Citigroup (C)

Updated April 18th, 2020 by Josh Arnold

Key Metrics

Current Price:	$45	**5 Year CAGR Estimate:**	23.7%	**Market Cap:**	$95B
Fair Value Price:	$88	**5 Year Growth Estimate:**	6.0%	**Ex-Dividend Date:**	05/01/2020[1]
% Fair Value:	52%	**5 Year Valuation Multiple Estimate:**	14.2%	**Dividend Payment Date:**	06/29/2020[2]
Dividend Yield:	4.5%	**5 Year Price Target**	$118	**Years Of Dividend Growth:**	6
Dividend Risk Score:	C	**Retirement Suitability Score:**	C	**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 over $70 billion in annual revenue, and has a market capitalization of $95 billion.

Citi reported Q1 earnings on April 15th, beating revenue estimates by a wide margin, but also posting lower-than-expected profits. Earnings-per-share came to $1.05 in Q1, well short of consensus for $1.44, and down precipitously from $1.87 in the year-ago period. Citi's business is much more exposed to higher risk consumer loans, such as credit cards, than some of the other large banks, so we expect its earnings to take a larger negative impact from the economic slowdown related to COVID-19.

Indeed, Citi posted a credit loss reserve build of nearly -$5 billion in Q1, with the CEO noting that COVID-19 is having a "significant" impact on its results. The allowance for loan losses at the end of Q1 was a staggering $20.8 billion, or nearly 3% of its entire loan portfolio. That compares to $12.1 billion, or 1.8% of the portfolio at the same time last year.

Total loans were up 6% year-over-year to $721 billion, while deposits soared 15% to $1.2 trillion. That puts Citi's loan-to-deposit ratio at just 60%, which is very low for any bank, and is the lowest among the big US banks by a wide margin.

Citi saw a huge swing in profits for its Global Consumer Banking segment, which was expected, as profit fell from $1.3 billion in last year's Q1 to a loss of -$754 million this year. Institutional Clients Group net income was up 7% year-over-year to $3.6 billion, while Fixed Income Markets and Equity Markets, respectively also had a very strong Q1 on increased market volatility.

We have slashed our earnings-per-share estimate to $3.30 for this year as the impact of COVID-19 has become a bit clearer. We note this decline in earnings should be temporary, but significant for 2020.

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	***$3.30***	***$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[3]	2,906	2,924	3,029	3,029	3,024	2,954	2,772	2,570	2,369	2,114	***2,080***	***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 on a normalized basis, and growth of 6% annually. This year's results will be much worse than that.

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, which was evident again in Q1. That is a headwind, at least temporarily, as it results in higher deposit costs without commensurate lending revenue, crimping top line and

[1] Estimated date
[2] Estimated date
[3] Share count in millions

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.

margin growth. In addition, the company's buybacks could be good for a mid-single-digit reduction in the share count annually, although this is temporarily suspended. 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 other banks, so the yield curve is not as critical, but the cost of deposits is important for its massive credit card business. Continued deposit growth that is outpacing lending growth is starting to weigh on margins. Losses to the credit card portfolio will be significant this year.

We're using normalized earnings power of $8.40 per share for our fair value and valuation calculations, which is where we believe Citi would have been without COVID-19 this year.

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	***5.4***	***10.5***
Avg. Yld.	0.0%	0.1%	0.1%	0.1%	0.1%	0.3%	0.9%	1.5%	2.2%	2.8%	***4.5%***	***2.8%***

At just 5.4 times normalized earnings power, Citigroup's price-to-earnings ratio is well below its historical norms. We see a very strong tailwind to total returns from the valuation normalizing over the next five years. We expect the yield to fall over time from its very high level of 4.5% today, to 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%***

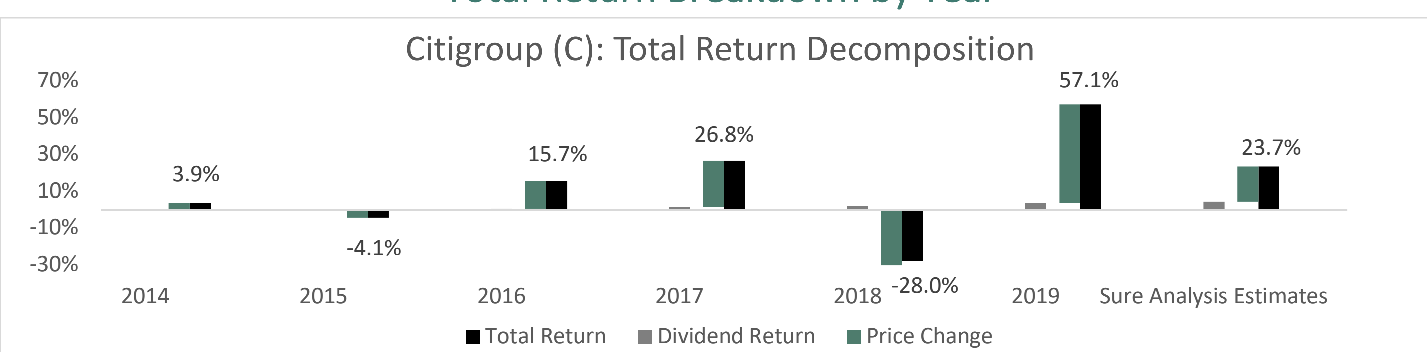
Citi's payout ratio is still just one-quarter of normalized earnings power, and we see it rising to near 30% in the coming years. Citi has spent the past several years trying to build its dividend back to a normalized level, and it is nearly in-line with competitors. Given strong earnings, we see the 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 23.7% total annual returns over the next five years, thanks primarily to its very low valuation. Citi has become an income stock once more and we see it as attractive for those seeking dividend growth, earnings growth potential and deep value. We note that 2020 will be challenging for Citi given its exposure to credit card losses, but the stock is rated a buy.

Total Return Breakdown by Year



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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	3905
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	-18,170
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	-8.02

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