TRANSCRIPT

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HOST
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SPEAKER
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QUESTION AND ANSWER

BETSY GRASECK: Thanks everybody for joining us this afternoon. I have a disclosure to read and then we'll kick off. For important disclosures, please see Morgan Stanley research disclosure website at www.morganstanley.com/researchdisclosures. If you have any questions, please reach out to your Morgan Stanley sales representative.

With that, I'm pleased to have with us this afternoon Mark Mason, CFO of Citigroup. Mark, thanks so much for joining us this afternoon.

MARK MASON: Thank you, Betsy. Great to see you. Great to be here.

BETSY GRASECK: So, there's a couple of different questions I wanted to kick off on. The first one has to do with your global footprint, and really these are strategic questions for Citi. I notice your globe in the background, so it's a good prompt here for me. But could you give us some color on what you're hearing from clients and what you're seeing from a macro perspective around the world? You're one of our truly global organizations at the US Fins Conference. So would appreciate your color on that.

MARK MASON: Sure. Sure. And hopefully next year we can do this in person, but as I mentioned great to be here. And look, I think that – I think we can all agree that we're in a very different place this year than we were last year and we're thankful for that. Now, when I think about where we are as a global economy, much of that is driven by the significant take-up that we've seen as it relates to vaccinations here in the US and increasingly so more broadly.

When I look at this recovery, it's being led largely by the US and China. And when I look at the US in particular, things like the stimulus have proven to be key. When I look at the prospect of infrastructure and dollars or spend around that, that seems to provide some promise for longer term continued recovery. When I think about the conversations that we're having around inflation, whether that's transitory or not, the levers that the Fed has to manage that – even talk of tapering. All of those things kind of speak to the strength, if you will, of the recovery that we're seeing here in the US.

When you look at China, that seems to be consumer-led as well. There is some concern around overheating there. You look at Europe, and while that's a bit delayed, it does not appear to be derailed. Emerging markets has some fits and starts. We've seen some increases in terms of cases there. When you look around the world, there does seem to be some path to recovery, which is promising.

You asked about corporate clients. The corporate clients that we spend time with, it varies by sector in terms of the sentiment. But overall, I'd say there are some general optimism there. There remains a lot of liquidity in the market. Balance sheets are strong. Most of our clients are either in the midst of a transformation or certainly considering a transformation. And that's not that surprising when you look at digitization and the impact that that had on many of these sectors. When you look at even going direct to consumers as companies contemplate that. When you look at how supply chains have to be reconsidered or even changes in demand, it's no wonder that many of our clients are talking, as I mentioned, about a transformation or how they rethink their business model.

I mentioned it's been a consumer-led recovery, and you can see that in spend levels. Spend levels have increased across our Cards portfolios for example. You could also see that in higher payment rates as there remains a lot of liquidity with our consumers, higher savings rates, again, a byproduct of the stimulus that we've seen kind of play into these economies.

And so, again, the promising thing here is that there seems to be a path, and we're on it, and I think that's promising.

BETSY GRASECK: Great. Okay. Thank you for that. Before I dig into some of the key topics for Citi like the strategy work that you're doing, I just did want to get a sense from you as to what the key trends are that you're seeing for this quarter, 2Q'21. Maybe you can give us an update on the guidance that you laid out during the earnings call.

MARK MASON: Sure. So, again, I kind of hearken back to where I've started which is very different place than we were a year ago. If you think back to the second quarter of 2020, at least for Citi, we were looking at Markets revenues back then that were up 50%. We had seen record levels of debt issuances from our clients. We ourselves took down expenses pretty meaningfully in the second quarter last year in light of going remote and the shutdown.

Fast forward to where we are today in the second quarter and there's still a quarter left – when I look at our Markets business and I look at revenues for fixed income and equities, revenues are likely to be down in the 30s percent range – low 30s percent range. Again, a mix of continued strong performance in equities, offset by fixed income in light of the strong prior-year fixed income performance, as I alluded to earlier, so down in the low 30s percent or so for Q2.

When I look at Investment Banking, Investment Banking revenues are likely to be down in the mid-to-high single-digit range. We do see strong M&A performance, and we do feel good about the pipeline and the dialogue that we're having in Investment Banking.

If I think about our North America consumer business, again, here, and I alluded to it earlier, the good news is that we are seeing good purchase sale activity. We're also seeing continued high payment rates, and that's putting pressure on our ANR, on the lending volumes. When I look at revenues for the quarter for North America consumer, likely to be down at similar level to what they were in the first quarter in terms of the year-over-year performance.

Expenses. I think there's a range out there now; I think the Street expectation is roughly about $11.2 billion. Betsy, I think you have us at about $11.6 billion. I think we'll end up probably somewhere in the middle of that range. And when I look through that, again, last year this time, we took expenses down pretty meaningfully, but we also, as you know, have spend that we're making in the way of transformation. We've also continued to invest strategically. Areas like Wealth, areas like Investment Banking, areas like our TTS franchise we continue to invest in. And so, expense is kind of in the middle of that range, if you will.

And then, lastly, cost of credit. And the trends that we're seeing in terms of delinquencies continue to be very stable. I'd expect our cost of credit to be relatively benign. And I am expecting a release in the quarter, but not at the level – probably less than what we saw last quarter. So that gives you a little bit of a sense of how we're thinking about it thus far. Like I said, still some quarter left, but that's kind of where we are currently.

BETSY GRASECK: Okay. All right. Great. That's very clear. So, appreciate that color and context, Mark.

MARK MASON: Sure.

BETSY GRASECK: Let's dig in to the strategy refresh that you are in the middle of doing. And I did want to kick off on the TTS business. We have been doing some work on TTS here at Morgan Stanley, and we are looking at what we believe is a very high ROE business.

You have strong share. You've got a great franchise. You've got superior scale. It is a fragmented business though. So maybe you can help us understand is there opportunity for additional share consolidation? What kind of share are you targeting? And then maybe we can get into some of the technology investment spend you're doing here and how you're competing with fintechs?

MARK MASON: TTS, so this is a core part of our franchise without question. And as you know, when I think of – when we look at this franchise, it is a servicing platform and model for our large multinational clients. What do I mean by that? This TTS franchise, we provide integrated working capital solutions that include payments, receivables, liquidity management, corporate commercial cards, as well as trade lending to large multinational clients. We also service large financial institutions. We cover 80% of the Fortune 500 corporate clients. We cover public sector clients. And we also cover kind of new digital economy clients.

And we're able to do that because we are uniquely positioned with a presence in nearly 100 countries. And not only do we have a presence there and expertise there, but we're connected to over 250 clearing centers and we're able to transact with our clients in over 145 currencies. And in many ways, that uniquely positions us, not just to continue to grow with these large multinational clients, but also to more deeply penetrate their wallets and the wallets of commercial and middle-market clients. And that is in fact what we're doing. That is in fact why we're investing in this part of the franchise.

And so what are we investing in? We're investing in our digital capabilities. And frankly, we've been doing that for a number of years now, and that has played to our benefit through this crisis. We're now able to do digital onboarding with clients in over 50 countries. We're also investing in our instant payment capabilities. We're able to offer that in 27 markets and that'll increase by another eight markets by the end of the year. And so, there's significant opportunity to do more with clients, significant investment being made in our capabilities.

You mentioned fintech and you mentioned, kind of, share consolidation. I'll talk about share first. We've got a very solid share in a fragmented market with our multinational clients. And we expect that we will be able to grow that in part because of how we're seeing this market shift towards demand for more digital capabilities, towards the ability to actually go direct to consumers. And I believe that the investments that we're making will allow us to win some of those additional opportunities as clients migrate there. And some of the larger players I think will fare best on the other side of that.

When I think about fintechs, I think about three buckets so to speak. So, one is partner. So think partner, client, competitor. And for us, we end up dealing with fintechs largely in the first two buckets. And so, when I think about partnering capabilities – particularly for our large multinational clients who want to do business with the larger providers such as us – fintechs serve as partners for us to expand the capabilities of our solutions.

And so, you've heard me talk about in the past how we've worked with corporate clients to help them better understand how they can manage and mine their receivables and reconcile those receivables. We've done that in partnership with fintechs who provide those capabilities that we can add on to our solutions. We also see fintechs as clients, particularly when we are dealing with digital economy clients. Fintechs actually leverage our rails in order to bring their solutions to bear to some of the segments that they cover. And then competitors less so, but I don't want to dismiss fintech as competitors. Fintechs certainly inspire us, if you will, to stay on top of our investments and expanding our capabilities.

And so this, again, core part of our franchise, large business, over $9 billion in revenues, very good margin, low capital intensity, high returning. Jane talks about strategy refresh. This is going to continue to be a focal point for us.

BETSY GRASECK: And I estimated that the RoTCE in this business is somewhere in the mid-30s. Does that sound in the ballpark to you?

MARK MASON: In a normal environment, roughly in that range. I think we talked about a couple of years ago being significantly higher than the 20s. But in a normal environment, roughly in that range.

BETSY GRASECK: And so, a normal environment, meaning a higher interest rate environment?

MARK MASON: Rate environment. Exactly. Yeah.

BETSY GRASECK: Okay. Got it. So, if rates do pack up – back up like 100 bps, I know that sounds like a lot in this world, but we would see it in this business line.

MARK MASON: Certainly, some upside for this business. Remember, this is a business that has over $600 billion of deposits around – globally. And so, yes, we would see some upside with an improved rate environment.

BETSY GRASECK: Okay. So let's turn to wealth management. That is another sleeve that I know Citi is increasing its investment spend in. Could you give us a sense as to how you're focusing on the growth opportunities here? There's geography. There's segment. There's client type. Maybe give us a sense as to how you're prioritizing among those opportunity sets.

MARK MASON: Sure. So wealth is a core segment for us. And I think the first thing I'd point out, Betsy, is that one of the first things that we did as Jane announced was we rethought the structure around how we wanted to cover this client segment. And so, we brought together the private bank with the wealth activity that we have in the consumer part of the franchise. And in many ways creating that combined segment, if you will, ensure that we're able to leverage the products, the services, the platform that we have in getting after this market. And so that was a very important step.

You would have heard earlier this quarter that we announced the management team to support that new structure. And we believe that there's significant opportunity globally but specifically in the US and in Asia. And you've heard us talk specifically about getting after the Asia wealth opportunity. You can look back over the past – the last 20 years or so, we've seen that market grow from $5 trillion to $42 trillion. Big opportunity for us. We've got a very strong brand in that market already.

When you look at the US, over the next 15 years or so, we would expect some $25 trillion of wealth to change hands. Again, we believe we're well-positioned to get after that given the platform that we have, and we're investing in the platform. And what does that look like? So, in Asia, we've hired some 400 relationship managers between July of last year and where we are today. We're continuing to invest in front-end hiring and bankers both here in the US and around the world. And those types of capabilities are what we believe is important in order to get after this in earnest.

BETSY GRASECK: So, when you think about the opportunity set between where you are today and where you'd like to be, how much of that investment spend have you done already and what's left to come in the run rate?

MARK MASON: Yeah. Look, we're working through that as part of the refresh. But we're not waiting, right? So, we've got a new management team that we've put to this business. They're working on fleshing out what the multi-year plan looks like as part of this refresh that Jane and I are driving. And on the other end of that will be, I'm sure, a continued need for investments. But we've started to make it already and we'll continue to make it kind of through the balance of the year and next in support of that strategy as it comes together.

BETSY GRASECK: And is it fair to say that of the investments you've made already, are you beginning to see some results with regard to the revenue?

MARK MASON: Look, we're very optimistic about it. I mean that's – we are managing out of this crisis and into a recovery, but we're very optimistic about it. We've proven the capabilities here as it relates to bringing on new private bankers or bringing on new relationship managers and then building out their client set. This is, in some ways – in that regard, this is not new territory for us. And so, we feel very good about the investments that we've made, thus far, and that they're going to pay off for us.

BETSY GRASECK: Okay. So, on the flip side, you announced Citi is going to be exiting consumer operations. I believe it's in about 13 markets in Asia and EMEA. The question is how did you determine what to exit? And can you give us a sense of any updates on timing and how shareholders should be benefiting from this move?

MARK MASON: Sure. So, look, in many ways, strategy is as much about what you decide you're going to do as it is about what you decide you're not going to do. And as you've heard, Jane described and I've described in other forums, we've taken a very clinical approach to this strategy refresh. We've looked at businesses where we have a competitive advantage where we think we can win, where we've got scale that will drive growth and returns across the franchise. And as we look at these 13 markets, while they are good businesses, we don't have scale in them. And in many ways, they'll be better businesses for other owners.

And so we took the decision and feel very good about the decision. And we've had very active dialogue to date with potential buyers. We've got investment memorandums that are out there for consideration. I'd expect that we'll be hearing back from potential buyers over the next month or so, and then we'll continue down a path of execution accordingly from that point on.

What should shareholders expect? Look, I think that this is a path towards a simpler Citi in some regards. And so that is a good thing, a more focused organization strategically. I think, obviously, this is an opportunity to free up capital and resources and freeing up the capital and resources allows for us to deploy it in areas where we think there's more growth. We've talked about wealth. We've talked about commercial. We've talked about TTS, but also an opportunity where there is excess capital to return that to shareholders. And so I think from a shareholder point of view, these types of strategic decisions over time are upside, without question.

BETSY GRASECK: And I did get a question in on this well, it appears you've decided to keep Mexico. And the question is why did the Mexico consumer business stay in the pack as opposed to be on the side of the ledger for exit?

MARK MASON: Yeah. I guess Mexico has come up from time to time over the years, huh?

BETSY GRASECK: Yeah.

MARK MASON: Look, I think that when you look at it think about some of the things that I referenced, the importance of scale, places where we have a competitive advantage. You take a step back, I mean, Mexico in many ways, there's a more positive outlook on how that economy is going to turn. GDP estimates have gone up to 5% or so for Mexico. They've got a labor advantage that's there as clients start to reconsider supply chains. That could certainly play to the advantage of Mexico as the US drives this recovery, that could certainly play to the advantage there, so some broader market positive implications potentially over time for Mexico.

And then we've got Citibanamex. We've got a leading market franchise in Mexico that's of scale, that is high returning. We also have – and we've made investments there in terms of our capabilities. We're seeing growth digitally and mobily with customers there. And we've got – it's integral to the broader corporate network. And so there are a lot of positives as it relates to Mexico and we're optimistic about it over time. But those were certainly factors that went into the refresh as we continue to go through it or make the refresh.

BETSY GRASECK: So as we think about the operating leverage that you could get from Mexico, do you anticipate that would be coming more from the revenue side of the equation or the expense side of the equation?

MARK MASON: Again, we're managing kind of out of this, as we speak. And so I think that as the recovery unfolds, we'll see some upside on the top line. But we'll see how things kind of play out.

BETSY GRASECK: Okay, great. So there's a next theme I wanted to dig into was the consumer a little bit more. And before I do that, I did get a couple of questions to ask you to repeat what the outlook is for the guidance on consumer. I guess there were some questions here on what exactly you mentioned. Could you repeat that please?

MARK MASON: Yeah, sure. So I was – I gave guidance with regard to North America consumer. And what I mentioned was that in light of kind of the way things are evolving through the quarter in terms of purchase sales versus payment rates and loan volumes, et cetera, that we'd likely see consumer revenues that are down year over year at a similar level perhaps a little bit better than what we saw in the first quarter. First quarter, I think, was down some 15% or so year over year, so similar levels, maybe a little bit better in terms of second quarter year-over-year performance.

BETSY GRASECK: And is that primarily a function of the payment rate that you're seeing in your card books, or what's driving that?

MARK MASON: Yeah. So again, if you kind of just – as things have kind of played through this crisis, there's been significant pressure on the volumes, on lending volumes. And so again, while we are seeing good purchase sale activity, and in fact, in some ways purchase sales are back to pre-COVID levels. We are also seeing continued high payment rates. So yes, Betsy, and those continued high payment rates are in part a byproduct of all the liquidity that's still in the market, as we've seen the stimulus kind of take hold. And so that is continuing to put pressure on the volumes, on the ANR that we see across the portfolio, and therefore you see that in the top line revenues.

BETSY GRASECK: And when you think about how your portfolios are operating, you've got the branded card, you've got the retail partner card side, any differences there with regard to either spend levels or payment rate levels, any differences in behavior?

MARK MASON: Yeah. So, look, I mean, in terms of both of the card portfolios, we are seeing spending levels as of end of March back to kind of pre-COVID levels, and that has continued to play through, which is a good thing. They are different portfolios, obviously, right. The Retail Services portfolio tends to be more partner driven. And so the nature of the sectors that your partners are in are an important factor. But we are seeing, like I said, solid spend levels across both and similarly continued high payment rates; albeit, they'll be different for branded cards versus retail services.

BETSY GRASECK: How do you think about the loan growth opportunities here, when are you thinking or seeing signs of inflecting positively in cards, specifically?

MARK MASON: Yeah. So, again, we're expecting that we will see loan growth start to pick up in the second half of 2021. But again, we're seeing this dynamic kind of play through as a result of the stimulus. But our estimates right now are that we'll see that pick up in the back half of the year.

BETSY GRASECK: And what about the credit box, where are you on the credit box with not only card but your other consumer offerings? And is there any room to widen that? Would that make a difference?

MARK MASON: Yeah. Look, I mean, the important thing I think for us is that we kind of open back up the spigot, so to speak, in a timely fashion. And so we've started to do that. We don't want to make the mistake of being late to kind of go out and start to acquire new customers again or extend credit where that makes sense inside of our credit boxes. So we've started to do that very proactively, and that's part of the spend level that you see flowing through our expense line.

We are – at some point, we'll be kind of back to the levels that we were pre-COVID in terms of where we are against our existing credit box. But we have not, at this point, kind of looked to expand our risk profile in any way. We're sticking to the risk profile that we've set for the Consumer segment and really just trying to ensure that we get after it as the recovery is unfolding, and that's what we're doing.

BETSY GRASECK: Okay, great. So then on to the topic of Macy's. I'm sure you know there was – in the Macy's 10-K or 10-Q or 8-K, one of those, a notice that you had indicated to them that you sent them a notice of cancellation on the retail partner card relationship that you have. Maybe you could help us understand how you think through that type of decisioning because from an investor perspective, it feels like this is a high ROA business, maybe 2 to 3 percentage points, and it's a little bit of a head-scratcher why you would opt to potentially indicate lack of interest in that book.

MARK MASON: Yeah. So, look, I mean, as I said earlier, the Retail Services business is a partner relationship, and we've been a partner with Macy's for 16 years. And as they stated and you referenced in their recent 10-K, I think it was in March, they referenced that they saw their retail sales levels decline and declined to a level where they triggered a termination clause as part of our contract. In order to preserve our contractual rights, we issued a notice of termination to them while we continue to have a dialogue and conversations around a path that's optimal for both parties. And so that's what we're doing. We're actively engaged with them.

As I think about the Retail Services business, we feel very good about it. It is a core part of our Consumer business, if you will. It is high returning both on an ROA basis and both – and also on an RoTCE basis. And we'll continue to look for opportunities that make good economic sense with strong partners in the retail services space. The conversations we're having with Macy's, like I said, are ongoing. There's no impact to the customers as a result of any action that we've taken at this time and we'll keep you posted as appropriate on how that evolves.

BETSY GRASECK: Okay. The termination – you were required by the contract to move forward with that in order to have the negotiation with them. Is that how I'm – that's what I'm hearing from you, is that accurate?

MARK MASON: No, what I'm saying is that in order to kind of protect our contractual right, so we have – obviously, when that trigger is hit, we have the ability to issue the notice and we took advantage of the ability to issue the notice, but we are continuing the dialogue and discussions with them.

BETSY GRASECK: Okay, great. Moving on to the institutional side, you mostly bank large multinationals, the capital markets are wide open. Large corporates have significant amount of surplus cash. Is there an opportunity there for loan growth eventually, or are you moving on to other areas to drive loan growth?

MARK MASON: Yeah. I – given the liquidity that's in the market and all the debt issuance activity that we saw last year I'm not expecting corporate loan growth. We, obviously, are here to serve our clients and we'll continue to do so with the episodic activity and demands that they have. But I don't expect significant loan growth in the balance of the year on the corporate side. That said, we are seeing more broadly opportunities as it relates to trade and in markets and in the private bank. And we'll continue to – and I mentioned earlier consumer expecting that on the back half, but not on the corporate side at this stage.

BETSY GRASECK: And it seems like you have some more room in your GSIB surcharge bucket to add more risk in markets and trading and that type of thing. Is that a fair statement?

MARK MASON: Yeah. It's interesting, as you point out for many of us in the industry with the increase in deposits, we've seen kind of the GSIB score take off, and in some instances into the next bucket. As you know, there are a number of different factors that influence capital, not just your GSIB score, but the stress capital buffer and risk-weighted assets and all of those things, and so number of different factors there. We're looking at capacity and in alignment with our strategy refresh. So, where does it make sense to allocate capital that's consistent with our desire to improve our returns and narrow the gap to peers. And we're doing just that.

In the case of very specifically fixed income and equities that you point out, we're looking to make ensure we're optimizing the capital that we have allocated there already and doing that in a way that's consistent with the client demand and opportunities that are available to us. And so not necessarily looking to allocate more, but certainly looking to make sure that we're optimizing what we've allocated thus far.

BETSY GRASECK: Okay. Two quick last questions here in the moments we have left. One is just a question from the audience on the expenses. Some people interpreted the expense commentary that you gave for 2Q 2021 to be a little bit of an uptick since it's, I believe, between 11.2% and 11.6%. And so should we take that into the back half of the year as well? The basic question here is, is there a change in the outlook for full year 2021 expenses?

MARK MASON: Yeah. So I'm not changing my guidance for the full year at this point. We'll obviously have another opportunity to get together at earnings, and as we continue to flesh out plans and what have you. So, not giving full year guidance at this point.

BETSY GRASECK: Okay. And then just on the capital return question, the SCB, obviously, is coming soon in a couple of weeks. How should we be thinking about how flexible you can be when the SCB goes into place?

MARK MASON: Yeah. So, look, I think the thing I – I'd point out a couple of things. One is better place than we were last year, right. We were able to start doing buybacks earlier this year. We certainly took advantage of that in the first quarter at the – and did buybacks to the capacity we were allowed to do so. We're able to do that, again, in the second quarter, we're out taking advantage of that capacity as well this quarter. As I look about the go-forward, as you mentioned, the stress capital buffer will be an important factor. We'll see what comes out of the most recent CCAR analysis. But assuming that that's consistent, we'll be operating in a way that is aligned with the CET1 target that we've set for ourselves, so the 11.5%. As of the last quarter, we were at an 11.8%. So there's capacity there, obviously. And we would operate in accordance with that going forward.

I would point out that over time, it would be my intention to continue to take a look at the CET1 target we have of 11.5% and look for opportunities to bring that down/operate inside of a range.

BETSY GRASECK: Okay, great.

MARK MASON: The ability to return capital is, obviously, driven by the income we generate, the utilization of the DTA. And our objective would be to put capital to work where we can generate returns that make good sense and anything that was excess to return it to shareholders.

BETSY GRASECK: And relative to the dividend, how do you think about the buybacks versus dividend?

MARK MASON: Well, look, I mean we obviously want to ensure that we're taking advantage of where we're trading relative to book. And so where it makes sense to do that, we will. We, obviously, know that there are investors who get a lot of value out of the dividend as well. And so we want to make sure that we protect their interests, too. And so doing – trying to balance that would be something we'll continue to do.

BETSY GRASECK: Great. Okay. Mark, thank you so much for your time today. Really appreciate it.

MARK MASON: Betsy, thank you. Good to see you.