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HOST
Richard Ramsden, Goldman Sachs Analyst

SPEAKER
Mark Mason, Citi Chief Financial Officer

QUESTION AND ANSWER

RICHARD RAMSDEN: Okay. So, I think we're going to start with the next presenter. We're very excited to have Mark Mason, who is the Chief Financial Officer at Citigroup. Mark has been with Citi for 19 years. And prior to being named CFO three years ago, he was the CFO of ICG. And previously, he ran the Private Bank and Citi Holdings. This is, I think, the third consecutive year that Mark has presented at this conference, and we're delighted that you can join us again.

MARK MASON: Thank you, Richard. It's great to see you. I'm sorry I'm not there with you, but it's great to see you.

RICHARD RAMSDEN: It's good to see you as well. So, Mark, maybe we can just start off with your assessment of the macro environment. And I know, look, you have a unique footprint. It gives you a unique insight into the global growth picture. And I know there's still a lot of unknowns but can you just start with the assessment of the health of the key markets you operate in? And talk a little bit about your expectations for economic growth in those regions heading into 2022.

MARK MASON: Sure. Richard, I get asked that question somewhat often and I have to start it the same way certainly over the past number of quarters, and that is that we're in a much better place than we were just a year ago. And I think you can probably attest to that through nearly every lens that you look at.

When I think about the corporate clients and the consumer clients that we have and that we serve, I would say they, too, have demonstrated, I think, a pretty meaningful pace through the recovery. When I look at the corporate client base, the balance sheets are very strong. We have very good pipelines in terms of transactions and activities. We have very rich dialogue with the corporate client base. They're looking at M&A activity. They're looking at putting more CapEx to work. They're looking at investing in digital capabilities.

All of those things are at the core, there's lots of liquidity on both the corporate and the consumer sides. When I think about the dialogue we've been having with them as of late, a lot of discussion around supply chains, a lot of discussion around unanticipated demand and the shortage of inputs required to meet that demand. As you would imagine, we're talking a lot about inflation and the impact of inflation on the input costs and whether that plays out from price or not, what happens with monetary policy to address that over the next 12 months, so, a lot of rich dialogue around that.

When I talk to consumers and look at the performance in our business on the consumer side, again, still seeing deposit growth, seeing good spend activity through the quarter. We had a healthy month of November. But we're also seeing continued high payment rates. And with that, we're seeing very good credit performance and low delinquencies play out.

And so, when we look at those dynamics again, I think it shows good signs of continued recovery. When I step back and think about the things that we have on watch, we're certainly watching the broader macro, we're watching inflation, as I mentioned earlier, we're watching how supply chains evolve, and we're a critical part of that dialogue with our clients.

We're watching China. And what that means more broadly in terms of its potential slowdown, but also what happens as it relates to supply chains there. And then more recently, we're all talking about the recent COVID variant. And in fact, that is a big part of what we're watching over the next number of weeks to see how that plays out, so net-net I think a good pace to recovery thus far, but a number of things that we're keeping at the fore.

RICHARD RAMSDEN: Yeah. So, before we start talking about strategy and go through some of the business lines in more detail, maybe we can just talk about the current environment. Maybe you can talk a little bit about the overall outlook for the fourth quarter, and maybe you can touch on net interest income, capital markets, expenses and credit and how those are shaping up relative to what you thought when you reported back in October.

MARK MASON: Sure. So, let me start with just touching on the full year outlook. So, I'd given some guidance around the full year outlook, and I think I'd start by saying that we expect that to play out consistent with the guidance that I've given. So, what does that mean? On the top line I talked about revenues being down in the mid-single-digit range when you adjust – or adjusted for the divestitures that we have coming out of Asia, I expect that to play through.

We continue to see good fee revenue growth across our ICG businesses. That's offsetting some of the pressure that we're seeing in markets. And so, feel good about that guidance.

On the expense side, I've talked about expenses being up in the mid-single-digit range, again excluding divestitures and the impact of those Asia exits. I still expect more expenses to play out in that fashion as well, with a mix of that being, obviously, transformation expenses, as well as business-led investments that we've been making.

When I look at the fourth quarter, specifically, and I look at kind of the consumer business, we are seeing consumer revenues pick up a bit, certainly sequentially. They'll likely still be down in the mid-single range year-over-year. When I think about our markets revenues we're seeing the normalization that we were expecting in fixed income play through.

We're also seeing pressure from just the trading environment. But that's being offset in part by some of the strong equities performance that continues. And so, when I look at trading quarter-to-date in the fourth quarter, trading revenues are down modestly to the fourth quarter of 2019. Think about 2019 as being a more normal year. And I would expect that for the full fourth quarter that trading revenues play out in the same way, so, flat to modestly down versus 2019 for the fourth quarter.

Next point, expenses in the quarter, expenses in the quarter will be impacted by the market exits. In particular, as you know, we announced the wind down of our Korea business, our Korea consumer banking business. And I would expect that we incur in the quarter somewhere around $1.2 billion of expenses related to the Asia divestitures, with the vast majority of that being associated with that Korea consumer banking line now.

RICHARD RAMSDEN: Got it. Okay. That's helpful. So, let's talk a little bit about strategy. You've talked about both the strategic refresh and the transformation happening in parallel. So, can you just remind us of the priorities and goals of the strategic refresh? Talk about the progress that perhaps you've made to-date, and then also perhaps talk about what we should expect from here in terms of updates?

MARK MASON: Sure. So, I'd start by saying, both Jane and I have been spending a lot of time with investors and with our shareholders, and our goal is to ensure that we have a simpler, less complex business company that is able to take advantage of the competitive strengths that we have and focus on some of the key areas of growth.

And the actions that we've taken to-date, as you've started to allude to, really reflect three priorities. So, one, the transformation; two, the strategy refresh; and the third that you've heard us talk about is the importance of culture and talent.

Now, Richard, on March 2nd, we're going to have an opportunity to have an Investor Day. And I think that's an important – a very important date for us. It's going to be an opportunity to bring all of these things together. And to articulate the vision for the firm, to articulate not only the strategy, but specifics around each of the core businesses that we are going to focus on, to articulate the key performance metrics that we're holding ourselves accountable to, and to give our investors a sense for how we want to run and manage the company. So, we're very much looking forward to that. That is, I think, the next important meaningful update around how all of these things come together.

Around transformation, you know Richard, that in the third quarter, we actually submitted our plans to both regulators around the transformation effort that's underway and specifically around the consent order items that needed to be addressed. We have now pivoted to execution, and we continue to make, I think, very good progress in terms of investing in our risk and controls, in terms of standing up the governance model around such a large body of work that we have here. And so, we're continuing to progress that.

On the strategy refresh, you've heard us talk about a number of things over the past number of quarters. And so, we've talked about services and the ICG and specifically our TTS business, our security services business, and we've continued to invest in client onboarding. We've continued to invest in our digital capabilities on both of those platforms. And I think we're making continued good progress there.

You've heard us talk about wealth, and you've heard us – we've been investing in wealth as well. In fact, we have onboarded some 500 bankers and advisors and investment consultants across both the private bank and our consumer wealth business. We've also been investing in our corporate and investment bankers and we've hired some 200 bankers across the franchise to really flesh out or build out some of the important sectors for us, including tech and FinTech and sponsors' coverage group.

And so, we've been moving ahead with those key strategic areas that we've referenced before, and I shouldn't leave out the commercial banking business, which is another area that we've continued to kind of invest in over the past couple of quarters, including the leadership.

And the last point I'll make on this, Richard, is around talent and really ensuring that we've got the right talent in the right roles, non-siloed thinkers with a real sense of urgency to get this done. And it's interesting if you look around Jane's table, if you look at the executive management team, nearly all of the executive management team members are new to their seats inside of the last few years.

And as Jane has said on some of our prior earnings calls, in many ways, this is a new Citi. The combination of these things, the transformation, the strategy refresh, and the focus that Jane has on culture and talent is exactly the right mix of things that we need in order to ensure that we deliver long-term shareholder value. So hopefully that gives you a sense but again, looking forward to March 2nd where all of this comes together and I'm sure it will be a useful update in that forum as well.

RICHARD RAMSDEN: Okay. That's very helpful. So just briefly on Korea, can you just talk about why you chose to wind down that business versus pursuing a sale? And maybe you can talk a little bit about the $2 billion of capital that is allocated to that business and whether or not the charges impact your ability to release that capital.

MARK MASON: Sure. So, on October 25th, we announced that we're going to wind down our Korea consumer banking business. We did run a sale process, but we determined that winding down the business made the most sense economically. Look. Korea is and will continue to be a challenging market to operate a consumer banking business in.

And as we look at the wind down, as you know because we disclosed it, we estimated that we would recognize somewhere between $1.2 billion and $1.5 billion in cash charges between now and through 2022 related to the voluntary retirement program that we've been discussing with employees and in consultation with unions.

And as I mentioned earlier, we're going to take about $1.2 billion or so related to Asia divestitures this quarter. As we wind down this business over the next couple of years, we will release about $2 billion of allocated tangible common equity associated with it.

And what's interesting, Richard, to your point, we've done the analysis. So, we looked at the path of a sale. We looked at a path of continuing to operate this franchise. And we've looked at the wind down path. And as we've looked at that, even including those wind down costs, the economics of the wind down are more attractive than if we continued to operate the franchise. And that's because the costs are lower through the wind down period and we have the release of that $2 billion over time.

And so, this was the right economic decision for our shareholders when we looked at that. And again, we're looking forward to being able to release that $2 billion and return that over time.

RICHARD RAMSDEN: Okay. And then, perhaps since we're talking about this, you can just give us an update on the remaining 11 markets that you expect to exit from over the next year or so. And perhaps talk about how you think those exits or divestitures could impact capital as well.

MARK MASON: Yeah. Look, we've seen a lot of positive momentum. I know there was some news coverage on this just a day or so ago. But we're approaching this with a real sense of urgency. We've been out in the market. I expect to have some updates in the first quarter. We're deep into the second round bid discussions around this. And so, we feel good about the interest that we're seeing in these other 11 markets. There are a couple of aspects to it that I think are worth mentioning. One, you alluded to.

So remember, these are consumer banking businesses where we were subscale and the returns associated with them were not above our cost of capital. And so, when I think about capital allocation, when I think about how we drive shareholder value creation, this was absolutely the right path to take. And so, part of executing on these exits is to free up that capital. And remember, there's about $7 billion or so of capital associated with these 13 markets.

About $800 million is associated with the Australia business. We announced that just a number of weeks ago and we would expect that closing in the first half of 2022, so that's $800 million of the $7 billion or so of allocated TCE. And then we just talked about another $2 billion that's tied to Korea, that's been allocated to Korea that we should see released over time.

So, one aspect is freeing up the capital. It'll happen over time about $7 billion of allocated TCE. The other aspect we don't talk about a whole lot is that it simplifies the organization, and one of the things that Jane has been keenly focused on is ensuring that we're driving the stranded cost from these types of exits out of the company. And we both have deep experience in doing that, having run holdings, Jane having run Latin America. But if you think about what happens in these countries, they have in-country expenditures. They have regional allocations for the oversight that regions actually provide to the countries. And in many instances, they have global allocations that go through those countries as well.

What Jane is pushing for, what we're focused on is not just the direct costs going out, but how do we rethink our operations and our structure and organizational design to make sure that we're also getting rid of those otherwise stranded costs that are allocated to these types of countries. So freeing up capital, ensuring we drive costs down are two important components coming out of these exits. But we're getting after it with a real sense of urgency, Richard.

RICHARD RAMSDEN: Okay. So, on the transformation and on the risk control side of the equation, I know you're restricted in terms of what you can say because of confidential supervisory information, but you have talked about how these investments should drive improved operating results over time. So, can you update us on where you've got to in terms of the transformation work, from your perspective how that work is progressing? And then, perhaps again, talk through what we should expect in terms of communications from here around that.

MARK MASON: Sure. So, the first thing I'd say is that, again, we submitted in the third quarter our plans. We submitted both to the OCC as well as to the Fed. We are firmly pivoting, as I mentioned, to execution. In doing that, it's important and we focused on setting up the right governance and oversight for such a large body of work.

So, we've set up a Chief Administrative Officer and she, Karen Peetz, has a large team that's providing that governance and oversight. There's a project management office that reports into that team. And that's ensuring that we are marching against the milestones that we've put forward in that plan. And those milestones in many ways are geared towards how do we reduce and address risk associated with the different important components of the consent orders and of the transformation work. And I'd say we're making good progress with that.

Another important element of this is ensuring that we're hiring the right people. We've got the right skills to ensure that we can execute against the plan, and we're making good progress as it relates to that as well. You asked about the benefits a little bit, one of the key areas of focus, obviously, risk and controls. Another one is data, and data, I think, is a good example of the nature of the benefits that we expect to come out of the transformation. So, data is everything from the governance around data, the standards we're setting for data, the clear accountability for who owns data.

And if you think about the nature of that investment, it's everything from the technology and infrastructure that supports the intake of that information, the intake of that data into our system, in a standard and at a quality that requires a lot less reconciliation work and rework through that process to get to the output of management information that we need to run the firm.

And by investing in data, it allows for us to not only improve the operating cost of running our firm because of reducing the manual work, because of reducing the reconciliation and rework required, because of having controls through the process, but it also actually enables us to leverage that data more rapidly in the way we serve clients. And so, in many ways, the investment we're making in data as an example has a dual benefit of reduced cost and getting after more upside on the top line as well. So, that's just one example, Richard, of how we expect benefits to play out over time through some of the investments we're making.

RICHARD RAMSDEN: Okay. Maybe you can just give us an update on the costs of the transformation work. I think you've said in the past there's 3,000 people working across this and that it's going to be a multiyear effort. Has your assessment of the costs associated with the transformation work changed, and what are you thinking about now in terms of the overall timeline in terms of resolution around this?

MARK MASON: Yeah. So, I'm not going to give guidance as it relates to the go-forward costs. I would say a number of things, because we have – I think we do have more clarity and you would expect we gain more clarity as we kind of move through the design phase of the plan and move into different phases of implementation. So, as I mentioned earlier, the cost for 2021 is going to drive about 3 percentage points of the growth that we see in our expenses in the year.

So, we've got obviously clarity on that. We've got clarity, frankly, on the idea that it's a multi-year spend, and that is going to peak and then level off and ultimately we'll see some benefits as the costs come down. When I look at the breakout of the spend, that's going to evolve over time as well. So, if I look at that spend today, I'd say some 45% or so is tied to third-party resources, consulting spend etcetera, that spend that's required to stand this up to get it through design phase and, frankly, to carry us while we onboard more resources.

So, the next big bucket is headcount. We've been hiring. You referenced the 3,000 in order to fill the roles that we need to move through this early part of the execution. And the balance right now from a P&L point of view is technology, that 20%. Obviously, it's a lot larger when you think about the cash spend that's tied to that. That mix is going to change over time. That third-party consultant spend is going to come down. We're going to see an increase related to the impact of heads. And over time, technology is going to pick up in terms of that spend.

That's going to allow for us to deliver the benefits that we are expecting in the way of productivity and the efficiency in how we run these operations and so, a lot of work underway. We'll talk more about how the spend will evolve over time, I'm sure, in the coming quarters. But hopefully, that gives you a sense for how the mix will likely shift and how we're focused on it as we play into this execution phase.

RICHARD RAMSDEN: Okay. Great. And then, just more broadly on expenses, you're being consistent in terms of talking about mid- single-digit incremental increases in expenses for the full year. Obviously, some of that is tied to higher volumes. Some of that's tied to higher investment. But can you just take a step back and talk more broadly about how you're thinking about the trade-off between investing in the franchise versus delivering operating leverage as we head into 2022?

MARK MASON: Sure. Yeah. Now, Richard, I'd start by saying that I take a long-term view on this, and I highlight that because, in many ways, I view the investments that we're making enabling long-term sustainable operating leverage over time, right. And so, you mentioned that we have given guidance in terms of mid-single digits that excludes the impact of the divestiture-related costs, but the spend that we have is really focused on three areas.

You've heard me talk about transformation. You've heard me talk about business-led investments. And then, you've actually heard me talk about productivity that we would – that we are managing to, that we're delivering on in order to help fund some of those investments going forward. So, the transformation piece we've talked about already a little bit in terms of addressing the consent order and driving towards the broader targets that we're looking to deliver on there.

But business-led, I kind of alluded to earlier, areas like the commercial bank and the investment bank and the digitization of our network. And then, that final piece is investing in technology but also ensuring that we get productivity throughout our expense base. And you've heard me say we're looking at every expense line.

We generate some $300 million – we're finding some $300 million to $400 million a quarter of productivity savings in everything from real estate to digitization to simplification, etcetera. And that's going to be an ongoing part of how we think about our expense base in the investments and offsets to those investments going forward. But I think of the investments as being an enabler of both top line revenue, as well as in many instances, operational efficiency in terms of how we run the firm.

RICHARD RAMSDEN: Okay. Great. So I think we've got a few minutes left. So, let me ask about capital and capital returns. I think you're very close now to your 11.5% CET1 target. I think at the end of the third quarter, you were around 11.7%. So, could you talk a little bit about your approach to capital allocation, capital returns and whether you have a preference in terms of dividends versus buybacks, given the valuation of Citi today?

MARK MASON: Sure. First thing I'd say is that, our philosophy around capital really hasn't changed, and what I mean by that is our interests are aligned with that of our shareholders. So, we're committed to returning capital. Through the third quarter, we've returned close to $12 billion of capital between buybacks and dividends.

We've got a robust framework for how we think about capital allocation. It starts with strategy and ensuring that our strategy is geared towards the competitive advantages that we have across the franchise. We look at businesses that allow for us to capture growth with our clients and businesses that generate returns that are above our cost of capital and we try to prioritize those businesses with how we think about our resource and capital allocation.

So when I look at businesses like TTS, returns north of 20%. I look at client segments like commercial banking, returns in the mid-20s. I look at security services and, well, all high returning parts of the franchise. We want to allocate resources to those. They are likely to be growing as well and we think we're well-positioned to do that.

So, it starts with that strategy. The other component to that is that there are parts of the franchise like these 13 markets that don't necessarily have prospect for growth or aren't of scale or don't return the types of returns that we need to be above the cost of capital and those we actually take away from as we're deciding to exit those.

I feel good about and have talked and described before how we generate capital capacity, so the income generation capabilities that we have I think that is proven to be quite resilient, the utilization of the DTA. We'll utilize roughly $1 billion, I'd estimate, this year of DTA. And the legacy asset rundown will generate more capital that we can return to shareholders.

I'd point out, Richard, that this quarter is a bit of an anomaly. And I say that because we've got obviously the Korea charge that we'll be taking, but we also have in front of us the impact of SA-CCR, which will come into play in January of next year. And so, we've been working really hard to create capacity for SA-CCR. Our estimate of the impact is somewhere between $60 billion and $65 billion of risk-weighted assets and that'll equate to roughly 50 to 60 basis points on the CET1 ratio.

And so, we've been working to reduce our risk weighted assets. We've been looking at low yielding risk weighted assets. We've been looking at opportunities for trade compression in order to bring those down. We've been looking at the pricing and economics around those impacted by SA-CCR. And we've been looking at our capital actions, at buybacks, and we're going to pause buybacks in the quarter, just for this quarter and resume those in the first quarter, probably at the levels close to what we saw in the third quarter all in order to maintain the 11.5% target upon SA-CCR adoption.

And so lots of work around that. But I'll end where I started, which is that, our interests are aligned with that of shareholders, and we're looking to return any capital that we're not using to invest at levels above our cost of capital. We've done about $12 billion thus far, and we're looking forward to do more as we get out of some of these other markets.

RICHARD RAMSDEN: Okay. So, I think, sadly, with that, we're out of time. There's a lot of other questions we could ask, but, Mark, thank you very much for taking the time to join us and look forward to seeing you both in March and hopefully in person at this conference next year. But thank you very, very much for...

MARK MASON: Thanks for having me, Richard. I look forward to it.

RICHARD RAMSDEN: All right. Thank you. Thanks a lot.

MARK MASON: Thank you everyone.

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