TRANSCRIPT

2020 Credit Suisse Financial Services Forum

Friday, February 28th, 2020

HOST
Susan Katzke, Credit Suisse Analyst

SPEAKER
Naveed Sultan, Global Head of Treasury and Trade Solutions

QUESTION AND ANSWER

SUSAN KATZKE: So good morning, everybody, and thank you. Thank you, Thomas, for joining us this morning. We at Credit Suisse look forward to your leadership in the years ahead. So as Thomas said, we're back for day two of our 21st annual Credit Suisse Financial Services Forum, and I'm pleased to kick off the day welcoming back Citigroup. I'm not just welcoming back Citigroup. I'm welcoming back Naveed Sultan who heads up TTS, Treasury and Trade Solutions for Citigroup. He joined us here in February of 2016. A fair bit has changed since 2016, including it's about 35% growth in related TTS revenue and related TTS-driven deposits, if you look at 2019 versus 2015. So without further delay, let's get started here. We'll have a fireside chat and then Naveed will be available afterwards for a breakout session.

NAVEED SULTAN: Thank you, Susan.

SUSAN KATZKE: Thank you.

NAVEED SULTAN: Good morning, everyone.

SUSAN KATZKE: Okay. Day two. So let's get started, if you would, at kind of a higher level with maybe a brief overview of the TTS businesses, maybe just to level set here on size, scope, composition of the businesses.

NAVEED SULTAN: Yeah, thank you. You know, as you think about the TTS business, it's very strategic and foundational for Citigroup's business and operating model. And we deliver a wide range of working capital management solutions to our clients around the world, leveraging our global platform. It includes products and solutions in payments area, receivables areas, liquidity management services, commercial guards, trade finance, trade services and foreign exchange. Our engagement with the clients is wide-ranging. So we do business with corporate clients – 80%-plus Fortune 500 companies use our platform around the world – government entities, public sector entities, financial institutions including banks, digital economy clients, the Big Tech, the Fintech, as well as the commercial banking clients.

As far as the digital economy clients are concerned, digital economy clients are on an accelerated path to globalization. And our platform is a very natural fit for them to achieve that goal. In terms of the size and scope, we are in 98 markets where we actually have banking licenses. And in some of those markets we have operated well over 100 years. We are connected with over 250 trading systems including several, on top of that, several alternative payment mechanisms and channels. So on average, we process about $4 trillion worth of flow, which could go up to whatever, $5 trillion, $6 trillion on a peak day. And that's essentially 145 currencies around the world. And we have a market share of about 15% of the Swift dollar flows.

Now, if you look at this business from a client perspective, it has both operating and strategic relevance. The operating relevance is that we are deeply embedded in our clients' operating environment, in their operating processes and help them do business around the world on a day-to-day basis. Strategically, because we provide working capital management solutions and help our clients become more efficient, the companies who have more efficient working capital management tend to outperform their peers on four critical dimensions: growth, reinvestment, dividend payout, and market cap. So both from an operating and strategic standpoint, it's very, very relevant to our clients.

Now, in terms of its contribution to Citi, 2019 was the sixth consecutive year of growth. We delivered about $10 billion worth of revenues, over 20% of the company's net income and 45% of total company's deposits which, as of December 31, average was about $559 billion. And that mostly is the operating deposits.

Highly efficient business according to independent objective studies, and consistently has delivered well over 20% return on equity. Last year we grew our deposits by 10% on a constant dollar basis. And I think the correlation between the operating activity in the deposits is very, very tight and close, post Basel III and all the rest of it. So therefore, it doesn't reflect your growth in deposits, operating deposits, doesn't reflect the growth in the underlying populating drivers. So that's more or less, like I said, it's a very strategic business. It's fundamental to our business and operating model.

SUSAN KATZKE: And so let's back up a second. Based on the numbers that you gave me, the pre-tax margin and the ROE are fairly above the average for Citi as a whole. How have those trended over time?

NAVEED SULTAN: For the last six years – like I said, we have delivered the sixth consecutive year of revenue growth. We have a very sharp focus on scalability and operating efficiency. And if you look at the trajectory of all the key ratios in the last six years, they have been a positive trajectory.

SUSAN KATZKE: Okay.

NAVEED SULTAN: Despite different macroeconomic environments, geopolitical context and interest rate volatility in the US and elsewhere in the world.

SUSAN KATZKE: Okay. And in terms of the deposit flows, up 10%, I think you said last year, and we threw out the number of having grown about 35% over the last four years. Can we talk a little bit about the key drivers of the deposits and what's going on with deposit flows in a – what goes on in a risk-on versus risk-off environment?

NAVEED SULTAN: I think the deposit growth is an outcome of your client engagement, and your ability to continue to improve your operating drivers. So that is you are delivering more solutions to your clients around the world. You're expanding in different markets. You're going into new customer segments. And since we are so embedded into their operating processes, next market geographically, or next business segment is a very logical extension of our engagement with our clients.

SUSAN KATZKE: Okay.

NAVEED SULTAN: So once that happens, you see the deposits picking up because operating liquidity is, by definition, what is needed to finance the underlying flows of a client. Then we have been seen continuously gaining more market share, not only with existing clients but of course also with the new age clients. And because of the platform we have, whenever there's a consolidation in the marketplace, there is a natural gravitation towards our platform. So all those, some new solutions of course. New solutions, and the thing is the clients are continuously becoming more sophisticated. They need advice from partners like us to help them navigate an environment which is going through structural shifts. The economies are in transition; finances in transition; globalization is in transition. So if you look at in that context, we are very compatible with how the clients want to do business globally. And we assist them navigating those shifts. That leads to more business and that gives an outcome for our liquidity, for our deposits.

SUSAN KATZKE: Perfect. So you've touched on some of these elements already, but let's talk about the growth strategy with Treasury and Trade Solutions, and maybe talk about how you maintain that market leadership over time and how you maintain this, let's call it mid to high-single-digit growth rate, although I don't think that you would assume that that was a naturally sustainable growth rate for this business.

NAVEED SULTAN: Yeah. Well, like I said, if you think about the nature of a network, it is – I – we talk about it a lot and you sometimes hear a debate in the industry that some synthetic network is going to come and replace these traditional networks. But just to explain what the network is, because it really gives us a very differentiated and a unique position in the marketplace. So the network is really first of all in 98 markets where we have banking licenses. We understand the legal and regulatory jurisdictions. We understand the business environment and risk relating to those markets and we have very close relationship with the regulators and policymakers and we have been a significant participant in those economies. So that's one component of our model.

The second one is that our core technology infrastructure is global and is consistent around the world. On top of that infrastructure, which is really our digital channels, online channels, our payment systems, trade system and things of those – commercial card systems, on top of that we have built a very rich set of functionalities, products as well as our solutions. So that's the third component.

The fourth component is our coverage model. We, in our coverage organization, are organized exactly the way the client is organized. So they are in many, many markets. They have many subsidiaries, many buying centers, regional treasury centers, global treasury centers. So we cover them between our relationship managers and sales people exactly how they are organized and therefore we have very embedded relationships with these buying centers. So having explained the uniqueness of this, that particular network continues to facilitate a greater share of clients' wallets, be it our existing clients or be it new age clients.

In addition to that, if you look at how the digital economy is evolving today, we are also attracting flows from this new breed of Fintech's, which we call aggregators. So what do the aggregators do? They aggregate flows from those customer segments we don't directly do business with. So these could be the consumer bank, consumer clients, it could be small businesses around the world. And then they are looking for a platform to distribute it around the world. And I think what is very important for us to remember is that the globalization is becoming very inclusive. Today, one can produce anything, anywhere and distribute it everywhere using these digital platforms. And therefore, that access to a global platform is very, very important. So we feel very confident.

And then, of course on top of that, we are continuously investing in our innovation, improving the client experience, broadening our product capabilities, operational resilience. So we believe that we are unique; our positioning, we feel good about our positioning, that as the environment evolves, as we go into the future, we will be able to maintain that growth despite the – of course, we will have impacts of the economic headwinds or interest rate volatility, but through the cycle, we believe that our growth rate will be over the GDP growth rates.

SUSAN KATZKE: So let's talk about the competitive landscape a little bit. You're in 98 countries with banking licenses. So it's very hard to replicate the presence that you have had for as long as you have had it. Several banks, and it's a small handful, have a similar infrastructure and capability. But there's always change in the competitive landscape, whether it's new entrants into the treasury services business or otherwise. Can we talk a little bit about what you're seeing there in terms of the competitive landscape?

NAVEED SULTAN: Yeah. I mean clearly, there is a widespread recognition in the market that this is a very attractive business. So you're seeing both traditional and non-traditional players coming into this particular space. And as far as we are concerned, like I made the point in the earlier discussion, that we have a very unique and differentiated position. Our strategy is informed by two things: what the client needs are, and secondly, that we want to be the financial platform for global commerce. If you look at today, how the world is evolving with seven of the top most valuable companies in the world today are platform companies. And we have a unique opportunity because of these assets we have built to make the transition into becoming the financial platform for global commerce. And therefore, we are really making a lot of investments in four areas: client experience, connectivity and data, innovation, and safety soundness and operational resilience. So we believe that our competitive position is strong and we will continue to gain the market share.

Now, if you look at the non-traditional players, the non-traditional players which would really – you think about the Fintechs. The posture of the Fintech on the institutional side has become more collaborative. On the consumer side, it's more competitive because the Fintech on the consumer side think that it's easier to disintermediate the consumer relationships. On the institutional side there is a recognition that the relationships are so embedded, therefore it's very difficult to disintermediate. And particularly in our case, because of relationships' global scale, the Fintechs find our platform very attractive to come and work with us from an operating standpoint. So therefore we work very closely with the Fintechs as partners as well as our clients. In fact, we have built a practice within our financial institution group, what we call Fintech. So as clients we want to facilitate them to grow their business around the world. And as far as the collaboration is concerned, partnerships, we integrate their capabilities into our solutions. They bring new ideas, technology, we have the scale, the trust and client access. So that relationship works exceedingly, exceedingly well. So I think this comparative interest is a confirmation of the opportunity. And we actually find it a very positive motivator to make sure we don't become complacent and we stay ahead of the game.

SUSAN KATZKE: It's interesting when I think about this change in the competitive environment and you talk about it as a catalyst. One of the things that's so attractive about these businesses is that the market is huge, right. It's huge whether you look at just the US version or the global version, and obviously you're looking at the global version. It's massively fragmented. Right? There's very little good data available, but your market share is somewhere between let's call it 5% and 6%. I think JPMorgan told us on Tuesday that theirs was about 6%, which I'm going to assume you're then close to 6%-ish as well. But these market shares haven't really moved; the top three players are all in the 5%, 6%-ish range. And there's only a top three or top five players. What is, in your view, the driver of incremental market share consolidation? Because in every other business you should be looking to be at 2x of market share.

NAVEED SULTAN: I think it's absolutely, it's a great question. So like you said, I think the market is very fragmented. And it depends upon what lens you are using, and it's difficult to estimate. Coalition actually puts our market share around 9%, 9% to 10% considering our revenues last year of $10 billion. So total addressable wallet you can say give and take about $100 billion. That is large corporates, our formally defined target market, but we are not competing in the rest of the market. So this could be a different lens, if you say 5% is much bigger – overall by...

SUSAN KATZKE: I'm using the overall market.

NAVEED SULTAN: Yeah. Overall, yeah, exactly.

SUSAN KATZKE: Right.

NAVEED SULTAN: So no, no, it's a very, very, very good question. So what we believe is that if you look at how the consolidation or how the transition has been happening over the years, in the past, whatever the underlying driver of consolidation, so let's say post financial and economic crisis, we saw many of our peer group retrenching closer to their home markets geographically or they're exiting the related business lines. The natural flow of that business was our platform. So it got consolidated on our platform. That is another very important driver which is not very well understood. Then, the clients – because the trend of efficiency and value creation is secular, that's where the clients are going.

So when they look at the value creation, either on the top-line or becoming more efficient, they start looking at consolidation of some of their activities. So we are the market leaders in supply chain finance, in addition to the overall market leadership and commercial cards. Now, these are fairly recent business lines. So say up till a few years ago, this particular business was allocated by our clients to disparate providers in different geographies around the world. And that obviously is very inefficient. That's fragmented. You have to deal with so many different providers. When they started looking for the benefits of scale, consistency of experience and one single provider, we were the natural beneficiaries. And so they started consolidating their supply chain business with us. They started consolidating their commercial card business with us.

If you look at the – amongst other things, if you look at the impact of digitization and globalization, it's going to go towards consolidation. And by and large, they're looking for a global platform. And as you very well know, that the industry boundaries, industries are converging into ecosystems. So therefore, we believe that our strategy of being the financial platform for global commerce is absolutely the right one. And our in-depth relationships across different segments will allow us to continue to gain the market share, either by consolidation, offering them new solutions as they navigate these changes in the marketplace, and thirdly, to your point which was the right one, that it actually broadens our access to the market beyond that $100 billion. The example I gave of the aggregators, the flows which aggregators bring are not part of our formal defined market. So once, when you are a platform, your ability to access much broader market improves quite considerably. So I think net-net we believe that we are extremely well-positioned, for growth and there are multiple sources of growth, both how we engage with the market traditionally as well as how the new flows are being created, and we believe this platform is in a much better position to service it.

SUSAN KATZKE: And just to clarify here, if we were sitting here 15 or 20 years ago, we would have talked about very high switching costs. Right? I believe that, given where technology is today, the switching costs are far lower. So while relationships are embedded from a human standpoint, the technology to make that switch from one provider to the next, or add another provider to a platform is much easier facilitated today.

NAVEED SULTAN: Again, I think it's a great question because your conventional thinking tend to suggest that the switching cost being high is a good thing. That the inefficiency or how much you get connected with the client and all that. I think the way the world is going, your switching cost is delivered by your quality of your client experience. The technology allows you to switch very quickly. I mean, if you look at different cab services providers or transport services providers, you can switch just by clicking a few icons on your smartphone. But what keeps you with one particular provider is the quality of the experience they give you. And I think that's exactly what our strategy is. So we are making a huge amount of investment into improving the client experience.

So I'll just give you one example. In the traditional lens which was like the switching cost, and it's a very pertinent point because it will take about two, two-and-half months to open an account of a client or onboard it. So if you think about it, it is a very high switching cost. So if a client has already a relationship with you and saying, well if a new client, new bank, it will take me another two, two-and-half months to open an account. Yes, fine. These guys are not perfect, but the switching cost is very high. I don't want to switch. We have reduced that down to 48 hours.

It's all digital. It's live in 34 markets because we believe that you've got to keep the client with yourself through delivering economic value and if you're scalable, you have a great client experience, very easy.

The opposite of very easy connectivity is that you can also very easily leave. Right? So if you have those attributes, we believe actually in our case the sources of value get very diversified. Because you're attracting all the flows, it's very easy to do business with, your marginal cost is approaching zero because it's very scalable. And then you're offering not only your own proprietary solutions, third party solutions are also coming onto your platform, and therefore I think your ability to continue to grow, it's basically reflecting all the attributes of a platform business model, as we see it in the industry today.

SUSAN KATZKE: So if I connect a few dots here, at the beginning of our conversation we talked about not just growth but consistent pre-tax margin improvement, and the amount of technology investment it sounds like you've made in the business to be down to onboarding a client in 48 hours. If I tie these things together it would indicate to me that you've invested pretty aggressively in the operating infrastructure of the business to reduce the marginal cost, the unit operating cost of transacting. How much is it about reducing – tie together for me maybe the benefit of reducing the unit operating costs as well as – that seems to be what's translating to better customer service and it's really very tightly married together.

NAVEED SULTAN: Absolutely. You're absolutely right. So like I said, if you are executing that particular strategy and when you're making investments in improving the client experience, reducing the redundancies, friction points, your marginal unit cost is reducing and that is an outcome of the fact that you are taking out the redundancies. You are taking out the friction points vis-à-vis the clients and that in turn gives the clients incentive to direct more flows into your platform because they're so easy, it's a great experience. And of course if your marginal cost is approaching zero over a period of time, you also have – and part of that, you can always pass it on to your clients based on, that's an economic decision you have to make, but you have the flexibility to pass part of that on to your clients.

So it's a very interesting dynamic that you improve your unit cost, you take out the friction, you make it a lot easier for clients to do business with you. On the other side, it starts building the scale and it creates that virtuous cycle of more scale and more volumes, reduce the marginal cost, economic incentive flowing back to the client, more volumes coming through. And then of course, you're always adding new innovations. You're bringing in technology from your partners.

So I gave you two examples recently; HighRadius which is one of our Fintech partners. We have also taken an equity position. They use machine learning and artificial intelligence and natural language processing to solve one of the big pain points in the industry. And that is essentially when a payment comes in, how you reconcile with the receivable side. And that has been one of the big pain points. We launched that within a span of about three to six months in the partnership.

So the reason I'm highlighting that is that it's not just the scale and the marginal cost. We're also adding more products, more solutions, proprietary or third party and that is exactly the characteristics of a platform, that the interaction of the those four continues to create non-linear growth. So we are in this transition right now, but we are very excited about the prospects of the platform we have.

SUSAN KATZKE: And so, let's just talk about data on that platform for a minute because data and analytics and artificial intelligence are all taking the – not just your unit operating costs down but also providing value added to the customer. So let's talk about for a minute how it is that you're harnessing the data that's available to you across Citi for both Citi and for the clients.

NAVEED SULTAN: Yeah. A lot has been said about data and one expression which I find very interesting is that data is the oil of 21st century. And we generally believe that the generation, management and monetization of data in a systematic manner at the institutional level is going to create a very significant differentiation. And our approach is that when these new technologies come in, we don't want to deal – engage with these technologies on the periphery of how we do business with it today. We want to fundamentally rethink how we do business so that we can leverage the full outcome of these technologies.

So what we have done is in data, we're making a lot of investments into the underlying infrastructure of organizing the data so that it is accessible and we can drive client insights out of it. In TTS, we have created four horizontals, and one of the horizontals is data. What does a horizontal mean? Some of these technologies don't lend themselves to vertical organization because they cut across your different business lines. So this data horizontal cuts across products, geographies and customer segments, so that we can build the right infrastructure and the relevant. So our investment is driven by that we are embedding data in all our solutions and products, as well as the client journey with us.

So I'll give you two, three examples really to make it real for you. So when we start engaging with a client in terms of developing a solution or helping them solve a pain point, we analyze their data, we model it, we benchmark it based on several variables which the client give us: how they're organized around the world; what is the legal regulatory jurisdictions, foreign exchange restrictions; where they want long liquidity, where they want short liquidity. All the rest of it. So it's actually hundreds of variables. So we put all of those into our model and then we create the best possible outcome which can be actually, and this interactive on digital, front end and you can sit in front of a client and keep moving until the client thinks, I think this is the optimum outcome.

So that is when you start creating a solution. When you bring the client on board, the Know Your Customer compliance requirements, as well as opening the account, entitling the products, we look at all our internal data. We go to third party sources and get information relating to the company. And then we ask the client minimal questions in terms of additional information so that we don't cause inconvenience, and that has one of the drivers why we have reduced it down to 48 hours.

Once the client is onboard, start doing business, we use biometrics, we use artificial intelligence, obviously exploiting the data to fraud prevention, giving them the best possible execution, reconciliation as well as financing utilization and predicting the liquidity flow.

And fourthly, once they are in a BAU environment with us doing business, our exploitation of data, usage of data, we keep proactively giving them suggestions that this particular geography has made these changes in the regulation. Your company has done this particular acquisition. Or even if you're staying with your current structure, we believe that if you organize this particular way, you have a better outcome for your liquidity and for your assets. And particularly these days as we know the global supply chains are shifting for different reasons.

So the clients are looking at their operational footprint again. They are looking at how the new supply chains are going to look like. So our knowledge of the market, deep understanding of the local rules and regulations coupled with the understanding of the client, we proactively give them recommendations based on data. So as you can see, we are embedding data in a very thoughtful manner in the client journey with us in every step. And we believe that is the right way to do it as opposed to just have a peripheral approach to data which superimposes on your current operating environment which may or may not be compatible. And by the way, that is true for other technologies as well.

SUSAN KATZKE: That seems to me as one more element of kind of completing and accelerating the journey around the virtuous cycle.

NAVEED SULTAN: Yes.

SUSAN KATZKE: In this business.

NAVEED SULTAN: Absolutely.

SUSAN KATZKE: Okay. So I'm at zero on the clock. If I have you back in three years, let's see another 35% growth. I know that's a little bit difficult to do, but we do look forward to watching your growth outpace GDP growth.

NAVEED SULTAN: No, no, absolutely, and I think – I can't put a number out there, but we are very, very excited about the prospect of this. And the way to look at this business is in the context of financial platform for global commerce. The world is increasingly becoming global despite the geopolitics, trade tensions and tariffs. And I think some of these global changes and structural shifts go unnoticed because of these headlines. But fundamentally, the global supply chains are becoming more knowledge intensive, more services intensive. Only 18% of the global trade today is driven by cost arbitrage. And there are many other factors at play. So the point I'm making is that every client of ours, because of our global experience and deep relationships into those markets, wants to have our advice and insights into how they rethink and navigate in this changing world. And that's we believe is what offers us an exciting opportunity as we move forward.

SUSAN KATZKE: Thank you.

NAVEED SULTAN: Thank you, Susan. It's always a pleasure to be here.

SUSAN KATZKE: Thank you. Citi will be available for a breakout session in I believe it's the Plaza 1 Room to the right.

NAVEED SULTAN: Thank you so much.

SUSAN KATZKE: Thank you.