Citigroup (C)

Updated January 16th, 2020 by Josh Arnold

Key Metrics

Current Price:	$81	**5 Year CAGR Estimate:**	10.1%	**Market Cap:**	$172B
Fair Value Price:	$88	**5 Year Growth Estimate:**	6.0%	**Ex-Dividend Date:**	01/31/2020
% Fair Value:	92%	**5 Year Valuation Multiple Estimate:**	1.7%	**Dividend Payment Date:**	02/28/2020
Dividend Yield:	2.5%	**5 Year Price Target**	$118	**Years Of Dividend Growth:**	5
Dividend Risk Score:	D	**Retirement Suitability Score:**	F	**Last Dividend Increase:**	13.3%

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 bank has grown into a global juggernaut in credit cards, commercial banking, trading and a variety of other financial activities. It has thousands of branches, produces $75 billion in annual revenue and has a market capitalization of $172 billion.

Citi reported Q4 and full-year earnings on January 14th and results were strong once again. Total revenue in Q4 came to $18.4 billion, a 7% increase year-over-year. Strength was seen across the bank's lines of business as the Global Consumer Banking business saw a 5% gain, while Institutional Clients Group produced a 10% increase. Operating expenses were up 6% as the bank produced some cost saving efficiencies and wound down legacy assets, but that was more than offset by higher incentive compensation and volume-related costs.

Cost of credit rose 15% in Q4 and the allowance for loan losses rose 4% to $12.8 billion. In addition, total non-accrual loans grew 12% to $4.1 billion, with consumer non-accruals declining -10% to $1.8 billion, and corporate non-accruals rising 45% to $2.2 billion.

Total loans were $699 billion at the end of Q4 and total deposits were $1.1 trillion, rising 2% and 6%, respectively. That puts Citi's loan-to-deposit ratio at just 64%, which is extremely low, even for a mega bank.

Full-year earnings-per-share came to $8.04 after the strong Q4, a 21% gain over the prior year. The significant reduction in the share count was responsible for about half of the gain in earnings-per-share, while dollar earnings growth made up the balance. For 2020, our initial estimate is $8.40, reflecting mid-single-digit growth following the huge gains that have been made in the past few years. We see further share count reductions as aiding earnings-per-share growth, but caution that the yield curve is unfavorable for banks and that credit quality is slowly deteriorating.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$3.50	$3.59	$3.86	$4.26	$2.20	$5.44	$4.72	$5.33	$6.65	$8.04	***$8.40***	***$11.24***
DPS	---	$0.03	$0.04	$0.04	$0.04	$0.16	$0.42	$0.96	$1.54	$1.92	***$2.04***	***$3.29***
Shares[1]	2,906	2,924	3,029	3,029	3,024	2,954	2,772	2,570	2,369	2,114	***2,000***	***1,700***

Citi's earnings-per-share history is clouded by the immense struggles it endured following the Great Recession. However, years of hard work have paid off, and earnings have continued to move higher over time. We see Citi producing $8.40 per share in 2020 and growth of 6% annually thereafter.

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. We believe Citi is pulling back on lending at the moment due to less than favorable spreads on loans. That is a headwind, at least temporarily, as it results in higher deposit costs without commensurate lending revenue, crimping top line and margin growth. In addition, the company's buyback should be good for a mid-single-digit reduction in the share count annually. We note that even in the recent tumultuous interest rate environment, Citi is performing well. Citi is not as tied to traditional lending as most

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[1] Share count in millions

other banks, so the yield curve is not as critical, but the cost of deposits is extremely important for its massive credit card business. Continued deposit growth that is outpacing lending growth is starting to weigh on margins.

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 slightly outpacing earnings expansion.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	11.4	10.4	8.4	11.4	22.8	9.8	9.7	12.3	10.4	8.4	***9.7***	***10.5***
Avg. Yld.	0.0%	0.1%	0.1%	0.1%	0.1%	0.3%	0.9%	1.5%	2.2%	2.8%	***2.5%***	***2.8%***

At just 9.7 times expected earnings, Citigroup's price-to-earnings ratio is below its historical norms. We see a modest tailwind to total returns from the valuation normalizing over the next five years. Indeed, Citi continues to boost earnings while the share price languishes, leading to a favorable valuation. We expect the yield to remain near where it is over time, just under 3%.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	---	1%	2%	2%	9%	7%	9%	18%	25%	24%	***24%***	***29%***

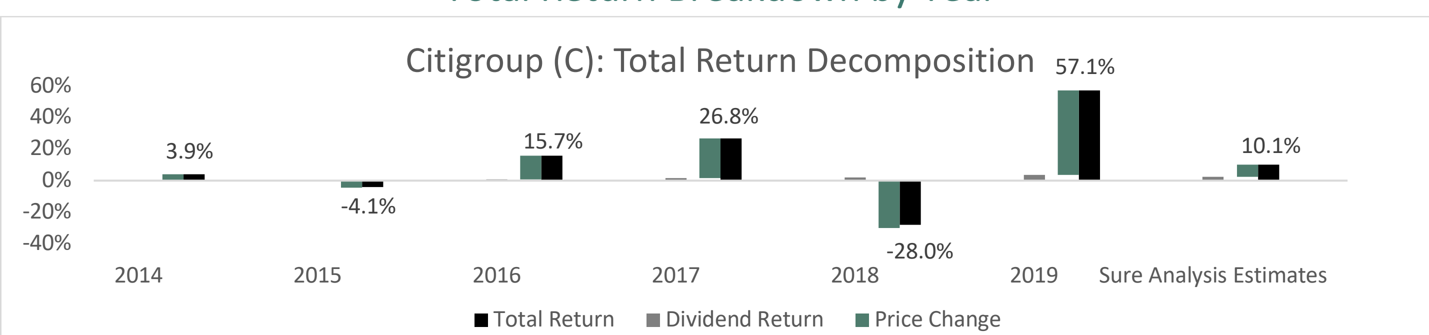
Citi's payout ratio is still just one-quarter of earnings, and we see it rising to near 30% of earnings in the coming years. Citi has spent the past several years trying to build its dividend back to a normalized level, and it is nearly in-line with competitors. Given strong earnings, we see the dividend as continuing to rise nicely in the coming years.

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 recessions as it nearly went out of business in 2008/2009; the next downturn will likely not be kind to Citi, although we note that the bank is in much better shape than it was heading into the financial crisis from a balance sheet and business mix perspective.

Final Thoughts & Recommendation

In total, we see Citi as an underpriced security with a few levers to pull for growth. We are forecasting robust 10.1% total annual returns over the next five years, consisting of the nearly-3% yield, a moderate tailwind from the valuation and 6% earnings-per-share growth. Citi has become an income stock once more and we see it as attractive for those seeking dividend growth, earnings growth potential and value. Despite the fact that the stock has moved much higher since our last update, we continue rate Citigroup a buy given its growth prospects and current yield.

Total Return Breakdown by Year



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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.

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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	86,601	77,331	69,190	76,724	77,219	76,354	70,797	72,444	72,854	74,286
SG&A Exp.	30,999	32,937	33,112	31,991	32,239	29,897	29,303	29,698	29,892	30,026
D&A Exp.	2,664	2,872	2,507	3,303	3,589	3,506	3,720	3,659	3,754	
Net Profit	10,602	11,067	7,541	13,659	7,310	17,242	14,912	-6,798	18,045	19,401
Net Margin	12.2%	14.3%	10.9%	17.8%	9.5%	22.6%	21.1%	-9.4%	24.8%	26.1%
Free Cash Flow	33,323	61,347	-13,966	59,754	42,957	36,539	50,977	-12,135	33,178	
Income Tax	2,233	3,575	7	6,186	7,197	7,440	6,444	29,388	5,357	4,430

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets ($B)	1,913	1,873	1,864	1,880	1,842	1,731	1,792	1,842	1,917	1,951
Cash & Eq. ($B)	190	184	138	198	160	133	160	180	188	193
Acc. Receivable	31									
Goodwill & Int.	38.210	34.582	33.312	32.783	30.003	27.851	28.337	27.402	27.266	26.948
Total Liab ($B)	1,748	1,694	1,673	1,674	1,630	1,508	1,565	1,640	1,720	1,757
Accounts Payable	51.749	56.696	57.013	53.707	52.180	53.722	57.152	61.342	64.571	48.601
LT Debt ($B)	459	377	291	280	281	222	236	281	264	293
Total Equity ($B)	163	177	186	197	199	205	205	181	177	175
D/E Ratio	2.81	2.13	1.54	1.37	1.34	1.00	1.05	1.40	1.35	1.52

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	0.6%	0.6%	0.4%	0.7%	0.4%	1.0%	0.8%	-0.4%	1.0%	1.0%
Return on Equity	6.7%	6.5%	4.1%	7.1%	3.7%	8.5%	7.3%	-3.5%	10.0%	11.0%
ROIC	1.7%	1.9%	1.5%	2.8%	1.5%	3.7%	3.3%	-1.4%	3.8%	4.1%
Shares Out.	2,906	2,924	3,029	3,029	3,024	2,954	2,772	2,570	2,369	2,114
Revenue/Share	29.18	25.79	22.94	25.22	25.43	25.39	24.51	26.85	29.20	32.79
FCF/Share	11.23	20.46	(4.63)	19.65	14.14	12.15	17.65	(4.50)	13.30	

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.