TRANSCRIPT

Citi First Quarter 2017 Fixed Income Investor Review

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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 moment, 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 reminder 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 2016 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 first quarter 2017 results. Second, I'll cover recent balance sheet trends, notably growth in loans and deposits. Third, I'll review our issuance program and provide updated issuance guidance for 2017. And finally, I'll discuss our capital position which remains among the strongest in the industry.

For reference, slide three summarizes our first quarter 2017 results. We reported net income of $4.1 billion for the first quarter and achieved an efficiency ratio of 58% as well as an RoTCE of 10.2%, excluding the impact of disallowed DTA.

On slide four, we show average balance sheet trends over the past five quarters in constant dollars. On this basis, our balance sheet increased by $60 billion, or 3% from the prior-year period. This growth was largely driven by deposits as we continued to accommodate client demand. Loan growth was somewhat muted, in part due to lower demand for episodic financing from our corporate client base as well as lower average retail loans in Asia as we continue to optimize the portfolio for improved returns. And cash balances increased year over year.

Slide five presents trends in our loan portfolio on an average basis in constant dollars. Total Citigroup loans increased 2% year over year and 5% in aggregate across our core Consumer and Institutional businesses. In our core Consumer business, average loans grew 7% year over year, driven by 13% growth in North America. This included a 28% increase in Branded Cards, driven primarily by the acquisition of a Costco

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portfolio as well as modest organic growth. International consumer loans declined 1% year over year, as growth of 6% in Mexico was more than offset by a 3% decline in Asia consumer loans, as we continued to optimize our portfolio in the region to generate higher risk adjusted returns.

On the Institutional side loans grew 3% year over year, driven by growth in lending in our private banking segment. Corporate lending declined 2% as we saw a lower level of episodic borrowing needs within our target market compared to the prior-year period. The majority of our target clients are investment grade and generally in strong liquidity position. And in the first quarter they accessed capital markets to fund ongoing, longer term financing needs given the continued attractive rate environment. TTS loans increased 1% as we continued to support our clients' needs while utilizing our distribution capabilities to optimize balance sheet and drive returns. At the same time, our legacy portfolio, which is now included in Corporate Other, declined by 32% primarily driven by decline in our North America residential mortgage portfolio as well as divestiture activity.

On slide six we show credit quality trends in our GCB and ICG loan portfolios. In GCB, the NCL rate in North America increased from last quarter, but should trend lower for the remainder of the year as Costco conversion related losses are now behind us, and we should benefit from normal seasonality. Credit trends in Asia consumer remained stable this quarter and the NCL rate in Latin America was 4.4%, up somewhat from the prior quarter mostly driven by lower loan growth but still in line with our near-term outlook. And in IGC, total non-accrual loans declined to 74 basis points of total loans, driven by net upgrades as well as pay downs.

Turning to slide seven, we show trends in average deposits over the past five quarters in constant dollars. Total deposits increased 4% from prior-year period as we saw strong customer engagement across all major businesses and regions. Additionally, the liquidity value of our deposits remained high at over 74%.

Now let me highlight our Issuance Program starting on slide eight. Including the $4.5 billion issuance earlier this week, we have issued a total of $10.5 billion of parent level benchmark debt including just under $10 billion of senior and $750 million of subordinated debt. These issuances have been diversified across tenors and structures and have a weighted average maturity of approximately 10 years. In addition to our benchmark debt, we also issued roughly $5 billion of credit card securitizations so far this year. Lastly, we launched our new bank note program in the first quarter, issuing $2.5 billion, consistent with our goals of optimizing funding costs and diversifying funding sources.

On slide nine, let me cover our issuance and redemption expectations. In 2017, we continue to expect gross issuance of approximately $25 billion of parent level senior and subordinated debt, including the roughly $10.5 billion we've issued year-to-date. $6 billion of debt matured so far this year out of a total of $15 billion expected for the full year. We expect buybacks in the range of $2 billion of benchmark debt in 2017, including the roughly $1 billion we repurchased thus far. This combination of new issuance, maturities, and redemption would result in net issuance of benchmark debt of approximately $8 billion in 2017.

We now expect approximately $15 billion of bank level issuance this year, including the roughly $7 billion of credit card securitizations and bank notes we have issued year-to-date. We've increased our issuance estimate in the context of resolution planning and expect to issue from the bank in order to maximize the efficiency of our overall funding profile.

On slide 10 we show the composition of our long-term debt outstanding. During the first quarter, our total long-term debt increased to $209 billion, primarily due to issuances at the bank. Parent and other debt remained flat at $157 billion. And the weighted average maturity of our long-term debt declined modestly to 6.9 years, while the weighted average maturity of our TLAC-eligible debt increased to 7.6 years.

On slide 11, we show Citigroup's net interest revenue and margin trends split by core accrual revenue, trading-related revenue, and the contribution from our legacy assets in Corporate Other. Total net interest

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revenue declined 3% year over year in constant dollars to $10.9 billion as growth in core accrual revenues was more than offset by the wind-down of legacy assets as well as lower trading-related net interest revenue.

In the Accrual businesses, net interest revenues of $9.5 billion were up 3%, or $280 million, from last year, driven by the addition of the Costco portfolio, other volume growth and the impact of the December 2016 rate hike, partially offset by lower day count, an increase in our FDIC assessment, and higher long-term debt. However, our core net interest margin declined 9 basis points to 340 basis points, as higher net interest revenue was more than offset by balance sheet growth, particularly in cash balances.

Looking forward, and assuming one additional rate hike midyear, core accrual revenues should grow year over year by roughly $1.5 billion in total over the next three quarters, with just under two-thirds of that amount coming from higher rates and the remainder mostly reflecting higher loan volumes and mix. This $1.5 billion estimate taken together with the nearly $300 million of net interest revenue growth we saw in the first quarter results in a $1.8 billion expected increase in core accrual revenue year over year for the full year. However, as previously noted, we do expect this increase to be offset by a roughly $1 billion decline in the net interest revenue generated in the legacy wind-down portfolio in Corporate Other, resulting in net growth of approximately $800 million in total accrual net interest revenues for the full firm. Of course, this estimate does not include changes in our trading-related net interest revenue. However, any such variances should be evaluated in the context of our overall trading performance.

Turning to slide 12, let me summarize our regulatory capital position, which as we discussed remains among the strongest in the industry. During the quarter, our CET1 and total capital ratios increased to 12.8% and 16.5% respectively, driven primarily by earnings, partially offset by $2.2 billion of common share repurchases and dividends. And our supplementary leverage ratio increased modestly to 7.3%, driven by an increase in Tier 1 capital, partially offset by an increase in total leverage exposure. Citibank's SLR also increased slightly from 6.6% to 6.7%.

Moving to our last slide, let me summarize several key points. First, we earned $4.1 billion of net income in the first quarter, generating an RoTCE of 10.2%, excluding the impact of disallowed DTA. Second, we continue to maintain a strong, regulatory-compliant balance sheet, met our TLAC requirement achieving a long-term debt ratio of 9.2% of risk-weighted assets as of 1Q 2017 or a $3 billion surplus. We maintained a highly liquid balance sheet with an average LCR of 123% and an estimated NSFR of greater than 100%. And we achieved a CET1 capital ratio of 12.8% and an SLR of 7.3%. 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 Scott Cavanagh with APG. Please go ahead.

SCOTT CAVANAGH: Good morning, guys, and thanks for holding the call. Always appreciate it.

JAMES VON MOLTKE: Good morning, Scott.

SCOTT CAVANAGH: A couple questions for you. First of all, on the issuance, for the bank level and the securitization I know that went up a little bit on the guidance for full year. Could you break down how much of that entire bucket you expect to come from the bank level?

JAMES VON MOLTKE: I don't want to be precise on that, Scott. As you point out, it's a $5 billion increase from the guidance that we gave earlier this year. And as I mentioned in my prepared remarks, that is taking

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place in the context of resolution planning that we are undertaking. How much of it will be securitization versus bank notes is not something that we've settled on.

SCOTT CAVANAGH: Okay. Then moving on more of a macro perspective, what's your current all-in exposure to South Korea? I ask this in the background of the growing tensions with North Korea at this point.

JOHN GERSPACH: Scott, its John. I don't have the South Korea exposure but you should be able to figure it out from the 10-K. You've got a table there that lays out the consumer exposures and everything by – I don't have a page reference – but it is in the 10-K. I just don't have it in front of me right now.

SCOTT CAVANAGH: Okay. And I have it pulled up right now. It's $34 billion. However, when I look at that I'm just trying to think of, how do I think of it? If there is some sort of tensions, what type of measures have you guys put in place to kind of hedge a risk there? If you can?

JOHN GERSPACH: We have been through so many different crises in so many different parts of the world, we don't necessarily put in specific hedging programs. There's certainly nothing to indicate anything right now that would say that we're in some sort of crisis mode. So we closely monitor these situations and take the actions that we believe are appropriate when the circumstances dictate them.

SCOTT CAVANAGH: Okay, that's fair enough. Then lastly, when I think about the resolution topic and specifically looking at H.R. 1667, have you guys given any thought about that and how that involves in your living will process or how you think about going forward?

JAMES VON MOTLKE: We are following the discussions in Congress and H.R. 1667, as you note. We look at potential additions to the bankruptcy code for financial institutions as potentially a positive development for the industry overall. But at this point, we're really just waiting and watching developments.

SCOTT CAVANAGH: Thank you very much, guys. Always appreciate it.

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

HIMA INGUVA: Thank you. Thanks for doing the call. As always, very, very helpful. I'm going to start with a couple of higher level questions and then I had a few on issuance. The first one I want to ask was, John, we know it's early in the process but how do you think about deregulation this year? Do you expect to see any movement in that and also in tax reform considering the health care bill was shut down?

JOHN GERSPACH: Again, we all went into the year with a certain amount of optimism. I'd say there still is optimism that something will get done. Timing is difficult to predict, so I'd say the expectations would still be that we will see something, I just can't tell you when.

HIMA INGUVA: Right. But do you think deregulation, or I guess peeling back of certain parts of regulation, has a chance or you think they'll get to tax reform first?

JOHN GERSPACH: I think that the administration has already indicated some movement as far as deregulation where they've been able to use the Congressional Review Act. There's been some movement there. And I guess the big thing that everyone is waiting on is what are they going to do with Dodd-Frank? And there – again, I don't think you are going get a complete repeal of Dodd-Frank. I don't think you'd want a complete repeal of Dodd-Frank. But I do think that the administration will eventually find some areas where they can lessen the burden on businesses and certainly on banks.

Some of the things that we've talked about before would be with regard to the Volcker Rule. We absolutely support the fact that banks should not be involved in proprietary trading. And clearly, proprietary trading is

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not part of our business model. However, I don't think that the current construct of requiring so many different analyses to prove that we're not involved in proprietary trading is necessarily cost effective. So these are areas that I think the administration will continue to look at and I do anticipate some changes at some point in time.

HIMA INGUVA: Great. Thank you. And then moving on to MiFID II, as the implementation date gets closer in 2018, how are you preparing for that? And then do you think it will have a longer-term impact on the research business? Either in the U.S. – I mean in the U.S., either directly or indirectly?

JAMES VON MOTLKE: I'd say first of all, we are working to prepare for the implementation of MiFID II and, in particular, working with our research organization and our clients to ensure that we adapt, but also that our clients value the research that we provide. I think it's too early to say how it will change the industry or business models. But it obviously does shine a light on the value of trading ideas and macroeconomic research provided by the Street.

HIMA INGUVA: Sure. That's helpful, thank you. And then on credit quality, in the U.S. overall, as well as in cards, do you think we are at an inflection point now given the very benign credit environment that persisted over the last few years?

JOHN GERSPACH: It's John again. When you use terms like inflection point, it's difficult to answer that with a yes or a no. But I don't think that we are at some major shift at this point in time. What we will see, and what we've said is, we would expect our credit cost to reflect normal seasoning. We've made a lot of investments in our Credit Card business and so there'll be some seasoning there. But, our outlook would be for the NCL rate in our Credit Card businesses to actually come down for the balance of the year. Our Branded Cards business ran an NCL rate of 311 basis points in the first quarter.

There are some things that impacted that like the bubble that we created due to the Costco conversion, but our guidance is that – our anticipation is that U.S. Branded Cards should have an NCL rate for the full year of 280 basis points. So that would suggest, clearly, that the NCL rate will decline from the first quarter. So we certainly watch everything very, very closely, but there's nothing to indicate right now that we have hit an inflection point or that an inflection point is staring us right around the corner.

HIMA INGUVA: Great, that's very helpful. Thank you. And my last question is on issuance. Two parts to it. The first one is that do you see a need to issue sub debt this year? What portion of the $25 billion issuance will be in subs, considering you have already issued about $750 million or so?

JAMES VON MOLTKE: So as we've talked about before on this call, we've gotten to the point of adding over 200 basis points of Tier 2 capital in our stack. And so we're basically replacing the decay or sub debt that's rolling into the window. And that is running at a little less than $1 billion a year and that's informing our issuance plans. But I don't want to go into precise detail on future plans. And how much of what remains to be issued this year would be in sub debt form.

HIMA INGUVA: Fair enough. And then the last part of the last question. On redemption, you've redeemed about $1 billion year-to-date and slide nine shows you expect to redeem another $1 billion remainder of 2017. That seems a little low relative to the $5 billion you've redeemed last year. Should we think that you'll be opportunistic in redeeming more than $1 billion or is it set at $1 billion?

JAMES VON MOTLKE: It's never final, so I don't want to hedge myself in completely. We are opportunistic in that program but I'd remind you that we've come off years of very significant liability management actions. And so over time, I won't say we've exhausted the opportunities but we look to take economic steps and obviously also support our curve and investors in terms of liquidity. For this year, I think that more or less sizes our appetite, but it will be dynamic based on a variety of factors.

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HIMA INGUVA: Excellent. Thank you very much. Fixed income investors really appreciate you doing the call. Thanks a lot.

JOHN GERSPACH: No problem, thank you.

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

ROBERT SMALLEY: Hi. Good morning and I too thank you both for doing the call. A couple of questions, first on trading and financing, a second on capital, and a third question about issuance. First, trading activity in Equities and Fixed Income was robust this quarter. Could you talk about your client financing for that business? And by that I mean both sides of the equation. First, on prime brokerage and investing clients and how utilization of that balance sheet has contributed to greater turnover and profitability. And secondly, lending to issuing clients, particularly in Fixed Income, and then getting underwriting fees from that as well as enhanced volumes. And if you can quantify the impact of using the balance sheet and the benefits of that, I'd appreciate it.

JOHN GERSPACH: So, it's John. So from an equities point of view, clearly we're putting more balance sheet to work. I can't give you the exact dollar figures, but we talked about the fact that one of the advantages that we have in having the Supplementary Leverage Ratio that we do is that we have the capacity to put that balance sheet at work. We've also said that Equities is clearly an area in which we are investing. So yes, we're taking advantage of the opportunity that we have created through balance sheet management by now being able to deepen relationships with investor clients by offering them more capacity through prime brokerage. And I think you can see that it is having an impact if you take a look at our equity trading revenues for the quarter, we're up 10% year over year. Now, it's not all due to prime brokerage, and I don't want to say that it's a run rate for the balance of the year, but again, its evidence that we are making progress and I think if you compare our year-over-year performance with our peers, it certainly looks like we had a slightly different performance in the first quarter than others.

When it comes to your question on Fixed Income, we look at overall client relationships. And so a lot of our Fixed Income business, we've talked about this before, we have a higher percentage of our Fixed Income business, notably rates and currencies, that is centered on corporate clients rather than investor clients. Those corporate clients, the good thing about that is, again, it's a nice steady base, because corporate clients really are engaged in working capital management, and its part of our overall relationship with those corporate clients. These are corporate clients that we will manage their cash through our Treasury & Trade Solutions business. We'll provide them payment services. We'll provide them with the capability of hedging their rate risk, their foreign currency risk. We'll issue debt for them and, if they need loans, we'll give them loans. But it's really in support of an entire relationship.

ROBERT SMALLEY: Okay, that's helpful, particularly on the Equities side. On capital, just one quick note, you mentioned on the other call, you said that you had $327 billion tied up in operational RWAs. Could you talk about how much is in credit and market RWA and what you're doing to mitigate the operational line, if at all?

JOHN GERSPACH: Sure. So if you look in the deck, the risk-weighted assets for the first quarter under the advanced approach is $1,194 billion. And that $1,194 billion breaks down between $794 billion would be credit, $73 billion would be market risk, and then the balance, the $327 billion, is the operational risk number that you mentioned.

When you take a look at the operational risk number, quite frankly, there is little that we can do to mitigate that number right now. We can certainly stop it from growing by avoiding operational losses, and I'd say that we've done a fairly good job of minimizing that impact. But the models that go into developing that number are still under discussion with the Fed. And so right now, it's more of a longer term – you avoid losses, and then sometime over a 10 to 15 year period, you'll eventually see a reduction in your op risk risk-

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weighted assets. Now I think the entire industry would like to see a little bit more cause and effect in those numbers, so I'd assume we're all working towards that, but we're not there yet.

ROBERT SMALLEY: Okay. And in terms of the right level of capital, overall, was said on the other call that need about 11.5% to run the company prudently. You have been a very fixed-income-friendly company in terms of capital levels in the past, but you, like the rest of the industry, is under pressure to start returning capital to shareholders. How do you balance these two almost contrary type of demands? And have you looked at lower levels of capital's impact on your cost of funds? And if you were to run the company at a little skinnier capital levels, would that materially increase your cost of funds?

JOHN GERSPACH: I'll let James handle the second part of that question. For the first part of the question, when we put that number out, 11.5% was actually I'd say the upper end of the range that we think that we should be able to run the place at, and, again, prudently. And I'd say it's more in the range of somewhere between 11% and 11.5%. Depending upon what happens with the stress-capital buffer, you may end up in 11.25% but it certainly is within that range. And we do look at the proper mix between equity and debt financing in order to, again, optimize the balance sheet and prudently run the business. You don't want it overly weighted towards equity, and you don't want it overly weighted towards leverage. We understand that.

So, again, when we look at it, 11.25%, 11.5% seems like the right range to target. And I think if you look at our capital stack right now and certainly our CET1 ratio compared to some of our peer institutions, we're more heavily weighted towards capital at this point in time than others. If you look at our regulatory requirement, just a straight regulatory requirement would get you to a 10% figure.

And so if you think in terms of, well, you need some buffer over the regulatory minimum, the question is, well, how much is that? I think most institutions have talked about a buffer of somewhere between 100 basis points and 150 basis points. That would get you into that 11% to 11.5% range. We're currently operating with a buffer over our regulatory minimum of 280 basis points. And again, I'll let James finish it, but I don't think that we're benefiting right now from carrying that excess capital.

JAMES VON MOLTKE: I don't have that much to add. I would just say, we're mindful obviously of spreads that we issue at and that feeding into our total cost of funding. But what I'd say is the capital and capital structure is only one of a number of factors that go into both rating agencies' assessment, as well as investors' assessment of our credit, and, therefore, feeding into spreads. We have wanted to be very clear with our Fixed Income Investors about the intention to return capital, and, therefore, over time, bring down the ratio. But as I say, we think of it as only one of a number of influences on spreads.

ROBERT SMALLEY: Thanks, and just one quick one. It's a James question. You've done both senior and subordinated issuance in a 30-year tenor. I know a lot of other banks kind of reserve the 30-year point on the curve for sub issuance given the capital treatment. So when we look at senior issuance for 30 years, is that a rate and spread play? Is that a – are you funding particular assets there? And I noticed you had a TLAC WAM line in the deck. Is that something that is an important number for you, or is that just fallout from the issuance?

JAMES VON MOLTKE: There's a lot in that. So I'd say, first of all, we don't think of the 30-year maturity or tenor as being reserved for sub debt really. It's one of a number of tenors in which we have an issued sub debt. But as you saw this week, we also see it as, depending on the market environment, a good place to issue in senior as well. The last part of your question, the TLAC WAM, which we've started to disclose this quarter for the first time, we do think that's important. And in some ways, given the way the TLAC rule works, it is as important, the weighted average maturity, as the more global metric that we've provided to you in the past. I hope that answers your question, Robert.

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ROBERT SMALLEY: Yes. Yes, it does. Just one comment. John, I know there was an article about your overly conservative estimates inter-quarter. We in fixed income, we're good with that. So, thanks. And thanks for answering my questions.

JOHN GERSPACH: No problem, Robert.

JAMES VON MOLTKE: Thanks, Robert.

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

ARNOLD KAKUDA: Thanks a lot for the call, guys. I appreciate it. So congrats on the TLAC compliance, you have a surplus. It seems like your surplus that you have, it's on long-term debt. So how are you thinking about that going forward in terms of buffer level? Are you targeting a certain amount, a couple, let's say $10 billion or so, of buffer or are you thinking in terms of a percentage above, let's say RWA or leverage?

JOHN GERSPACH: Sure. Thanks, Arnold, and good morning. As we note, the long-term debt measure was the most binding of the four TLAC constraints. And so that's been the one that we focused on in terms of our disclosure and our discussions. We've talked about the buffer a little bit in the past and I wouldn't say our thinking has changed significantly that we think that that buffer is really a time-based measure around market access. And we talked on the last call, based on the weighted average maturity point that we were just talking about, that in essence drives the amount of additional debt you would need to carry to sustain the company over a period of not having market access, while remaining above the minimum level.
So that's been our thinking. That translates into a buffer, we think in the $6 billion to $7 billion range. But that's still preliminary as we think about it. There's still analytical work to do and we'll also observe how market practice evolves over time, but that's been the range of our thinking to date.

ARNOLD KAKUDA: Okay. Great. And then – so looking at your funding plan change, is it just a coincidence that there's an increase in the debt funding plan by $5 billion just as you submitted your CCAR capital return ask?

JAMES VON MOLTKE: No. As I said in the prepared remarks, our focus really has been on resolution planning and they are really the adequacy and positioning of funding across the company and in our material legal entities in that process. So we're in the process of finalizing our analysis ahead of the submission on July 1. And it's in that connection that we decided to increase our issuance plans and guidance for the year.

ARNOLD KAKUDA: Okay. Got it. And then – so the Dodd-Frank replacement plan, that I believe the House Financial Services Committee is visiting, offers a bank a choice. Basically, you stay under the existing financial regulatory regime or be exempted by meeting a 10% leverage ratio. So assuming the off ramp is a 10% Supplementary Leverage Ratio for the biggest U.S. banks, that would imply that Citi would need over say $60 billion of Tier I capital to be exempted from the higher U.S. regulation. So given the large amount of the extra capital required for the off ramp, is it accurate to say that this Dodd-Frank replacement plan is not really helpful for big banks like yourself?

JOHN GERSPACH: This is John. I think it's too early to comment on any of the impacts or the proposed impacts of this topic because I wouldn't even say that its proposed legislation at this point in time. It's a series of discussions. Let's see how those discussions evolve and whether or not there's any "stick" to those discussions, and then we'll be happy to talk about it.

ARNOLD KAKUDA: Okay, got it. And lastly, so we've had a few Fed rate hikes already. You're signaling the Fed is getting more comfortable with the economy. And I believe the Fed can raise capital requirements for big banks by implementing a countercyclical buffer of up to 250 basis points. My question is, do you think the Fed should implement a countercyclical buffer when the economy is improving?

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JOHN GERSPACH: I really don't think that it's going to do any of us any good to muse on topics like that at this point in time.

ARNOLD KAKUDA: Okay, got it. Thank you.

JOHN GERSPACH: Thanks, Arnold.

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

MICHAEL ROGERS: Yes, good morning, gentlemen. We are certainly at an extended part of the cycle where we're getting a little long in the tooth, I guess, with the economic cycle. And I'd like your updated thoughts, if I might, on where you may be observing excesses in the extension of credit or other areas which are just getting you increasingly worried as we approach this point in the cycle.

JOHN GERSPACH: This is John. We are a little long in the cycle, then again, this is a rather unusual cycle. I don't think that we've ever had a growth cycle that has so underwhelmed people. So when you're looking at a growth cycle that GDP has averaged less than 2% during the course of the cycle, I don't think any of us have seen a cycle like that before. So we may be getting long in the tooth, but there's no indication that anything is overheating at this point in time.

You know, we've just gotten to the point where the Fed is comfortable enough to actually begin to raise rates. So who would have ever thought that you'd get into year, I don't know, year eight of a growth cycle before the Fed actually got comfortable that there was sufficient growth that they actually could start to begin to raise rates? So I don't see that.

The only place where I think right now you see evidence of anything that would suggest perhaps overheating, oddly enough, is with student lending. And that is a market that is being driven by the government not by banks or private interests at all. So let's see how it goes. We're very comfortable, as I said, with another question as far as where we are with our lending program, our target markets, the clients that we deal with both on a corporate and a consumer basis. We monitor it vigilantly, and right now we just don't see any signs of overheating anywhere in that spectrum.

MICHAEL ROGERS: Appreciate that answer, John. I guess if I could follow up and ask another unrelated question. One of your larger competitors, I guess within the last couple of months, was able to receive a positive outlook out of one of the rating agencies. Do you believe that you are progressing in a similar way which would merit similar treatment from the rating agencies at some point in the near term?

JAMES VON MOLTKE: Michael, its James. We will not comment on the status of discussions with the rating agencies, but what we do day to day is work with them closely to help them understand our business model, how it's evolving, where we're making investments, and obviously how the firm is performing.

MICHAEL ROGERS: Appreciate that, James. Could I ask about Mexico? How are you feeling about the credit prospects in Mexico right now given the target that it appeared to have been for the administration for a time, better, worse, or about the same?

JOHN GERSPACH: We feel really good about the credit performance that we've seen in our business in Mexico. We went into the year talking about the fact in our consumer business that we expected Mexico to be at about a 450 basis point NCL rate for the full year 2017. I think the first quarter came in at about 440 basis points, and we feel like we're right on track for that estimate. Delinquencies are in line with expectations, both 30 days and 90 day-plus. So again, we're very comfortable with the credit position that we currently have in Mexico.

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MICHAEL ROGERS: Thanks very much.

JAMES VON MOLTKE: Thanks, Michael.

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

MARK KEHOE: Hi, good morning. Just one question. One of your Midtown peers has mounted a strong defense as to why its conglomerated banking model creates significant revenue synergies. And I'm wondering whether you have studied what benefits you derive from being a conglomerate? Or perhaps as a corollary, if we were to see a 21st century Glass-Steagall, how would that cause your business model to change and could we see increased costs and your ability to lend to be impacted? Thank you.

JOHN GERSPACH: So it's John. We also have looked at the benefits of our universal banking model and we do think that there are compelling reasons why the model is the way it is and how it benefits both shareholders as well as the overall economy. So, yes, we do think that it makes sense to run the bank together. As far as the topic of a 21st century Glass-Steagall or I've heard it referred to as Glass-Steagall 2.0, there's a lot of different terminology that get thrown around, but every time that subject comes up, the question I ask is, what exactly does that mean? What is a 21st century Glass-Steagall? And if we're going to talk about a 21st century Glass-Steagall, then how does that fit into the Administration's overall approach where they've said that they want to focus on reducing regulations and they really want to try to catalyze growth in the economy. So I don't know how a – I don't know how to define a 21st century Glass-Steagall and I really don't know how a 21st century Glass-Steagall then would fit into some of the Administration's other clearly-stated goals.

MARK KEHOE: Thank you.

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

DAVID JIANG: Hi, John. Question on the Card business. Within Branded Cards and Retail Services, I was wondering if you've changed any of your parameters for risk appetite in terms of the, kind of the FICO spectrum given how well-behaved that portfolio has performed.

JOHN GERSPACH: Yeah – no. The answer to that is, no, not at this time.

DAVID JIANG: Okay. And within Retail Services, are you seeing any signs of stress with the retail community with regards to renewals or relationships that you've had to negotiate?

JOHN GERSPACH: Again, the answer would be, no.

DAVID JIANG: Okay. So the uptick in that book is just seasonal then, in the credit metric?

JOHN GERSPACH: In the credit metrics, yes. And I think we referred to that a bit on the call that we did last week. But, again, that's another business where our guidance for the full year going into the year was that Retail Services should have an NCL rate of something around 435 basis points. And despite where the first quarter came in, we do believe that that business for the full year is right on track to produce a 435 basis point NCL rate.

DAVID JIANG: Okay. Great. Thank you.

JOHN GERSPACH: No problem. Thanks, David.

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

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

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

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