Citigroup Inc. (C)

Updated October 12th, 2018 by Josh Arnold

Key Metrics

Current Price:	$70	**5 Year CAGR Estimate:**	10.2%	**Volatility Percentile:**	62.3%
Fair Value Price:	$69	**5 Year Growth Estimate:**	8.0%	**Momentum Percentile:**	41.8%
% Fair Value:	102%	**5 Year Valuation Multiple Estimate:**	-0.4%	**Growth Percentile:**	72.0%
Dividend Yield:	2.6%	**5 Year Price Target**	$101	**Valuation Percentile:**	50.2%
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Total Return Percentile:**	62.1%

Overview & Current Events

Citigroup was founded in 1812 when it was known as the City Bank of New York. In the past 200+ 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 $74 billion in annual revenue and has a market capitalization of $175 billion.

Citigroup reported Q3 earnings on 10/12/18 and results were once again quite good. Earnings-per-share rose 22% against last year's Q3 despite revenue that was largely unchanged. The bank's efficiency ratio is in the area of 57%, which is helping to boost margins as support expenses fall as a percentage of revenue. Total assets grew 2% year-over-year, while deposits rose 4% and loans added 3%. Book value is $72.88 per share and while Citigroup's capital buffer continues to shrink, it is off of very high levels. Citigroup returned $6.4 billion to shareholders in the third quarter alone, continuing a recent trend that has seen it accelerate its capital return efforts. This is generally beneficial for shareholders, but as Citigroup is no longer hoarding capital, its capital buffer is declining (as expected). We have boosted our earnings-per-share estimate for this year to $6.55 after another strong report.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$64.20	$7.60	$3.50	$3.59	$3.86	$4.26	$2.20	$5.44	$4.72	$5.33	**$6.55**	**$9.60**
DPS	$11.20	$0.10	$0.00	$0.03	$0.04	$0.04	$0.04	$0.16	$0.42	$0.96	**$1.80**	**$3.00**
Shares	545	2,847	2,906	2,924	3,029	3,029	3,024	2,954	2,772	2,570	***2,500***	***2,100***

Citi's earnings-per-share history is clouded by the immense struggles it endured following the Great Recession. 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 $6.55 in 2018 and robust growth of 8.0% 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 and that should remain the case so long as the yield curve doesn't continue to flatten or invert. Citi is not as tied to traditional lending as most other banks, so the yield curve is not as critical, but the cost of deposits is extremely important for its massive credit card business. Profitability metrics through Q3 of this year remain strong, so 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 is not wasting any time. The recent dividend increase has the payout ratio more in line with its competitors and looking forward, we see dividend growth as roughly keeping pace with earnings expansion.

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	**10.7**	**10.5**
Avg. Yld.	5.9%	0.3%	0.0%	0.1%	0.1%	0.1%	0.1%	0.3%	0.9%	1.5%	**2.6%**	**3.0%**

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

Citigroup's price-to-earnings ratio has bounced around some in the past several years but today, at 10.7, it is right in line with its historical average. We see just a 0.4% headwind to total returns from the valuation changing. We expect the yield to move higher due to the payout's growth outpacing the stock price, leading to a 3%+ yield in 5 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%	**0.90%**	**0.92%**
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	17%	1%	--	1%	2%	2%	9%	7%	9%	18%	**27%**	**31%**
Std. Dev.	68%	146%	36%	40%	37%	19%	15%	21%	33%	15%	**22%**	**33%**

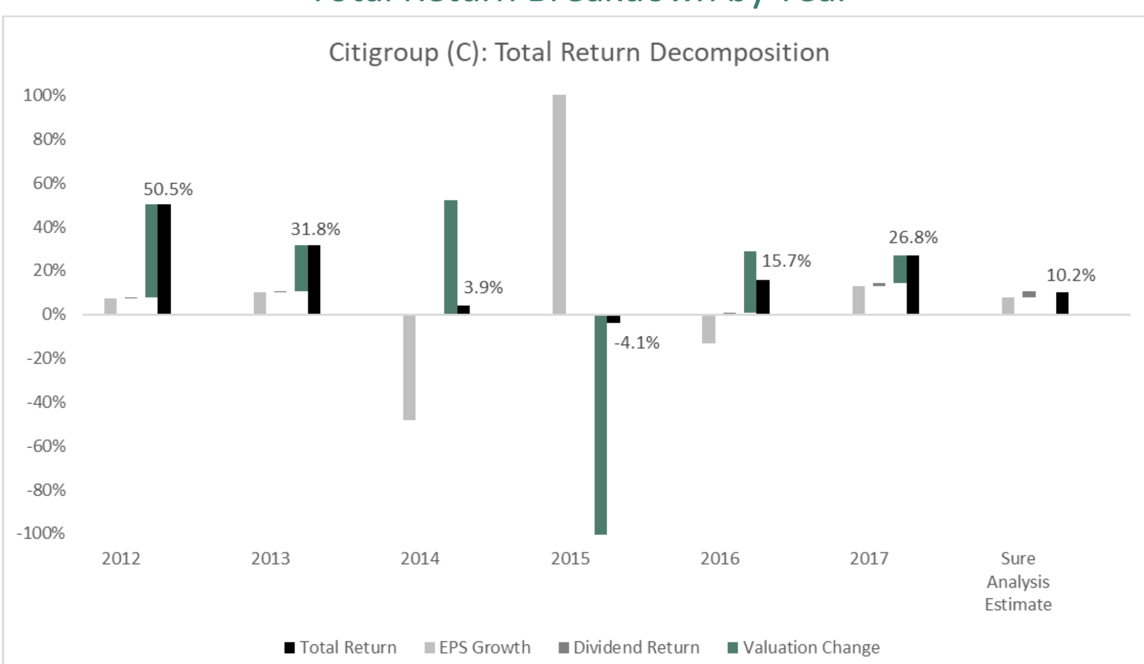
Citigroup's quality metrics have been remarkably steady in recent years given the tremendous amount of change and de-risking that has occurred within the business. Its return on assets has hovered in the area of 85bps for two years now and we expect it will improve slightly. Citigroup's heavy reliance upon credit cards – a business that has been suffering from higher losses industrywide – should keep a lid on ROA expansion. 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 continue to 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 10.2% total annual returns over the next five years, consisting of the 2.6% current yield, a -0.4% headwind from the valuation and 8% earnings growth. The pieces are in place for Citigroup 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 should look elsewhere. We rate Citigroup a buy given its growth prospects and current yield.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	51.60	80.29	86.60	77.33	69.19	76.72	77.22	76.35	69.88	71.45
SG&A Expense	39.28	31.62	31.00	32.94	33.11	31.99	32.24	29.90	29.29	29.68
D&A Expense	2.47	2.85	2.66	2.87	2.51	3.30	3.59	3.51	3.72	3.66
Net Profit	-27.7	-1.61	10.60	11.07	7.54	13.66	7.31	17.24	14.91	-6.80
Net Margin	-54%	-2.0%	12.2%	14.3%	10.9%	17.8%	9.5%	22.6%	21.3%	-9.5%
Free Cash Flow	93.98	-56.87	33.32	61.35	-13.97	59.75	42.96	36.54	51.18	-11.95
Income Taxes	-20.3	-6.73	2.23	3.58	0.01	6.19	7.20	7.44	6.44	29.39

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	1939	1856.6	1913.9	1873.9	1864.7	1880.4	1842.2	1731.2	1792.1	1842.5
Cash & Equivalents	199.6	192.9	190.4	184.5	138.6	198.9	160.2	133.1	160.5	180.5
Accounts Receivable	0.0	33.6	31.2	27.8	22.5	25.7	28.4	27.7	28.9	38.4
Goodwill & Int. Ass.	46.9	40.6	38.2	34.6	33.3	32.8	30.0	27.9	28.3	27.4
Total Liabilities	1794	1701.7	1748.1	1694.3	1673.7	1674.2	1630.5	1508.1	1565.9	1640.8
Accounts Payable	70.9	60.8	51.7	56.7	57.0	53.7	52.2	53.7	57.2	61.3
Long-Term Debt	486.3	432.9	460.0	377.9	291.5	280.1	281.4	222.4	236.9	281.2
Shareholders' Equity	71.0	152.4	163.2	177.5	186.5	197.6	199.7	205.1	205.9	181.5
D/E Ratio	3.4	2.8	2.8	2.1	1.5	1.4	1.3	1.0	1.1	1.4

Profitability Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	-1.3%	-0.1%	0.6%	0.6%	0.4%	0.7%	0.4%	1.0%	0.8%	-0.4%
Return on Equity	-30%	-1.4%	6.7%	6.5%	4.1%	7.1%	3.7%	8.5%	7.3%	-3.5%
ROIC	-4.2%	-0.3%	1.7%	1.9%	1.5%	2.8%	1.5%	3.7%	3.3%	-1.4%

Note: all figures in billions of U.S. Dollars.