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, Regina. 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 Review, 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 the subject to uncertainty and changes in circumstances. Actual results and capital and other financial conditions 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 Factor 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 are 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 over to Eric, however, there are some key points of our second-quarter results that I would like to highlight on slide 2.

Earlier this week we reported earnings of $181 million for the second quarter of 2014. Excluding the impact of the mortgage settlement that we announced on Monday, as well as CVA DVA, net income was $3.9 billion, up slightly from last year. Before I get into our operating performance, I briefly want to discuss the settlement.

The comprehensive settlement with the U.S. Department of Justice, the state AGs and the FDIC resolved all pending civil investigations related to our legacy RMBS and CDO underwriting, structuring and issuance activities. We also have now resolved substantially all of our legacy RMBS and the CDO litigation.

During the quarter, our Institutional businesses performed well outside of Markets where macro uncertainty and historically low volatility reduced client activity, clearly impacting our fixed income and equities revenues. Corporate and Investment Banking revenue strengthened, led by strong equity and debt underwriting. And our Treasury and Trade Solutions business again saw underlying revenue growth as volumes continue to increase.

In Consumer Banking, year-over-year comparisons continue to be affected by lower mortgage refinancing activity and our repositioning efforts in Korea. But we believe these businesses have now stabilized, and we're better positioned for growth in a second half of year.
Excluding the settlement, Citi Holdings turned a profit for the first time since its formation. And we recently announced agreements to sell our Consumer businesses in Greece and Spain, which will further reduce Holdings’ assets in the third quarter. As Eric will cover in more detail, we maintained a compact balance sheet. And our net interest margin benefited from our focus on efficiently funding our operations.

Despite the mortgage settlement, our capital and liquidity continued to strengthen. We reached a Basel III Tier 1 Common Ratio of 10.6% in the quarter, and our liquidity position remains strong, with $435 billion in high-quality of liquid assets.

On slide 3 we show total Citigroup results, adjusted for the settlement and other items noted on the slide. As I just discussed, on this basis we earned $3.9 billion in the second quarter and $8.1 billion for the first half of 2014, up slightly from prior periods as lower non-interest revenues were offset by growth in net interest revenue, lower operating expenses and a decline in credit costs.

Overall, we grew both loans and deposits while improving our operational and balance sheet efficiency. And with that, I’ll turn it over to Eric.

ERIC ABOAF: Thank you, John. Let me start on slide 4 with a review of how we are managing our balance sheet to achieve several business objectives. We have deliberately held our balance sheet flat at around $1.9 trillion over the past few years, while expanding our client activity. Managing a compact balance sheet helps us achieve our ROA and leverage ratio goals. This quarter our assets increased by $15 billion to just over $1.9 trillion.

On the asset side of our balance sheet, net loans were up 4% year-over-year, as the loan growth in Citicorp remains strong. Cash and investments were 27% of our assets, consistent with recent quarters, after we maintained a liquid balance sheet. We have grown investment portfolio over the past year to manage our interest rate position and deploy some of our liquidity. Trading assets and reverses, by contrast, were down 5% year-over-year, given more muted markets activity.

On the liability side we maintained 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 increased by $4 billion during the quarter, as we increased bank-level debt and held debt at the parent company flat. And repo balances declined as we have reduced our reliance on secured funding at our broker-dealers. Finally, our equity base grew each quarter over the past year through both retained earnings and preferred stock issuance.

Now turning this to slide 5, let me discuss our loan growth, which has contributed to our uptick in net interest revenue. Total Citigroup loans increased 3% year-over-year, excluding the impact of FX, and were generally funded with additional deposits.

Consumer loans grew 6%, with broad-based growth across our regions and products. The Best Buy portfolio acquisition and growth in our U.S. mortgage portfolio led to a 6% growth in North America consumer. International consumer loan volumes increased 5%, led by growth in Asia.

Corporate loans grew 8%, with contribution from all four regions. Traditional corporate lending balances increased 9%, as we funded previously extended commitments and generated new loans to our target clients. Trade loans were roughly flat, as we sold the larger portion of our originations to optimize returns. And private banking loans grew 19%, with growth both internationally and in North America.

Citi Holdings’ loans decreased 18% year-over-year due to expected runoff in asset sales. During the quarter we moved over $3 billion of loans to held-for-sale, including $2.5 billion of loans related to the sales of our Consumer franchises in Greece and Spain. North America mortgages now represents 81% of total Holdings loans and credit trends continue to improve, as you can see on slide 31 in the appendix.
On slide 6, I'd like to review the credit trends in Citicorp's consumer and corporate loan portfolios. The top half of the page illustrates Citicorp's consumer credit trends across our four regions. In the second quarter, global consumer credit trends remains favorable, with net credit losses declining at 2.39%.

In North America, strong credit trends during the second quarter improved our outlook, and we now anticipate the full-year NCL rate to be roughly in line with the first-half results, slightly better than our previous estimate of around 3%. Asia remains stable, with net credit losses of 85 basis points. In Latin America, we saw a modest uptick in net credit losses driven by Mexico Cards, as that portfolio continued to season and consumers continued to adjust to fiscal reforms and the impact of slower economic growth.

The bottom half of the page highlights the high quality of our corporate portfolio. Non-accrual loans as a percentage of corporate loans continued to improve and were approximately 41 basis points for the entire portfolio at the end of the second quarter.

On slide 7 we quantified both the developed and emerging markets' exposures in our loan portfolios. 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 countries representing less than 30% of all consumer loans.

The bottom half of the page highlights the geographic diversification of our corporate loan portfolio. 47% of our corporate loans are in emerging markets, and no single emerging market country accounts for more than 6% of our total corporate loans.

On slide 8 we provide further context for our consumer credit performance in the emerging markets. We believe that our favorable credit performance is due in part to our target market focus, which we describe on the left side of the page. In most of our consumer markets, our retail strategy targets the affluent and emerging affluent in the world's largest Citi's.

In credit cards in some geographies we may target a broader spectrum of consumers, including a portion of the mass market. We believe that these target customers are generally more resilient than the overall market under a wide range of economic conditions. The Consumer Bank vaults includes our commercial banking business, which serves small and medium-sized businesses, with a focus on companies that value Citi's global capabilities.

On the right side of the page you can see our consumer credit statistics, as well as an assessment of our performance relative to industry benchmarks for several sub regions of our franchise. The industry comparison data represents a composite of statistics available in each country, such as delinquency, non-performing loans or net credit losses, and it includes only the portfolios where reliable, industry-wide data exist.

Our credit metrics compare favorably to local peers in most of our markets. In Mexico, where we target a broad spectrum of consumers, our credit performance has been consistently better than or in line with the industry. In many of our Asian markets, we have executed our target market strategy, yielding low loss rates and favorable credit performance versus industry peers.

Our credit performance in Korea has been stable, with 90 basis points of NCLs in the second quarter, and overall credit quality has been generally aligned with peers. Our repositioning efforts in Korea will more closely align our strategy and target market in Korea with what you see in our large Asia markets.

On slide 9, let me describe our corporate clients, who we serve through a network spanning nearly 100 countries. Target clients in our institutional businesses are the world's largest corporations, whom we can serve in many countries and across our business segments. And who we also believe are more resilient under a wide range of economic conditions.
To a significant degree, the geography and composition of our loan portfolio reflects our clients' geographic presence and banking needs. About three-quarters of our corporate client revenues come from clients we serve in five or more countries. And approximately 80% of our revenues come from companies with sales greater than $5 billion.

We provide solutions for our clients for a variety of products, including cash management and trade services, foreign exchange, lending, capital markets and strategic advisory. Our emerging market strategy is consistent with our overall corporate strategy and focuses on the overseas operations of U.S. and European multinationals, as well as the emerging champions in these emerging markets. And roughly 80% of our corporate credit exposures are rated investment grade.

Now turning to slide 10, let me discuss changes in our deposit base, which continues to serve as the primary source of funding for the lending activities in our Bank. Excluding FX, average deposits grew 4% year-over-year, despite continued transfers of deposits to Morgan Stanley following our sale of the MSSB joint venture.

Consumer deposits increased 3%, with growth in each of our regions. Corporate deposits increased 9% year-over-year, as we saw continued strong deposit flows in both Latam and North America. Our total cost of average deposits decreased 5 basis points year-over-year to 51 basis points. But increased 2 basis points quarter over quarter due primarily to increases in euro rates and central bank interventions in some of our emerging markets countries. Deposit costs again declined in North America, quarter over quarter.

On slide 11 we highlight the quality of our deposit base across multiple dimensions. Our franchise focuses on sticky low-cost deposits to ensure funding stability in times of market stress, and which should help insulate our franchise somewhat from the reversal of the U.S. quantitative easing. As you see in the first column, approximately 40% of our deposits are in the U.S., with 60% abroad.

The second column compares time deposits to operating deposit balances. We have continued to reduce our high-cost time deposits in favor of stickier accounts, such as checking and savings accounts for consumers and cash management accounts for our institutional clients.

The third column illustrates the liquidity value of our deposit base under the Basel III LCR rules. Under the LCR, deposits are assigned liquidity values based on their expected stickiness and the type of client served -- generally, 90% to 97% for retail deposits, 60% to 75% for corporate deposits, and 0% to 75% for financial institution deposits.

The liquidity rules prioritize operating accounts of consumers and corporations, and discourage the non-operating balances, in particular for financial institutions. Focusing on the deposits that have LCR value, our consumer deposits, including retail and commercial banking deposits, provide approximately 91% liquidity value. While our institutional businesses have 73% liquidity value, reflecting regulatory runoff values associated with certain types of deposits.

$104 billion of our institutional deposits have no liquidity value under the Basel III rules, including, for example, Correspondent Banking balances, some short-tenor time deposits and some deposits by financial institutions. Our historical data suggest that some of these deposits are actually stickier than the regulation suggests.

On slide 12, let me cover our long-term debt, which is the 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 the second quarter, our long-term debt balances increased by $4 billion to $227 billion. Sequentially, this $4 billion was at the bank as we prepared for the U.S. version of the Basel LCR.

We increased credit card securitizations and long-term FHLB advances a bit as we purposely strengthened our liquidity buffers to meet the more stringent proposed U.S. standards.
Through the remainder of 2014, we are likely to see further modest growth in long-term debt at the bank across a mix of securitizations and FHLB advances.

By contrast, parent company debt remained flat during the quarter, although we did continue to refinance high-cost debt with new issuance at lower levels. We expect parent company debt to decline modestly through year-end 2014.

Slide 13 details our debt issuance and redemption activity at our parent company. For 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 half of 2014, we issued approximately $15 billion, $9 billion of which was benchmark debt. We have deliberately diversified the composition of our debt issuance this year with offerings ranging from three years to 30 years, senior to subordinated, and in euros as well as dollars. We expect maturities of $26 billion in 2014, of which approximately $14 billion occurred in the first half of the year.

We continue to expect to repurchase or redeem $10 billion of debt this year. In the first half of the year, we repurchased $5 billion through open market buybacks, tender offers and trust-preferred redemptions as we continued to refinance our higher-cost debt at more attractive rates to lower our cost of funds. And we announced a tender offer this week for up to an additional $2 billion of securities.

Additionally, since 2012 we have issued approximately $9 billion of preferred stock, including $1.7 billion during the second quarter. As of June 30, our additional Tier 1 Capital represented approximately 80 basis points of risk-weighted assets. We expect to continue to issue preferred stock between now and when the Basel III rules are fully implemented in 2019, at a measured pace.

As we have previously indicated, we expect our preferred stock issuance volume in 2014 will be below 2013 levels. Market developments, 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.

On slide 14 we cover Citibank's recent securitization activity and our issuance plans for 2014. Our securitization activity helps us diversify Citibank's funding sources and optimize the Firm's liquidity position at cost-effective pricing levels.

Throughout 2014 we expect to issue a total of $15 billion of securitization debt, primarily backed by credit cards, somewhat more than our previous book guidance and in response to investor demand and growth in our bank balance sheet. This additional securitization activity will complement the deposit growth and other funding sources as we plan for the U.S. LCR rules.

Separately during the quarter, OneMain Financial successfully completed its inaugural securitization, establishing independent source of financing. OneMain issuance is not included in this slide.

On slide 15, 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 regulator-defined stress scenarios on a consolidated basis and at our operating units. As of June 30, we had $435 billion of high-quality liquid assets based on the Basel III LCR rules, up by $10 billion from last quarter. Our Basel III LCR rose to 123% from 120% last quarter, driven by increased bank-level debt issuance and an improvement in our deposit quality.

We purposely increased our liquidity buffers to prepare for the U.S. LCR, which we expect to be finalized later this year. As we have indicated previously, the proposed U.S. rules are more stringent than the Basel standards. Based on a current interpretation of the U.S. LCR proposal, we believe we exceed 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.

We are also assessing the impact of the Basel Committee standards regarding the Net Stable Funding Ratio, which measures our liquidity under a 12-month stress scenario. Based on what we know today, we believe that we are in compliance with the NSFR, based on the Basel Committee standards. We expect further clarity from the Basel Committee later this year, and an NPR from the U.S. regulators in 2015.

On slide 16 you can see how our active balance sheet management has helped us maintain a stable net interest margin during an extended low-rate environment, while growing our net interest revenue. Net interest revenue was $11.9 billion in the second quarter, up 2% from last year, driven by higher loan volumes and an improvement in funding costs. Sequentially, our net interest margin declined 3 basis points to 287 bps in the second quarter, driven by lower asset yields, partially offset by lower funding costs.

As I described earlier, deposit costs increased by 2 basis points this quarter due to increases in prevailing rates in euros, as well as central bank interventions in certain emerging markets. This increase was more than offset by continued declines in the cost of our long-term debt of 19 basis points this quarter and 68 basis points year-over-year as we refinanced maturities at lower rates and bought back higher-cost debt. We currently believe that net interest margin should remain roughly flat to second-quarter levels for the remainder of the year.

Turning to slide 17 let me summarize how we have positioned our balance sheet to create opportunities for higher revenues 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 we have adjusted our interest rate position progressively over time, with the intention of benefiting from potential increases in interest rates. As of June 30, we estimate that a 100-basis point parallel rate shock would increase our net interest revenue by $1.9 billion in the first year, of which $1.3 billion relates to U.S. dollar positions. This would benefit our net interest margin by 11 basis points. In this rate scenario, we estimate that the value of our securities portfolio will lead to a decline in AOCI of approximately $3.4 billion, for a reduction of approximately 38 basis points in our Basel III Tier 1 Common Ratio. In scenarios two and three on the right side of the page, we illustrate that our net interest revenues would benefit more from increases in short rates than from long rates.

However, these rising rate scenarios only capture part of the potential benefit to net interest revenue. In many cases, we would expect to see even more revenue upside in later years as we reinvest our cash at higher rates further out to the curve.

These estimates necessarily incorporate many assumptions about customer behavior, new business, pricing decisions and prepayment rates, for example.

Turning to slide 18 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 second quarter increased to 10.6% from 10.5% in the first quarter, despite the mortgage settlement costs in the quarter.

Risk-weighted assets under the Advanced Approaches increase by $13 billion, in line with balance sheet growth. Under the Standardized Approach, our Basel III Tier 1 Common Ratio decline to 10.8%. Risk-weighted assets under the Standardized Approach grew due to balance sheet growth, including growth in loans and ongoing refinements to our models. Our estimated SLR increased to 5.7%, aided by the $1.7 billion of preferred stock we issued this quarter. Citibank's SLR remains in excess of 6%.
On slide 19 we detail the growth in our regulatory capital this quarter, which led to an increase in our capital ratios, as I just described. On the right side of the page, you can see that both Citicorp and Citi Holdings contributed to the $1.1 billion of DTA utilization.

On the left side, we show that the Basel III Tier 1 Common Equity increased by almost $4 billion this quarter. Of that, $2.2 billion was due to DTA utilization and an increase in the amount of allowable DTA under the 10% and 15% buckets. The remainder was primarily related to an increase in AOCI, related to gains in our securities portfolio.

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 in a difficult operating environment. We resolved another major legacy issue with our mortgage settlement. Citi Holdings turned a profitable quarter on an adjusted basis. And we utilized another $1.1 billion in DTA.

Second, we have actively managed our balance sheet, with an eye towards achieving our overall financial targets, maintaining total assets around $1.9 trillion and optimizing our assets and liabilities to support stable net interest margin in 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 2014 issuance plans are on track and are designed to support the operating and regulatory demands of both the Bank and the Parent.

And lastly, our capital and liquidity position remains strong, relative to the industry.

That concludes our Fixed Income Review. John and I will be happy to take your questions.

Question and Answer

OPERATOR: Our first question comes from the line of Ryan O’Connell with Morgan Stanley. Please go ahead.

RYAN O’CONNELL: Thank you. Very thorough presentation, and in particular I really appreciate the added detail on the various Consumer businesses. Two questions, if I could. One, as you know, Goldman reported that it had reduced the amount of repo financing as providing to certain clients for reasons they spelled out -- CCAR, Basel III, things like that. And so my first question is, has Citi changed the level of its activity in that area?

ERIC ABOAF: Ryan, it's Eric. You can see on our balance sheet report in our supplement that if you look at repo as one individual line, reverse repo activity is down about $10 billion, $15 billion versus the prior year and prior quarter. So it is down modestly, but it really bounces around on that line.

I think the broader answer to your question is that active balance sheet management for us is nothing new. We've been at it for two, three, four years. We've been disciplined about supporting our clients in their financing needs. You see our loan book has gently grown over the years. And we've also been disciplined on the other side with some of our markets activities, where we see less demand and less activity.

And you see that we're pretty willing to adjust our positions in a way that's quite thoughtful. I think the net result of that has really been a balance sheet that is pretty flat in a time where it could have grown. And it is something that we would like to continue.
RYAN O’CONNELL: Okay, thanks, that’s very helpful. Then, second question is just the outlook for International Consumer, which is down about 30% year-over-year and down a quarter or two. So I think John had talked about this on the call, the cost of the Korea repositioning, the higher Korea provisions in Latin America. And one, I wanted to clarify the comment on the conference call. I think, John, you said that repositioning charges would stay at the Q2 level for a while. Did I get that right?

JOHN GERSPACH: Ryan, I think the comment you are referring to is that the repositioning charges I said for the second half of year for all of Citigroup will be about the same level as we had for the first half of the year.

RYAN O’CONNELL: Okay, so not specifically for International Consumer?

JOHN GERSPACH: No, that was a comment for the overall repositioning charges at the Group level.

RYAN O’CONNELL: Okay, that’s helpful. Then just in terms of what’s going on with credit quality in Mexico -- again, you’ve been very candid about that. Given what’s going on with the 90+ DPD and NCLs, is it reasonable to assume that provisions will stay at this level for a while for Latam?

JOHN GERSPACH: Well, what we said on the call was that our expectation is that the NCL rate for Latin America for the second half of the year, again, should be roughly equivalent with what we had in the first half of the year. So we will let it stand at that.


JOHN GERSPACH: Not a problem, Ryan. Thank you.

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

ROBERT SMALLEY: Hi. A couple of different questions, and thanks for doing the call, John and Eric. John, you started off, you mentioned the settlement. In there, there’s a material amount of consumer relief. Could you talk about the accounting for that? Do these loans get written down, then go back on performing?

And I think you’ve had another settlement where you’ve had another amount of consumer relief as well. How do you look at that in terms of drag on the NIM, or just not as productive assets as they could be?

JOHN GERSPACH: The answer to your questions are not quite, yes, and a little bit. So in starting where -- I think you started with the consumer relief portions of the current settlement. There are a lot of different elements that comprise the consumer relief portion of the settlement that we announced on Monday. Some of them involve forgiveness of loans or interest on loans. A good portion of them also involve where we will provide financing to help the various government agencies -- HUD -- provide affordable housing, that's specifically construction of rental units in certain areas of the country. So there are a variety of elements.

Some of the loans where we will be providing very specific relief, those are loans where we may have already taken write-downs. And then some of them could be loans where we’re taking new actions. So depending upon what category the specific consumer relief comprises, you are going to get different treatments on the assets.

ROBERT SMALLEY: That's helpful. And just in terms of the overall P&L impact, some -- but not a lot -- is your answer?

JOHN GERSPACH: Well, what we've done is, we've looked at all the different components of the $2.5 billion worth of consumer relief. We've come up with an estimate as to what those components will cost
us over the timeframe in which we will be conducting those relief efforts. And that cost -- what we estimate to be the full cost of those efforts -- was included in the $3.8 billion charge that we took in the quarter.

ROBERT SMALLEY: Okay. That makes sense, thank you. Secondly, on OCI -- and thank you for the other detail on slide 34 -- and I was hoping to link the two. When I'm looking at slide 17, you've got a 10-year rate rising by 100 basis points. And the Basel III Tier 1 effect, 13 basis points, I'm mapping that to on page 34 what we saw in the second quarter of 2013 where we had the 64 basis point rise. And if I'm reading this right, then in terms of rate and other OCI, that cost 14 basis points.

So what it appears to me is that if you've got the extra, call it 36 basis points, similar type of impact. So what have you done with the portfolio between then and now to insulate against higher rates? And have you actually tried to take out more of the risk of spikes, as opposed to just a general rise?

ERIC ABOAF: Rob, it's Eric. Let me give you a little bit of color, first in terms of interpreting the slide 17 scenario and the slide 34 actuals. And then I'll touch on the question a little more broadly. Just to be clear, slide 17 is a very simple rate shock. It's a 100 basis point shock in interest rates across the full curve, from overnight all the way to 30-year. It is around the world for every interest rate in every currency. So it's a globally synchronized shock. And we do that just as a point of reference.

What you see in contrast on page 34 is actually the actual rate changes that occurred, where we listed out here just for reference the U.S. dollar 10-year yield change across each of those quarters, including the 64 basis points that you referenced in the second quarter of 2013. But obviously the curve didn't move in a full parallel shock in the U.S., let alone by those amounts in each of those international currencies. So that's what's going to result in a different amount of AOCI change that you see on the table at the bottom of page 34, relative to what you see on page 17. Just to try to be clear.

And then, I think the broader question you asked is, did we adjust our interest rate position on our portfolio? And the answer is that we have gently adjusted the position. You see that on page 17. But it moved a little bit on a one-year interest rate exposure basis. And as we've said, we like to run short to be prepared for rising rates. And what we'll do as we see shifts in the curve -- whether it's a dollar curve, the euro curve or some of the emerging market currencies -- where we will tactically adjust our positions at the front end or the back end. And that's really what ends up moving the IRE numbers on page 17 around that you saw.

ROBERT SMALLEY: Okay. But no dramatic changes in strategy or outlook?

ERIC ABOAF: No, not at this point.

ROBERT SMALLEY: Okay. Last one for me. On FICC earnings, everybody came in a little bit better than expected, where flat or slightly down was much better than down a lot. As far as your operations go, your FICC trading business and underwriting business are as big as anyone's at this point. I think last call we talked a little bit about trying to dimension or size the operation with respect to the market.

My question is, what kind of metrics are you using to judge success here, in terms of return on equity targets? What are they? Allocated capital? And are you including some of the other ancillary things you need to do to do those businesses? Say, extending loans and revolvers to clients in order to get equity and debt underwriting businesses in that calculation?

JOHN GERSPACH: Yes, Robert; it's John. I'm not going to go into the individual metrics of the businesses. But first and foremost, we look at the overall returns of the ICG. Because, again, for us the ICG is not so much a collection of individual product areas; it's really a client-centric business. So we view all of these product areas as means to provide solutions for our clients.
Our first set of targets really are the overall returns, both from an ROTCE and ROE, and an efficiency ratio measurement that we establish for the ICG. And we've shared with you the efficiency target that we have for the ICG. In the investor deck that we used both at the conference that we spoke at, at the end of May, as well as with the deck that we used with Monday's investor call, we also showed you the current return on allocated tangible common that we are getting out of the ICG.

So those are the real measurements. After that, it becomes one of how do we want to apportion our resources then? And what's the right capacity in each of the product areas that we use to provide solutions for our clients? And that's been an ongoing recalibration.

We've had a certain amount of discussion, both within our shop and I think the whole industry has, as far as how much of the impacts that we've all seen in the FICC markets had been cyclical impacts, as opposed to secular. So we have clearly adjusted our capacities in each of the products, both from the amount of balance sheet that we will devote to the FICC products, as well as the level of front office and back office headcount that we have in those businesses. So it's very much an ongoing recalibration of the business as we try to manage to the overall returns for the ICG.

ROBERT SMALLEY: That's very helpful, thanks a lot. Appreciate it.

JOHN GERSPACH: Not a problem.

OPERATOR: Your next question will come from the line of James Strecker with Wells Fargo. Please go ahead.

JAMES STRECKER: Good morning, guys. Thanks for having the call, and I just wanted to echo what Ryan and Rob both said -- we really appreciate the additional color here. I think it differentiates you versus your peers, and definitely helps your spreads, in all honesty.

A couple of high-level questions, and maybe more one on the funding side. Going back to the settlement from Monday, any color you can offer on the CDO component of that as we try to size that piece of it?

JOHN GERSPACH: No. As we said on Monday, it was a comprehensive settlement, negotiated over a pretty extended period of time. So I'm not going to break the various cost elements down. I'm not quite sure that I could give you precision there. But clearly for us, it was very important that we get as broad a release as possible on the CDO activities. We think that the terms of the settlement as announced give us the release that we were looking for, with regard to the CDO-structuring activity that we had.

JAMES STRECKER: Okay, fair enough. Figured I'd ask. Then just jump into the funding side of it. As we sit here and try to dimension the ultimate Tier 2 bucket for the Advanced Approaches banks, I know it is pretty hard to do right now because you've got differences in terms of transitional, whether you are being held to the Standardized versus Advanced Approach in any given quarter.

But if we try to look at it from a fully phased-in basis, is it fair to say that you all would try to run as close as possible towards the 60 basis points of allowable loan loss reserves? Or how should we think about that bucket? Because obviously it makes a big difference in terms of potential sub debt need.

ERIC ABOAF: James, it is Eric. I think in asking a question you actually threw out a number of the dimensions that we'd look at. And whether it is Basel I, whether it is Basel III transitional or Basel III fully phased-in, and therein lies some of the answer, as you surmise. Which is, over time we'll find a way to converge, but it will take time.

In terms of if you fast forward to a Basel III era, clearly Tier 2 capital has two components. It's got the underlying qualifying sub debt. And then it has what are actually excess reserves over expected credit losses, which is a risk-based calculation.
And we will have to see how we run year after year and quarter after quarter on that latter category. And then we'll effectively fill in the rest of the 2 percentage points of Tier 2 with sub debt. You'll see us monitoring that. You'll see us phasing that in, and just like some of our other work that we've done, like in the alternative Tier 1 space, we'll do that over time.

JAMES STRECKER: Okay. Is it fair to say that, given that regulators and investors are presumably looking for an elevated level of loan loss reserves versus the pre-crisis norm, that you would view that more favorably? I'm not trying to box you into anything here; I'm just trying to think about potential supply. And since you need to have it anyway, why necessarily come to the sub debt market to fill that entire bucket? Is that fair?

ERIC ABOAF: I think that's a fair hypothesis. The way I would say it is: pre-crisis, there were not very many loan loss reserves on the books of banks. So they wouldn't have gotten the benefit in the Tier 2 bucket of excess reserves as it's now calculated. I think going forward it is much more likely that we will have some contribution from the excess reserves. The question will be how much. And that will be the first port of call, as to how to think about Tier 2, and then the balance will be sub debt.

JAMES STRECKER: Okay. And then maybe a high-level one for John, if you don't mind. Obviously the situation in the Ukraine and Russia has escalated in the last day. In Q2, Citi called out some hedging losses in EMEA, presumably around this same situation. How should we think about your exposure there, your willingness to put on additional hedges, things like that, for the current quarter?

JOHN GERSPACH: Well, let's separate it actually into two separate discussions. One is, as we did in the first quarter 10-Q, we will clearly update you as to what our various positions in Russia are. And in general, I think we laid out our exposure in Russia as about $9.6 billion or so worth of credit exposure, and a capital base of $1.7 billion or so. We'll update you on those figures. You can assume that the exposure is down somewhat from the first quarter.

With regard to the losses that I spoke about on the call on Monday, they were not losses specific to our Russia franchise. They were de-risking positions that we had put on for our overall equity portfolio back early in the second quarter, when we were first looking at what some of the impacts might be. Those positions, as I said, were lifted because the markets did not react as badly as we thought we had, and we absorbed the losses that we had on those positions in the second quarter.

As to what extent we'll think in terms of putting on hedges for the current situation, I'm really not going to go into that at this point in time.

JAMES STRECKER: Okay, understandable. One last ticky-tacky one, if you don't mind. Was there a market gain in the quarter? And what was the geography of that, if there was one?

JOHN GERSPACH: We did have a gain on the equity investment that we had in market. It was included in our equities figures.

JAMES STRECKER: Okay, perfect. Thanks a lot.

JOHN GERSPACH: Okay.

OPERATOR: Your next question will come from the line of Michael Rogers with Conning Asset Management. Please go ahead.

MICHAEL ROGERS: Yes, good morning. You mentioned in the early comments that the settlement had resolved all pending civil investigations. I'm just wondering, are there any criminal investigations that remain ongoing?
JOHN GERSPACH: All I can say as far as ongoing investigations is, we give you a listing of all the significant investigations that we are currently involved with in our 10-K and our 10-Q. And you should take a look at what's going on there.

MICHAEL ROGERS: Okay. I will check that, John. Secondly, any update on when we can expect -- I know this is an ongoing question, certainly it's getting a little old -- but on when we can expect any further info on OLA? And related to that, to the extent that S&P uses that as the catalyst for a possible one- to two-notch downgrade of you and some of your peers’ senior debt ratings, how might that affect counterparties' ability to continue to do business with you in the same magnitude that they were able to do before any downgrades?

ERIC ABOAF: Michael, it's Eric. We don't have any new news on OLA. I think we're waiting on some rule-making or some announcement, but I don't know that anything is imminent, and we really don't have a timing at this point. So probably I think we're all in the same bucket of wait and see.

In terms of catalyst, I suppose it could be a catalyst for S&P. S&P has been clear that they're monitoring the situation. They, on an ongoing basis, are taking a look at it, and we'll just have to see.

I think to the more tactical question you asked, which is how would that affect your position with counterparties and so forth. I'd have to tell you that the last couple of years, as we've seen, ratings changes, we've not seen a lot of changes in terms of those willing to do business and not willing to do business with us. You've seen our CDS has not reacted, and our bond spreads have not reacted very much. So we don't really see much of an impact.

MICHAEL ROGERS: Okay. Well, thank you for that. And the last one, I would have for John. John, aside from the geopolitical risks that have already come up in the discussion, what would be your chief worry at the present moment?

JOHN GERSPACH: I'd be afraid to give you that on the basis that I would miss two or three others. I think if you asked any of our peer institutions' CFOs, they would tell you that they tend to sleep at night like a baby; they wake up every two hours and cry. I'm not quite sure that there's any one in particular item that I would give you.

MICHAEL ROGERS: Okay. Thank you both.

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

PRI DE SILVA: Good morning, John and Eric. Is the cash consideration of the settlement reflected in your second half funding plans?

ERIC ABOAF: Pri, it's Eric. The funding plan that I've given you is an all-in funding plan for the whole company, and includes all the changes in the balance sheet that we expect. It includes changes in lending assets, in trading assets and reverses. I could go down the 10 lines of the asset side of the balance sheet and the 10 lines on the liability side of the balance sheet. And so it absolutely incorporates everything, including any sort of settlement.

PRI DE SILVA: And the second question that I have, and Ryan kind of went in there, in terms of the SLR, I know we all had some time to evaluate the finalized version. How do you see it impacting the balance sheet, particularly on the repo side and the trading book? And also, do you see it impacting
various businesses and leading to lower levels of activity, and also wider bid-ask spreads, especially for the fixed income side?

**ERIC ABOAF**: Pri, it's Eric. I think that's a fair question. I think you saw that we reported an SLR of 5.7%, so we are well above the standard and we have every intention of staying there.

I think what you have seen is, the SLR has had different impacts on different banks around the U.S. and around the world, right? Some banks are a good bit below the 5% standard and have to literally exit portions of their book, and we've seen some of that over the recent quarters. And other banks, like us, have actively managed our balance sheet for a number of years and so we haven't had to take any drastic actions recently.

I think what you'll see us do is continue to be careful and disciplined in how much client financing in the form of reverse repo that we do. We don't have the largest book out there; we don't have any intention of having the largest book out there. We'll continue to run it in a very targeted and thoughtful way for our best clients. That's what we do. And in other areas, we'll also be very disciplined. You saw our loan book continues to grow in the mid-single digits. We've seen some nice opportunities in corporate loans in particular that have grown high single digits.

On the other hand, in trade finance, we've seen more limited opportunities to earn the returns and spreads that we would like that would support our ROA or SLR objectives. And so we've moved to more of an originate-to-sell model and actually limited the balance sheet growth in that product. Those are the kinds of actions and approaches we're taking. And like I said, it's something we've been doing for several years and obviously will continue to do as we conform to the variety of rules and incentive.

**PRI DE SILVA**: Thank you, that was actually very helpful. Thank you.

**OPERATOR**: Your next question will come from the line of Gerard Cassidy with RBC Capital Markets. Please go ahead.

**GERARD CASSIDY**: Thank you very much for having me participate in the call, John. Question for you following up from the call earlier in the week regarding the Shared National Credit exam. I wasn't completely clear whether your results reflect the possible reclassifications that may have occurred to some of the loans on your books from the Shared National Credit exam that the regulators of course do every spring. Is that the case? Or is the reserving not really reflective of that yet?

**JOHN GERSPACH**: No, Gerard, always nice to talk to you, especially twice in one week. We don't have a rule against double-dipping, so more than happy to talk to you twice.

**GERARD CASSIDY**: Thank you.

**JOHN GERSPACH**: It's okay. As I tried to say on Monday's call, we still don't have the final report. And obviously the results -- since they are regulatory communications, our specific results are going to be confidential. Having said that, we have gotten the preliminary feedback from the regulators concerning this year's exam. And I would say that, based upon that preliminary feedback, we'd have minimal changes to either our ratings, our classifications or our reserving actions.

**GERARD CASSIDY**: Great, that's very helpful. And another question. There was a couple of stories in the Wall Street Journal in June about some potential problems in China with loans that are secured by, I think, inventories of some types of commodities, and there may be some fraud-related. But Citigroup was mentioned in this story, along with Standard Chartered and maybe a few others. Do you guys have any further color on that?
JOHN GERSPACH: When you look at the stories that are hitting the paper, in total, our exposure is, we’ve got roughly $400 million worth of repo commodity financing to our clients in China. I’d say approximately $280 million or so of that exposure is related to the two ports that are most in question, Penglai and Qingdao. Those are the two ports that I think most people have mentioned, as far as being involved with fraud around the sale and storage of physical metal. But at this stage, we believe the activities are isolated and just specific to those very specific locations.

Now, it's important that when you take a look at the numbers that I've given you, the financing I'm talking about, we have provided to clients that are non-Chinese subsidiaries of large multinational corporations, and the contracts are guaranteed by the parent companies. So we have no direct exposure to local Chinese counterparties.

GERARD CASSIDY: That's very helpful, thank you. And then finally, I know it's been since April when Mexico came out with their competitive studies, how they want the financial services industry in Mexico, the banking industry to become more competitive. Have you guys given it more thought on the long-term implications of what that might do for Banamex? Will it affect its profitability? Have you been able to determine that yet on what you understand what these changes are going to be?

JOHN GERSPACH: No, Gerard, we're still working through all of the implications of the report. It's something that we will certainly continue to discuss, and we will take all of that into consideration as we think in terms of how to position the franchise for 2015 and beyond.

GERARD CASSIDY: Thank you, John, I really appreciate it. Thank you again.

JOHN GERSPACH: Not a problem, Gerard.

OPERATOR: Your next question will come from the line of Louise Pitt with Goldman Sachs. Please go ahead.

LOUISE PITT: Good morning guys, thanks very much for doing the call. I guess it's good afternoon just now. A lot of them have been asked, but I just wanted to clarify some of the comments that you made about potential issuance. Specifically, you said that you would do fewer prefs this year than you did in 2013. You've seen what we've done this year so far in aggregate. And I think we've been pretty clear we'd like to continue to issue, but we are planning on doing less than last year. I give you that data on a full-year basis; I think it's a little more helpful that way. And hopefully that helps you.

ERIC ABOAF: Louise, it's Eric. Fair question. I think last year we did just north of about $4 billion of issuance. You've seen what we've done this year so far in aggregate. And I think we've been pretty clear we'd like to continue to issue, but we are planning on doing less than last year. I give you that data on a full-year basis; I think it's a little more helpful that way. And hopefully that helps you.

LOUISE PITT: Okay, great. Then just a follow-up question. I make it from the numbers that you provided for maturities, redemptions, issuance, et cetera, that there's probably slightly over $10 billion of benchmark issuance left for this year. Are you looking primarily at the dollar market for that? Or are you done for this year?

ERIC ABOAF: Louise, we tend to do the bulk of our issuance in dollars. I think you've seen that over the last few years. That said, some of the foreign currency basis and the embedded credit spread that we can issue at in euros has started to normalize with dollars. Yen has gotten a little closer. So we continue to look around the world and see where there are opportunities.

But in effect, what we do, because we are a dollar-based Firm is, we look at it on an apples-to-apples basis. So I think primarily dollars, and we will supplement that outside as we see some nice opportunities. Clearly, we like a wide footprint. So we'll continue in that direction.
LOUISE PITT: Okay, perfect. I'm sorry, just a last, more detailed question. In terms of the liability management exercises, I know you guys always provide a generic reason behind it, but given the one that you announced this week, is there anything specific behind the bonds that are included in this latest one? I know I always ask the same question, but it's a little random from you guys.

ERIC ABOAF: Nothing particularly specific. We continue to look for opportunities. I think if you had a chance to look on our average balance sheet schedule, which shows our cost of funds and our yield, you'd see our cost of funds have been systematically brought down on the long-term debt line. And a lot of what we've been actively doing in liability management is working those funding costs. So the general heuristic is we look for debt that is more expensive than it should be, that might trade wide to the curve, and we tend to like to retire those bonds and then re-issue something that is closer to benchmark.

LOUISE PITT: Okay, perfect. Thanks a lot.

ERIC ABOAF: Thank you.

OPERATOR: Your final question will come from the line of Jeff Bernstein with Cutwater. Please go ahead.

JEFF BERNSTEIN: Hi. I had a question about Citi Holdings. Obviously we've been watching the charts for quite a long time, and watching the numbers come down and improve. How long would you say we should be looking for Citi Holdings as an entity -- on a run rate basis, we could be looking at this thing for a very long time. I want to know if you had made any comments as to how long this could go on.

JOHN GERSPACH: Hi, it's John. I don't want to put a time span on Citi Holdings. Taken to the extreme, to your point, if we wait until the absolute last mortgage pays off, Holdings could go on for decades yet. I don't see that happening. At the same point in time, I don't see it going away while we still have the level of assets that we currently have in Holdings, and the fact that it still includes a wide array of businesses in it.

I think it has served a very useful purpose for us by being able to one, differentiate the future of Citi, as opposed to the past. And more importantly, from a management point of view, by putting a very specific team against the Holdings assets, I think that it has really enabled us to bring those assets down much faster. With a much more concerted effort than we would've had, had we left all of those assets in the various businesses. So I'd say it's got some time yet to run, but I wouldn't say it's going to be around very long.

JEFF BERNSTEIN: Thank you very much.

JOHN GERSPACH: Okay, not a problem.

OPERATOR: That concludes the question-and-answer session. Mr. Kapp, do you 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 in Investor Relations. We'll talk to you again next quarter.

OPERATOR: Ladies and gentlemen, this concludes today's conference call. Thank you all for participating. You may now disconnect.
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