Citigroup (C)

Updated July 14th, 2018 by Josh Arnold

Key Metrics

Current Price:	$67	**5 Year CAGR Estimate:**	10.0%	**Volatility Percentile:**	67.7%
Fair Value Price:	$67	**5 Year Growth Estimate:**	8.1%	**Momentum Percentile:**	34.5%
% Fair Value:	100%	**5 Year Valuation Multiple Estimate:**	0.0%	**Valuation Percentile:**	54.2%
Dividend Yield:	1.9%	**5 Year Price Target**	$98	**Total Return Percentile:**	61.1%

Overview & Current Events

Citigroup traces its roots back to 1812 when it was known as the City Bank of New York. In the past 206 years, the company has grown into a global juggernaut in credit cards, commercial banking, trading and a variety of other related activities. It has thousands of branches, produces $74B in annual revenue and has a market capitalization of $171B.

Citi reported Q2 earnings on 7/13/2018 and the report wasn't received well by investors. Revenue was up 2% during the quarter but the cost of credit was higher, crimping margins. Earnings-per-share rose 27% from the prior quarter, due mostly to a lower tax rate and an 8% reduction in the float from Citi's substantial buyback activity. Credit quality was roughly flat against last year's Q2, but Citi did receive a non-objection for its plan of returning at total of $22B to shareholders in the next year, mostly via buybacks. Due to these sizable capital returns, Citi's capital ratios have declined somewhat, but its balance sheet is still very strong and capital levels are certainly not a concern here.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	--	--	$3.50	$3.59	$3.86	$4.26	$2.20	$5.44	$4.72	$5.33	***$6.35***	***$9.35***
DPS	$11.20	$0.10	$0.00	$0.03	$0.04	$0.04	$0.04	$0.16	$0.42	$0.96	***$1.28***	***$3.00***

Citi's earnings-per-share history is clouded by the immense struggles it endured following the Great Recession, given there was reasonable doubt the company could even continue to operate. However, years of hard work have paid off and earnings have continued to move higher over time. We see Citi producing $6.35 in 2018 and robust growth of 8.1% annually thereafter, fueled by a number of tailwinds.

We believe Citi will continue to see higher revenue as its institutional and consumer businesses gather cheap deposits and lend them prudently, leading to reasonable loss rates and favorable margins. In addition, the company's buyback should be good for a mid-single digit reduction in the share count annually. Margins have been a source of earnings growth of late – with the exception of Q2 – and that should remain the case so long as the yield curve doesn't continue to flatten or even invert. Citi isn't as tied to traditional lending as most other banks, so the yield curve isn't quite as critical, but the cost of deposits is extremely important for its massive credit card business, as evidenced in Q2. Overall, even with those risks in mind, Citi looks poised to deliver high single digit earnings-per-share growth in the coming years.

Citi was barred for years following the Great Recession from raising its dividend but now that it has permission, it isn't wasting any time. The payout ratio is still just a small fraction and we see that moving meaningfully higher in the coming years, culminating with a predicted $3 per share payout in five years. Citi certainly hasn't been an income stock in the past decade but we believe all the pieces are in place for that to be the case once more.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	--	--	11.4	10.4	8.4	11.4	22.8	9.8	9.7	12.3	***10.5***	***10.5***
Avg. Yld.	5.9%	0.3%	0.0%	0.1%	0.1%	0.1%	0.1%	0.3%	0.9%	1.5%	***1.9%***	***3.1%***

Disclosure: This analyst has no position in the security discussed in this article, and no plans to initiate one in the next 72 hours.

Citi's price-to-earnings ratio has bounced around some in the past several years but today, at 10.5, it is right in line with its historical average. We therefore see no impact to total returns from the valuation changing. We do expect the yield to move higher due to the payout's growth outpacing that of the stock price, leading to a 3%+ yield in five years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
ROA	--	--	0.59%	0.58%	0.41%	0.71%	0.40%	1.00%	0.83%	0.86%	***0.85%***	***0.90%***
Debt/A	95%	93%	92%	91%	90%	90%	89%	89%	87%	87%	***87%***	***85%***
Int. Cov.	0.7	2.2	2.5	2.1	1.9	2.7	2.6	3.7	3.3	2.8	***2.9***	***3.1***
Payout	--	--	--	1%	2%	2%	9%	7%	9%	18%	***20%***	***32%***
Std. Dev.	68%	146%	36%	40%	37%	19%	15%	21%	33%	15%	***22%***	***33%***

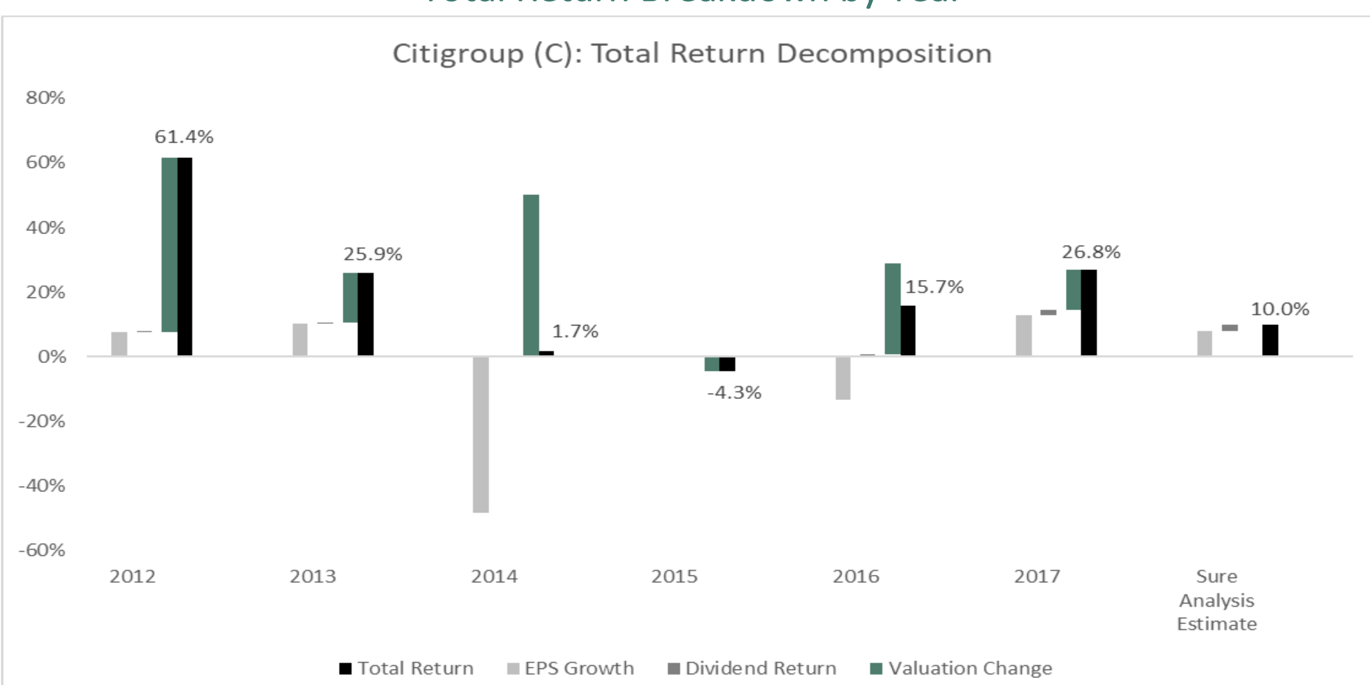
Citi's quality metrics have been remarkably steady in recent years given the tremendous amount of change and de-risking that has occurred within the business. Its return on assets has hovered in the area of 85bps for two years now and we expect it will improve slightly. Citi's heavy reliance upon credit cards – a business that has been suffering from higher losses industrywide – should keep a lid on ROA growth. We see continued deleveraging of the balance sheet but only slightly, and a minute improvement in interest coverage as that occurs. The payout ratio should rise to a level that is more in line with Citi's peers in the low-30% area, giving the stock a much-needed boost in yield. Overall, Citi is in much better shape than it was five years ago, and we see cause for optimism.

Citi's competitive advantage is in its global reach and its large position in the lucrative credit card business. Citi has differentiated itself from the other money center banks in these ways and it continues to serve the bank well. It is very susceptible to recession as it nearly went out of business in 2008/2009; the next downturn will not be kind to Citi.

Final Thoughts & Recommendation

In total, we see Citi as a fairly priced growth story with a few levers to pull for growth. We are forecasting robust 10.0% total annual returns over the next five years, consisting of the 1.9% current yield, no change in the valuation and 8.1% earnings-per-share growth. The pieces are in place for Citi to become an income stock once more and we see it as attractive for those seeking dividend growth, as well as growth at a reasonable price; value investors and those seeking a high current yield should look elsewhere. However, on the whole, Citi looks poised for solid returns in the coming years.

Total Return Breakdown by Year



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