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Citigroup Shifts Strategy as It Chases Rivals --- Investors need to watch how moves are executed

By Telis Demos
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Under new management, Citigroup is still aiming to close its performance gap to peers. But how it goes about that may be changing.

One of the bank's first big moves has been to shrink its global retail footprint, moving to exit consumer banking franchises in 13 countries in Asia, Europe and the Middle East. These units weren't necessarily part of the problem as Citigroup was striving to meet its target of a 12% return on tangible common equity, a measure of profit as a percentage of the bank's equity capital, before the pandemic. The yearslong drive to boost this key metric tracked by investors succeeded in bringing Citigroup closer to rivals like Bank of America and JPMorgan Chase, which boasted equity returns in the mid-to-high teens pre-pandemic.

The businesses being exited were allocated just $7 billion of tangible common equity on average last year, or less than 5% of the bank's equity base. This meant they had potential for high returns, or at least weren't likely to be major drags on capital efficiency as the bank strove to meet its targets.

Speaking last Friday at a Bernstein conference, Chief Executive Jane Fraser, who officially took the reins in March, described the international retail units as "good return businesses." But they also would have required a lot of investment in infrastructure and controls to continue to digitize them and get them to a larger scale. That is an area where Citigroup is already spending a lot of time and money, following a special consent order from U.S. regulators last year that cited deficiencies in risk management, data and internal controls.

Ms. Fraser noted that the bank's efforts to close return gaps with peers must focus not only on what businesses it will give priority to, but how it operates them. She said the bank would rather "monetize" those retail assets and redeploy the resources, either as part of capital return to shareholders or toward higher-return activities.

Though the bank did meet its return goal in 2019, and enjoyed outsize stock-price gains that year, a combination of the pandemic and the consent order last year saw its share performance drop off versus rivals. Citigroup is hovering around its price level from the beginning of 2020, while S&P 500 banks overall are now about 13% above that mark. Citigroup's return on tangible common equity dipped to under 7% last year, from 12.1% in 2019. It now trades at just over one-times tangible book value, compared with over two-times for Bank of America and JPMorgan, according to FactSet.

Coming out of the pandemic and under new leadership, now is a good time for the bank to undertake moves with a long-term payoff. One aim is that many retail customers in the soon-to-be-exited markets will stay with the bank in its regional hubs for wealth management. Global wealth is a high-return business the bank wants to make a core focus, though competition is intense as many other global banks have the same idea.

Within retail banking, Ms. Fraser said that the exits "will also enable us to have more focus on the home market" in the U.S., through both financial resources and human talent. Ms. Fraser pointed to her experience seeing a boost in the bank's Mexico retail banking performance after she oversaw the exit of other Latin America retail markets. She said she didn't believe "branches are dead yet" in U.S. retail banking and noted the potential for **digital banking** partnerships, like with retailers such as Home Depot.

U.S. retail will likely be a key part of closing the long-term return gap, as U.S. retail deposits are some of the cheapest and stickiest funding in the world. Autonomous Research's John McDonald has estimated Citigroup's relatively higher funding costs could explain as much as half of the gap between its core returns on tangible common equity and those of its closest peers at the end of last year. Citigroup's retail deposits were about half the size of its total loan book at the end of last year, versus over 90% at JPMorgan and Bank of America, according to Autonomous.

The bank may also get a lift from the U.S. economic recovery in its vast credit-card business, and that could help boost its share price. But investors should stay focused on how the bank is using this turbulent time to reshape some of its core economics.

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