TRANSCRIPT

Deutsche Bank 2018 Global Financial Services Conference
Tuesday, May 29th, 2018

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SPEAKER
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PRESENTATION

MATT O'CONNOR: All right. We're ready to get started here. Next up is Citigroup and joining us today is CEO of the Global Consumer Bank, Stephen Bird. Given the importance of the Consumer Bank at Citi and a number of strategic efforts in both credit card and Mexico, it does seem like a very timely time to have you.

Stephen has got some opening remarks, then we'll get into a fireside chat and questions from the audience. So, Stephen, welcome, and let me turn it over to you.

STEPHEN BIRD: Thank you, Matt. So, good morning. What I thought I would do is give a little bit of an overview of our business and our strategy and a bit of an update since our Investor Day in terms of the momentum that we're seeing.

Last year, our Global Consumer business generated $33 billion in revenues and net income of $4.6 billion. This platform is the world's number one card issuer. So, globally, we're the number one by loans, by – I feel 10% difference between us and number two, and we have streamlined this business to operate now in 19 countries. So, if you think of Citi's Global Consumer business, think about the U.S., which is 60% of the business, so, if you'd like, having access to and growing in the world's most advanced, developed economy, and 40% in international, and the 40% international is Mexico and Asia.

And if you think about Mexico with its tremendous demographics, its relatively low financial penetration and our leading brand position and leading positions in deposits and loans, you can see why we feel so good about the access to that emerging market that's got such good prospect.

Our Asia business, we are the leading wealth manager in Asia and we're also a Pan-Asia credit card business.

Our strategy in Citi is – we are a relationship bank. So if you think about the five needs that you have and we have, which is borrow, pay, save, invest, protect, we have built our model to allow us to access those needs through the cycle of your financial life. And our footprint, which is relatively light physical and high digital, is using data and technology to be able to seamlessly link those five things.

We operate a segment-driven business model across the globe. So if you think about Banking, Priority and Gold, that common segment-driven business model and our approach to operating the model with the right cost to serve characteristics by segment is common across the globe.

The Asia business – a particular feature of the Citi model when you think of U.S., Mexico and Asia, is our ability to develop and test something in one region and deploy it globally. A great example of that is the way that we're using agile development and using an open API model that allows us to connect into the relevant ecosystems for our clients. In Asia, you can think of those as WeChat, you can think of those as Alibaba. And in the U.S., you can think about the way that you can pay with points, a global ThankYou program, whether it be on Facebook or Amazon.

At Investor Day, we said that you could expect us to grow the top line at a rate of about 5% and generate continued positive operating leverage. Building on the track record that I showed that from 2014 to 2017, ex our large investment in Costco, we had virtually zero, in fact 0.3% expense growth. So you can expect to see that continued strong expense discipline and strong credit discipline.

So what did we see in the first quarter? You saw that the top line growth, first quarter of 2018, was actually 6%. If you net out any one-time benefits there, it was about 4%. And if you look across the portfolio, you can see that some businesses are a bit ahead, some are slightly behind the pace. The businesses that are ahead – Asia growing at 6% versus what we promised of around 4% through the pace to 2020; our Retail Services business, we said about 1%, in fact growing about double that driven by loan growth; our Retail Banking business in the U.S. actually on the pace that we said that we would be. And then some businesses a little bit behind – our Branded Cards business in the U.S., where we have seen a higher proportion of promotional and transactor balances has had slightly lower top line growth, but we expect that business to have underlying growth of like 2% in 2018.

So I think when you look at the track record, when you look at the projected potential of this business to get to what we said higher RoTCE of about – Investor Day, pre tax reform we said 19% RoTCE, you can see that we are sequentially growing the top line, maintaining the expense discipline and generating those improved returns, which I think all goes well for both the shape and strategy of the business. So I think we feel confident about the pattern that we showed you in detail last summer, and I think that as you look at Q1, you can see that it has confirmed that.

So with that, I think we'll turn over to Matt for Q&A.

QUESTION AND ANSWER

MATT O'CONNOR: Great. Thank you for that and for the update. Maybe start, just big picture, talking about some of the synergies across the businesses in your segment. We do often get asked the question what's the benefit of having retail partners and branded, the benefit of card in the U.S. and abroad. What are some of the synergies, whether it's within the same region, different products; or same product, but different region?

STEPHEN BIRD: So, first of all, I think that you can see that we share a common brand, so a strong brand in financial services. We are – if you look at the Fortune assessment of brand strength, Citi is the top 10 – I think the last time, we were number nine brand globally in financial services. And if you look in Mexico, number one brand. In the U.S., we have a strong brand. In Asia, we have a very aspirational brand, a high end aspirational brand which has played well into our wealth model.

Also, if you look at the fact that when you're running a $400 billion retail banking and commercial banking book, you have a source of low cost and stable funding. Of course, that's critical when you're running the world's largest credit card issuer. So branding, source of funding, but what we've added in the last couple of years – and it's really playing out, I think, very well for us and it's evident in the numbers in the financial disclosures that we give each quarter – is that the way we are using digital is really allowing us to cut through.

So if you think about this, in 2017, we released 1,600 pieces of customer-usable functionality, digital functionality and with great reuse of those capabilities across the three regions. Here in the U.S., I mean, if you look at the Citi Mobile App, which was the first combined checking, savings, brokerage app in the U.S. with many unique features; if you think of being able to stop/start your credit card, stop/start your debit card; if you think of being able to do person-to-person payment; being able to see your entire financial life, borrow, pay, save, invest, protect, through facial recognition without entering a password; seeing your FICO score, the trend of your FICO score and the elements that contribute to it; those things were co-created with customers.

And the way that we are developing those capabilities, which is turning Citi into a 21st century competitor, is by co-creating with our customers, co-creating with our customers in Asia. I was in Mexico three weeks ago, and the most encouraging thing is the way in which our Citibanamex business is deploying that exact same model. So in a market that is less digitized than the U.S. or Asia, but is rapidly figuring out how to put all services on smart devices, figure out how to acquire digitally, how to engage digitally, how to service digitally, that's really – we're trying to figure out how we put the business in a position where it can thrive in the 21st century.

So, if you think about branding, think about funding, think about the way that we deploy class-leading value propositions in a common way using an API architecture, that's the glue that knits together the Global Consumer Bank.

MATT O'CONNOR: And switching gears to the efficiency ratio, you gave us an update on the revenue growth that you're seeing in some of your different businesses. And there are some puts and takes on a reported basis, a little bit better than your target and you have a little bit below but call it mostly in line. As you think – as part of this three-year effort that you laid out at Investor Day on the efficiency side, how much of it is coming from the revenue side? And right now, I think most of it is, but if maybe the revenue tempers a bit, are there opportunities on the cost side as well?

STEPHEN BIRD: Great question, Matt. At Investor Day, – let's turn to the expense discipline, expense productivity, end-to-end digitization. We said that there would be, of Citi's $2.5 billion full year saves, we said that $1.5 billion would come from the Consumer business. So, this business, although it has a track record of delivering good expense performance, really has to continue to deliver to digitize the model. I actually view the $1.5 billion – we are on track for the 2020 commitments that we made. I would say that the most important feature of that though is actually the digitization of the model.

Yes, we accrue and throw off the $1.5 billion of expense saves. But as an investor and as a shareholder, what I'm really interested in is, are we making decisions that are going to help that business thrive and grow in the 21st century at the same time as it throws off expense saves because customers are being acquired digitally. More than half of our customers in the U.S. are being acquired digitally. We've got a model whereby we expect by 2020, that we would be predominantly acquiring digitally and servicing digitally, and that is critical.

So, of the total contribution to the improved return in tangible common equity, it's a mix of about half coming from revenue growth and 30%, 40% coming from expense and productivity, plus a little bit from interest rates. But that's the pattern, we really need each of those things.

Now, if the revenue growth wasn't there, we have contingency plans. Our job is to manage and produce a result irrespective of the environment that's there. We constantly re-pace and adjust investments based on what we're seeing in the revenue environment. And that's why we've been able to manage expenses carefully, and we'll continue to do that whilst we reposition the model.

MATT O'CONNOR: And you mentioned digital being very important to servicing customers opening new accounts. I think you did recently launch a National Digital Bank. Maybe you could talk about that effort, how it kind of meshes with the, call it, regional footprint that you have within the U.S.? And then, do you need a little more infrastructure to support that digital, maybe not opening branches everywhere, but a little bit more support?

STEPHEN BIRD: I mean, that really gets to the sort of core of competitive construct in terms of how we are operating the Citi model, which is a lighter branch model with a sort of high digital and data model. We have in the U.S. 700 branches. We have competitors with 4,000, 5,000 branches. We operate our $33 billion business with 2,400 branches in total globally. So we project our brand to punch above its weight. We project our brand to punch above the physical presence by making digital pervasive.

Now, I think good strategies are our strength finders, and our cards business is a highly, highly digital business. I mean, the cards business is a digital payments business. The credit cards business was conceived really as a digital business. We are, in the U.S., nationwide with our cards business. We are, in the U.S., a nationwide recognized brand, but our physical footprint in the retail bank is in six cities.

So if you think of those six cities – New York, Miami, Chicago, D.C., San Francisco, LA – there's a lot of money in those cities. It's a $6 trillion economy in those cities alone. But what we're trying to solve for is when you can take your bank with you anywhere and you have a recognized brand or a magnet that can attract you to that brand, we recognized there were a couple of things we had to do. One, cash is still important. So cash access, ATM access is still important because cash, as a category, believe it or not, is still growing in absolute terms, albeit as a proportion it's coming down, but cash is still important.

So that's why, Matt, we did the deal to effectively double our ATM network globally, which we did. We're now the largest fee-free ATM network in the United States. So what we're trying to do is leverage the brand, leverage the cash access, leverage the warm prospect base of the card customer who's already a card-carrying member of the Citi family, overlay that with the bank in your pocket.

Now, the National Digital Bank, let me turn to that. What this app does today – I use it all the time, if you look up the App Store, do it now or later, you'll see that that's a 4.8-rated app. You'll see that in our disclosures we've got the fastest-growing mobile base amongst all of our peers in North America, but that's for existing customers. Now, Citi has, globally, 110 million existing customers. But for new prospects, the National Digital Bank is about being able to join that Citi ecosystem from your phone. That's really what it's about.

And so, we are – it's currently – it's a multi-generational launch. We already have a – it's in friendly user test at the moment. We're designing a series of marketing offers and tests. And you will start to see those in the digital ether as we come through the third quarter.

It's very, very important. We know that we're going to have to test our way into it. Matt, we've hired a lot of people, people from Amazon, people from PayPal, people who have a track record of running these digital models because that's what the 21st century looks like.

So, you see us – when I showed the investments at Investor Day, that pattern of investments was heavy in digital, heavy in technology, because that's the thing that's going to assure our model going forward.

MATT O'CONNOR: And to attract customers to the national digital platform, I guess, what's kind of the incentive? Is it going to be rate? Is it going to be maybe like a sign-up promotion? You did talk about the fee-free ATM, which is obviously one of the value propositions. Any thoughts on promotional pricing to get some of the deposits to start?

STEPHEN BIRD: Yes, so let me explain the way that we are thinking about that because I don't like leading with rate, and I don't think that competing money over money is going to get us anywhere in the long run. I think you tend to attract hot money and then you tend to lose it.

Think of it this way. We have 110 million customers today in Citi. A whole cohort of those love American Airlines miles. So they are self-selected members of the American Airlines Club and they love miles. Until now, nobody has said to them, why don't you also earn those same miles on your checking and savings account? You're going to be able to do that.

We also have a lot – we have the largest and number one cash back card in the category with Double Cash, so we have a cohort of customers who said, we like Double Cash; 1% when I spend, 1% when I repay. We will make an offer to those customers.

And you think through our ecosystem, Citi has the number one airline partner in American Airlines. We have the number one warehouse wholesaler in Costco. We have the number one home improvement retailer in Home Depot. We have the number one cash back card in Double Cash.

So what the data – what the teams are working on is using the data to say, we think you should obsess over what customers do. The behavior tells you a lot. So when customers' behavior tells you they prefer this type of incentive, and then you offer a new way to double up and get that incentive, and if you do it in a frictionless way where you can access it on your device, we think that that's a good way to start acquiring customers across that spectrum of borrow, pay, save, invest, protect.

So this is real – this is digital ecosystem thinking. This is about leveraging the data that is in our system in a way that can create growth in a natural way and not get caught up in rate wars.

MATT O'CONNOR: Maybe to segue into credit card where you're doing both the value proposition of some of the things that you just mentioned on the digital bank, but then there is much more aggressive sign-on or promotional pricing, not just Citigroup, but the industry overall with rewards. But talk about that and, I guess, specifically with Costco, where the balances are much larger than, I think, you had assumed, but at the same time, from the outside, it's hard to see the revenue lifts that come from that deal because of some of the promotional pricing. So you could talk maybe Costco, but then more broadly speaking, the investments that you've made just on the balance transfers and as you start monetizing that.

STEPHEN BIRD: Yeah, let me explain the thinking there. So the credit card business, what it's really all about is building a balanced and sustainable annuity of growth, and you get different things from different parts of the credit card business. With co-brand partners, and I mentioned some of those co-brand partners, so think of American or Costco or Home Depot, and Costco has been a huge success. Costco has grown much faster than it was – than we had modeled, and it's actually growing faster than American Express ever achieved. What you get from the co-brand business and these partners is you get scale effects. So you get large portfolios, you get large groups of customers. So you can build the pyramid and get scale, but of course you're sharing the economics with a partner.

You then balance the scale effect to get higher returns by having your own proprietary business with only your branded product. So you think about the Prestige product, you think about that whole array of good, better, best in this wealth and premium segments, you think about the Simplicity, the value segments, you think about the Cash Back segment, but those proprietary Citi-branded products have got a higher return because you're not sharing the economics with somebody else.

So what you're trying to do is build, and I think we've been successful in doing this, build a balanced book of business that allows you to get the scale that you would expect from being the number one issuer in the world, which is a mix of partners and proprietary.

Now, within the proprietary business, because our co-brand business was growing faster than modeled, we knew that we wanted to turn up the pace of acquisition in our Citi-branded business and we used promotional offers as one way of doing that. So we had a variety, an array of different offers of 0-for-12, 0-for-18 to bring balances across.

And you're right that we saw good growth in promotional balances, but the key factor then is that for those promotional balances to stay with you at the end of the promotional period so that they become interest-bearing balances. So you say, well, okay, I get the strategy, it's a balance business, you're looking for scale and you're looking for returns, so how are you doing? Well, you want to see high engagement across the whole platform, so the first thing you look to there is sales.

The sales growth you saw in the quarter, 8% sales growth, strong across the whole book, so good engagement. Average loan growth, 5%, healthy, but tell me about interest-bearing balance growth because that tells me whether your promotional balances are also converting. Interest-bearing balance growth was 6% in Q1. So I'm describing our strategy, the metrics that you look at to assess whether it's performing to model, and I can tell you it is.

Now, I mentioned in my opening comments that this large business will produce about 2% underlying top line growth in 2018, and it will. Of course, that's being masked a bit because we did some partner deals to lock in our partners for the longer term. And that has a dampening effect – two factors of a dampening effect: one, those partnership deals; and, secondly, the higher rate environment because whilst those promo balances are getting to the point of flipping, I'm still funding those balances in a higher rate environment. So those are the two things that are dampening effects that dampened underlying 2% growth.

But I can tell you, we manage the underlying attributes for the portfolios and the models. It's a forensic business, and the model is performing. And through time you will see that the investments that we made in the cards business are going to bear fruit. And, secondly, I mentioned those iconic partners. We now have locked in all of our partners in both our Branded Cards business and in our Retail Services business through 2022 and beyond. So a sustainable annuity of growth demands that you lock those partners in, and that's why we did it and that was what we did.

MATT O'CONNOR: I mean, it seems like for all those factors you should get an acceleration in maybe both the core and reported growth as we think about 2019 and 2020. I can't remember right now what kind of three-year growth targets you had out there, but maybe you could talk about the revenue growth for 2019 and 2020, given you're not going to have added renewal costs and then more of the promotional balances flipping to full pay, I would imagine.

STEPHEN BIRD: Well, Matt, we're standing by – we've said the – overall, we're solving for Global Consumer to grow 4%, 5% CAGR, top line CAGR. So you think $33 billion business, we're going to be adding a $1.6 billion business each year. We're not moving that number up, so we're going to grow 4%, 5% top line, that's what we're trying to solve for.

We're trying to do that in a way that has got a range of drivers where everybody has to contribute. The U.S. has got to contribute and international has got to contribute. The pattern that you saw in Q1 was the U.S. underlying was growing at 4%, international was growing at 8%, blending out to achieve about a 4% top line growth.

So that's – we're standing by the numbers. The Branded Cards business itself will go up by 2% at top line once you get past the partner effects and these promo balances comes out. We'll see the topline growth of about 2% of the Branded Cards business as you get past those effects into 2019 and 2020. And it still is – I was just chatting with someone before we came onto the stage. The credit card business is still terrific and an attractive asset class. It's a large, slow-moving annuity. It rewards people that make long-term investments and get those broad brushes in the right place, but it takes some patience. I wouldn't – it's somewhat frustrating when you're trying to build a 21st century competitor and you're being measured every 12 weeks. So I wouldn't – if you look at Q1 and you see, well, in Q1, you have 37% growth in your net income, well, we're not going to do that every quarter and you didn't get too frothy and excited about that. But likewise, don't get too disappointed as you move to other quarters. It's going to blend out. 2018 is going to be on the pace for what we promised.

MATT O'CONNOR: And one more question on card in the retail partners. You recently re-upped with Sears. I think that had been an area of concern among some given that it's a big portion of your partners business and the sales pressure at Sears that's been going on. Maybe just a couple of bullets on the logic of re-upping and what it means to Citi going forward.

STEPHEN BIRD: Yeah. That was an important thing to do. A couple of facts that I think are important in Sears. First of all, in our Retail Services business, we are an incredibly valuable partner for our retail partners. If you think of a Home Depot, you think of a Best Buy, when you think of a Macy's, you think of the recently announced L.L.Bean partnership, and if you think about Sears, Eddie Lampert and Sears, we are a very important partner for those companies, and we help them drive growth, and we help them navigate through good times and bad.

The Sears partnership is a 15-year-old partnership. And we re-upped it because one, to stand by the partner, but, very importantly, to secure our ownership of the MasterCard general purpose portfolio that when you consider that 70% of the spending in that portfolio takes place outside Sears. So it's a general purpose MasterCard. And those are – it's a very valuable portfolio of customers, and the bulk of the spending is actually off Sears.

So we did two things. We paid Sears $425 million to secure our ownership of that portfolio in any future scenario. And we will amortize the cost of that $425 million over the longer period, which is the balance of the new contract. So it was the right thing to do. I reviewed the economics very, very carefully, and we're helping Sears to manage the transformation and we think they're doing the right things. We think they are focused on creating more of a digital business. It's hard, but our position in that and the fact that we have this large portfolio that also has got a large general purpose portion of spend was our motivation.

MATT O'CONNOR: Any questions from the audience? So we still got a lot of time. More on the U.S., but Mexico is obviously – been very important to you. At Investor Day, you talked a little bit about some of the investments that you're making there to modernize it. I think the digital comment is kind of tied to that, but where are you kind of in that process?

And then, for a lot of us, it's hard to tell what's going on among – with the Mexican consumer, and whether it's good or bad given some of the headlines out there. So how do you think about that business overall and the operating environment?

STEPHEN BIRD: So, overall, Mexico is a compelling opportunity. Put the politics aside, put the headline news about walls and NAFTA and elections to one side, Mexico is still going to be on the border of the U.S. Mexico is still going to have amazing demographics. Mexico is still going to have an underpenetrated financial services market, and Mexico is going to progressively have more and more people joining the middle class.

Now, if you think about the election and you think about AMLO or no AMLO, and you take the view of AMLO, when he was mayor of Mexico City, he was a pragmatist and we had a very good relationship with him. If you think of NAFTA or no NAFTA, obviously, we'd rather have NAFTA, but Mexico has got its own currency, so it's got a shock absorber in terms of if you have a devaluation, it's going to be more competitive at doing a lot of things that it does today. So we feel Mexican customers are still going to be borrow, paying, saving, investing, and protecting in pesos no matter what happens. So we feel that Mexico is a good opportunity.

Citibanamex has got a great position. I mean, it's got number one brand in Mexico. And every day in Mexico, 25% of anything basically runs through Citibanamex. That relative strength is valuable. We had underinvested in the platform, particularly during the global financial crisis because we had other things to focus on, but we have focused very much on doing the right things in Citibanamex. I mentioned that was just during the year, even since Investor Day, and I mentioned about investments, we don't cast an investment plan and then check in four years later and see what it looks like. We calibrate all the way through it. Even since Investor Day, we've put more investment into technology, more investment into digitization, a bit more into creating an agile workforce and software development cycle there, a little bit less into branches than we had originally been forecasting, and that's smart. That's what you're supposed to do.

When – I looked at a lot of data that said that the rate of smartphone adoption was faster than originally I had seen. And when I looked at that data cut by my customers, the vast majority are already something well in excess of 80%. In Mexico, we're already on smartphones. So, I could see that what was working in the U.S. and what is working in Asia can get traction in Mexico. So, that's why we made that tweak since Investor Day, and we'll continue to dynamically adjust that type of thing.

MATT O'CONNOR: We're out of time. But, Stephen, thank you so much.

STEPHEN BIRD: Thank you, Matt. Appreciate it. Thank you.