Host
Tom Rogers, Head of Fixed Income Investor Relations

Speakers
John Gerspach, Citi Chief Financial Officer
James von Moltke, Citi Treasurer

PRESENTATION

OPERATOR: Hello. And welcome to Citi's Fixed Income Investor Review with Chief Financial Officer, John Gerspach; and Treasurer, James von Moltke. Today's call will be hosted by Tom Rogers, 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. Rogers, you may begin, sir.

TOM ROGERS: Thank you, Thea. Good morning and thank you all for joining us. On our call today our CFO, John Gerspach, will speak first. Then James von Moltke, our Treasurer, will take you through the fixed income investor presentation, which is available for download on our website, citigroup.com.

Before we get started, I'd 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 2015 Form 10-K.

With that said, let me turn it over to John.

JOHN GERSPACH: Okay. Thank you, Tom, and good morning, everyone. We're pleased to be hosting our Fixed Income Investor Review this quarter. I'd like to begin by highlighting some key points from our second quarter 2016 results. After that I'll turn the call over to our Treasurer, James von Moltke, who will provide an update on our balance sheet and issuance plans. Then we'll be happy to take your questions.

Last week we reported net income of $4 billion or $1.24 per share. These results were driven by our core businesses and reflected our ability to generate solid earnings in a challenging and volatile environment.

Additionally, we continue to make progress in key areas. We grew loans and deposits in both our Institutional and Consumer businesses. We continued to utilize deferred tax assets, bringing the total utilized to $10 billion since the peak in 2012, driving $15 billion of regulatory capital growth. We significantly improved our efficiency ratio, return on assets and return on tangible common equity relative to the first quarter. And we continued to make progress in winding down Citi Holdings.

Corporate and Consumer credit quality was stable this quarter. And we saw a significant decline in corporate cost of credit, particularly in energy, as the portfolio benefited from the stabilization of oil prices and increased capital markets activity.

We maintained a diversified funding profile. Our deposit quality remains strong. We continued to execute against our debt and preferred stock issuance plans. And we reduced our estimated TLAC shortfall. And our regulatory capital, leverage and liquidity ratios remained robust.

On slide 3 we show total Citigroup results. As I noted a moment ago, in the second quarter we earned $4 billion. Revenues of $17.5 billion were down 8% from last year, and expenses decreased 5%, each driven primarily by the continued wind down of Citi Holdings, as well as the impact of foreign exchange translation.
Citicorp revenues were flat to the prior year in constant dollars. And credit costs improved, reflecting lower net credit losses, partially offset by a smaller net reserve release compared to the prior year.

As I noted earlier, Citicorp was the predominant driver of profitability in the second quarter, contributing 98% of total net income. And importantly we saw a significant improvement in results in Citicorp relative to the prior quarter with pre-tax earnings of $5.7 billion, growing over 25% sequentially on higher revenue, lower operating expenses, and improved cost of credit.

We reduced Citi Holdings assets by $7 billion this quarter, ending the period with $66 billion of assets or just 4% of total Citigroup, with signed agreements in place to sell $7 billion of this amount.

And now let me turn the call over to James.

**JAMES VON MOLTKE:** Thank you, John. Beginning on slide 4 we show balance sheet trends over the past five quarters. On a reported basis total assets decreased by nearly $11 billion in the past year but increased $18 billion from the first quarter.

To better reflect underlying trends, we’ve presented this slide and several others in today's presentation on a constant dollar basis. On this basis our balance sheet increased $10 billion from the prior-year period or approximately 1%, as we continued to grow our core businesses while winding down Citi Holdings.

Cash and investments, which are predominantly high quality liquid assets, increased 5%, as we continued to maintain a strong liquidity position.

Citicorp loans grew 6%, reflecting the continued strength of our core customer franchises as well as the impact of the Costco portfolio acquisition, which closed on June 17 and added about $11 billion of loans as of the end of the second quarter. And Citigroup deposits grew 5%.

Sequentially, assets increased $27 billion from the first quarter, driven primarily by 4% growth in Citicorp loans. At quarter end, cash was down sequentially by $8 billion. However, on an average basis the cash balance was $18 billion higher quarter over quarter, due in part to higher cash balances that we maintained in advance of the Costco portfolio acquisition.

Slide 5 presents trends in our loan portfolio in constant dollars. Total Citigroup loans increased 2% year over year, despite continued reductions in Citi Holdings. We grew Citicorp loans 6%, as we continued to serve our high quality target client segments in both the Consumer and Institutional businesses.

Consumer loans grew 6% year over year, driven by 12% growth in North America. This included a 20% increase in branded cards, which was primarily driven by the acquisition of the Costco portfolio.

International consumer loans declined 1% year over year, as continued growth in Mexico was more than offset by a 3% decline in Asia consumer loans. This decline reflected the repositioning of our portfolio away from lower return mortgages as well as some de-risking in our commercial portfolio, partially offset by growth in higher return card and personal loans.

On the Institutional side loans grew 6% year over year in total. Our Corporate Lending portfolio increased 6% on new business and funding of transaction related commitments to target market clients.

TTS loans remained relatively flat. And markets and private bank loans grew 11% during the year, as we saw continued opportunities to support client activity.

Citi Holdings loans decreased 35% year over year, driven by an $18 billion reduction in North America mortgages, including transfers to held-for-sale. Nearly 80% of Holdings remaining loans are North America mortgages. And Holdings credit quality remained stable in the second quarter.
On slide 6 we show credit quality trends in our Consumer loan portfolio. Consumer credit performance remained broadly favorable again this quarter, with stable to improving NCLs, delinquency rates, and reserve coverage. The NCL rate in Latin America showed particular improvement this quarter, reflecting seasonal payment trends. We expect the NCL rate in Latin America to return to around 4.5% for the second half of the year.

Given stable credit trends across the Consumer franchise, we expect future loan loss reserve builds to be driven primarily by volume, reflecting both organic loan growth as well as the impact of the Costco portfolio acquisition. Under purchase accounting, we acquired the Costco loans at fair value without any corresponding loan loss reserves. As these loans pay down and we originate new loans, we will build loan loss reserves related to the new loans. And this is expected to drive somewhat higher net reserve build upfront, as we build to a sustainable LLR balance on the portfolio over several quarters.

While we have only had the portfolio for a short period, we currently expect the biggest impact in the third quarter, with an estimated LLR build in the range of around $150 million related to the Costco portfolio.

Turning to slide 7, let me discuss our Corporate credit performance. During the second quarter ICG cost of credit of $82 million was up from last year, but down significantly from the first quarter. The cost of credit related to energy was minimal, as net credit losses were mostly offset by previously established reserves as the portfolio benefited from the stabilization in oil prices.

Also, given our target client focus on high quality corporate credits, certain energy credits were able to access the capital markets, as the market environment became more favorable in the second quarter. This allowed these clients to improve liquidity, resulting in either pay downs or improvement in the credit quality of our exposures.

And our reserve based energy exposures declined this quarter by roughly $400 million in ICG, reflecting the impact of the spring redeterminations. We provide more detail on our energy portfolio in the appendix to our presentation.

Outside of energy, the cost of credit was concentrated in a few specific credits. Non-accrual loans increased $135 million from first quarter levels to 79 basis points of loans. EMEA non-accrual loans increased to 106 basis points of loans, driven by two specific credits. But this does not result in any incremental cost of credit, due to a combination of existing reserves, collateral coverage, and structural protections. Latin America non-accrual loans decreased to 63 basis points of loans, driven by one write off and one pay down. Finally, the ratio of LLR to corporate non-accrual loans was 1.2 times at the end of the quarter.

Turning to slide 8, we show the composition of our deposits, which fund over 50% of our assets. Total deposits increased 5% from the prior-year period, despite reductions in Citi Holdings. Citicorp grew deposits by 6% in constant dollars with continued high quality deposit flows across our franchise. The liquidity value of our deposits remained stable.

Consumer deposits increased 2%, including 5% growth in international markets. Corporate deposits increased 5% year over year with TTS accounting for roughly half of this growth, as we continued to support clients’ local liquidity needs, particularly in North America and EMEA.

On slide 9 we update our regulatory liquidity metrics. Our average LCR was 121% in the second quarter, up slightly from the first quarter, reflecting an increase in average HQLA to roughly $411 billion, partially offset by higher average net outflows. The increase in average HQLA reflected an increase in cash, while growth in average deposits and the impact of the Costco portfolio acquisition resulted in higher modeled net outflows. While we continue to work to deploy the additional liquidity efficiently and expect to bring our average LCR down over time, we do expect it to remain elevated for the next several quarters.

The proposed net stable funding ratio, or NSFR, rule was jointly issued by the U.S. agencies early in the quarter. The proposal is largely consistent with the Basel Committee’s final NSFR rules. However, similar
to LCR, the proposed U.S. rule includes a narrower definition of liquid assets and more stringent recognition of deposit insurance programs, among other differences.

The proposal would require full implementation of the NSFR beginning January 1, 2018. As with the international rules, we currently estimate that our NSFR under the U.S. regulators proposed rule is comfortably above the 100% minimum requirement, based on what we know today. We're currently reviewing the proposed rule, and along with the rest of the industry, we will provide constructive feedback on the proposal through the comment process.

On slide 10 we show Citigroup's net interest revenue and net interest margin. Our NIM was 286 basis points in the second quarter, lower than our initial outlook of around 292 basis points, driven by an equal combination of higher cash balances, lower trading NIM, and lower loan yields. While the cost of long-term debt did increase sequentially by 4 basis points, as our issuance included longer dated as well as subordinated debt, this was incorporated into the previous guidance.

Looking to the second half of the year, NIM should recover to around 290 basis points or slightly higher, driven by a 3 basis point improvement from the addition of the Costco portfolio as well as normalization of average cash balances. This is lower than our previous outlook of around 295 basis points for the remainder of the year, reflecting somewhat lower loan yields, as well as the absence of a previously assumed rate increase in the U.S.

Our estimate of the net interest revenue benefit from a 100 basis point instantaneous parallel rate shift increased slightly to just under $2 billion. And the portion attributable to U.S. rates remained stable at approximately $1.4 billion. We remain conservatively positioned for interest rates, consistent with market expectations for further rate moves.

On slide 11 we show the composition of our long term debt outstanding. During the quarter our total long term debt decreased slightly to $207 billion, as our continued issuance of benchmark debt was more than offset by declines in other funding sources, including securitizations. However, credit card securitizations remain a cost effective option to optimize our overall liquidity position. And we do intend to resume issuance later this year.

While the weighted average maturity of our long term debt remained at 7 years in the second quarter, we expect to end the year somewhat longer than 7 years, as we extend the tenor of our new issuance. And our preferred stock outstanding is $19 billion or just slightly higher than our targeted level of roughly 150 basis points of risk weighted assets.

Turning to slide 12, let me cover our issuance and redemption expectations. In 2016 we expect gross issuance of up to $25 billion of senior and subordinated debt, of which we issued $14 billion during the first half of the year, slightly ahead of pace and not including the $1.5 billion of subordinated debt we issued earlier this week.

Year to date we have had $8 billion of maturities and executed $3 billion of buybacks. For the balance of the year we expect additional maturities of roughly $5 billion and additional repurchases of roughly $1 billion of benchmark debt, bringing our expectation for net issuance of benchmark debt to approximately $8 billion in 2016.

At the end of the quarter, we had achieved our targeted Tier 2 capital level of 200 basis points of risk weighted assets. And giving effect to our recent issuance earlier this week, it is now slightly above target, as we anticipate the timing of amortization of capital credit and RWA variability.

And finally as we've stated in the past, we completed our planned preferred stock issuance early in the second quarter.

On slide 13 we update our estimates of our total loss absorbing capacity, based on the Federal Reserve's November 2015 proposed rule. Based on the assumptions set forth, we currently estimate that we meet
our expected requirement under the total loss absorbing capacity definition, as we show in the middle column on this slide. Accordingly, we expect our estimated long-term debt requirement of 9% to remain our binding constraint under the TLAC rule. Our estimate of this measure is shown in the right-most column.

We estimate we have reached a ratio of 8.2% of our risk weighted assets as of the end of the second quarter, equating to a long term debt shortfall of $9 billion. The $1.5 billion improvement from last quarter reflects both the growth in our benchmark debt outstanding as well as a reduction in our risk weighted assets.

As we note on the slide, the estimate excludes the impact of non-U.S. law debt being rendered ineligible, which could add approximately $10 billion to our need if the final rule is consistent with the proposal in excluding this debt. Our current outstanding long-term debt includes $20 billion of non-U.S. law debt. $10 billion of which will roll off between now and 2019.

Of course our estimates are necessarily subject to the final rules once adopted. However, based on our current analysis, we continue to believe the proposal's impact on our issuance plans and earnings to be manageable.

Turning to Slide 14, let me summarize our regulatory capital position, which remains among the strongest in the industry. During the quarter our CET1 capital ratio improved 20 basis points to 12.5%. Our total capital ratio increased 40 basis points to 16.1%. And our supplementary leverage ratio improved to 7.5%, while Citibank’s SLR declined slightly from 6.9% to 6.8%.

Moving to our last slide. Let me summarize four key points. First, despite a challenging and volatile environment we earned $4 billion of net income in the second quarter. We utilized approximately $2.4 billion of DTA year to date. And we continued to make progress in winding down Citi Holdings.

Second, we have maintained total assets of $1.8 trillion, while serving clients by growing deposits and loans in our core Citicorp businesses. Asset quality was broadly stable.

Third, we have continued to prepare our business and balance sheet for the ongoing resolution of the regulatory landscape from a position of significant strength. We reported a CET1 capital ratio of 12.5%, an SLR of 7.5% and average LCR of 121%.

And finally, our funding base remains a key strength. Our deposit base is stable and high quality, and our long term debt issuance plans are on track.

Before we turn to questions, I'd like to take the opportunity to welcome Tom Rogers, who was recently appointed head of Fixed Income Investor Relations, replacing Peter Kapp, who has assumed oversight responsibilities for our Capital Management activities. We’d like to thank Peter for his many contributions over the past several years and welcome Tom to his new role.

And with that, John and I will be happy to answer your questions.

**QUESTION AND ANSWER**

**OPERATOR:** (Operator Instructions) Our first question will come from the line of Pri de Silva with CreditSights.

**PRI DE SILVA:** Congratulations, Tom, on your new role.

**TOM ROGERS:** Thank you.

**PRI DE SILVA:** Yeah. John and James, good morning.

**JOHN GERSPACH:** Good morning, Pri.
PRI DE SILVA: It's been almost a month since the Brexit vote. And have you noticed any meaningful changes in CEO confidence or corporate finance activity since then?

JOHN GERSPACH: Yeah, Pri. The mark – I mean we had obviously in the beginning there was a pullback. But I'd say that pretty much since, immediately following, like within 36 hours after the vote, markets have been open. We've seen good customer engagement. So there hasn't been – there's been a lot of discussion about plans for the future.

But again, everyone is still a bit uncertain as to exactly what that timeframe will be and what the ultimate implications are. So there's a lot of discussion about planning. But there's very little tangible that's being done at the present time. And as I said markets remain open. The engagement with customers is good. And so we really haven't seen any big pullback at this point in time.

PRI DE SILVA: Great. Thank you very much. And, John, thank you for the color on the preferred stock target. And as you alluded to last quarter and the issuances early this quarter, will your targeted ratio change if the Fed instituted a – let's say a 3% SLR requirement for the next year's CCAR process?

JAMES VON MOLTKE: Pri, it's James. We're going have to look at that when and if the Fed issues new rules for CCAR. And whether the GSIB is incorporated into each of the capital measures or more focused on CET1. So it's too early to say whether it would affect sub debt or preferred issuance in addition.

PRI DE SILVA: Okay. Thank you very much.

JAMES VON MOLTKE: Thank you.

PRI DE SILVA: I appreciate the color as always.

JAMES VON MOLTKE: Thanks for the questions, Pri.

OPERATOR: Your next question comes from the line of Robert Smalley with UBS.

JOHN GERSPACH: Hi, Robert.

ROBERT SMALLEY: Hi. How are you?

JOHN GERSPACH: Good.

ROBERT SMALLEY: Thanks for doing the call. Just a couple of quick questions. On slide 8, talking about deposit trends. We've seen inflows. Given the changes in money market regulation, are you anticipating more of those funds coming over to you in the form of deposits? Or – and have you seen that already? I guess is my question.

JAMES VON MOLTKE: So to answer the second part, we haven't seen significant shifts recently in the mix, if you like, of bank versus money market activity. And at this point I think it's too early to say whether changes in the structure of that industry are really driving customer behavior.

We're also obviously cognizant of rate changes over time potentially driving customer behavior. So that the industry structure is only one of a number of influences in fund flow into the money market world.

ROBERT SMALLEY: Okay. Thank you. And second question. The Institutional Clients Group has done pretty well certainly this quarter and compared to peers. Given that your capital ratios are very strong, can you see putting more of your capital into that business than maybe some of the more RWA dense businesses within that area?
JAMES VON MOLTKE: Robert, it's – we – at this point the number of different rules and ratios against which we're optimizing as you know has proliferated over the last several years.

ROBERT SMALLEY: Correct.

JAMES VON MOLTKE: RWA is only one. And as it relates to sort of capital allocation therefore to ICG versus GCB or even within ICG, the specific activities, I'd say it's much more complicated than just RWA. But also I think in terms of capacity we have – we look at capacity across a number of different dimensions well beyond RWA.

JOHN GERSPACH: Yeah. But, Robert, let me – this is John. We definitely have the capacity to serve the needs of our clients. And I think that's what's the most important thing. So our balance sheet is open for business, as James said. We're mindful of the various constraints, whether that be CCAR or LCR or any other R that's out there. But the most important thing for us is to make sure that we have the capacity and the capability to serve the needs of our clients. And that is what we're focused on. And we have a balance sheet that is open for business.

ROBERT SMALLEY: Understood. Thank you.

JAMES VON MOLTKE: Thank you.

OPERATOR: Your next question comes from the line of Brian Monteleone with Barclays.

BRIAN MONTELEONE: Hi. Good morning, guys.

JAMES VON MOLTKE: Hi, Brian.

JOHN GERSPACH: Hi, Brian.

BRIAN MONTELEONE: Hey. I had a question about the legacy grandfathered trust preferred securities, the Citi Ns. I believe you've now gone through I guess two CCAR processes where you could've requested redemption of those, as they were callable. And it seems like you haven't yet. Can you talk a little bit about how you see those? Is that more of a permanent part of the capital structure at this point?

JAMES VON MOLTKE: Brian, I don't like to talk about specific securities that are outstanding. But as I think I've mentioned before, we do look at that security from an economic perspective from time to time. And as you say, we haven't chosen to call it to date.

BRIAN MONTELEONE: Got it. And in terms of the capital credit it receives, I think it was just $1.4 billion of Tier 1 capital, additional Tier 1 capital. And then there's also some Common Equity Tier 1 capital, correct?

JAMES VON MOLTKE: That's correct.

BRIAN MONTELEONE: Okay. Great. And second question I just wanted to clarify that I heard it correctly. The NSFR you were saying you were above 100% under the Fed's proposal?

JAMES VON MOLTKE: Yes. That's also correct.

BRIAN MONTELEONE: Okay. Great. Thank you.

JAMES VON MOLTKE: Thanks, Brian.

OPERATOR: Your next question comes from the line of Scott Cavanagh with APG.

SCOTT CAVANAGH: Good morning, guys, and thanks for holding this call. Always appreciated.
JAMES VON MOLTKE: Hi, Scott.

SCOTT CAVANAGH: So I wanted to kind of get your higher level thoughts. There’s been a lot of kind of incendiary commentary coming from both political parties, most recently with the proposal of Glass-Steagall coming back. I wanted to kind of get your guys thoughts about this?

And within the context of the TLAC proposal, the potential removal of all covenant protection for bondholders. And really how you’re thinking about this when you think about new base indentures? And particularly looking at the Credit Roundtable proposal for new covenant protection?

JOHN GERSPACH: Yeah. I'll let James – this is John. I'll let James go into some of the TLAC things.

I think it's way too early to start speculating as to what may or may not happen with Glass-Steagall. So let's not even try to go there. I mean I think if there's anything to do with Glass-Steagall and with everything else that's going on, you're clearly now saying, okay, what about the uncertain and the unknown? And so let's just deal with the uncertain. And I'll let James handle that as opposed to dealing with the unknown.

JAMES VON MOLTKE: So, Scott, on the indentures since we last spoke, I have to say we haven't really been focused on our indentures. We've been following the Credit Roundtable and other discussions on adjusting to the TLAC rule. But frankly, until we see a final rule, we're sort of reactive at this point.

SCOTT CAVANAGH: Okay. So when the new rule comes out, how are you thinking about that next issuance? Is there going be a period of interaction with investors to come up with something that works for both constituencies? Or how are you looking to approach that?

JAMES VON MOLTKE: I think much as you refer to there being industry efforts to think about the indentures and changes to language, the industry, the issuers will react. And each issuer will put out their new language.

I think one part of the answer to your question is, how long the conformance period is in the final rule. So is all debt from the date of the final rule required to meet whatever the guidance is in the rule? Or is there some period of time over which the market is – will be able to adjust? I think that's a critical question for us as well as our peers.

SCOTT CAVANAGH: Okay. I think most investors on this call would welcome more interaction with you and your peers. I think it would be beneficial for both of us. Thanks.

JOHN GERSPACH: Understood. Thanks, Scott.

JAMES VON MOLTKE: Thanks, Scott.

OPERATOR: Your next question comes the line of Mark Kehoe with GSAM.

MARK KEHOE: Hey. Good morning, thank you for the call. You talked about lengthening the duration of your debt. And I'm just wondering whether – how does that interplay with the fact that some of the 30-year debt under the current TLAC proposal may not be TLAC-eligible? You may have to tender for it. Would that mean that you would roll the existing 30s into a new indenture and thereby kind of lengthening your duration of your senior unsecured? Or what are your thoughts around that please?

JAMES VON MOLTKE: Sorry. I could hardly hear your question acoustically. But you’re referring to 30-year debt. And is the question about a grandfathering provision related to longer dated debt that might be ineligible?

MARK KEHOE: Correct. I think you mentioned in your comments that you may extend the duration of your debt from – average at 7 years further. And what I'm thinking about also is if the 30-year debt isn't grandfathered, or TLAC-eligible, would you then tender for it? Or turn it into a new 30-year instrument? So
you almost are automatically able to kind of extend the duration of your debt by rolling all the existing buyouts of a 30-year into a new eligible 30-year.

JAMES VON MOLTKE: So let me take it in two parts. The first part was extending our tenders. And that is something that we are intending to do gradually over the TLAC conformance period. Because as I think we've talked about before, given the decay inside 2 and 1 years, extending the debt is efficient. And there's an efficient point in terms of the weighted average maturity of the total debt outstanding.

The second question to – relating to ineligibility of debt. Once we see the final rule we'll need to look at the eligibility of all of the outstanding debt, including debt that falls outside of grandfathering periods for one reason or another. Whether that's non-U.S. law debt or to do with acceleration periods or otherwise – or acceleration clauses or otherwise. And then we'll need to address how we manage that ineligible debt, especially long-dated, whether through redemptions and reissuance or through consent procedures or otherwise.

MARK KEHOE: All right. Thank you.

OPERATOR: Your next question will come from the line of Hima Inguva with BofA Merrill Lynch.

HIMA INGUVA: Thank you for taking my question. And as always, thanks a lot. It's really good color.

JOHN GERSPACH: Our pleasure.

HIMA INGUVA: Two questions. Thank you. Two questions from here. One is, I wanted to confirm the calculations for TLAC. You're currently assuming that the non-U.S. law debt is not eligible?

JAMES VON MOLTKE: Yeah. The calculation we show on page 13 assumes that the non-U.S. law debt is eligible or grandfathered. But what we also note sort of in an italicized line halfway through the table is the amount of non-U.S. law debt that is actually outstanding.

The other comment that we make, and this is what's really called out in the yellow box, is that by the time the rule is active on 1/1/19, $10 billion of that $20 billion that's outstanding will have matured. And we will have rolled it into eligible debt.

HIMA INGUVA: Sure. Okay. And then in terms of timing, many other banks have guided towards getting clarity in the – I guess in the next quarter or so. Do you have any read into that?

JAMES VON MOLTKE: That would be our expectation as well, in at least the next half, but likely the next quarter in terms of the Fed coming out with a final rule, based on the comment period coming to an end.

HIMA INGUVA: Okay. Great. That's very helpful. And the last one is on FICC trading. Just wanted to get your read on how you see this business, considering banks are under tremendous pressure to run with very skinny balance sheets if you will. And broader – in the broader horizon if you look at it, how do you see this business shaping up for investment banks, let's say in the next out years, like 4 years or 5 years?

JOHN GERSPACH: Well I think – this is John, Hima. I'd say that the FICC business is one that we've been I think fairly open about, as being a business that has been under tremendous transformation certainly over the last 5 years. And will likely continue to be so for some period of time.

And so we have clearly already adjusted our capacity in the FICC business. And I think many have. FICC remains a business that on a going-forward basis is one that's going to favor institutions with scale. And when you take a look at probably the cornerstone of our FICC business, which is rates and currencies, it's clearly one where we have scale. And not just because we just happen to have a large balance sheet, but because we actually have got a very vibrant customer base, in which we are servicing.
We noted last week that 40% or so of our rates revenues this quarter were really coming from corporate clients. And so that's the way that we have been building not just our rates and currency business but our overall FICC franchise, as one that is again focused on servicing the needs of our clients.

And so we've got the scale. We got the client set. And I'd say that we're poised then to continue to succeed in this business. Obviously as rules change, as market appetites change, we'll conform our capacity accordingly. But again we've got a very client focused FICC franchise.

HIMA INGUVA: That's very helpful. Thank you very much.

OPERATOR: Your next question comes from the line of Donna Halverstadt with Morgan Stanley.

DONNA HALVERSTADT: Thank you. My questions were already asked.

JOHN GERSPACH: That's great. Okay, Donna.

JAMES VON MOLTKE: Thank you.

OPERATOR: Your next question comes from the line of Michael Rogers with Conning and Company.

MICHAEL ROGERS: Yes. Good morning. With the low or negative interest rate environment that prevails in so many jurisdictions right now, I'd be interested in your observations as to whether or not this has or is at increased risk of causing overly aggressive corporate lending by Asian – particularly Asian or European banks.

And secondly, I'm also interested in your observations on the health of the consumer credit asset class? And how long can it stay as good as it presently is?

JAMES VON MOLTKE: This is James. I'll take the first question. You're absolutely right. Obviously we've all seen central bank actions and reduced market expectations for rate rises and negative rates in a number of currencies in countries. And that is challenging for banks around the world.

I don't want to speak to specific securities or corporate loans or specific banks from regions. But certainly I think your overall comment is true that negative rates in certain countries is driving investors to look for yield around the world, including in U.S. dollar assets. So that's certainly a feature of the securities markets. Again I don't want to talk to corporate loans or specific banks around the world.

JOHN GERSPACH: And this is John. As far as the question as far as the state of the consumer, we continue to see certainly in our Consumer franchise, very favorable credit trends. I mean we mentioned that. And that's the case with our business, whether it's in the U.S. or in Asia or in Latin America, in Mexico. Part of that is the overall environment is a fairly stable environment. But a good part of it also is the client base that we have targeted.

So again our Consumer franchise is largely targeted on what you would call more credit worthy customers, the mass affluent, the emerging affluent. And I think that also provides a certain amount of resiliency. I wouldn't want to predict that NCL rates are going to go any lower. But at the same point in time I don't see any catalyst on the horizon that would suggest that they're poised to increase either.

So for us at least for the foreseeable future, we do see that we will most likely have some increase in consumer cost of credit. But that's likely to be the result of the need to build reserves on increased volume of loans and nothing more.

MICHAEL ROGERS: Okay. Thank you, John. Thank you, James.

JOHN GERSPACH: Not a problem.
JAMES VON MOLTKE: Thanks, Michael.

OPERATOR: Your next question comes from Jeff Bernstein with Insight.

JEFFREY BERNSTEIN: Good morning. Thank you.

JOHN GERSPACH: Hi, Jeff.

JEFFREY BERNSTEIN: Most of my questions have been asked and answered. But regarding CET1, do you provide a target range for that number?

JOHN GERSPACH: This is John. We've done that in the past. And then we found that as all the rules changed, we were constantly driving higher. So we have not published a new target at this point in time.

I will say that – and we've said this in the past – currently CCAR would be our binding constraint on our CET1 ratio. And so as the CCAR requirements change, so would our target change.

So let's ask – let me ask you to just have a little bit more patience. We'll see what the next round of changes that Governor Tarullo has mentioned are forthcoming, how those play out. And then we'd be able perhaps to give you a better guidance as far as what our long-term targets are.

JEFFREY BERNSTEIN: Okay. And then as a somewhat follow up, where do you see the business over time on an ROE basis? I mean I realize we're in a tough environment now, but I mean just in general.

JOHN GERSPACH: Yeah. We continue to believe that our current business, as we're currently running it, the current model that we have on both Consumer and Corporate, focused on the target client base that we're focused on may – in a more normal environment is capable of producing an ROTCE of 14%, maybe a little bit higher.

We've defined in the past when we've been asked that question, when people said, well what do you mean by a more normal environment? We pointed to an environment where interest rates might be perhaps 200 basis points higher than they are today. So clearly not back to where interest rates were in 2005, 2006, or thereabouts. But clearly higher than where they are today at near 0%.

And it's an environment where you would expect U.S. GDP to be growing something in the 2.5% to 3% range, with global growth of say 3% plus. So not an outrageous environment, but one that is clearly a little different than what we're running today. But that's what we're built for.

JEFFREY BERNSTEIN: And so I mean these are questions, these – not necessarily directed at you in particular. But if that environment takes a long time to materialize, how long can you run a business with these returns?

JOHN GERSPACH: That's a very good question. And that's going to be one that's going to be determined about – do you think that that environment is coming in 10 years or in 2 years? And I think what you've seen is that us, as well as others, have adjusted their business models already. And if the environment that I described begins to look to be even more elusive to ever see how we get there, then we will continue to make additional adjustments.

JEFFREY BERNSTEIN: Okay. Thank you very much.

JOHN GERSPACH: Okay.

OPERATOR: Your next question comes from the line of Don Jones with Amherst.

DON JONES: Good morning, James and John.
JOHN GERSPACH: Hi, Don.

DON JONES: A couple quick questions. The cat got out of the bag earlier this year around living will and approvals. And I don't know if you can give any broad stroke types of description about what you think it was that made Citi stand out among its peers in terms of structure or planning or whatever it might have been?

JOHN GERSPACH: I certainly couldn't give you any insight into that. I know that we did our work. And we worked hard at it, as I'm sure other institutions did. But at the end of the day the Fed and the FDIC made their judgments.

So we're quite happy with the result that we have received. And it doesn't mean that we're not going to continue to work to actually then improve on the update that we need to give in October, and then the next full submission that we need to do in July next year. We're still hard at work on addressing the shortcomings that we know that we have and to meet some of the new guidance that has been put out there.

DON JONES: Sure. I can expect that's not a very easy set of hurdles to get over either. And kind of a bit along the lines here, and I've asked this question in a different way. But if in the course of the Fed coming up with final TLAC rules, they come to determine that nonbank OpCos within the entity can issue debt that would also be TLAC qualifying, would you consider issuing out of or something related to the broker dealer? Or is that something that's even been a subject with regulators?

JAMES VON MOLTKE: It's James. It hasn't really been a subject with regulators. I mean the real focus of the TLAC and MREL in Europe rules has been parent company. And then from an internal TLAC perspective, how does that parent company downstream the debt that can fund the operating subsidiaries?

We do – as we've pointed out, we do fund in other ways out of our operating subsidiaries, particularly to the bank. But to date TLAC hasn't really driven changes in our funding structures as you describe.

DON JONES: All right. Okay. Thank you very much.

JOHN GERSPACH: Not a problem.

OPERATOR: Your next question will come from the line of Arnold Kakuda with Bloomberg Intelligence. Please go ahead.

ARNOLD KAKUDA: Great. Thanks a lot. The call is always very helpful, so thank you. In terms of your equity versus debt valuation, some discrepancy there. And I just want to get your thoughts.

So from our side I guess you've had – you're winding down the non-core unit. That's gone very well. You're not – throw that back into – not going to report that anymore after this year. You've had two clean CCAR passes. And then on the living will you did better than peers.

So how is it that on the debt side I guess your CDS kind of trades in the middle of the peers, while on the equity side I guess your price to tangible book value is towards the bottom of peers. So what are some of the different conversations that you're having between kind of the debt investors and the equity investors?

JOHN GERSPACH: Well we have a lot of different conversations on a lot of different topics. And clearly from an equity investor point of view, the focus is on our ability to improve. I'd say both our return on capital that we have employed in the business, as well as our return of capital to shareholders.

And with two CCAR passes we've been able now to build up to a more acceptable level I'd say of return on capital. But we still have some work to go on the return on capital. And we're not satisfied where we currently are with the return on tangible common equity. And we are endeavoring to improve that over time. And we will improve that over time.
I mentioned that on a longer term basis in a normal environment, we feel we're capable of producing an ROTCE of 14% as a full franchise. We've laid out targets of 20% for our Consumer business and 14% or so for our Corporate business. And I think now it's a matter of demonstrating to equity investors that we have the capability of generating those returns. So it's a matter of producing sustainable high quality earnings. And that's what we're focused on.

From a debt point of view, I think when we take a look at some of the balance sheet considerations that debt investors focus on. I think it's more clearly evident the progress that we have made on those measures. We've operated with a highly efficient balance sheet over the last several years and becoming even more efficient. Through our work on Holdings, we've de-risked a lot of that balance sheet. And I think that has been evident in both our risk-weighted assets and other measures.

And when you take a look at our ability to achieve some of the regulatory requirements, whether those be the liquidity measures of LCR or some expanded balance sheet measures like SLR, you've seen that we have the capability of either being the first major bank to hit those requirements or very close to the first bank to hit those requirements.

So we may be a little bit further ahead in demonstrating our capabilities to the fixed income investors at this point in time.

ARNOLD KAKUDA: Okay. Got it. Thanks. And then I guess when you talk about the returns, and I guess some of your peers have announced some more kind of cost saving initiatives and stuff like that. And so can you just remind us again where you are with kind of what sort of cost initiatives that you guys have now? I think you are making investments I think in branded cards and stuff. And I think you have a comp target, a ratio target in ICG. But is there something else that you guys had in the pipeline again?

JOHN GERSPACH: Being able to manage to an efficiency ratio is something that I think we were the first bank to actually put out an efficiency ratio target. We said that we believed that our Citicorp franchise should be capable of operating in the mid-50s%. We gave ourselves that target for 2015. We achieved an efficiency ratio of 57% at the beginning of the year. We did have a slip in the first quarter, I think as many banks did. But our revised guidance is that we are operating – our goal is to operate at a 58% efficiency ratio for 2016.

So we focus very much on managing to a very specific efficiency ratio, as opposed to giving guidance on a specific expense number. But I think that if you take a look at the efficiency ratio that we've targeted, it lines up very nicely with some of the other firms when they have given you specific expense targets. And again we think that longer term, it's much more beneficial to be operating towards an efficiency ratio, which tends to be more permanent, than one specific expense number.

So for us managing expenses is an ongoing point of emphasis. We certainly manage to be the most efficient institution that we have. That requires a lot of re-engineering efforts and everything else. Our difference is, no, we haven't put out efficiency programs with specific names. That's just something that we call good management.

ARNOLD KAKUDA: Okay. Got it. And then I think in 4Q, when you announced 4Q, you mentioned that the GSIB – your estimated GSIB buffer went down to the 3% bucket. And then I think recently on the 2Q call, you mentioned that the GSIB score kind of got close to the 630 level, which I think would – might put you back on the cusp of the 3.5%.

And so my question is where does the Fed kind of – do you need to get there in 4Q? And that's kind of your number for the year? Or do you expect to hear kind of Fed kind of final kind of reassessment I guess of your GSIB score sometime soon?

JAMES VON MOLTKE: Okay, Arnold. The rule as written is a December 31 snapshot moment in time measure. And so, yes, at the end – in January we disclosed that we were in the 3% bucket, and – but at the high end of the range. And last week, John mentioned that we were, as of the end of the second quarter, at a 630 score.

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JOHN GERSPACH: That was our estimated score that we got.

JAMES VON MOLTKE: And so that is something that we're focused on. But to answer your question, it's a moment in time measure.

ARNOLD KAKUDA: Okay. Great. Thank you very much.

JOHN GERSPACH: You're very welcome.

OPERATOR: Your next question will come from the line of John Carolan with Fidelity.

JOHN CAROLAN: Hi. Thanks for the call.

JOHN GERSPACH: Hey, John.

JOHN CAROLAN: How are you? I just wanted to follow up on the topic of covenants to address the uncertainty of outcomes for debt holders in the risk of an organic decision to break up, however remote it might be at this stage.

I guess I wanted to highlight that we have situations where MetLife and GECC evidencing it taking place. We see Fed Governor Kashkari prominent in the headlines. We see occasional but steady sell-side notes from the equity community calling for it. We see an election, uncertainty, regardless of the party outcome. We have a living will process that seems to be making it organizationally more feasible to occur over time. We see external versus internal TLAC rules coming out, which seem to sort of do the same thing. We see ROEs that are challenged, as has been discussed on the call.

And while you and others have done a good job expressing the value of the synergies of the universal banking model, which have been very helpful, in this backdrop why wouldn't you consider doing something like this to further emphasize the commitment to this business model for long term debt investors?

JOHN GERSPACH: Yeah. I'm sorry, but you went on so long I actually lost the gist of what your question was.

JOHN CAROLAN: So I guess the framework is that there's a lot of things going on now that really haven't been around for as long as I've been involved in analyzing banks in terms of how the world has changed. And there seem to be proposals from the Credit Roundtable around installing some covenants that would help allay concerns, however remote there may be, about an organic decision to separate the different segments of the bank.

And I guess it's already come up on the call, and I just wanted to clarify why it's not something that you'd be doing? Because it seems like it's in lock step with the message that you've already shared with the equity community about the value of the universal banking model and the synergies that you get across the businesses.

JAMES VON MOLTKE: So I think – it's James. John, one thing I'd say is it's too much of a hypothetical really to respond to in terms of the overall framework. It's something that if you look at our history, as we evolve the company through especially the Holdings restructuring, we've been very mindful of the position of our creditors.

As it relates to new covenant language of indentures, I would separate the TLAC discussion that we had earlier from all the other sort of hypotheticals that you mentioned. So hopefully that's a fair answer to your question.

JOHN CAROLAN: Thanks.
OPERATOR: The final question will be a follow-up from Michael Rogers with Conning and Company.

MICHAEL ROGERS: Hi. Thanks for the double dip. Anything new in the evolution of the ongoing discussions that you had with the rating agencies? For one, I've seen that S&P is soliciting comments on potential changes to their so-called RAC capital ratio, which it appears could in the end have potential to impact ratings of some institutions. But is there anything, including that, that you're seeing that – a part of that evolution?

JAMES VON MOLTKE: No, nothing that I'd comment on, Michael, at this point. And we don't like to comment about our – on our dialogue with the rating agencies generally. But we are actively engaged with them, particularly on the changes in the regulatory environment that we're all living through.

MICHAEL ROGERS: Okay. Thank you.

JAMES VON MOLTKE: Thanks, Michael.

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

TOM ROGERS: 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 soon. Thanks, Thea.

OPERATOR: Yes, sir. Ladies and gentlemen, thank you for participating in today's conference call. You may now disconnect.