Citigroup Remains a Sub-scale US Bank

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Image Source: Matt Buck

Even if Citigroup achieves improved return-on-capital targets, it would remain a sub-scale US bank from a nationwide perspective, and it remains overly reliant on Corporate and Investment banking, which is an overtraded and competitive field globally.

By Matthew Warren

Citigroup (C) reported middling first-quarter results April 15, with revenues down 2% versus last year, to $18.6 billion. Thanks to strong operating expense control (-3%), lower taxes, and a 9% lower share count, earnings per share advanced 11%, however. With a common equity tier 1 ratio of 11.9%, Citigroup was able to return over $5 billion to shareholders in the quarter. The bank reported a 11.9% return on tangible equity in the quarter, barely better than the cost of capital, and this without including goodwill and intangibles in the equation.

On the earnings call, CFO Mark Mason confirmed that the bank is targeting 12% return on tangible common equity in 2019 and 13.5% or greater in 2020. Citigroup is hoping to reduce its common equity tier 1 ratio to 11.5% from the current 11.9% (requires regulatory approval), but the rest of the improvement would largely come from reducing the efficiency ratio from current levels, which the bank has been doing for the past several quarters. The CFO also seemed to indicate on the earnings call that it considers current loan losses to be mid-cycle or normalized, which is highly questionable in my opinion, giving the extremely benign economic conditions that the US economy has been enjoying for some time.

More realistically, Citigroup's earnings could come under substantial pressure in an environment of considerable job losses. Even if the bank hits these improved return-on-capital targets, Citigroup would remain a sub-scale US bank from a nationwide perspective, and it remains overly reliant on Corporate and Investment banking, which is an overtraded and competitive field globally. There are simply too many players and some of them are national champions in Europe, where overcapacity is pronounced. Many of those banks are operating with limited earnings power, yet they continue to fight for market share. Our fair value estimate remains $71 per share.

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