lining up against or facing off against on regulatory change, and you know maybe one thing that might stand out is something like Living Will?

And related to that, as you've gone through this CCAR process now and had some speed bumps a couple times now in the last three years, is there something that you think is endemic to your business model even though it didn't directly lead to the failure this year? Is there something endemic in the business model and/or strategy that puts you at sort of a higher risk of not being able to check the CCAR box?

JOHN GERSPACH: No, as Mike said on Monday, and I said again today, there certainly is nothing in our discussions with the Fed that would indicate that there's any concerns with either our business model or our strategy. And when you think in terms of, you used the term Living Will, let's talk about recovery and resolution planning, we've been able to produce resolution plans that so far have met the requirements that have been put out there. There's nothing to indicate that there is some sort of problem with trying to meet the various regulatory requirements just because of our business model.

I think that it's incumbent on us to be able to produce the data that we need to produce at the level of specificity that we need to produce it at in order then to meet these requirements. But that's on us and our ability to generate the data. There is nothing in either the format of the regulation or the form or the substance of the conversations that we've had with the various regulatory bodies that would indicate anything differently.

DAVE MACGOWN: Helpful color John, I appreciate it.

OPERATOR: Your next question comes from the line of Pri de Silva with CreditSights. Please go ahead with your question.

PRI DE SILVA: Thank you. Dave MacGown asked part of the question that I had in mind, and related to the expected NPR on wholesale short-term funding, I know it's early to say without knowing what the NPR is, but how will it impact your funding strategy and the funding plans for the company?

ERIC ABOAF: Pri, it's Eric here. It's hard to say without seeing something, so in truth were going to have to react and adjust to what we see, but I think you can be assured it's going to be an industry-wide kind of reaction. We have a repo book, it's not the largest in the industry, it's about average in size and we have an ability to make adjustments in the size of the book, tenor structure and so forth, but it will over time mean adjustments for how repo counterparties for the industry work with us as well. If the regulators see some evolution that they'd like, by virtue of either capital charges or requirements, specific requirements on repo books, then we'll obviously have to work that through, and that'll come through not only in our balance sheet in terms of adjustments but also clients.

PRI DE SILVA: And from the client's perspective I think one of the concerns we have is how will it impact market liquidity?

ERIC ABOAF: That's a very good question. Undoubtedly, less repo will mean less liquid markets in some of those underlying instruments, and I think many have raised that that's an important consideration.

PRI DE SILVA: Thank you, Eric.

ERIC ABOAF: You're very welcome.

OPERATOR: Your next question comes from the line of John McDonald with Sanford Bernstein. Please go ahead with your question.

JOHN MCDONALD: Hi. Good morning, Eric and John. A question on the net interest revenue, not necessarily the margin percentage but the net interest revenue per day that you showed on the slide, which shows a pretty nice trend of modest growth over the last eight quarters. It looks like that metric has not historically had a second quarter dip, so I know that you mentioned that the NIM percentage may dip in second quarter due to some seasonal dividend payments that come up, but does that actually impact the NII dollars? Or is that dividend issue just kind of a NIM percentage issue?

ERIC ABOAF: John, it's Eric. Good question. There are lots of components of what impacts the NIR, the net interest revenues themselves, and then what impacts the NIM, the net interest margin that we typically calculate in basis points.

I think in the second quarter we tend to see a seasonal expansion in some of those quarters of the balance sheet, and so that would expand the balance sheet denominator, which would reduce the net interest margin in basis points. And we've typically seen that – sometimes that has to do with the dividend season in certain geographies and we'd expect some amount of that to happen this second quarter.

In terms of the net interest revenues themselves, that particular dividend season may not be a particularly large driver of that but we tend to see in previous quarters just fluctuations in the trading book net interest revenues, which tend to be volatile and move up and down by a couple million dollars per day and impact this number. And then there's always a little bit of lumpiness, whether it's a little extra cash on the balance sheet, a reserve sometimes, or an accrual on the interest revenues comes through. And so it's hard to predict kind of to the last dollar, to be sure.

JOHN MCDONALD: Okay. That's fair. So you don't have a predetermined view on net interest revenue going forward on the near-term basis. You think over time, as the balance sheet grows you expect it to improve but no predetermined view for the second quarter on that.

ERIC ABOAF: That's correct. No predetermined second quarter and we clearly had it flat but trending a tiny bit up and obviously that's what we're focused on continuing to do as we build out the earning assets. You've seen the decent growth in loans, as an example; that's part of our strategy to support the lending activities or the borrowing activities of our clients.

JOHN MCDONALD: Yeah, and then on that note, Eric, one potential hope for NII growth is card balances given your loan mix. Just kind of wondering, across your branded and retail services portfolios, have you seen any signs of life on card balances? Any increased propensity to revolve or draw on lines from existing card holders yet?

ERIC ABOAF: John, I think probably there's an internal and an external perspective on that. I think when you think about the market wide data on cards balances, I think for the first time this past fall they've started to stabilize after a long series of quarters and years where we saw customer deleveraging. So I think we're hopeful as an industry that it's not that the cards balance, and cards lending in general, is not going to continue to shrink.

That said I think you saw and probably heard Jud Linville out there describing our branded cards business. You've seen our Best Buy activity on the private label side and we clearly have a number of initiatives in place to drive growth, whether it's new value propositions, refined service offerings and so on and so forth. And so that's obviously an important priority for us. It's hard to predict when the business and the market – because both have to come together, the market has got to expand and the businesses has got to expand – it's hard to call when that will be the case but that's clearly an important focus and something that we're doing right now.

JOHN MCDONALD: Okay, great. Thanks very much, guys.

JOHN GERSPACH: No problem, John.

OPERATOR: Your next question comes from the line of David Jiang with Prudential. Please go ahead with your question.

DAVID JIANG: Hi. I had a question on page 12 of your funding plan. It doesn't seem like it's changed much post the CCAR objection. I was wondering that, given that you have potentially an incremental $7 billion of capital that may not be redeployed for another year or so, that there could be lower issuance or higher liability management exercises here?

ERIC ABOAF: David, it's Eric. Clearly there are always changes in our balance sheet that are going on. The absolute size moves around quarter by quarter and what we've done here is a set of projections. I think we'll certainly see how the balance sheet plays out, but also on the customer activity side we may see more or less inventory that we may need to hold for market making, more or less for borrowing by our clients and so I think it's a little premature to re-estimate or update the guidance that we've given here. We're certainly going to take into account some swings but I think for now we're pretty comfortable with what we have out here in terms of issuances, buybacks and the net reduction that we expect to see in long-term debt, small net reduction by the end of the year.

DAVID JIANG: Great. On page 22 on the rate cap structure and getting to the 1.5% bucket, how do you look into legging into, I guess, the additional 75 basis points? Is it really just a function of the environment and rates or other considerations?

ERIC ABOAF: David, it's Eric again. I think we've said before that we're going to leg into the next 75 basis points or so that we need of additional Tier 1 capital in a measured way. Recall we're solving for multiple objectives if we – we wouldn't want to issue all the preferreds tomorrow because there's a cost of the common equity holder of doing that. On the other hand we wouldn't want to wait all the way until 2019 because, you know, supply and demand wouldn't map out that smoothly.

So what we've said is that we want to do it in a measured way. If you count the years, there are literally five years to go. I think if you translate the 80 basis points or so that we need here that's roughly $10 billion more or less. And so if you wanted to, you could straight-line that. Obviously, we don't want to get to the very end and not be done. And so that's why we said we've done it – we'd do it on a measured pace. I think last year we had $4 billion of issuances. We said this year we'd have less than $4 billion. If you kind of compare that to what we need to do in the five years, I think there's kind of a reasonable range in there.

I think what we will factor in is market demand, appetite and pricing, right? And so if we're seeing better pricing, may act a little sooner. If we think rates won't move, we may act a little later, so I think you'll see us go to market every year on prefs but it'll be measured and, you know, within a range.

DAVID JIANG: Given the excess Tier 1 common buffer that you have right now, do you need to get to 1.5% or can you run at 1% given you have higher quality capital counting towards Tier 1 ratio?

ERIC ABOAF: I think in the short-term one can always run at less than 1.5% if you've got the common equity over and above what you need on the minimums there, the 9%.

That said, I think over time we'd like to have a balanced capital structure, and so that's partly why we don't feel we should fill up that bucket tonight or tomorrow, let's say, but over time we do want to have the 1.5 points of alternative Tier 1 preferred because that actually is probably the most cost-effective capital structure for our shareholders.

DAVID JIANG: And I'm sorry, one last question, business question. On the OneMain business, can you just size that up for us in terms of how big it is? And where – does it fall into Citi Holdings' book? And I think it's been relatively profitable. Does it make sense to hold onto that or is there still plans to fully exit? Is it too much of an RWA drag?

JOHN GERSPACH: Yeah, hi. It's John. In no particular order, the answers to your questions would be: yes, OneMain is in Citi Holdings. It's been in Citi Holdings since we first formed Citi Holdings. Two, it's about $9.5 billion, $10 billion of assets right now. We don't disclose the profitability of that business but in the past when we broke out the pre-tax margins, it was profitable at that point in time and you can assume what's happened since.

As far as longer-term, does it make more sense to hold onto it? The issue there is that, that business just doesn't fit our strategy. Again, we said it's a good business, it's very much a unique business in the current environment, but it just doesn't fit our strategy, and therefore, over time we would still look to dispose of it.

DAVID JIANG: Great. Thank you for your answers.

JOHN GERSPACH: Not a problem.

OPERATOR: Your next question comes from the line of Don Jones with Sterne Agee. Please go ahead with your question.

DON JONES: John, Eric, thanks for hosting the call. One quick question and I don't know if you have any guidance on this, but in the course of any regulatory discussions around OLA funding, has there been any guidance as to whether or not they might have non-bank operating subsidiaries also issue? And in your mind, this is kind of a judgment call, in your mind would it make sense for the Fed and the other regulators to force non-bank OpCos to also have issuance, in the sense that it might help ease the way that you guys structure your living will proposals and what not?

ERIC ABOAF: Don, it's Eric. There's been a lot of speculation, a lot of industry and regulatory discussion on OLA and trying to design a system, a process, a set of entities that make sense under resolution.

From our perspective and I think for many others, the single point of entry approach that has been, I think, the core of that OLA discussion, as far as we understand presumes the need to issue at the holding company, so that then what initially starts off as debt can get converted into equity and down streamed into the subsidiaries. And that particular single point of entry structure simplifies a number of the legal issues around converting debt into equity within a subsidiary as opposed to the downstreaming approach that I think has gained quite a bit of momentum.

So we – I think our perspective is that the simplest approach to this, though nothing is simple in resolution and recovery, is to have the issuances of the debt at the parent or at the holding company and to downstream some amount of that debt into the operating subsidiaries whether it's the dealers or the banks.

DON JONES: Okay. Great. Thank you very much.

OPERATOR: Your final question comes from the line of Scott Cavanagh with APG. Please go ahead with your question.

SCOTT CAVANAGH: Thanks for the calls guys, this is very helpful. So on page 22 I want to explore the topic, you have a number of different buffers above the Tier 1 but when we look at the counter-cyclical buffer and what the penalties are should it not be met, I wanted to know how you guys think about kind of an additional buffer beyond all these buffers just to make sure that you're not impinging upon any of these other regulatory stated buffers when I think about bonuses, dividend impairments and potentially looking at Tier 2 capital?

ERIC ABOAF: Scott, it's Eric. We certainly need to be conscious of not only the minimum requirements here, which is what's on the page, but as you describe operating somewhere above those minimums. I think we've been quite public that we need to operate with a buffer above these. We've said it would be approximately 50 basis points, and so that gives you a sense for what we think is appropriate.

What that buffer would naturally address is some of the fluctuations that you could see quarter to quarter, right? The balance sheet size or risk weights could move up or down, right? But they will change quarter to quarter. There may be some movement in interest rates which would affect the AOCI account which we covered earlier in the call, so that's something that would need to be factored into that buffer. So those are the kinds of elements that we've obviously given quite a bit of thought in terms of sizing, and where we come down today is that we would expect to run at about 50 basis points or so above these requirements.

SCOTT CAVANAGH: Thank you very much, and again, please keep up the good work with this presentation.

ERIC ABOAF: Okay, Scott. Thank you.

OPERATOR: Thank you. That concludes the question-and-answer session. Mr. Kapp, do have any closing remarks?

PETER KAPP: Thank you, everyone, for joining the call today. If you have follow up questions, please don't hesitate to reach out to us at Investor Relations, and we'll talk to you again soon.

OPERATOR: Thank you this concludes today's conference call. You may disconnect.

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