TRANSCRIPT

Citi Fourth Quarter 2016 Fixed Income Investor Review

Thursday, January 26, 2017

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.

TOM ROGERS: Thank you, Brent. Good morning and thank you all for joining us. As Brent mentioned, I'm joined this morning by our Chief Financial Officer, John Gerspach, and our Treasurer James von Moltke. In a minute, James will take you through the fixed income investor presentation which is available for download on our website, citigroup.com. Afterwards, John and James will be happy to take your questions.

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 cautionary statements referenced in our discussion today and those included in our SEC filings including, without limitation, the Risk Factor section of our 2015 Form 10-K. With that said, let me turn it over to James.

JAMES VON MOLTKE: Thank you, Tom, and good morning, everyone. On today's call I will cover a number of topics. First, I'll briefly discuss our 2016 results. Second, I'll review balance sheet trends notably growth in loans and deposits. Third, I'll review our issuance program and discuss issuance guidance for the full year 2017. Next, I'll provide an update on our liquidity position. And finally, I'll discuss our capital position which remains strong despite the significant capital return to our shareholders which we executed in the fourth quarter and the negative impact on other comprehensive income, or OCI, resulting from the movement in interest rates.

For reference, slide three contains a summary of our fourth quarter and full year results. We reported net income of $14.9 billion for the full year and achieved an efficiency ratio of 59% which corresponded to a 58% efficiency ratio in Citicorp, in line with our revised guidance.

On slide four, we've summarize the progress we've made with respect to our regulatory requirements. As you can see on the slide, we have a strong capital and liquidity position and we are well prepared for each of the requirements coming into effect over the next two years. This balance sheet strength gives us the capacity to continue supporting our target clients as they grow and transact around the world within our well-established risk management framework. As we will discuss later, we've made significant progress towards compliance with a total loss absorbing capacity, or TLAC rule, with a long-term debt ratio of 8.8% of risk-weighted assets at year-end under our interpretation of the final rule. This translates into $2 billion shortfall and we've already issued over $5 billion of TLAC eligible debt so far this quarter.

On slide five we show balance sheet trends over the past five quarters. On a reported basis, total assets increased by $61 billion in the past year. To better reflect underlying business 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 by $87 billion, or 5% from the prior year period. Trading related assets and liabilities grew with the increase in market activity we saw in the fourth quarter, compared to a relatively muted environment in the prior-year period.

We grew loans and deposits despite the continued wind down of Citi Holdings and long-term debt grew to $206 billion as we continue to make progress towards TLAC compliance. I'd like to take a moment to highlight the stability of our funding base and the strength of our capital and liquidity positions. As of year-end, over 50% of our assets were funded by deposits, including a high proportion of operating accounts in our retail and institutional businesses resulting in a liquidity value of 74% under the Liquidity Coverage Ratio or LCR rule. Close to another 25% was funded through the combination of long-term debt and equity outstanding, supporting our long-term debt and Common Equity Tier 1 capital or CET 1 ratios of 8.8% and 12.5%, respectively. And these stable funding sources supported a high-quality asset base, including over $600 billion of loans and $500 billion of cash and investments. Over time we will work to optimize the balance sheet further in order to increase efficiency while continuing both to meet our regulatory requirements and support client needs.

Slide six presents trends in our loan portfolio in constant dollars. Total Citigroup loans increased 3% year-over-year as 6% growth in Citicorp more than offset continued reductions in Citi Holdings. In our Consumer businesses grow loans grew 8% year-over-year driven by 14% growth in North America. This included a 28% increase in branded cards, driven primarily by the acquisition of the Costco portfolio. International consumer loans declined 2% year-over-year, as growth of 7% in Mexico was more than offset by a 5% decline in Asia consumer loans, as we continue to optimize our portfolio in the region to generate higher returns.

On the institutional side, loans grew 4% year-over-year, driven by growth in lending to our high net worth target clients in our private banking segment. Corporate lending declined 1% primarily driven by repayments near year-end. This type of activity is not unusual as changes in balances are driven by the episodic nature of client's needs. TTS loans increased 1% as we continue to support our clients' needs while utilizing our distribution capabilities to optimize the balance sheet and drive returns.

On slide seven we show credit quality trends in our Citicorp loan portfolio. Consumer credit remained broadly favorable again this quarter in every region. The increase in NCL rate in North America mostly reflects the impact of the Costco portfolio, seasonality and the impact of regulatory changes on collections in cards. And in ICG total non-accrual loans were essentially flat quarter-over-quarter as improvement in North America was offset by an increase in EMEA. This increase in EMEA non-accrual loans was primarily driven by exposures to two credits, in respect of which we benefit from structural support.

Turning to slide eight, we show the composition of our deposits. Total deposits increased 4% from the prior year period in constant dollars, with continued high-quality deposit flows across our franchise. Consumer deposits increased 3%, driven primarily by growth in international consumer deposits. Corporate deposits increased 6% year-over-year, driven primarily by TTS.

Now let me highlight our issuance program starting on slide nine. In 2016 we issued $30 billion of benchmark debt, including $26 billion of senior and $4 billion of subordinated debt. These issuances have been diversified across tenors, currencies and structures and have a weighted average maturity of approximately eight years. In addition to our benchmark issuance, we issued $2.5 billion of preferred stock in 2016. As we previously mentioned, we've completed our preferred stock issuance having achieved a level of 162 basis points of risk-weighted assets at year-end. Earlier this year we issued $5.3 billion of benchmark debt all under our new indenture which we believe is TLAC compliant. This included a callable structure that was well received by the market. We're pleased to have seen this market continue to develop and we plan to continue to issue in this format in the future.

On slide 10 we summarize our issuance resumption expectations for long-term debt in 2017. As I mentioned during 2016 we issued $30 billion of senior and subordinated debt. Maturities for the year were $14 billion and we redeemed $5 billion resulting in net benchmark issuance of $12 billion. We also issued over $3 billion of securitization debt from the Citi credit card issuance trust in the fourth quarter of 2016 backed by Citi branded cards receivables. While not TLAC eligible, our credit card securitizations are attractive from a cost perspective and also diversify our bank funding sources.

Looking to 2017, we expect gross issuance of approximately $25 billion of senior and subordinated debt including the roughly $5 billion we issued earlier this month. Contractual maturities of long-term debt are $15 billion and we are currently planning for roughly $2 billion of buybacks resulting in approximately $8 billion of net benchmark issuance. We believe this amount of issuance is appropriate, taking into consideration our business as usual funding and liquidity needs as well as those in the context of resolution planning and TLAC compliance including some amount of buffer. We also expect approximately $10 billion of bank level issuance including credit card securitizations and banknotes. These banknotes will be part of a new program that we expect to launch this year and will assist in further diversifying our funding sources for the bank.

On slide 11 we show the composition of our long-term debt outstanding. During the fourth quarter our total long-term debt decreased modestly to $206 billion primarily due to a decline at the bank. Parent and other debt remained flat at $157 billion, a modest increase in benchmark debt offset by decline in customer related debt. And the weighted average maturity of our long-term debt remained at around seven years in the fourth quarter.

Turning to liquidity on slide 12, we update our LCR metrics and drivers. Our average LCR was 121% in the fourth quarter, up slightly from the third quarter as average HQLA remained unchanged at $404 billion and average net outflows declined slightly. We expect our average LCR to remain around this level over the next several quarters as we continue to manage our legal entity liquidity profile in the context of resolution planning guidelines. As to the proposed net stable funding ratio or NSFR, we continue to estimate that measure, under the US regulators proposed rule, to be comfortably above the 100% minimum requirement based on what we know today.

On slide 13 we show Citigroup's net interest revenue and net interest margin. Citicorp net interest revenues grew 4% from the prior-year period driven by loan growth as well as the net impact of higher short-term rates offsetting continued declines in Citi Holdings. Turning to NIM, our net interest margin of 279 basis points in the fourth quarter declined by roughly 7 basis points sequentially driven mostly by lower trading NIM and higher funding costs and the higher mix of promotional rate balances in our cards businesses.
On a sequential basis our cost of long-term debt increased by 25 basis points driven primarily by the increase in short-term rates that we saw throughout the quarter in anticipation of the Fed rate hike in December. Finally, our estimate of the net interest revenue benefit from the 100 basis points instantaneous parallel rate shift increased in the fourth quarter from just under $2 billion to just over $2.1 billion with a portion attributable to US rates increasing from approximately $1.4 billion to $1.6 billion.

On slide 14 we update our estimate of our total loss absorbing capacity based on our interpretation of the Federal Reserve Board's December 2016 final rule. Overall, the final rule is largely consistent with the proposed rule. We were pleased with the Federal Reserve's decision to permanently grandfather non-US law debt and senior notes with acceleration clauses issued prior to December 31, 2016. We believe this will substantially reduce friction costs to achieve compliance.

As we previously stated, we expect our estimated long-term debt requirement of 9% relative to risk-weighted assets to remain our binding constraint under the TLAC rules shown in the right most column. We estimate we reached a ratio of 8.8% of our risk-weighted assets as of the end of the fourth quarter, resulting in a long-term debt shortfall of $2 billion.

The $5 billion improvement from last quarter reflects issuance, the inclusion of $6 billion of customer related debt rendered eligible in the final rule and a reduction in our risk-weighted assets, partially offset by the impact of maturity haircuts, as well as FX. And giving effect to our $5 billion issuance earlier this month, we are currently in compliance with our minimum long-term debt ratio.

Going forward our issuance will be driven by a number of considerations, but from a TLAC perspective, it will primarily be driven by the replacement of debt subject to the rules maturity haircuts as well as the establishment and maintenance of a buffer. We also have plans in place to comply with the clean holding company provisions of the final rule, on a timely basis.

Turning to slide 15, let me summarize our regulatory capital position, which as we discussed remains among the strongest in the industry. During the quarter our CET 1 and total capital ratios decreased slightly to 12.5% and 16.2%, respectively, as the benefit of earnings and the decline in risk-weighted assets was more than offset by share buybacks, dividends and the impact of OCI movements. And our Supplementary Leverage Ratio decreased modestly to 7.2%, driven by a modest decline in Tier 1 capital, partially offset by a decrease in total leverage exposure. Citibank's SLR also declined slightly from 6.7% to 6.6%. Before we move to the next slide, I'd like to note that as a result of the work we've done to reduce our estimated global systemically important bank, or GSIB indicator scores, we ended the year comfortably within the 3% surcharge range.

Moving to our last slide let me summarize several key points. First we earned $14.9 billion of net income in 2016, driven by earnings in our core franchise. Second, we continue to maintain a strong, regulatory compliant balance sheet. We have met our TLAC requirements and also achieved a CET 1 ratio of 12.5%, an SLR of 7.2%, an average LCR of 121% and estimated NSFR of greater than 100%. And finally, we continue to maintain and further diversify our funding base.

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

QUESTION AND ANSWER

OPERATOR: Your first question comes from the line of Hima Inguva with Bank of America. Please go ahead.

HIMA INGUVA: Morning, thank you for taking my question and thanks a lot for doing the call. It was very helpful.

JAMES VON MOLTKE: Sure. Good morning, Hima.

HIMA INGUVA: Good Morning. My first question is a little broader, considering you have given all the color on issuance we need. It's around tax deductibility and broader corporate tax reform. So if tax deductibility on interest is removed due to tax reform from the new administration, how would that affect Citi and with that drive up issuance in foreign currency? And I would like to know your thoughts on broader corporate tax reform opportunities and challenges you see in addition to all the detailed color you provided on DTAs on our earnings call and our conference as well.

JOHN GERSPACH: Yeah, hi, Hima. It's John. That is a very broad question and we have yet to see anything even closely approximating a proposal that would come out from the administration on tax reform. So it's a little early to start speculating on some of the things that you've talked about. As far as tax deductibility, at least what we've seen in some of the language that exists, it's more a net interest type of deductibility question. And so if that's the way it goes, obviously we have on a net basis interest income and therefore our initial read on that is that we would not be impacted by those types of things. But, again, I just think it's too early to start speculating about elements that people are talking about because it's going to be the package that really matters and we haven't seen the packages yet.

HIMA INGUVA: Yeah, that’s fair enough. That's helpful. Thank you. I'll make it a little more specific, my next question is on TLAC call structures and if you see that decreasing your NSFR by advancing the applicable maturity date?

JAMES VON MOLTKE: Thanks for the question. No. We see the callable structures as having a benefit both for TLAC and NSFR as we read the rules. The NSFR rules refer also to the final maturity date and there's a small one half-year benefit that is achieved through the structures under NSFR.

HIMA INGUVA: Okay, great. And then finally on management buffer, I wanted to know if you hold and to what extent do you hold a buffer over the TLAC requirement. Wells Fargo gave 100 basis points number as a broad guidance but I just wanted to know what the number was, how you're thinking about it.

JAMES VON MOLTKE: Yeah. We talked little bit about that on these calls before and I've said that it's been early to give an answer. We've obviously been giving it thought, and as I mentioned on these calls before, we think about it in terms of time because it's really a market access measure. And we think about time, and again it's early, there's more work we want to do in the details and thinking about our risk appetite, but if you think about a ballpark of six months of market access and the current level of TLAC eligible debt that we have of ballpark $108 billion with a weighted average maturity of eight years. Over a six-month period and with a relatively level maturity, sort of ladder, you'd expect us to need something in the ballpark of $6 billion to $7 billion of debt to create that buffer. Again, it's very early days and we're going to continue to analyze this and we'll have more to say in time but to give you a flavor of how we're thinking about it, that's a reasonable construct.

HIMA INGUVA: That's excellent. Yeah. It's very helpful. Thanks a lot. Okay. Thank you very much.

JOHN GERSPACH: Thank you.

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

PRI DE SILVA: Thank you John and James for having the call. It's been extremely helpful for us. A broader question to start with, Citi's revenues have somewhat lagged the broader global systemically important banks. What options does the company have in terms of improving the revenue growth going forward? I know you talked about the equities business, et cetera, in the earnings call, but if you can be a little bit more specific?

JOHN GERSPACH: Yeah, I'd say that you have to break the question down. You take a look at the revenues in Citigroup. We have been, for the last, well, several-several years been winding down Citi Holdings. So, when people just look at the revenues, you get a mix between what's going on in the businesses that we're looking to grow in Citicorp and the revenues that are dissipating as we continue to run down Citi Holdings. We talked a little bit about that on the call last week as far as the impact on net interest revenue but it has that effect on the overall revenue as well.

So, you have to separate the two, I think, between what's going on in Citicorp and what's going on in Citi Holdings. Within Citicorp, I think if you take a look at the ICG businesses, we've got very good momentum building up on what I would say would be the core banking accrual type businesses – TTS, Security Services, Private Bank, even the loan book – there, when you take a look at the revenues, and again the additional thing you have to do is adjust it for changes in foreign currency rates. As the dollar strengthens or weakens, it does have an impact on the revenues that we earn elsewhere. Those businesses are all growing 6%, 7% a year, and most of them have been doing that for the last several years. So we think we're doing really well in those businesses.

When you take a look at the markets-related businesses, our FICC franchise is either the strongest or one of the strongest that is out there and so that continues to perform well. Our rates and currencies business increased 5% year-over-year growth in a bad 2015 and it grew over 20% in a fairly decent 2016, which you may remember 2016 got up off to somewhat of a bad start in the first quarter. So we think that we've got the right momentum building in ICG and there is additional growth that we can get coming through our investments in equities. So we feel that we're actually performing very, very well when we look at the ICG franchise.

When we talk about consumer, we just finished two consecutive quarters of getting revenue growth and positive operating leverage out of our international consumer franchise. So again, we think that we're on the right path there and with the North America consumer we've been, I think, fairly public about the investments that we've been making in that business. And the fact that those investments both are investments in proprietary cards which we began to make midway through 2015, and the investment that we made in the acquisition of the Costco portfolio will really reach full maturity in the second half of 2017, this year. So again we feel that we got the makings of a very good revenue growth story that should be especially visible, both revenue growth and earnings growth, in the second half of 2017 as those cards investments mature.

PRI DE SILVA: John thank you. That was very helpful. And if I may follow up, in terms of subordinated debt issuance, do you generally look at the modernization of Tier 2 capital treatment or the maturities when it comes to replacing maturing securities?

JAMES VON MOLTKE: Yeah. It's James, Pri. Thanks for the question. We look at the amortization of the Tier 2 capital treatment as we think about replacing sub debt that's outstanding.

PRI DE SILVA: So that will be the main driver?

JAMES VON MOLTKE: That will be the main driver.

PRI DE SILVA: Great. Thank you very much for hosting the call and for taking my questions.

JOHN GERSPACH: Our pleasure, Pri.

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

ROBERT SMALLEY: Hi. Good morning **a**nd thanks for doing the call and the information. Couple of questions. One, on slide 27, on the OCI, you've laid out pretty well the impact of interest rates changes last quarter on net interest margin, and potential impacts for future shifts in the curve. Could you talk a little bit about how you see the first quarter shaping up in terms of OCI with respect to investment securities and the strength of the dollar? That's my first question.

JAMES VON MOLTKE: Sure. Thanks, Robert. I guess first of all, it's far too early in the quarter to tell rates and FX movements over the full quarter. Ultimately, the end of quarter numbers are a point in time. What I will say, and thank you for pointing out this slide on page 27, two points to note. One is the effectiveness of the FX net investment hedging program that you can see in the chart of the darker blue line. And that's something we've talked about on these calls in the past. Obviously, in our OCI accounts we are exposed to movements in interest rates and you saw that in the fourth quarter. But I'll point out there as well that on a year-on-year basis we were able actually to slightly improve our net unrealized loss position relative to the prior-year's fourth quarter. And the last point I'll make is to your question ultimately, OCI sensitivity is one of a number of considerations that we have as we think about portfolio positioning and one that we look at very closely in the context of our risk appetite framework.

ROBERT SMALLEY: Okay. Thank you. That's helpful. Second one, you mentioned an upcoming banknote program. Could you talk a little bit more about this and I'm coming at it from last week we saw Treasury Secretary designate in that hearing say that he's looking for a 21st Century Glass-Steagall with no details, and nobody asked him any details, but I guess looking at that, are you getting a jump on that kind of thought with maybe some funding from the bank and then looking at your general holding company unsecured funding as having more of an element from the investment bank and other elements?

JAMES VON MOLTKE: No. It's unrelated to any sort of possible changes in the marketplace. Robert, we simply look at the diversification of the funding sources that we have in the bank. And if you think back the last couple of years, we've been focused on building our TLAC debt, which has been at the parent company. A significant portion of that increase has been pushed down to the bank. Now that we've achieved TLAC compliance we think of other, in most cases less expensive, substitutes for parent level debt, and that's really been the drivers of both diversification and efficiency of the bank funding sources.

ROBERT SMALLEY: Okay. And then my last one, just generally on Mexico and the Mexican business, we've seen obviously, get a lot of attention with the new administration. Early days in terms of economic impact, but maybe you could just talk a little bit about your franchise and why it may be more or less vulnerable to any potential changes in trade flows, etc. that we might see out of the administration.

JOHN GERSPACH: Hey, Robert. It's John. Again, we still don't know very much about what specific changes may be coming in trade policy, in the re-negotiation of NAFTA; so very, very early to talk about. We do think that, broadly speaking, Mexico does have a lot of advantages, and those advantages as an economy would continue no matter what would happen between trade with the U.S. you still have an incredible labor advantage within Mexico. I think it gives them the chance to compete in the broader globe as far as being more competitive.

If there was some impact from a trade that could end up weakening the peso, a weakening peso would again give them even more of a competitive edge. So we still think that there's a lot to like about Mexico, and when you take a look at our franchise in Mexico, it's a franchise that, again, we do need to make some investments in and we laid those investments out. We talked about investing $1 billion over four years. We're on pace to keep that going, and that is a lot of infrastructure and customer service type of investments and we think that it'll still yield good results and good returns.

ROBERT SMALLEY: Great. Thanks very much and again, appreciate the call.

JAMES VON MOLTKE: Thanks, Robert.

JOHN GERSPACH: Our pleasure.

OPERATOR: Your next question comes for line of Mark Kehoe with Goldman Sachs Asset Management. Please go ahead.

MARK KEHOE: Good morning. Just wondering if you could talk about how you think about the composition on the size of your balance sheet if and when the Fed changes its balance sheet and it kind of takes out some of the excess reserves from the system and you may see some deposit outflows? Does that mean that you have to change course in terms of protecting the LCR and maybe then kind of pressuring the regulators to change what's eligible in the LCR calculations?

JAMES VON MOLTKE: Sure, Mark. It's a great question and something we spend a lot of time thinking about. First of all the way in which the Fed will ultimately sort of remove monetary accommodation and stimulus is still very uncertain and so the timing and path of potential reductions in the Fed's balance sheet is something that's hard to judge. In our case, we really manage the deposit businesses as customer businesses. We obviously assess them based on a lot of detailed analysis and modeling. And so we are prepared for a number of eventualities in terms of how the marketplace evolves. We manage our LCR based on a number of measures that we've talked about with you in the past including LCR value of our deposits. And so we believe we're well positioned to preserve and grow the deposit base, retain the LCR value of the deposits, even in a rising rate environment and one in which the Fed may be reducing its own balance sheet.

MARK KEHOE: And within the model then the way you maintain the value of the deposits in the LCR, is it true showing that they are sticky, that you pay a higher rate to retain them? Or how do you make sure that in the model that they still have that kind of high content value?

JAMES VON MOLTKE: We think of them as sticky because they're operational deposit accounts and so they're the accounts that both individuals and corporate clients used to manage their day-to-day payments and receipts. And as a consequence, they have both high stickiness and in the rules a high LCR value.

MARK KEHOE: Great. Thank you.

JAMES VON MOLTKE: Thank you, Mark.

OPERATOR: Your next question comes from the line of Kevin Maloney with BlackRock. Please go ahead.

KEVIN MALONEY: Thank you. Further to Rob's question about the Mexican franchise, you've mentioned in the past you want to reinvest in the business, the $1 billion and through that period of time you're going to create positive operating leverage which suggests that it's going to be self-funding. And I guess the question is, is there going to be more investment on the retail side of the business which is much smaller than the corporate business that you have? And is it going to be a branch expansion? Or is it's all going to be digital and upgrading technology?

JOHN GERSPACH: Very, very good question, but let me just correct your premise. The consumer franchise that we have in Mexico is much larger than our corporate franchise in Mexico. When we talk about investing in Mexico, most of the investment, but not exclusively, but most of the investment is geared towards consumer. We talked about the fact that some of the investment will go towards branch, not necessarily expansion, but we do need to refurbish the branches. We will be shutting down some of the older branches, transitioning some of the existing branches into smart branches similar to what we have in other geographies. There's a lot of work they've done on infrastructure. There's introduction of new ATMs. So one of the reasons why the investment is, as you put it self-funding, is that it's not really being driven by a big expansion of our Mexico business, but a lot of it is core infrastructure that will actually serve to reduce the expenses that we currently incur in order to run that business. So we think that we end up with a much more efficient Mexico consumer franchise and one that provides our customers with a much better customer experience.

KEVIN MALONEY: Okay. Great. Thanks. And one last question about Mexico. Do you have any internal TLAC needs for that operation? It's a significant subsidiary.

JAMES VON MOLTKE: Well first of all, the internal TLAC rules we're going to have to look out when they come out but from the perspective of the current structure, it's well-funded and capitalized as of today.

KEVIN MALONEY: Great. And the banknote program, which is something new for you guys, I imagine that's Citibank N.A. that will be the issuer?

JAMES VON MOLTKE: That's correct.

KEVIN MALONEY: And is it being done for optimizing the NSFR or is it something else?

JAMES VON MOLTKE: No, really as I said to the earlier question, we think it's an attractive source of funding and a reasonably flexible source of funding and one that's from a cost perspective, obviously, superior to the parent benchmark program. So that's really been the driver from our perspective in introducing that program.

KEVIN MALONEY: Okay, great. Thanks. That's all I have.

JOHN GERSPACH: Thanks.

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

ARNOLD KAKUDA: Great, thanks. Thanks for the helpful call. So you have a peer that has the same credit ratings as you. About six month ago they announced a cost cutting program and recently Moody's changed the rating outlook on that peer to positive citing the outlook for profitability has improved. And then recently you've announced a target to cut your expense ratio for 2017. Do you think you can make solid progress on hitting your efficiency ratio target over the next six months? Or will the improvement happen more in the second half of the year?

JOHN GERSPACH: Yeah. Hi, it's John. We have not given a timeframe for hitting that ratio. We tend to look at the ratio as being exactly as it is. It's for the full year. But it is one that should progress as the year goes on, obviously, because the further on guidance that we gave is that we thought that we could be operating in the band of the mid-50%s, as early as 2018. So I haven't given a timeframe as to exactly when we will hit that 58%, but think of that as being an ongoing program.

ARNOLD KAKUDA: Okay, great. And then as you mentioned you hit your 2016 efficiency ratio target. But I guess arguably the revenue environment, at least on the trading side, improved more than expected in the second half of the year. So if revenue for the second half of 2016 didn't improve, what levers would you've had to hit the efficiency ratio target last year?

JOHN GERSPACH: When we look at the ratio for the full year, I just want to correct you slightly, only because we did not hit our target for the year, we hit our revised target for the year. We went into the year looking to hit a target for Citicorp of 57% and on the heels of a disappointing revenue performance in the first quarter that resulted in our achieving a, or posting a, efficiency ratio north of 60% – I can't remember if it was 60.2% or 60.3% in the first quarter – we therefore said that we felt that the rest of the year we'd be able to manage to a 58% ratio. That included expectations of the revenue that we had for the balance of the year. You have to think in terms of the fact that along with that improved revenue performance that we saw in the trading businesses in particular, in the second half of the year we had additional comp. And therefore had we not paid that additional comp we would've had a lower ratio. If we had not had the revenues we wouldn't have had the additional comp and we still would have come somewhere close that 58% that we hit.

ARNOLD KAKUDA: Okay, great. Thanks John. And then maybe for James, on the TLAC slide on page 14, previously you had excluded the customer related debt discounting for TLAC, so what kind of changed your mind in saying that out of the $26 billion maybe $6 billion would count as TLAC. And maybe is this another source of potential issuance for this kind of security for TLAC purposes?

JAMES VON MOLTKE: Sure. Really we were being conservative in the interpretation of the proposed rule. It was a potential opportunity that we knew might come as the final rule defined eligibility criteria, and there is a sort of population of what we call customer related debt, it's relatively plain vanilla at the parent company, which under our reading of the final rule is eligible.

ARNOLD KAKUDA: So would there be continued issuance of this type of security? Or would you just roll that into kind of your benchmark issuance?

JAMES VON MOLTKE: They'll be continued issuance and those are programs that, again, are customer related. They satisfy customer demand that's in the businesses, and we would continue to issue small amounts out of the parent, but related to that customer demand.

ARNOLD KAKUDA: Okay, great. And then just my last one, on the GSIB buffer, can you explain to us again how the Financial Stability Board, they increased your surcharge based on your balance sheet as of the end of 2015. And then using the same 2015 data point, I think it was last year, you said that your Federal Reserve method to surcharge declined. So can you talk about that discrepancy and how that can be?

JAMES VON MOLTKE: Sure. The very quick answer is FX rates. Method Two is something that we manage carefully, it's a key driver of our required capital levels. Method One, and this is a feature of the method one calculation that the FSB had devised, which we had pointed out to the Fed was a potential flaw, a flaw that the Fed we think addressed in their final rule. And that is that the denominator for the method one is expressed in euros, and for us, foreign currency.

So if you look at each of the drivers of the Method One calculation, we actually became less systemically risky. In other words our balances came down in dollar terms but the associated scores went up because the associated denominators had moved in FX terms, and that was really the driver. And I would note that we went into that bucket by only one point, despite all of that, I think a 13% currency movement against us.

JOHN GERSPACH: Again if you go back and we mentioned this in one of the early calls, that the, as James put it, the flaw in Method One is that the denominator is the aggregate of 78 or 80 institutions from around the world but with everything converted into euros, which given the strengthening of the dollar was going to put all US banks at a disadvantage. You could actually, as we did, reduce your systemic footprint and still end up under Method One being looked at as being a riskier institution all because of fluctuation in currency rates. And when the Fed came out with Method Two, I'm not saying that I agree with everything they did in Method Two, but huge applause for the Fed in taking that FX rate variability out of the measure. What that allowed us and other US banks to do was to actually manage the risk, reduce your footprint and therefore reduce your systemic charge, which is exactly what we have done.

You know, when they first came out, it looked like we might be in the 4% bucket. We then reduced ourselves to the 3.5% bucket and now the last two times that we've done measurement on the method two survey, we've held in that 3% bucket. So I think that the Fed did exactly what it wanted to do which is to encourage institutions to actually see results for the process that they would put in place to actually reduce their risk. And that's what has gone on.

ARNOLD KAKUDA: Okay, great. Thanks very much.

JOHN GERSPACH: Thanks.

OPERATOR: Your next question comes from the line of Don Jones with Amherst Pierpont. Please go ahead.

DONALD JONES: Great. Thank you, John and James. This is always a very helpful call. I appreciate it.

JOHN GERSPACH: No Problem.

DONALD JONES: One topic, two questions I suppose. Within M&A it seems there have been a couple recent, I think its third quarter, two targeted divestitures. Do you think there are more on the horizon for you, internationally or even domestically?

And then secondly, do you anticipate, and this might not be an answerable question, but anything within the change of regulatory perspective or viewpoints of the regulators where Citi or where you could have larger transactions, acquisitions potentially down the horizon?

JOHN GERSPACH: Let me start with the first question and I'm not quite sure what you're referring to unless it's the deals that we signed to sell the consumer franchises in Argentina and Brazil which go along with the fact that we move them into Holdings at the end of 2015, and therefore had told everybody that that's exactly what we intended to do was to sell those franchises. So that pretty much went along with that strategy.

And as for the second question, we just got finished doing the Costco acquisition in the middle of 2016. We bought 11 million new card members, initial loan value was $10.6 billion. So I think we've been fairly active in that space and we remain open for business. As far as acquiring portfolios, that makes sense with our existing strategy.

DONALD JONES: Right. No, that's right. Yeah. And I was thinking like the Costco transaction is obviously very big but I didn't know if there were other like full franchise types of acquisitions and it might just be prohibitive given the regulatory environment but no, that's helpful. Thank you.

JOHN GERSPACH: Beyond just being the current environment, again, for us any acquisition would really have to fit our stated strategy. And so when you think about – on the ICG, we're focused on serving the needs of roughly 15,000 large multinational corporate and investor clients, and so you'd have to find something that would fit there in order to make it – makes sense for it to work from an ICG point of view. And then on the GCB side, other than Mexico, where we've got a broader based franchise, we're really focused on serving the needs of wealth management clients in large urban areas in key countries. And then with the cards book, you'd be hard pressed to find a franchise acquisition that would actually fit that type of strategy.

DONALD JONES: Okay. Great, Thank you.

OPERATOR: Your next question is a follow up from Pri de Silva with CreditSights. Please go ahead.

PRI DE SILVA: Thank you.

JOHN GERSPACH: Hey, Pri.

PRI DE SILVA: How does the deposit beta differ between the consumer and the commercial side?

JAMES VON MOLTKE: It's a broad question. Obviously...

JOHN GERSPACH: Somewhat.

JAMES VON MOLTKE: But, just some simple thoughts. The liquidity coverage or the – the liquidity value of the consumer deposits under the rules are higher, given the granularity of that deposit base as well as behaviors. And on the institutional side, it depends on the type of deposit. So a corporate transactional account is treated a little differently from a financial institution account, let's say in the custody business. And so there are gradations, if you like, on the corporate side that blend to a liquidity value that is lower, as I mentioned, than the individual accounts.

PRI DE SILVA: Yeah. Just changing tracks; is the callable debt structure suitable for foreign-currency debt? I'm guessing it's more challenging due to the FX hedging needs but if you could comment on that?

JAMES VON MOLTKE: I think it's less around FX hedging. It's obviously a market that we haven't yet tested. We may in time and it will depend also on investor appetite in these other currencies, but it's something that we'll look at over time.

PRI DE SILVA: Great. Thank you very much again for taking the call.

JAMES VON MOLTKE: Thanks, Pri.

OPERATOR: Your next question comes from line of Scott Cavanaugh with APG. Please go ahead.

SCOTT CAVANAUGH: Thanks guys for holding the call, always good. My question is going back on to the final TLAC rules. I'm sorry to beat a dead horse here...

JOHN GERSPACH: It's Okay. Obviously that horse isn't dead yet otherwise we would have stopped beating it.

SCOTT CAVANAUGH: Yeah, I know, I still like to beat it. When we think about the indentures, the old versus the new, and then versus existing subordinated indenture, how should we really be thinking about this from just a bankruptcy scenario, taking FDIC potential off the table? But I kind of struggle to look at what the actual difference is between subordinated indenture and the new senior indenture? I just wondered if you could walk me through your thought process on that.

JAMES VON MOLTKE: Sure. Well, starting at the big picture, as we looked at the indenture and the final rule, our goal was to preserve the protection that had been in the original senior indenture, while removing the acceleration clauses that, as you know, were the concern that the regulators had in the final ruling. So we kept as we could the covenants that were there but without acceleration clauses. We then look, to your point Scott, at the comparison of the senior and subordinated indentures, and we added at least one feature from the subordinate indenture into the senior, which is the ability to act and take action through indenture trustee, which we thought was a useful addition. But beyond that, so to your question, one, it's obviously in the documentation that the claim is senior, in the senior notes compared to subordinated. And there are also in subordinated there aren't acceleration clauses for non-payment of interest and principal. So those would be the two principal differences today.

SCOTT CAVANAUGH: Okay, and then following up on that, if we switch over to the FDIC has there been any additional insight provided of how the waterfall might be viewed there? Are they viewing the old legacy indentures and the new as equal? Or is there any distinguishment between the two from a regulatory point of view?

JOHN GERSPACH: I'm not aware of any distinction that they're making between old and new. To me the grandfathering was the right decision and a practical decision. As you've heard me say, Scott, I didn't view there to be a significant difference between the sort of bail-in ability of pre and post debt. I think it takes one risk off the table going forward, but allowing the existing debt under the old indenture to run off over time addresses that concern that the agency's had over time.

SCOTT CAVANAUGH: And then lastly, when we think about disclosures going forward, obviously you've been very good in your Fixed Income presentations, but when we think about going forward in our SEC filings and other filings, are you going to be more detailed in your TLAC i.e. on a regulatory basis footprint basis on a currency basis, the runoff, the head room over time? Is that something we should be expecting?

JAMES VON MOLTKE: Yeah Scott, that's' something we're continuing to look at and work on and we do intend to make some changes in our disclosures over time to give investors clarity on what we think are TLAC eligible instruments, again under our reading of the rules. And so you should expect us to make some changes over time as we get comfortable with our reading of the rules, and really find the right ways to provide you with those additional disclosures.

SCOTT CAVANAUGH: Thank you very much.

JAMES VON MOLTKE: Sure, thanks for your question, Scott.

OPERATOR: Your next question comes from the line of Jeff Bernstein with Insight. Please go ahead.

JEFF BERNSTEIN: Hi, thanks. Most of my questions have been asked and answered. Just one little question left, slide 26, the trust preferred security you have at the bottom there, could you just remind us of the cost benefit of having that out there?

JAMES VON MOLTKE: And that question comes up from time to time, Jeff. It has AT1 treatment for us so it is a capital instrument, so to our mind that's the benefit. It's obviously higher cost than other AT1 instruments, which is something we're also aware of.

JEFF BERNSTEIN: Would you need permission to call that?

JAMES VON MOLTKE: In the capital plan that we submit to the Fed on an annual basis, we would need to ask for permission.

JEFF BERNSTEIN: Okay. Thank you.

JAMES VON MOLTKE: Thanks.

OPERATOR: Your next question comes from the line of Sandeep Malangee with PPM. Please go ahead.

SANDEEP MALANGEE: Thank you so much for having the call, I really appreciate it. A couple of questions for you. As you think about 2017 issuance, I think you had $25 billion on page 10, do you sense that you'll hit the 30-year part of the curve a little bit more given the past couple years? I think most banks in general were not hitting that given TLAC uncertainty?

JAMES VON MOLTKE: We look at all parts of the curve, Sandeep. So yes, I would expect that we'll issue in the 30-year tenor over time. I can't tell you when, or in what size, but we look at all maturities and structures and currencies.

SANDEEP MALANGEE: Okay, great. And then given the callability notes that had been coming out with all the institutions, I guess my big question there would be how do you view that call? In most call structures there's a significant amount of interest rate but in this case the reason for this is because of regulatory needs. Do you see the regulatory portion of that being significant, A. And number two, is the bullet structure gone? Meaning we're not going to – it's not necessary on the go forward and we're going to see the callable given if that market is open?

JAMES VON MOLTKE: So I'll answer the second question first. We don't think the bullets are gone. We would anticipate there will continue to be some issuance in bullet format and it's a question of size, investor demand and cost. On the first part of your question, the callable structures are absolutely an efficient structure from the issuers' perspective. The base case is that in the example of our 11 non-call 10 this will be outstanding for 10 years, but the structure under the rules gives us the ability to keep it outstanding for longer and that's, I think, an effective feature both for the issuers and the regulators under the rule.

SANDEEP MALANGEE: So there's a higher propensity, all else being equal, that you would call that for regulatory purposes in year 10?

JAMES VON MOLTKE: A higher propensity that we would call it in year 10.

SANDEEP MALANGEE: Because of regulatory issues.

JAMES VON MOLTKE: I wouldn't think of it is a regulatory decision in year 10.

SANDEEP MALANGEE: Okay. Given that you don't get any favorable treatment from a TLAC perspective from year 10 to 11. In this case, I think I have to go back to the indenture, I think there's only one call on that, correct, at year 10?

JAMES VON MOLTKE: There is actually, just before maturity, there is also a call feature, but the point that you're driving at is, it's an economic decision in year 10, the call decision.

SANDEEP MALANGEE: Okay. I think that answers my questions. I really appreciate your help today.

JAMES VON MOLTKE: Perfect. Our pleasure.

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

DAVID JIANG: Hi, guys.

JOHN GERSPACH: Hi.

DAVID JIANG: On your callable TLAC issuance, is there a structure you prefer in terms of the back end, the call last year, in terms of the fixed to floating aspect of the last call – the call in the last year?

JOHN GERSPACH: Yes. Obviously these callable structures, for this specific purpose, began to be introduced last summer by, us among others, and I think the market has been iterating to what the quote unquote best structure or conventional structure will become for the securities. We think the fixed to float, we spent a lot of time thinking about the natural structure here, and we think the fixed to float that we issued earlier this month is a logical and natural structure for the securities. It borrows, as I'm sure you know, from preferred structures and we think represents the right balance of incentives, to Sandeep's question a moment ago.

DAVID JIANG: Great. So going forward, your callable structures will likely include that fixed to floating element?

JOHN GERSPACH: It won't be exclusive. As I said on last quarter's call, we like the floating rate note format as well, so we'd be likely to issue in that format for callable notes. If we think about the fixed to floating it's certainly something that you'll see us issue in the future.

DAVID JIANG: Okay. A question for John. I know your folding Citi Holdings and the reporting aspect after this year, there is still about $100 billion of risk-weighted assets there, does that mean, is there any intentions of still getting, selling down what's in Citi Holdings and it's mostly North American mortgages, I presume?

JOHN GERSPACH: What we said on the call, there's 54 if you think about GAAP assets, there's $54 billion worth of GAAP assets we have signed contracts to sell $9 billion of that. And as we talked about it with the previous caller, there's Argentina and Brazil that we've already announced that we've got under contract. And then there are some other mortgage assets that we already have under contract.

So we will continue to wind down Citi Holdings as we have in an economically rational manner, and that's been our approach since we put Citi Holdings into existence. And Citi Holdings itself did not go away it's just that now it's gotten so small, it seems silly to keep it as a separate management segment. But we will go and we will continue to wind that down.

From a risk-weighted asset point of view, as you mentioned, there's about $100 billion, $104 billion worth of risk-weighted assets remaining in Citi Holdings. And the one thing I'll caution you is we've said in the past there's about $49 billion of that $104 billion that represents operational risk-weighted assets, and that's likely to stay with us for some time, as the operational risk has a very long tail associated with it. So as we wind down those assets, there's really – it's the other $55 billion worth of risk-weighted assets that will come down in the next year – two, three years – as we wind our way down to those remaining assets.

DAVID JIANG: Got it. Thank you.

JOHN GERSPACH: You're very welcome.

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

TOM ROGERS: I'd just like to thank everyone for joining the call today. And of course if you have follow-up questions, feel free to reach out to us in Investor Relations.

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

Certain statements in this document are "forward-looking statements" within the meaning of the rules and regulations of the U.S. Securities and Exchange Commission. These statements 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 those included in these statements due to a variety of factors, including the precautionary statements included in this document and those contained in Citigroup's filings with the U.S. Securities and Exchange Commission, including without limitation the "Risk Factors" section of Citigroup's 2015 Annual Report on Form 10-K.