TRANSCRIPT

Citi Second Quarter 2019 Earnings Review

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Host
Elizabeth Lynn, Interim Head of Investor Relations

Speakers
Michael Corbat, Citi Chief Executive Officer
Mark Mason, Citi Chief Financial Officer

PRESENTATION

OPERATOR: Hello and welcome to Citi's Second Quarter 2019 Earnings Review. Today we are joined by Citi's Chief Executive Officer, Mike Corbat; Chief Financial Officer, Mark Mason. Today's call will be hosted by Elizabeth Lynn, Interim Head of Citi 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 call is being recorded today. If you have any objections, please disconnect at this time.

Ms. Lynn, you may begin.

ELIZABETH LYNN: Thank you, operator. Good morning and thank you all for joining us. On our call today, our CEO Mike Corbat will speak first, then Mark Mason, our CFO, will take you through the earnings presentation, which is available for download on our website, citigroup.com. Afterwards, we will be happy to take 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 conditions may differ materially from these statements due to a variety of factors, including the precautionary statements referenced in our discussion today and those included in our SEC filings, including without limitation, the Risk Factors section of our 2018 Form 10-K.

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

MIKE CORBAT: Thank you, Liz, and good morning everyone. This morning we reported earnings of $4.8 billion for the second quarter of 2019. Our earnings per share of $1.95 were 20% higher than one year ago. We increased our return on assets year-over-year to 97 basis points and generated a return on tangible common equity of 11.9%, over 100 basis points better than last year. We delivered positive operating leverage for the 11th straight quarter and improved our efficiency, while again growing loans and deposits. These results stemmed from strong execution of our strategy across our lines of business and show the benefits of our global franchise and product mix.

Global Consumer Banking saw 4% revenue growth overall in constant dollars with a contribution from every region. In North America, that was led by continued strong performance in Branded Cards and again we saw encouraging momentum in deposit growth which accelerated from the first quarter, and internationally net income was up 25%. In Mexico, performance was driven by good underlying revenue growth, expense management and credit discipline. In Asia, higher deposit revenues and a recovery in investment revenues drove growth in the region.

In our Institutional Clients Group, we delivered continued growth overall in our steadier transaction and accrual type businesses showing the strength of our global client network, while we saw pressure in our market-sensitive businesses reflecting the broader industry, even in products like Investment Banking where we continued to gain share.

During the quarter, we received a non-objection from the Federal Reserve for our 2019 CCAR submission. That means we will meet the goal set at Investor Day to return at least $60 billion in capital over three CCAR cycles. Our $21.5 billion capital return will increase the three-year total to $62.3 billion and includes raising our dividend to $0.51 and continuing to buy back shares of common stock at roughly the same level as last year's plans. These buybacks have reduced our common shares outstanding by over 10% in the last year alone and helped drive our tangible book value per share of 10% over that same time period.

Given the current environment and market conditions, we'll stay flexible with a focus on making steady progress towards our financial targets through client-led growth and resource discipline, including balance sheet, credit and expenses. As we look to the second half, we'll continue to take a close look at our capacity to make sure that we're right-sized for the operating environment. However, we won't change our commitment to safety and soundness and to making investments necessary to strengthen our infrastructure and control environment.

Client engagement remains strong and we continue to enhance our capabilities to serve our clients the way they want to be served across our network. That said, there remains uncertainty with respect to the economic market and rate environment, but I think we've shown that our franchise can manage through these by focusing on the things that we can control.

I'll now turn it over to Mark and then we'll be happy to take your questions. Mark?

MARK MASON: Thank you, Mike, and good morning everyone. Starting on slide 3, net income of $4.8 billion in the second quarter grew 7% from last year, including a roughly $350 million pre-tax gain on our investment in Tradeweb, which benefited EPS by $0.12 per share. Excluding the gain, EPS of $1.83 grew by 12%, mostly driven by a decline in our average diluted shares outstanding as well as a lower tax rate.

Revenues of $18.8 billion grew 2% from the prior year, reflecting the Tradeweb gain as well as solid results in consumer and overall growth in our accrual businesses in ICG. However, this growth was partially offset by lower market-sensitive revenues in ICG as well as mark-to-market losses on loan hedges in our Corporate Lending portfolio.

Expenses declined 2% year-over-year as volume growth, along with continued investments in the franchise, were more than offset by efficiency savings and the wind-down of legacy assets, resulting in our 11th consecutive quarter of positive operating leverage. And cost of credit increased driven by volume growth and seasoning as well as a normalization in credit trends in our corporate loan portfolio, while overall credit quality remained stable.

Our return on assets was 97 basis points for the quarter and we generated an RoTCE of 11.9%. Our effective tax rate for the quarter was 22%, slightly better than our outlook. We expect our tax rate to be between 22% and 23% for the back half of the year. In constant dollars, end-of-period loans grew 3% year-over-year to $689 billion, as 4% growth in our core businesses was partially offset by the wind-down of legacy assets, and deposits grew 5% with contribution from both our Consumer and Institutional franchises.

Looking at results for the first half of 2019, we saw continued momentum in consumer as well as the accrual businesses in ICG which helped to offset the headwinds of lower market-sensitive revenues, along with the continued wind-down of legacy assets. And while we did benefit from the Tradeweb gain, this was largely offset by the impact of mark-to-market losses on loan hedges in our Corporate Lending portfolio. We delivered positive operating leverage with a 3% decline in expenses. EPS grew by 15% and our RoTCE was 11.9% for the first half.

Turning now to each business, slide 4 shows the results for Global Consumer Banking in constant dollars. The Consumer business showed continued momentum in the second quarter. Revenues grew 4% with contribution from all regions, while expenses were up 1%, driving continued growth in operating margin and earnings. For the first half of the year, excluding the Hilton gain last year, we generated 4% Consumer revenue growth on flat expenses, resulting in 8% growth in operating margin and 13% growth in net income.

Slide 5 shows the results for North America Consumer in more detail. Second quarter revenues of $5.2 billion were up 3% from last year. During the quarter, we continued to enhance our digital capabilities and launched new products to lay the foundation for a more integrated, multi-product relationship model. Our deposit momentum continued to improve as net deposit inflows in the first half of 2019 more than doubled compared with last year. We are growing deposits with both new and existing retail bank customers in and out of our branch footprint and through both digital and traditional channels.

In digital, we further enhanced our account opening process and launched new products designed to deepen our client relationships, including relationship-based offers that leverage our proprietary Thank You and Double Cash rewards across both card and deposit products. We generated more than $1 billion in digital deposit sales in the second quarter, bringing our total for the first half to over $2 billion. Nearly two-thirds of these deposit sales were outside of our existing branch footprint and of this amount roughly half were with card customers who previously did not have a retail banking relationship with us. Results from our new digital lending product Flex Loan also continued to be positive following its launch in January, as loan originations more than tripled from the first to the second quarter, while maintaining a strong credit profile. And we will continue to roll out new features and products in the second half of the year. So, again, while many of these initiatives are still new, we feel good about our progress.

Turning now to the results of the individual businesses, Retail Banking revenues of $1.4 billion were roughly flat year-over-year. Excluding mortgage, Retail Banking revenues grew 1% as the benefit of stronger deposit volumes was partially offset by lower deposit spreads in commercial banking. Average deposit growth accelerated to 2% year-over-year. And looking at deposits and assets under management in aggregate, we grew customer balances by 4%. Mortgage revenues were largely stable again this quarter on a sequential basis, but declined year-over-year mostly reflecting higher funding cost.

Turning to Branded Cards, revenues of $2.2 billion grew 7% year-over-year. Client engagement remains strong with purchase sales up 8% and we continued to generate growth in interest-earning balances this quarter up about 10%. This growth in interest-earning balances drove a year-over-year improvement in our net interest revenue as a percentage of loans or NIR percent to 896 points this quarter.

Looking forward, we would expect to remain broadly around this level of spreads, as we look to maintain our current mix of interest-earning to non-interest-earning balances. Average loan growth improved to 2% this quarter, as we saw a smaller drag from promotional balances in the prior year and we expect loan growth to continue to improve as we go into the back half of the year.

Finally, retail services revenues of $1.6 billion grew 1%, driven by loan growth, partially offset by higher contractual partner payments. Total expenses for North America Consumer were up 2% year-over-year, as higher volume-related expenses and investments were largely offset by efficiency savings.

Turning to credit, net credit losses grew by 12% year-over-year, reflecting loan growth and seasoning in both cards portfolios. Card NCL rates were essentially flat quarter-over-quarter. And consistent with the pattern seen in prior years, we expect card NCL rates in the second half of the year to be lower than the first half of the year. Our performance year-to-date is in line with our full NCL rate outlook for both Branded Cards and Retail Services at 300 to 325 basis points and 500 to 525 basis points, respectively.

On slide 6, we show results for International Consumer Banking in constant dollars. Second quarter revenues of $3.3 billion grew 4%. In Latin America, total Consumer revenues grew 3% or 5% on an underlying basis, excluding the impact of the sale of our asset management business last year. Loan and deposit growth was muted in Mexico again this quarter, reflecting the current environment where we are seeing a deceleration in GDP growth and a slowdown in overall industry volumes. But importantly, we're managing expenses carefully and maintaining credit discipline in order to preserve profitability and returns as seen again this quarter in our strong EBT growth year-over-year.

Turning to Asia, Consumer revenues grew 5% year-over-year in the second quarter or 3% excluding a one-time gain, mostly driven by higher deposit revenues as well as a recovery in investment revenues. We continued to see strong growth in our underlying wealth management drivers in Asia with 10% growth in Citigold clients and 7% growth in net new money versus last year. In total, operating expenses were down 1% in the second quarter, as efficiency savings more than offset investment spending and volume-driven growth. And cost of credit was down 3%, reflecting a smaller LLR build relative to the prior year.

Slide 7 shows our Global Consumer credit trends in more detail. Credit continued to be favorable again this quarter with NCL and delinquency rates broadly stable across the regions.

Turning now to the Institutional Clients Group on slide 8, revenues of $9.7 billion were roughly flat in the second quarter and down 3% excluding the Tradeweb gain, as continued momentum in the accrual businesses was more than offset by lower market-sensitive revenues and the negative impact from mark-to-market losses on loan hedges as credit spreads further tightened in the quarter.

Total Banking revenues of $5.1 billion were down 1%. Treasury & Trade Solutions revenues of $2.4 billion were up 4% as reported and 7% in constant dollars with growth in deposits, transaction volumes and trade spreads reflecting continued strong client engagement. Investment Banking revenues of $1.3 billion declined 10% from last year, while outperforming the market wallet. The decline was primarily driven by a strong prior year performance in M&A, partially offset by continued strength in debt underwriting. Private Bank revenues of $866 million were up 2%, reflecting growth with both new and existing clients, which drove higher lending, deposits and AUM volumes, partially offset by spread compression. And Corporate Lending revenues of $538 million were down 9%, reflecting lower spreads and higher hedging cost.

Total Markets & Securities Services revenues of $4.7 billion were down 4% from last year, excluding the Tradeweb gain, as growth in Securities Services was more than offset by the decline in our Markets businesses where the environment has been challenging and investor client activity has remained muted. Excluding Tradeweb, Fixed Income revenues declined 4% year-over-year, reflecting the challenging trading environment, particularly in rates. Equity's revenues were down 9%, reflecting lower client activity in cash equities and prime brokerage, partially offset by strong corporate client activity in derivatives. And Securities Services revenues were up 3% on a reported basis and 7% in constant dollars, reflecting higher rates as well as higher client activity.

Total operating expenses of $5.4 billion declined 2% year-over-year, as efficiency savings more than offset investments and volume-driven growth. And cost of credit was $103 million this quarter, reflecting a normalization in credit trends in our corporate loan portfolio. Credit quality remained stable and total non-accrual loans declined both sequentially and on a year-over-year basis.

Looking at the first half of the year in ICG, our operating margin improved by 1% as solid contributions from our growing, higher returning network businesses, most notably TTS and Securities Services, were largely offset by the decline in our market-sensitive business. We're focused on continuing to build upon the strength that we're seeing in our network businesses by making it easier for our large multi-national clients to do more business around the world. We are investing in technology to further digitize and improve our on-boarding processes, enhance our client-facing platforms, and roll out new capabilities across the franchise as we support the growth in cross-border flows that we are seeing with our multi-national clients, and we have a strong pipeline of initiatives going forward.

Slide 9 shows results for Corporate / Other. Revenues of $532 million increased 1% from last year, as higher treasury revenues and gains were largely offset by the wind-down of legacy assets. Expenses were down 20%, mostly reflecting the wind-down; and the pre-tax income was $73 million this quarter, somewhat better than our prior outlook. Looking ahead, we would still expect a modest pre-tax quarterly loss in Corporate / Other for the remainder of 2019.

Slide 10 shows our net interest revenue and margin trends. In constant dollars, total net interest revenue of nearly $12 billion this quarter grew by roughly $450 million year-over-year, reflecting higher rates, loan growth, and a favorable loan mix, as well as higher trading-related NIR, along with the absence of the FDIC surcharge.

On a sequential basis, net interest revenue grew by roughly $230 million, largely reflecting higher trading-related NIR, along with one additional day in the quarter. However, net interest margin declined 5 basis points sequentially, as the benefit of higher revenues was more than offset by higher cash balances, reflecting strong deposit growth in the quarter. In the first half of 2019, our net interest revenue grew by 6% or roughly $1.3 billion year-over-year in constant dollars.

Looking ahead to the remainder of the year, as a reminder, when we set our NIR outlook for 2019 back in January, we were assuming one U.S. rate increase in mid-2019, but the expected benefit of the rate hike had been relatively small. As of last quarter, we had taken that rate hike out of our assumptions. And now, we recognize that we may begin to see rate cuts as early as later this month. But keep in mind that the estimated impact of each rate cut remains relatively small.

We continue to estimate that each 25-basis-point cut in U.S. rates impacts revenues by roughly $50 million on a quarterly basis, but, of course, this will depend on the competitive environment for deposits and other factors. So, the rate environment continues to evolve, but we are managing our rate sensitivity carefully, and we continue to expect to generate net interest revenue growth this year of about 4% in constant dollars, which equates to roughly $2 billion of growth, as we've discussed on previous earnings calls.

Turning to non-interest revenue, on a full-year basis, we continue to expect total non-interest revenue to come in roughly flat to the prior year. In the first half of 2019, non-interest revenue declined by close to $900 million, all of which you saw in the first quarter. This decline was mostly driven by the gain on the sale of the Hilton portfolio in the prior year, as well as a very strong prior-year comparison in equities in the first quarter, along with the drag from mark-to-market losses on loan hedges. In the second quarter, while we saw pressure in underlying markets revenues, it was entirely offset by the Tradeweb gain, so non-interest revenues were flat to last year.

Looking ahead to the second half of 2019, as a reminder, in Consumer, we will be comparing to the third quarter of 2018 when we had a $250 million gain on the sale of our asset management business in Mexico. However, we should be able to more than offset this headwind with organic growth across the rest of our accrual and consumer businesses, and we should see a favorable comparison in markets revenues in the fourth quarter even if investor client activity remains muted similar to what we've seen so far this year.

On slide 11, we show our key capital metrics. In the second quarter, our tangible book value per share increased 10% year-over-year to $67.64, driven by net income and the lower share count, and our CET1 capital ratio was stable sequentially at 11.9%, as net income was offset by $4.6 billion of total common share buybacks and dividends.

To conclude, while the revenue environment has proved challenging for some of our businesses, we made continued progress in the first half of 2019. From a revenue perspective, we're seeing solid momentum across the consumer franchise and continued growth in our accrual businesses in ICG. And while we've seen pressure in some of our market-sensitive businesses, results have generally reflected the broader industry. We continue to believe we can generate modest year-over-year revenue growth in 2019, driven by continued growth in net interest revenue and more stable trends in non-interest revenue versus 2018.

On the expense side, our productivity savings have exceeded our incremental investments by roughly $300 million so far this year, putting us on track to achieve the upper end of the $500 million to $600 million in incremental net savings we had expected for full-year 2019. Expenses were down year-over-year in the first half, and we believe that was prudent given the revenue headwinds we faced.

Looking ahead, we will maintain this expense discipline relative to the revenue environment while continuing to make essential investments in the franchise, including investments in infrastructure and controls, but we do expect expenses to be lower on a sequential basis from the first half to the second half of the year. And while the operating environment is uncertain, we will continue to look to all of our return levers with a continued focus on our full-year RoTCE target of 12% for 2019.

Before we go into Q&A, let me spend a few moments on our outlook for the third quarter specifically. In ICG, we expect continued year-over-year growth in our accrual businesses as we continue to serve our target clients across our global network. And Markets and Investment Banking revenues should reflect the overall market environment. On the Consumer side, in North America, solid revenue growth should continue, driven by U.S. Branded Cards. In Asia, we expect continued year-over-year revenue growth. And in Mexico, as I just mentioned, we'll be comparing to the third quarter last year, which included a gain on the sale of our asset management business. On an underlying basis, similar to the results seen so far this year, revenue growth will likely remain somewhat muted, although we expect continued strong growth in pre-tax earnings. For total Citigroup, expenses should decline sequentially and cost of credit should continue to grow modestly year-over-year, reflecting volume growth and continued normalization in ICG.

With that, Mike and I are happy to take any questions.

QUESTION AND ANSWER

OPERATOR: Your first question is from the line of John McDonald with Autonomous Research.

JOHN MCDONALD: Hi, good morning, Mark. Wanted to ask about the...

MARK MASON: Good morning, John.

JOHN MCDONALD: How are you doing? Wanted to ask about the RoTCE goal, so 12% goal for 2019 you're on the doorstep so far with the first half of 11.9%, as we think about levers to kind of keep that up in the second half and push over the goal line to get above 12% for the year, second half often has not as strong capital markets, obviously, hasn't been so good this – so far this year. So just – what are the things to think about puts and takes for the second half that could get you over that 12% for the year?

MARK MASON: Thank you. So 12% remains the target for 2019. As you heard Mike mention, you heard me mention, we're obviously in an uncertain environment. The good news is that we have seen continued momentum in the Consumer franchise, particularly in Branded Cards as we've talked about over the past couple of quarters with very strong performance this quarter as well on the heels of us converting those promotional balances to more average interest earning balances. And we'd expect that revenue growth to continue through the balance of the year. You heard me mention, the international franchises which are growing to have continued growth in the balance of the year and where there's muted growth to have – to offset that with expense management and therefore have EBT growth particularly in the case of Latin America. So those will be two positive drivers I would point to. I obviously point to our accrual businesses and transaction businesses on the ICG side, 7% growth in both Securities Services and TTS this quarter. We'd expect continued growth from those businesses.

And on the expense side, we talk to or I talk to really being on the high end of those productivity savings outweighing investments. And I would expect to certainly come in with that – on the $600 million side of the range that we've talked to there. The big area where the uncertainty in the environment – you can pick the factor, whether it's the direct – what's going on with rates and volatility around that or trade and tariff discussions, it plays out through the market sensitive businesses. It plays out through the trading that you see on both Fixed Income and Equities. It plays out through Investment Banking. It impacts corporate sentiment and those things as you would imagine are difficult to predict.

We obviously feel good about the client dialogue that we've had, but that's – those are the factors that are a bit harder to manage. And when we see that softness what you saw in the first half is that we pulled levers that we could pull responsibly. And you should expect that we would continue to do that in the back half without compromising two things. One, the investments required to continue to grow the strong parts of the franchise, and two, infrastructure and controls. And those two things we think are critical to the long-term sustainability of the franchise.

We'll continue to manage credit very carefully. You saw our tax rate come in a little bit lower. This quarter we'll continue to do work around what we can do to get the tax rate as low as we responsibly can get it and you've seen us actually do more on the capital side. So that combination of things, we think is helpful and obviously trying to get to that target of the 12%. There is some unpredictability to that particularly on the market side. And to the extent that that plays out more severely than forecasted, we would expect to be in and around the range of 12%.

JOHN MCDONALD: I guess also you did say you're expecting to have lower card losses in the second versus the first, that should help. Is there any front-loading of marketing or any other expense kind of front-loading or investment front-loading that happens?

MARK MASON: I mean, when you look at the profitability just in general on the Consumer business, it does tend to skew towards the back half of the year, because of things like marketing spend. We also – and I mentioned this on the last call, we also pulled forward some of the repositioning that we were looking to do as we reorganized around different parts of the franchise. And so savings that we were expecting kind of later in 2020 we can – we'll see some of that benefit play out through the back half of 2019. So there are those things around levers and actions that we took in the first half that not only helped the first half but have the potential to help us in the second half as well.

JOHN MCDONALD: Okay. And just last thing from me on that note. You're still looking ahead towards a goal of 13.5% for next year?

MARK MASON: 13.5% remains the target for next year. Just – obviously, again, I'll point back to the environment that we're in. We'll see how the environment plays out. We'll see how the market reacts to rate reductions. Obviously, the activity we saw last week in the way of our market reaction was pretty favorable to having more certainty around the direction of rates. But we'll see how those – some of those things play out and it does remain the target. And if we have to identify additional levers to try and pull to get there we will. But as we stand here today that 13.5% remains our target for 2020.

JOHN MCDONALD: Great. Thanks.

MARK MASON: Thank you.

OPERATOR: Your next question is from the line of Glenn Schorr with Evercore.

GLENN SCHORR: Hi. Thank you very much.

MARK MASON: Hi, Glen.

GLENN SCHORR: Hello. Question on the net interest income trends, so if you look at the 12% decline in non-interest bearing deposits and the 9% increase in interest-bearing deposits and then also the seven basis point rise in deposit costs sequentially and then the drop in loan yields, those trends combined while not surprising you would think from the outside would be a more negative tone on NII, but I think your guide was actually pretty good. Are there offsets that we don't see and/or are some of those trends like the tail-end of things that had been in motion and they actually get better over the next couple of quarters?

MARK MASON: So in terms of the net interest revenue, we're obviously at about $1.3 billion of net interest revenue with a strong Q1, about $450 million in Q2. And as we look at that we've obviously factored in at this point not only the shift that you've mentioned from non-interest-bearing to interest-bearing, but also the likelihood of a rate reduction based on the talk that is out there. And so as we look at and we look at kind of the continued momentum on the cards side, and we look at the deposit growth that we're seeing particularly in the TTS franchise with higher volumes, a growth of 10% or so, we feel pretty good about our ability to get to that 4% growth in NIR, notwithstanding that there are other factors that come into play, not the least of which is how many additional cuts play out through the balance of the year. But as we sit here today, we feel pretty good about that the bigger driver – the biggest driver I think would be as I mentioned continued growth on the Branded Cards side, continued growth on the accrual businesses. Those are going to be the larger factors that play through the back half of the year.

GLENN SCHORR: Okay. Appreciate that. Maybe a little more color on the loan – on the loan yield side coming down. I'm assuming that is LIBOR based loans, and the follow-up I have on that is who makes the call on those loans meaning LIBOR-based versus prime-based? Is it you, or is it client-led? I'm just curious on how to think about that as we go forward. It looks like LIBOR does that, but prime didn't obviously.

MARK MASON: So, we certainly saw some revenue pressure on the corporate lending book. That was a combination of kind of the spread compression in addition to some hedging costs and that certainly played through here. In terms of the pricing of the loan that is both a by-product of what we're seeing in the market on the way of competition from a pricing point of view and obviously – and the funding costs that we have. I think what we've tried to be diligent about is where there are opportunities to both serve the client and not necessarily tie up the balance sheet, we have taken advantage of those opportunities particularly in our trade lending activity, so that we're not bringing on economic position that – or positions that are uneconomical.

We'll continue to see pressure from a pricing point of view in Asia. And so you've seen our Asia loans come down just because the combination of the economics not making sense again, as well as just really slowing demand given what's going on with trade. And so there is pressure from a spread point of view. We do have a view towards pricing that not only considers our own internal funding, but also the client demand and the competitive landscape and that combination of factors is what plays out through the yield.

GLENN SCHORR: Okay. Really appreciate it. Thank you.

MARK MASON: Thank you.

OPERATOR: Your next question is from the line of Jim Mitchell with Buckingham Research.

JIM MITCHELL: Hey, good morning.

MARK MASON: Hi, Jim.

MIKE CORBAT: Hi, Jim.

JIM MITCHELL: Hi. Maybe just following up on Glenn's question, just to zero in on deposits a little bit, interest-bearing deposit rates paid was up 7 basis points without any kind of a hike. Is that just a mix shift? You mentioned I think it looks like Asia deposits were up. I would imagine they are higher rates. Just trying to figure out, is there domestic pressure on rates paid, or is that just mix?

MARK MASON: So, there is some mix shift. I mean, there is some mix shift from non-interest-bearing to interest-bearing.

JIM MITCHELL: That would affect the rates paid on interest-bearing?

MARK MASON: That's right. So the other dynamic is in fact what we're seeing – there are two things. One, what we see in the market from a competitive point of view; two, there tends to be a lag effect from the betas that play through on the retail side. And then three, as we've been growing some of the U.S. deposits that I mentioned earlier, some of that has been growth out of our markets, but with HYSA – with high yield saving account type products.

JIM MITCHELL: So would you expect that to continue to creep higher a little bit or start to stabilize?

MARK MASON: It kind of depends on kind of what happens in the broader rate environment. We obviously are talking about rate cuts now and that ultimately over time would have an impact. I think the strategic way that I tend to look at it is the deposit activity that we have with clients is really geared towards the broader relationship that we have with them as you know. And so we had a lot of good deposit growth on the TTS side. That's around the broader solutions that we talk to and work with those clients around. The deposit growth we're seeing on the consumer side is really about demonstrating the digital capabilities that we have and really broadening the relationship we have them. So, yes, there is some pricing pressure. The rate movement in the future will certainly have an impact on how much more or less of that plays through, but we do think we're making progress against the broader strategic objectives.

JIM MITCHELL: Okay. And a clarification, for the $2 billion in NII growth this year, are you assuming now a rate cut in that number? Or I'm not sure if I heard you say that?

MARK MASON: We're assuming one rate cut in that number.

JIM MITCHELL: Okay. That's very helpful.

MARK MASON: Towards the back half of the year.

JIM MITCHELL: Right. And just one question on TTS and trade finance, you mentioned spreads being wider in trades, so is sort of the trade war helping you a little bit? Or have you seen a slowdown? Certainly trade flow seemed to have slowed. How do we think about that – you seem pretty confident in the growth in that business – or how you're thinking about the dynamics there?

MIKE CORBAT: I think from a trade perspective, I would say – I don't want to say BAU, but business activity remains fairly strong. I think we've seen some trade routes shifting. The example we give is, as oppose to soy from the U.S., soy from Brazil et cetera, so trade route shifting, I think our clients were kind of very engaged around kind of studying and trying to stay ahead of that. So, I don't think, we'd speak to any kind of slowdown as of yet, but clearly people paying a lot of attention to it.

JIM MITCHELL: Okay, great. Thank you.

OPERATOR: Your next question is from the line of Matt O'Connor with Deutsche Bank.

MATT O'CONNOR: Good morning.

MARK MASON: Good morning.

MATT O'CONNOR: So you guys are executing on the capital deployment strategy you laid out a couple of years ago and to be fair, I think there was some kind of debate or concern whether you could execute on that and you are. But now you're sitting here, you performed very well in DFAST. Some of your peers surprised the market and delivered more than expected. And it seems like you're positioned to do even more than what you had promised couple of years ago and just wondering your thoughts on whether you can do it and the timing and how you approach it?

MARK MASON: So, as you mentioned, back at Investor Day, we talked about $60 billion plus over the three-year cycle. We're going to exceed that. We just announced the $21.5 billion over the four quarters covered by this 2019 cycle. As you know, we have an objective of trying to obviously generate the highest return and return as much capital as we can to our shareholders. We currently manage to a CET1 target of 11.5% and that obviously has buffers in it for some of the uncertainty that's still out there, whether it be proposals like SCB or other things that impact the variability of capital.

As we get greater clarity on those things, we will obviously continue to kind of look at that, but that remains the target going forward. We're still running at 11.9% CET1 ratio. So, subject to growth needs, we will always be looking at how we ensure that we run that more tightly to that target of 11.5%. And the way we think about the return of capital, distribution of capital going forward is largely as we get close to that 11.5% which we expect to get close to towards the end of the year, we'll be around how much capital we generate juxtaposed against how much we need to continue to grow. And so we certainly have the objective of continuing to return as much as makes good sense given the growth opportunities for the franchise. If you look back over the three-year cycle, we've returned on average about 121% of our net income available to common. So we feel pretty good about that percentage albeit we started at a higher CET1 ratio years ago.

MATT O'CONNOR: And can you just remind us as we think about the 11.5% target, what are some of the areas of clarity that you're looking for in terms of reevaluating that? We obviously got some comments from the Fed in recent weeks that seems like the stress test might be a little bit easier than feared, as they bring in the stress capital buffer in. Just what are some other things specifically that you're looking for to potentially bring that down?

MARK MASON: So, look, you just mentioned, one, with the SCB that's one of the proposal that's still out there. We just got, as you mentioned, some clarity on that. We'll have to see how that factors in. There are a number of other proposals that are still outstanding. And the dialogue that we've heard from regulators is largely around ensuring that those things, that there is understanding of how those things will work in aggregate in terms of how they impact the amount of capital that institutions will have to hold, whether that's additional clarity on how to think about G-SIB. We obviously have CECL that will come into play in early 2020, but all of those factors are important. We've heard commentary around greater clarity or transparency as part of the CCAR process. We obviously support greater transparency. We think it'll help to remove some of the variability in capital planning. So as that starts to kind of continue to come into the fold that will be important to how we think about this. So, those are just a couple of examples.

MIKE CORBAT: And I think as we look at – Mark, when we think about the 4.5% plus 3%, plus the 3% what's in some ways on the table is the management buffer, the 100 basis points. And as you described, as we look at G-SIB and CECL and kind of all these things coming together, whether or not there's an opportunity to reexamine that or not.

MARK MASON: That's right.

MATT O'CONNOR: And then just lastly to bring it all together like as you think about some of these moving pieces, do you think you will have clarity before the next CCAR cycle that might motivate you to resubmit? Or is it more hoping to have clarity for the next cycle on these factors?

MARK MASON: These things kind of take time to play out, I think, as we've seen over the past couple of years. And so we'll just really have to see how much additional clarity we get over the coming months and we'll figure that out as time progresses.

MATT O'CONNOR: Okay. Thank you.

OPERATOR: Your next question is from the line of Saul Martinez with UBS.

SAUL MARTINEZ: Hey, guys. Good morning.

MIKE CORBAT: Good morning.

SAUL MARTINEZ: A couple of questions. First, Mark, I just wanted to clarify the NII guide. So I think you mentioned, you're still on track for $2 billion increase this year versus last year that and 4%, that does imply by my calculations that second half the quarterly run rate does continue to ratchet up versus the first half, something like $12.1, $12.2. Is that – I just want to clarify that's right and that's including a rate cut being baked into that outlook?

MARK MASON: Yeah. So, we are still targeting and on track for $2 billion for the full year as I've stated. We do have one rate hike that we're assuming.

MIKE CORBAT: Rate cut.

MARK MASON: Sorry. Rate cut that we're assuming. Excuse me. Rate cut that we're assuming in the back half of the year. Obviously, if that happens sooner, happens in July, that would have an impact on the NIR forecast that we have and candidly if there is more than one rate cut, that would have additional impact and so those are the factors. There obviously are other factors that come into play and that is assuming obviously a change in the U.S. rates. But we are still targeting the $2 billion recognizing there's some risk there.

SAUL MARTINEZ: Got it. But given the $50 million impact per quarter from each 25 basis points cut, presumably even if we do get one cut or two cuts it seems like you're confident that you can get NII growth in the back end of the year versus the first half?

MARK MASON: I think the broader issue is the uncertainty that Mike and I have referenced that's just out there. And so, if we just isolated this to two interest rate cuts in the scheme of a $47 billion NIR line, I mean, you're absolutely – you're right. But the reality is that, it's the broader uncertainty that's out there that's impacting the industry, and while that goes through the market-sensitive revenues and just kind of corporate sentiment more broadly.

SAUL MARTINEZ: Was there – in the past you've broken out this slide on page 10, where you break out the accrual versus legacy versus trading. Is there a reason why you're not doing that this time around?

MARK MASON: Just, I mean, as we kind of exited holdings and started to kind of wind down those legacy businesses that became less of a significant variable as you look these total revenues. It was probably 5% of the aggregate revenues in the first quarter on a constant-dollar basis. It's just wasn't as meaningful, and so we moved towards simplifying it with both the legacy breakout as well as the trading NIR breakout.

SAUL MARTINEZ: Okay. And one final one from me, a large portion of the expected profitability expansion in North America Consumer comes from rightsizing the profitability in Retail Banking and you gave some positive commentary obviously and you feel pleased about the momentum in terms of deposits, the inflows, the digital strategies, tapping your cards network or your cards clients. But you also have a lower rate environment and deposit spreads are likely going to come in and I think you didn't have any growth in revenues in retail banking. In a tougher rate environment, can you right size profitability? Or how much more difficult is it to right size the profitability of your Retail Banking business, if the Fed continues to cut?

MARK MASON: I'd make two points. One is, as I think about the back half of 2019 and even 2020 for that matter, I think that the work that we've done in Branded Cards is going to be a meaningful contributor or continue to be a meaningful contributor to the revenue performance that we see in Consumer North America.

The North America Retail Bank, as you mentioned, we run at a high efficiency rate at this point. We are seeing good traction as it relates to deposits increasing. But again, what that's really about for us is how we deepen the relationships and kind of broaden the penetration of those products and services into our card customer base. And so, over time, I think it's going to be more challenging to look at just the Retail Banking portion of that we breakout in income because of that broader client strategy. And so, I think that's kind of how we've thought about it.

That said, I mentioned kind of repositioning that we have taken in the first quarter that we've taken a bit of that in the second quarter, that's largely around the reorganization to support that strategy and moving from a product siloed-type of business model to one that is more geared towards the client, and we think that that will help. That obviously will help the margins as we continue to execute against the strategy.

SAUL MARTINEZ: Got it. That's really helpful. Thank you.

OPERATOR: Your next question is from the line of Mike Mayo with Wells Fargo Securities.

MIKE MAYO: Hi. I have one very short-term question and one very long-term question. The very short-term question relates to what was the dollar amount of the mark-to-market hedge losses? You said that roughly offset Tradeweb or was much bigger number than what was in the press release? What was that number?

MARK MASON: In the quarter, the mark-to-market losses on loan hedges were $75 million. For the half is what I was talking about. For the half, the number was about $306 million. So, about $231 million in the first quarter. And so, that's the number.

MIKE MAYO: Okay. And then, the longer term question is, how much runway do you have left with technology to improve Citigroup's efficiency? Mark, when you mentioned the levers that help meet your targets, the RoTCE target of 12%, you didn't mention technology, yet you mentioned the $300 million spread between the savings from the investments over the new investment levels. So, what's the runway left kind of short, medium, and long-term? Thanks.

MARK MASON: In that $500 million to $600 million for the year, the $300 million that we've done year-to-date, as it relates to productivity, are the benefits of the technology investments that we've been making. So, some portion of those savings is a byproduct of technology investments.

We continue – we see those technology benefits in the digital capabilities that we've built out and how that plays out at a lower cost to not only acquire, but lower cost to service the clients. You see things like the use of e-statements going up. We see things like volumes into call centers going down. All of those things are benefits that are generated as a byproduct of technology investments that we've made.

We expect a similar level of productivity saves in 2020. We do continue to invest in technology. In fact, what you heard me mention earlier in terms of one of the protected areas being infrastructure and control. There are couple of different ways to look at that protected area as we invest in technology around our infrastructure and improve the data quality that we have and things of that sort. Not only does it help us run a safer and more sound organization, but it also arms us with information sooner to enable us to react and serve our clients more quickly.

And so, yes, the answer is yes. We do see benefits from technology playing out in the expense line and in the productivity savings that I've referenced both in 2019 and 2020 and likely beyond, and those things will help in getting us to the lower levels of operating efficiency that we've talked about achieving over time.

MIKE CORBAT: Mike, I think if you go to page 21 in the deck, you can see we've put in there some different drivers and metrics. And I think from the way I think about it is, today, we really run the combination of an analog and a digital bank. And the faster we can continue to drive digital adoption and mobile usage, we know that that's cheaper, it's significantly cheaper when we're solving issues on your phone, when we're solving issues away from physical interaction or voice, and again, you can see, we've got roughly 30 million active digital users, we've got 20 million active mobile users between North America and International. And you can look at the year-over-year growth rates, I think probably amongst the highest in the industry. And so, we're on this journey. And, obviously, the investments that we can make to switch those over, we think yield quite high returns.

MIKE MAYO: And then, last follow-up. Mark, you reaffirmed the guidance to the RoTCE for this year and next. And Mike, do you also reaffirm that guidance? I assume you do.

MIKE CORBAT: Absolutely.

MIKE MAYO: So, Citi, this predates you, missed a lot of targets this decade as we approach the end of the decade, and consensus does not expect you to reach those targets, and look, we have a buy on the stock, we haven't always had a buy on the stock, and we don't even have you reaching those targets. So, where do you think the disconnect is? You think that Citi is going to get a 13.5% RoTCE next year and you're hard-pressed to find too many other people who agree with you. Assuming we don't have a recession or anything like that, where do you think the market is wrong?

MARK MASON: Let me try to answer that in a couple ways. First, let me go back to 2019 for a second because both Mike and I have said that the 12% remains the target for 2019. It absolutely does. You can also look at the first half of the year or the fourth quarter of last year and witness strength in the franchise on the consumer side, on the accrual side of the business, but you can also witness the impact of the environment that we're in and the uncertainty around that.

Despite that uncertainty, we've gotten to 11.9% in the first half through pulling a number of levers, and we would expect to continue to pull those levers into the back half of this year. To the extent that that uncertainty increases or there is more significant reaction from the market to the uncertainty, we'll, of course, look and work to find additional levers. But at some point, that becomes challenged in terms of getting to that 12% just given the things we want to protect in this franchise. And I believe that even if it were to become challenged that we'd end up in a range around that 12% and that is what we're working towards that target, that 12% target.

In terms of 2020 and the 13.5% target that we have for 2020, and the disconnect, I mean, we've talked through the disconnect in the past and it moves around, as you would know very well, but it's range from being a little bit of a difference of views on the top line, which I think we've started to narrow some of that gap given the performance we've been able to demonstrate through the first half of the year again in those strong areas. There's also been less of a disconnect on the expense line, as I've given I think a little bit more specificity around the guidance there. There's been a cost of credit difference of views in the past, and again, we feel pretty good about our cost of credit outlook, but we obviously recognize that where we are in the cycle. There's been obviously tax work that we've continued to do and will continue to do, and I gave some additional view on that. We've done more on capital than we originally talked about.

And so, it's those drivers and levers that we'll continue to pull through the balance of this year. We'll see how this year plays out given all of the uncertainty referenced and we'll go into 2020 with the 13.5% remaining our target and with clarity on where we think we'll end up against it.

MIKE CORBAT: And Mike, the way I think about it simplistically is, we're going to do everything within our power to get to those numbers with the exception of two things. One is we are going to continue to make the investments that are necessary to keep our business competitive. You can see a lot of things going on around this and I think around our franchises in Consumer or in our Institutional business, as an example, in TTS, or Securities Services, we think we just got to make those investments to stay competitive. And the second thing is around – is our commitment to our shareholders and our regulators to make sure that we're making the investments in terms of safety and soundness. And so, we won't put those at risk, but everything else is on the table.

MIKE MAYO: All right. Thank you.

OPERATOR: Your next question is from the line of Steven Chubak with Wolfe Research.

STEVEN CHUBAK: Hey, good morning.

MARK MASON: Good morning.

STEVEN CHUBAK: So, I wanted to start off with a question on the FICC business. You cited some of the pressures within FICC and rates in particular. Your business has always been somewhat unique just given the higher contributions from TTS, in particular with non-financial corporates, I think that's more than 30% of your total revenue there. I'm wondering whether you're seeing greater resiliency on that side of the business, which would suggest maybe even more pronounced pressure within Institutional?

MARK MASON: So, I guess, what I'd say is, obviously, our Fixed Income revenues for the quarter were down about 4% if you exclude the gain from Tradeweb. I think when you look at what transpired in the quarter, there was a fair amount of volatility around rates and rate movement. And what we saw was that play out particularly around the investor client base that we have. So, to the point we've made before, we continue to see stable corporate client activity, particularly in rates and currencies, where there's a strong linkage to our broader franchise and in particular TTS. But we did see decreased activity with our investor clients given all of the macro uncertainty that I've mentioned now a couple of times. Many of the investor clients remained on the sidelines. And frankly, it was the speed and the magnitude of the rate movements that created a challenging market environment and made it difficult to monetize client flows.

On the Equities side, well, you didn't ask about Equities, but on the Equities side, I mean, the trade war had a similar or trade discussions and war had a similar impact that kind of flowed through particularly again with investor clients, I mentioned earlier, impacting both cash equities and prime brokerage, but we did see, again, corporate client activity even in Equities kind of hold up nicely playing out through equity derivatives.

MIKE CORBAT: And the way I would say, Mark, is I think engagement is high. Engagement's very good. But I think right now the challenge is – and maybe it's the opportunity, in that we're clearly pivoting from an environment where we had predicted or thought or had been built in rising rates to at this point rates going lower. And I think from our perspective, we don't believe that the market has made that full adjustment, and there's probably some turn that's got to come as portfolios set up for that potential lower rate environment.

The question is, when will that come and to what degree will that come, will we get conviction in terms of the trajectory of this lower rate environment and portfolios have to reposition, because I think today, they're not positioned where they need to be fully.

MARK MASON: And again, to that point, just last week, when there appeared to be some signs of greater clarity on the move in rates, the reduction in rates and the timing of that, the Equity Markets responded very, very favorably to that. And so, to your point, Mike, I think clarity in direction should yield greater confidence and perhaps a more of a risk-on mentality as it relates to the markets.

STEVEN CHUBAK: Very helpful color. I appreciate that. And just one follow-up from me on ICG credit. You guided to – or indicate some normalization of credit trends, but the charge-off rate there is quite low at 8 basis points. I'm just wondering, is it fair for us to extrapolate that 8-basis-point loss rate as indicative of what you guys view as normalized? And can you maybe just speak to some of the unique aspects of the business, like trade finance that should drive some lower loss levels through the cycle since that was actually pretty encouraging commentary from our point of view?

MARK MASON: I mean, again, when you think about our Corporate Lending book and the quality of our exposure, the multi-national clients that we cover, 83% of it being investment grade-type exposure, historically, we've had loss rates that have been low in the way of number of basis points, 5 basis points to 6 basis points historically, and yes, we are starting to see some normalization of that.

I think the quarter cost of credit of the $103 million is reflective of that coming out of last year and representative I think of what we've talked to in the way of what to look to see in the way of normalization. And so, I think, it's a byproduct of the quality of the book that we have and the nature of the activity that we do in lending.

STEVEN CHUBAK: Okay, great. That's it for me. Thanks for taking my questions.

MARK MASON: Thank you.

OPERATOR: Your next question is from the line of Ken Usdin with Jefferies.

KEN USDIN: Hey, thanks a lot. Just a follow-up on the credit side. Mark, you pointed out that the – on the Consumer side of credit that things have also kind of just gone according to plan. You've maintained that guide. At what point do you see the end of the light in terms of the seasoning? Meaning, how long do you think you can kind of stay in this very benign zone for the card side, presuming that the economy stays in relatively good form? Any reason to see any change to that, I guess, is the question.

MARK MASON: Not at this stage. We gave kind of medium-term guidance, if you will, when we talked about those ranges of 300 basis points to 325 basis points, 500 basis points to 525 basis points. Again, certainly through the balance of this year, we expect to end up inside of that range. We look at probably all the things that would be obvious to folks and then some.

So, if you look at just on the macro front, we're obviously looking and watching closely the inverted yield curve and what that has been historically. But when we look at that juxtaposed against the internal metrics that we use whether that be card usage patterns or utilization or payment rates or the percentage of customers making minimum payments, I mean, thus far those indicators have all remained broadly stable. And so, I don't see any cause at this point for material concern.

KEN USDIN: Okay. And then, the tax rate you mentioned 22%, 23% in the back half, and you've also talked about there potentially being some more levers there. Can you help us understand, like, does that mean that over time you have the chance to still take the tax rate lower as you look into 2020 and as part of your plan for the RoTCE improvement?

MARK MASON: We're constantly looking at it and trying to identify opportunities looking at obviously where we book business and the client demands around that, and where there are opportunities to do that. But, at this point, I'm not taking down the guidance. I'm just obviously pointing out perhaps the obvious, which is that, it's one of the levers that we continue to push on and explore.

KEN USDIN: Understood. Last one, just on the deposit cost side, with the potential rates turning and some non-U.S. central banks already cutting, what's the lag effect here in terms of this quarter, the deposit costs were up 7 basis points? What's the rate of change that you need to see before you can see a leveling out of the basis point increases that we see on deposit costs side? Thanks, Mark.

MARK MASON: What we've seen during the rate rise or increases were that the beta on the Corporate side, on the Commercial side kind of tick up a lot faster and there tends to be a lag on the Retail Consumer side. And as things turn, I would expect to some extent similar type of direction notwithstanding that the retail deposit side still has that lag to it and there are other factors such as the competitive landscape that's out there for deposits.

And so, it's a little bit hard to kind of pinpoint exactly when that stabilizes just given all of those factors, but we're obviously managing it closely and managing it in the context of the broader strategy that I referenced a couple times now.

OPERATOR: Your next question is from the line of Betsy Graseck with Morgan Stanley.

BETSY GRASECK: Hi, good morning.

MARK MASON: Good morning, Betsy.

BETSY GRASECK: Couple questions. Just on the deposit business, a follow-up there. Could you give us a sense, I think you mentioned at the beginning of the call that you had a $2 billion increase in deposits that was from the digital efforts you've got, two-thirds outside your footprint and half of the $2 billion coming from folks that have your card, but didn't have a banking relationship with you. Could you just give us a sense of how that was relative to expectations and what you think the major drivers were for generating that growth speaking to rate versus marketing versus any other factors that you want to add?

MARK MASON: Yeah. So, one, I would say that is in line with what we were expecting in the way of deposit performance through the digital sales channel. We have seen kind of broadly just good activity with our Consumer retail clients, not just with the net deposits, but also retaining deposits as they shift into AUMs, and as clients start to make investments. And so, the flow levels have been very good if you include both AUMs and the deposits.

I would say we would expect continued growth in the deposits in the back half of the year. It is a combination of – and if you think about our strategy again to target card customers, a good portion of the deposit growth that we achieved were outside of our six markets, and with our card customers who did not have a Retail Banking relationship. It's a byproduct, I would say, of not only rates, so there was some portion that is tied to the high-yield savings account, although that – even that does demonstrate the power of the model, because we know these customers and it's not a cannibalization of what we gather inside of our market. But it's also a byproduct of the work we've been doing around creating a value proposition and understanding which of our clients are likely to respond to what rewards.

And so, you heard me mention ThankYou Points and Double Cash rewards. Those were part of the offerings to clients to join us in terms of the Retail Banking products that we offer in exchange for other more ThankYou Points or more benefits that accrue from the Double Cash rewards. So, it is a combination of marketing, targeted marketing in terms of knowing the customers we want to go after and what they're likely to respond to. Some of it is rate, yes, but it's a combination of all of those things and we expect continued growth.

BETSY GRASECK: And then, I know you mentioned that the NIM came under a little bit of pressure as you had significant increase in deposit growth, and the tie-in question here is, is there anything you need to see from these customers? Is there – like, do they need to keep their deposits with you for a certain amount of time before you're able to take some duration with these deposits on the asset side? Or should we anticipate that as you're growing your new deposits here out of footprint that that gets reinvested in the front end of the curve?

MARK MASON: So, I mean, obviously, there is LCR treatment for different types of deposits. These are largely time deposits that we've been bringing in. I think that we would expect that to – like I said, expect that to continue down the path. There's no reason for us to feel as though these are kind of short term in nature or anything of that sort.

BETSY GRASECK: Okay. But they'd be match funded or match invested I should say...

MARK MASON: Yeah.

BETSY GRASECK: ...is how you – okay. And then just two other questions. One, on the TTS business, could you give us a sense of how you expect the business operates or performs in a declining interest rate environment if we look at the forward curve? How should we expect TTS to behave? And then, you mentioned some strong pipeline with initiatives for the clients, maybe you could speak to that. And I'm kind of interested in understanding what you're planning on vis-à-vis the Libra announcement that came out of Facebook. Now, I know Libra seems like it's more personal related, but there is a C2B and a B2B element with that, so wanted to understand what your plans are because my basic question is why do we need Libra. It seems like you might have what companies need, so maybe you could speak to that a little bit. Thanks.

MARK MASON: I guess, I'll start and then Mike may want to chime in. So, just in terms of the TTS business, we obviously have seen very strong growth in the TTS business over the past number of years and quarters and even this quarter with 7% growth, which is probably a little bit lower than what we've seen in prior years which – and just as the rate increases have started to become fewer and now we move into a likely rate reduction. The impact to TTS is factored into at least the estimate that I gave you in terms of the impact of a 25 basis point reduction. It obviously would have an impact on the growth rate.

But I would say that the majority of the growth rate that we've experienced in our TTS business is not tied to the interest rate, but instead tied towards growth that we've had in both with multinational clients that are large and that we've been with for a long time, but also new emerging clients as they've entered into new markets, new countries. And we've been there to assist them with how they kind of grow their businesses and operations in those new environments, whether it be working capital or supply chain needs that they've had. And so, I would expect to see continued growth in TTS, albeit at a slower pace in light of the rate environment.

But again, our relationship with our clients are broader than just us taking their cash and holding their cash and we're offering them solutions that are a lot broader than just the rate that we pay them for cash. The other piece that I'd mention is that we have been and will continue to invest in technology around our TTS franchise. It is obviously a very competitive space, but it's one where we've had a strong position for a long time. It's been nicely growing. It's very efficient. It's higher returning.

We're nicely entrenched with many of our customers and we've got to continue to invest in the client experience in enabling faster cross-border activity for those clients. And so, good growth, I expect to see continued good growth; requires investment, we're in front of that investment to stay competitive and we'll continue to do so. And I'll let Mike kind of comment on some of the other pieces you mentioned.

MIKE CORBAT: Mark, I would just – in going back to TTS for one second, Betsy, operating in a declining rate environment is nothing new, it's certainly not new in the U.S. And you look at our TTS business operating around the world, many, many jurisdictions we operate we've been in declining rate environments for a period of time. And I think the work the team has done moving from interest rate-sensitive to more fee-driven types of relationships has been helpful in that.

On your question pertaining to what's going on from a technology perspective and in this case Libra, in particular, one is we are not dismissive at all of these. We look at them. We study them. As we've said, we are not part of the inaugural group. I've read the white paper several times at this point in time. And again, I look and there's, I think, some redeeming or there's some qualitative aspects that are appealing, and I think there's others that might raise some questions. And I think the way we think about it is that the market is moving and likely moving quickly towards 24/7 real-time, frictionless, ubiquitous global money movements and payments, and that's just a reality and that's going to happen, and I think we're pretty well positioned around that.

As I think of things like Libra, not a question of if, it's when the digital currency comes, it's a question is that currency, one that kind of operates as a consortium, or is it a Federal Reserve, or is it a central bank-backed type currency? And I think we're preparing for a world with both of those, where consumers, businesses are going to have flexibility in terms of their choices of what they choose to use and our goal, objective and mandate really is to be there with a system that's got the capacity to operate across all of those.

BETSY GRASECK: So, a lot of times big tech will highlight friction in the system and opportunities they have to cut friction out, meaning take out fee rates of legacy businesses. Could you speak to how you're thinking about that, because I think some people might view you as a legacy business with a margin that can be taken out? How do you answer that kind of question?

MIKE CORBAT: In there, Betsy, I would probably break our businesses into two components. I'd break it into a consumer business and into an institutional payments business. I think in the consumer business, it's clear that interchange as an example is a friction that has existed for a period of time and as we've seen elsewhere in the world will likely to continue to come down.

And I think that's one reason why you'd seen the disruptors or the innovators so focused on consumer versus institutional payments, because on the institutional side there's really not much money in the pure movement of money. It's in the operation of the operating account where, yes, you do get some float. But by the way, Libra has float and in their float, as I've read, they're actually not paying. That's where the partners are receiving their income.

There are frictions in foreign exchange. There are frictions in terms of rates and other things that we combine with that, but you got to have the back end that can provide those services, in today's age not only provide them, but provide them in a real time of scale way. So, again, not dismissive, but on the institutional side of things that from a payments perspective, you've got to have the full package. It's not just the movement of money. It's not the answer in there.

And so again, not dismissive, and that's why the investments in areas like TTS are so important that we're continuing to build out the front end. We're continuing to take pain points out, whether those frictions are in the forms of fees or money or probably to our customers' benefit even more so in the form of on-boarding and all the frictions that come in terms of account opening and making sure that we're investing in BSA, AML and those other pieces such that we can continue to distinguish ourselves with our clients as the place to go.

BETSY GRASECK: Great. Thank you.

OPERATOR: Your next question is from the line of Erika Najarian with Bank of America. And, Erika, your line is open.

ERIKA NAJARIAN: Yes. Hi. Can you hear me now?

MARK MASON: Yes. Good morning.

ERIKA NAJARIAN: Hi. Good morning. Thank you so much for answering the questions on your RoTCE targets. Maybe asking it a different way, the market seems to be now expecting three rate cuts between now and the end of 2020. I think previously you've set an efficiency goal of 53% for 2020 with 175 basis points of improvement in 2019 and 225 in 2020. And I'm wondering if we do get three rate cuts and corporate activity remains at current levels, is there enough productivity savings that you can identify to reiterate the efficiency targets as well?

MARK MASON: Look, I mean, obviously, the volatility around rate movement has been pretty significant over the past couple of quarters from an increase to now a reduction and possibly three reductions. And so, if we had significant moves in rates, we can kind of do the math as to what the implications would be. I think we'd also have to make some assumptions around those other factors that are in the environment and what happens with those, whether it's trade, in tariffs, et cetera, and whether to really have a fulsome answer in terms of what the implications would be on achieving the 13.5% and then being able to ascertain what levers we'd be able to pull.

So, it's a difficult question to answer as I sit here today as to which levers and how much of those levers we'd be able to pull, while protecting the things that Mike and I have referenced in still hitting a 13.5%. I think to some extent I want to see how this first rate cut plays out and what the implications are for additional rate cuts. Again, we could very well see, as Mike suggested, the market having to react to a rate reduction and certainty around the direction in a way that is favorable to trading businesses, but we've got to kind of wait and see how some of that plays out.

ERIKA NAJARIAN: Okay. Thank you.

OPERATOR: Your next question is from the line of Brian Kleinhanzl with KBW.

BRIAN KLEINHANZL: Morning.

MARK MASON: Morning.

BRIAN KLEINHANZL: So, a quick question on Branded Cards, you said you expect to maintain the current mix between the full rate and promotional. But I guess breaking that down, are you still expecting migration to be occurring from the promotional to full rate and you're just going to be relying on promotional for loan balances going forward or more heavily relying on promotional balances going forward?

MARK MASON: So, in order to maintain the mix that we have, we will need to continue to invest in promotional and bringing on promotional balances. And so, we will continue to do that. They will continue – we have obviously a track record of understanding how to do that and understanding the timing for which it takes for them to convert and flip into average interest-earning balances. But we now are reaching a mix that we think is a healthy mix for us. And in order to maintain that, we will need to continue to invest.

BRIAN KLEINHANZL: Okay. And then, secondarily, you mentioned that you're seeing – or macro conditions are slowing in Latin America, specifically Mexico, but there was additional levers you could pull on the expense side. I mean, what are examples of those additional levers that you have that are already in budget? Thanks.

MARK MASON: In Latin America and in Mexico, what we saw last year, we saw our expenses were up, I want to say, about 8% last year. And what I referenced this year or this quarter and last quarter was the growth that we were seeing in EBT. And the growth that we're seeing in EBT is a byproduct in some ways of the investment spend that we made last year now starting to pay dividends, so to speak, through 2019. And so, investments – or the digital capabilities that we invested in from a technology point of view, the organizational business model structure that we've put in place in terms of our retail activity there, all of those things are starting to play out as expected.

We're about, I don't know, halfway through the investment plan that we announced a couple of years ago. And we have the opportunity obviously to temper the remaining spend that was planned for to ensure that it's done consistent with the market opportunity that we see. And so, that obviously is a factor that would help on the expense line. And then, we're tempering growth in terms of loan activity, loan volume in light of what's going on in the economy and that obviously helps at least as we think about expected cost of credit and what have you. So, those are a number of the factors that play out there.

BRIAN KLEINHANZL: Okay. Thanks.

OPERATOR: Your next question is from the line of Marty Mosby with Vining Sparks.

MARTY MOSBY: Thanks for taking the questions this morning.

MARK MASON: Sure. Good morning.

MARTY MOSBY: To hit on the RoTCE targets again, would success be reaching those goals in the fourth quarter of each of these years? Or would success be ultimate success actually for the whole year? So, as you're kind of envisioning that, I kind of in my targets have you kind of reaching those by the end of each year, but you're really saying there's going to be 13.5% average for the whole year of 2020.

MARK MASON: So, the target that we've set was for a 12% was the full year return on tangible common equity target and as was the case for the 13.5% for 2020.

MARTY MOSBY: And then, when you think about capital markets or institutional business, it's been compressed or depressed for a while. We keep thinking this is uncertainty in the marketplace or it's related to something that's causing just a short-term hit. But is this somewhat more secular? And when you start thinking about your goals for next year, especially in 2020, are we assuming some of this pressure that we're in begins to release? And can you give us any kind of feel for the estimate of what you're kind of assuming the uncertainty and that has had an impact on the short-term capital markets types of businesses?

MIKE CORBAT: Marty, what I would say is that I think that there's part of it that is secular. But today I would argue the majority of it is cyclical, and what drives me to that statement is the intervention of central banks around the world and the amount of quantitative easing. If you tell me that QE is just there forever, then I would probably move towards the majority of it being secular. But at some point, the central banks have to start to back out of the market in terms of asset purchases, in terms of liquidity, and I actually think that there's going to be an opportunity for those that are there to step in and provide the liquidity and leadership on that front.

And again, what you see is – and you see, you follow it closely, you listen to what everybody says, we're not measuring trading by the year, we're not measuring it by the quarter. Trading in today's age is kind of day-to-day, week-to-week, month-to-month, a change of sentiment out of the Fed causes markets to react quickly. And I think it's what makes the forecasting, as either Mark or I speak at these conferences, so difficult. You tend to kind of speak mid-quarter and these things can change in either direction pretty quickly. And so, it's not a lack of engagement from a client perspective. It's a lack of conviction. And again, I think we've got the combination of that with a bit of overhang from an environmental perspective. And clearly, I think the central banks continuing to be actively involved that in some ways taking part of the role that ultimately the banks will need to play in the future.

MARK MASON: I'd add to that. As we see the pressures that we've talked about impacting the trading businesses, in many ways we're not just standing still as this happens. And so, you've seen us announce kind of the reorganization, if you will, of our spread products or in our spread products area. We've recently announced under the new leadership in markets combining kind of our rates and currencies business both in an effort to ensure that we're better covering our clients and better positioned to cover our clients.

And you'll continue to see as markets evolve and as the industry evolves for us to constantly be looking at our business model for ways to improve it and to improve the effectiveness of it, to improve the profitability and returns associated with it. And so, we're mindful of kind of how things are changing, to Mike's point they do appear to be cyclical in nature, but we're constantly evaluating our businesses and trying to position ourselves effectively.

MARTY MOSBY: Thanks. That was very helpful. And then, lastly, I wanted to ask you, as we think the Fed could begin to pull short-term interest rates down, are we preparing to be able to begin to lower deposit rates instead of actually increasing them? So, this has been a quick inflection point, but do you think that you'll be able to offset some of the impact as you're able to pull those deposit rates back down?

MARK MASON: I mean, look, we've seen – we talked a little bit earlier about the betas and how they vary from the corporate clients and commercial clients to the retail consumer client base. And I think there are other important factors as rates start to move in a downward direction. We have seen some of the players in the industry start to take rate down. The other factors include the competitive landscape that's out there and how players decide to adjust their pricing, but it also includes how you think about the relationship with the customer. And if it is, in fact, more than just that deposit relationship that's going to factor into how you think about pricing strategy, but I would imagine over time with a clarity on the direction that you will see betas respond over time.

MARTY MOSBY: And historically, we've seen the backdrop of higher deposit betas and rates initially drop, meaning you drop a little bit more and then eventually that has a slowdown, kind of reverse of what we had on the way up. So, thanks for your answers today.

MARK MASON: Yeah.

OPERATOR: Your final question comes from the line of Gerard Cassidy with RBC.

GERARD CASSIDY: Good morning, Mark. Good morning, Mike.

MARK MASON: Good morning, Gerard.

MIKE CORBAT: Good morning, Gerard.

GERARD CASSIDY: You guys did very well in the CCAR this year in terms of the amount of capital that was reduced during the stress test. I think you dropped about 500 basis points which was the lowest in maybe four or five years. What was the primary driver? Was it obviously de-risking the balance sheet, but it was primarily coming from Citi Holdings falling off? And then, second, if it continues to go this way, would you consider lowering your CET1 capital ratio, your target that is?

MARK MASON: So, as Mike kind of alluded to earlier, there are a couple of factors that are involved in the CET1 ratio just taking that part of the question first. And obviously, we've had a management buffer that is included there of about 100 basis points. We have kind of a 3% placeholder in terms of the SCB and we're getting more clarity on that, it seems like in some of the recent commentary. And as we get more clarity on the SCB proposal and other proposals and it takes out the risk of variability to how we think about capital planning, we will certainly take a look at the 11.5% and see that that still makes sense.

In terms of the ask that we made of the $21.5 billion and what was approved, we obviously ran our scenario with an eye towards the targets that were set, 11.5% in this base case, but also ensuring we can achieve at least the minimums during a stress scenario. And the mix of assets that we have on the balance sheet, we've been thoughtful first about the client needs through the course of 2018 with an eye towards what the implication would be from a stress point of view as we go into a CCAR cycle and the longer-term planning of the business and ensure that we ended the year in a place, again, that allowed for us to serve those needs, but was mindful of the return necessary in light of stress losses that maybe a byproduct of those types of assets. And so, that's what's kind of played out through the scenario and through the ask that we ultimately made.

GERARD CASSIDY: Very good. And, Mark, can you remind us, are they still implementing the operating risk capital charge for companies like yours that have exited businesses, but you're still being assessed the capital charge for those businesses even though you're not in them?

MIKE CORBAT: Yes.

GERARD CASSIDY: Very good. And then...

MIKE CORBAT: Op risk RWA.

GERARD CASSIDY: And how much is that for you folks that has cautioned you in terms of capital?

MARK MASON: I don't think we break that out.

MIKE CORBAT: We haven't broken that out.

GERARD CASSIDY: Okay. Is there any color do you think coming from the new regulatory regime to maybe give you and your peers some relief in this area?

MIKE CORBAT: I don't think so.

MARK MASON: I don't think so.

MIKE CORBAT: I think as we look across the industry peers, it's pretty consistent and that hasn't been contemplated.

MARK MASON: And just to be clear, I think you know this, but we're looking at or we utilize kind of a Basel III Standardized as it relates to our risk-weighted assets, right? That is the metric that is involved there.

GERARD CASSIDY: Very good. And then, shifting over to the Institutional Clients Group, Mike, I think you touched on in the markets area that there are some cyclical factors affecting them and you talked about the quantitative easing. In terms of secular in the cash equities area, did you guys see much of the MIFID II changes affecting your cash equity business this quarter?

MIKE CORBAT: This quarter? No. No. Again, I think that over the kind of glide path of implementations, we haven't seen really many surprises. And we actually went into this and continue to believe that we've got the ability as clients kind of rationalize the counterparties to people that they deal with that Citi is in a position to be a winner in that and I think we continue – I think as you've seen this continue to kind of climb up the tables – continue to take share there.

GERARD CASSIDY: Great. And then just a tie-in, can you guys give us a flavor for the Investment Banking pipeline? How does it look at the end of the second quarter relative to the end of the first quarter?

MARK MASON: I guess, again, on Investment Banking, kind of as you saw in the numbers, we ended down 10%, but better than what I talked about at Morgan Stanley. The strength we saw at the end of the quarter was really a pull-forward with both some ECM activity as well as in M&A. That said, the dialogue that we have with clients in Investment Banking remains strong and fully engaged and quite constructive, and we've seen particular strength in the U.S. M&A activity continuing. So, we kind of go into the balance of the year feeling good again about that dialogue, but also recognizing that all these factors that we talked about influences the corporate sentiment and willingness to take action.

MIKE CORBAT: And, Gerard, when I think of it – it's in some ways, the pipelines are fine. The pipelines are in pretty good shape, but what's the market willing to accept, what can get priced on what terms? And so, I think the pipelines are there. I think the question is in what ways are the markets open to get those deals done.

GERARD CASSIDY: Great. Thank you for the color, gentlemen. Thank you.

MARK MASON: Thank you.

OPERATOR: And presenters, do you have any closing remarks?

ELIZABETH LYNN: Thank you everyone. Have a good day.

OPERATOR: This does conclude Citi's second quarter 2019 earnings review call. You may now disconnect.

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