**TRANSCRIPT**

## Citi Second Quarter 2016 Earnings Review
*Friday, July 15, 2016*

**Host**
Susan Kendall, Head of Investor Relations

**Speakers**
Michael Corbat, Citi Chief Executive Officer
John Gerspach, Citi Chief Financial Officer

## PRESENTATION

**OPERATOR:** Hello, and welcome to Citi's Second Quarter 2016 Earnings Review with Chief Executive Officer Mike Corbat and Chief Financial Officer John Gerspach.

Today's call will be hosted by Susan Kendall, Head of Citi Investor Relations. They ask that you please hold all questions until the completion of the formal remarks, at which time you will be given instructions for the question-and-answer session. Also as a reminder, this conference is being recorded today. If you have any objections, please disconnect at this time.

Ms. Kendall, you may begin.

**SUSAN KENDALL:** Thank you, Brent. Good morning and thank you all for joining us. On our call today, our CEO, Mike Corbat, will speak first; then John Gerspach, our CFO, will take you through the earnings presentation, which is available for download on our website Citigroup.com. Afterwards, we'll be happy to take questions.

Before we get started, I would like to remind you that today's presentation may contain forward-looking statements, which are based on management's current expectations, and are subject to uncertainty and changes in circumstances. Actual results and capital and other financial condition may differ materially from these statements due to a variety of factors, including the precautionary statements referenced in our discussion today and those included in our SEC filings, including, without limitation, the risk factors section of our 2015 Form 10-K.

With that said, let me turn it over to Mike.

**MIKE CORBAT:** Thank you, Susan. Good morning, everyone. Earlier today, we reported earnings of $4 billion for the second quarter of 2016 or $1.24 per share. These results are a significant improvement from the first quarter, not just in the overall amount of earnings, but in the proportion generated from our core business in Citicorp relative to the assets we're winding down in Citi Holdings. The results also show our institution's ability to generate solid earnings in a challenging and volatile environment.

We grew both our consumer and institutional loan books, reduced our expenses, further reduced Citi Holdings' assets and utilized additional deferred tax assets. We meaningfully improved our efficiency ratio, our return on assets and return on tangible common equity from the first quarter. We generated and returned capital to our shareholders, and the plan which was just approved, significant increases to the amount of capital we'll return over the next year.

In our institutional franchise, both our Markets and Investment Banking businesses saw a rebound in client activity from the last quarter. And our Treasury and Trade Solutions business continued to grow revenues, as we won new mandates and supported our clients' needs around the world. These results really show the benefits of our global network and the competitive advantages it provides.

In Global Consumer Banking, we had positive operating leverage in our international franchise highlighted by solid year-over-year growth in Mexico and continued sequential improvement in Asia. And as you know, we've been investing in our U.S.-branded cards business. On June 17, we acquired the Costco portfolio, gaining over 11 million cardholders in the process. And earlier this week, we announced the renewal of our partnership with American Airlines, and in retail services, we are renewing our partnership with The Home Depot. We're excited about the growth prospects of these businesses.

In Citi Holdings, we drove another significant reduction of assets which were down 10% from the first quarter and 47% from one-year ago. For the eighth quarter in a row, Holdings was profitable and the $93 million in net income was just 2% of Citigroup's total earnings for the quarter.

We passed a significant milestone in the utilization of our deferred tax assets, and in the second quarter, we utilized $900 million in DTA, bringing the total to $10 billion since the DTA reached its peak in 2012. While our remaining DTA does hamper our return on tangible common equity, utilization helps fuel our generation of regulatory capital. And as you know, returning that capital to our shareholders has been a critical priority of ours.

During the quarter, we reduced our outstanding common shares by approximately 30 million, bringing the total to 105 million shares over the last four quarters. Even so, our Common Equity Tier 1 ratio increased to 12.5%. In addition, our tangible book value per share increased to $63.53 in the quarter.

We've been clear about our desire to increase the capital return over time, and earlier this month, we were pleased to learn that the Federal Reserve did not object to the capital plan we submitted. And as a result, we'll return $10.4 billion in capital to our shareholders over the next four quarters.

The plan includes more than tripling our dividend to $0.16 per share and repurchasing $8.6 billion in common stock. This result, combined with the feedback we received from the Fed and the FDIC on our Resolution Plan shows the progress we continue to make in becoming a safer and stronger institution.

Looking forward, the environment remains challenging. We're continuing to navigate the consequences of the U.K. referendum on the EU from its economic impact to how exactly we'll structure our legal vehicles to continue to best serve our clients. And while the U.K. has a new leader, the U.S. is still in the midst of a unique presidential campaign, and such geopolitical and economic uncertainty doesn't create a clear picture for potential interest rate increases.

I think we've navigated the most recent volatility very well as a result of our strategic client segmentation and strong risk management. Our credit quality remains very high and our institution is showing its resilience and strength of our model. While there's been a high degree of uncertainty in the wake of the referendum, the capital markets are open, strategic transactions are getting done, and we feel good about the client activity we're seeing.

And while we don't know what's coming – what will come in the months as we look forward, we're always going to be looking at and continuing to optimize our resources, and I believe we're very well-positioned from a capital, liquidity and capacity perspective.

John will now go through the presentation, and then we'd be happy to answer your questions. John?

**JOHN GERSPACH:** Thank you, Mike, and good morning, everyone. Starting on slide three, we show total Citigroup results. Revenues of $17.5 billion declined 8% from last year, and expenses decreased 5%, each driven primarily by the continued wind-down of Citi Holdings, as well as the impact of foreign exchange translation. And credit costs improved, reflecting lower net credit losses, partially offset by a smaller net reserve release compared to the prior year.

We earned $4 billion in the second quarter or $1.24 per share, each down 14% versus the prior period. Our preferred dividends were higher this quarter. However, we were able to offset this impact through share buybacks, which drove a 4% decline in our average diluted shares outstanding.

 

In constant dollars, Citigroup end-of-period loans grew 2% year-over-year to $634 billion, as 6% growth in Citicorp was partially offset by the continued wind-down of Citi Holdings, and deposits grew 5% to $938 billion.

On slide four, we show the split between Citicorp and Citi Holdings. Citicorp was the predominant driver of profitability in the second quarter, contributing 98% of total net income. Citicorp revenues of $16.7 billion were down 3% from last year on a reported basis. In constant dollars, Citicorp revenues were flat to the prior year, as growth in our institutional franchise was offset by lower consumer revenues and the absence of prior-period real estate gains in Corp/Other.

Citicorp expenses decreased 1%, reflecting efficiency savings and a benefit from FX translation, partially offset by continued investments in the franchise. And cost of credit grew 13% from the second quarter of last year, driven by a smaller reserve release versus the prior year. Credit quality remained broadly favorable across the franchise, and net credit losses declined 5% year-over-year.

Pre-tax earnings of $5.7 billion in Citicorp were down from last year, but improved over 25% sequentially on higher revenues, lower operating expenses and a lower cost of credit.

Turning to Citi Holdings, both revenues and expenses declined significantly year-over-year, as we continued to wind-down the portfolio. We reduced Citi Holdings' assets by $7 billion this quarter, ending the period with $66 billion of assets or just 4% of total Citigroup, with signed agreements in place to sell $7 billion of this amount.

Turning now to each business, slide five shows the results for North America Consumer Banking. Total revenue declined 3% year-over-year. Retail banking revenues of $1.3 billion grew sequentially, but were down 4% from last year, as continued growth in consumer and commercial banking was more than offset by lower mortgage activity. Average retail banking loans and checking deposits grew 10% and 9% respectively from last year.

In branded cards, revenues of $1.9 billion were down 1% from last year, as a modest benefit from the Costco portfolio, which we acquired on June 17, was offset by the continued impact of higher rewards cost in our existing portfolio, as well as higher payment rates. I'll talk more about branded cards in a moment, but we continue to see good momentum from the investments we're making in our core products.

In addition, the early results from Costco have been very encouraging. New account acquisitions have far exceeded our expectations at over 337,000 to date. Purchase sales for the first three and a half weeks totaled $5.7 billion, with roughly two-thirds being out of store. And the loan portfolio, which we acquired at $10.6 billion in size, had already grown to $11.3 billion by the end of the second quarter. Costco is a great partner, and we're excited about the potential for this business.

We're also very pleased with the renewal of our American Airlines partnership, which was announced earlier this week. We will continue to be the exclusive issuer of credit cards in the majority of acquisition channels, including digital and mobile channels, direct mail, email, phone and Admirals Club lounges. At the same time, we were able to maintain a high quality, growing portfolio and attractive returns. The impact of the renewal should lower pre-tax earnings by approximately $50 million per quarter through the end of next year, primarily due to higher expenses, including the amortization of intangibles. This impact on pre-tax earnings is expected to increase somewhat in 2018 and beyond, as certain additional revenue-sharing arrangements become effective.

Finally, turning to retail services, revenues of $1.5 billion decreased 4% from last year, reflecting the absence of two portfolios we sold in the first quarter, as well as the impact of renewing and extending several partnerships, principally Home Depot. We now have all of our significant partnerships in retail services secured through 2020 or beyond.

We expect revenues to remain around this $1.5 billion level per quarter through the end of next year, as expected volume growth is likely to be offset by the impact of absorbing the more competitive terms in our partnership renewals. We currently expect to operate the retail services business at an ROA in the range of 250 basis points. And we remain open to inorganic growth through new programs and acquisition opportunities given the right strategic fit and return profile.

Total expenses of $2.4 billion in North America increased 5%, driven by the Costco portfolio acquisition, as well as continued marketing investments, partially offset by efficiency savings. And finally, credit costs in North America increased 13% from last year, mostly reflecting a reserve build in branded cards, driven by volume growth and the impact of Costco compared to a reserve release in the prior period.

On slide six, we show results for International Consumer Banking in constant dollars. In total, revenues were flat and expenses declined 1% from last year. In Latin America, consumer revenues were up 4%, as continued growth in retail banking, which grew 7% year-over-year, was offset by a decline in cards. These retail banking results reflect strong volume growth, with average loans and deposits increasing 8% and 10% respectively.

Latin America cards revenues declined 3% from last year. However, we are seeing continued signs of recovery in that business with purchase sales up 7% versus last year. And finally, expenses declined 5% year-over-year in Latin America, mostly on lower legal and repositioning costs, resulting in significant positive operating leverage. Excluding the impact of the gain on the sale of our merchant-acquiring business, in the third quarter of last year, we expect this positive operating leverage to continue in the second half of 2016.

Turning to Asia. Consumer revenues declined 4% year-over-year, driven by lower wealth management and retail lending revenues, while cards revenues were flat to the prior year, which I'll discuss more in a moment. Expenses grew 2% in Asia, in part due to higher repositioning costs.

On slide seven, we show Asia Consumer in more detail. While wealth management revenues were down year-over-year, we did see sequential growth in both revenues and AUM inflows during the quarter, with a declining year-over-year trend in AUMs driven by the impact of lower equity market values. We also saw improvements in card revenues, which were flat to last year. And we continue to believe we are on track to deliver year-over-year growth in the second half of 2016.

Retail Banking revenues, excluding wealth management, were also up sequentially, but declined 2% year-over-year, mostly reflecting the repositioning of our retail loan portfolio away from lower return mortgage loans as well as some de-risking in our commercial portfolio. These actions were partially offset by 3% growth in personal loans, as you can see on the lower right. The net impact was a decline in lending revenues year-over-year in the second quarter. However, we expect these revenues to stabilize in the second half of the year with continued growth in higher return personal loans, and therefore, an improvement in the overall yield of the portfolio. In total, we expect Asia consumer revenues to return to growth in the second half of 2016, resulting in positive operating leverage year-over-year.

On slide eight, we show some key performance indicators for our global branded cards franchise, including year-over-year growth in purchase sales, average card loans and revenue.

In North America, as you can see, these trends show a positive improvement from the Costco portfolio acquisition. But, even excluding that transaction, we continued to show solid progress in our existing franchise with organic growth in purchase sales and average loans of 10% and 3% respectively, and an improving year-over-year revenue trend, which we expect to turn positive in the fourth quarter of 2016.

Turning to Asia, as I discussed earlier, card revenues were flat to the prior year, as we continued to move past many of the regulatory headwinds in that region. Growth in purchase sales slowed this quarter in Asia in part due to actions we took to lower the value of rewards on certain products in Australia in response to regulation that capped interchange rates in that market.

We moved ahead of the market in changing our rewards program and this had a dampening effect on purchase sales this quarter. However, we expect these trends to recover as peers follow suit and consumers adjust to the new programs.

We also reduced promotional rate balances during the quarter, which had a positive effect on yields, but combined with the slower purchase sales growth, this resulted in more modest loan growth year-over-year. We have continued to manage well through the economic environment in Asia, which have seen slower overall market activity relative to last year.

And finally, in Latin America, the trends are improving as well with a sustained recovery in purchase sales beginning to drive loans and revenues. With continued momentum in the back half of the year, we would expect to see loan growth turn positive again year-over-year with revenue growth to follow thereafter.

Slide nine shows our Global Consumer credit trends in more detail. Credit remained broadly favorable again this quarter with stable-to-improving NCL and delinquency rates in every region. The NCL rate in Latin America showed particular improvement this quarter reflecting seasonal payment trends. We expect the NCL rate in Latin America to return to around 4.5% for the second half of the year.

On slide 10, we show the year-over-year EBT walk for consumer on a year-to-date basis. We continue to face headwinds from market-sensitive businesses like wealth management and mortgage on a first-half basis.

As you can see, the continued impact of our cards initiatives on revenues as well, which should abate as we go into the second half of the year. But, the year-over-year impact from regulatory headwinds has slowed from the first quarter and the impact of business growth has become more pronounced driven by the momentum we're seeing in our retail and commercial businesses in North America and Latin America.

Our expense growth in the first half was predominantly driven by investments across our franchise as well as higher repositioning charges in the first quarter, and credit headwinds reflect the absence of prior-period reserve releases. Underlying credit quality has remained stable, with the net loss rate declining year-over-year.

Turning now to the Institutional Clients Group on slide 11, revenues of $8.8 billion in the second quarter grew 2% from last year driven by Fixed Income and Treasury & Trade Solutions. Total banking revenues of $4.4 billion declined 2%. Treasury & Trade Solutions revenues of $2 billion grew 9% from last year in constant dollars driven by continued growth in transaction volumes with new and existing clients.

We continued to capture market share and saw strong momentum across payment products such as U.S. dollar clearing as well as commercial cards, where purchase sales grew 9% year-over-year. Our focus remains on delivering integrated working capital solutions to our multinational clients, addressing their full spectrum of supply chain, trade services, liquidity management, procurement and payment needs around the world. We're seeing the demand for our services increase as corporations seek to optimize their resources in a slow growth environment. At the same time, some of our peers are pulling back from global strategies.

Investment Banking revenues of $1.2 billion were down 6% from last year mostly on lower industry-wide equity underwriting activity, but showed a significant improvement from the prior quarter reflecting a rebound in both market conditions as well as our wallet share in all major products.

Private Bank revenues of $738 million were down 1% year-over-year on lower managed investments and capital markets activity. And Corporate Lending revenues of $389 million were down 18% as higher loan volumes were more than offset by an adjustment to the residual value of a lease financing as well as higher hedging costs.

Total Markets and Securities Services revenues of $4.7 billion grew 10% from last year. Fixed Income revenues of $3.5 billion were up 14% from last year. Rates and currencies drove these results, with revenues up 25% year-over-year including particularly strong performance in the days following the UK referendum.

We saw continued growth in activity throughout the quarter with our corporate client base, which comprises over 40% of our direct-client revenues in rates and currencies.

We believe a greater portion of our rates and currencies revenues are generated with corporate clients relative to that of our peers, which is directly tied to the strength of both our global network and our Treasury and Trade Solutions business. We view this as a differentiating advantage and one that provides scale and stability to our fixed income platform. Spread product revenues declined this quarter versus last year. However, on a sequential basis, we did see a recovery particularly in securitized products.

Turning to equities, excluding the valuation adjustment in the prior year of approximately $175 million, our revenues were down 4% year-over-year, driven by lower market activity as well as the comparison to strong trading performance in Asia in the prior year. And sequentially, revenues grew 12%, reflecting improved performance in derivatives.

Finally in Securities Services, revenues declined 3% year-over-year in constant dollars, mostly driven by the absence of revenues from divestitures. Excluding this impact, underlying revenues were up 2%.

Total operating expenses of $4.8 billion were down 2% year-over-year, driven by repositioning savings and a benefit from FX translation. On a trailing 12-month basis, excluding the impact of severance, our comp ratio remained at 27%.

Total credit costs of $82 million were higher than last year, but down significantly from the prior quarter. Total net credit losses were $141 million, with roughly two-thirds offset by related reserve releases. We also built roughly $30 million of reserves related to non-accrual loans, which increased by approximately $135 million during the quarter.

The cost of credit related to energy was minimal as net credit losses were mostly offset by previously existing reserves and the portfolio benefited from the stabilization in oil prices as well as increased capital markets activity.

Given our target client focus on high-quality corporate credits, certain energy clients were able to access the capital markets as the market environment became more favorable in the second quarter. This allowed these clients to improve liquidity, resulting in either pay-downs or improvement in the credit quality of our exposures. And our reserve-based energy exposures declined this quarter by roughly $400 million in ICG, reflecting the impact of the spring redeterminations. We provide more details on our energy portfolio in the appendix to our earnings presentation. Outside of energy, the cost of credit was concentrated in a few specific credits. Looking forward, we remain cautious and the environment is uncertain, but we could see total ICG cost of credit in the back half of the year in the range of $300 million to $500 million.

On slide 12, we show the year-over-year EBT walk for ICG on a year-to-date basis, which shows significant improvement from the first quarter. We continue to see first-half growth, although modest, in our accrual and transaction services businesses despite certain headwinds this quarter, led by our continued momentum in Treasury and Trade Solutions. And with a strong second quarter performance in markets, we are now flat to last year in Fixed Income and Equities, but remain down year-over-year in Investment Banking, given lower overall market activity.

 

We remain disciplined in our core expense management as we work to realize the benefits of the repositioning actions taken earlier this year to address the structure and capacity in certain parts of our franchise. These higher repositioning costs alone drove approximately $240 million of EBT decline year-over-year in the first half. The remaining EBT drivers were the write-down of our investment in Venezuela, mark-to-market losses on loan hedges driven by spread movements, and of course, the higher credit costs in energy in the first quarter.

Slide 13 shows the results for Corporate/Other. Revenues decreased year-over-year mostly reflecting the absence of real estate gains in the prior year as well as lower debt buyback activity. And expenses increased, driven by higher corporate-wide marketing expenses and an increase in legal and related costs.

On slide 14, we show Citigroup's net interest revenue and margin trends. The bars represent net interest revenue per day for each quarter in constant dollars, showing consistent growth year-over-year in Citicorp while Citi Holdings has continued to shrink.

Our net interest margin was 286 basis points this quarter, lower than our initial outlook of around 292 basis points, driven by an equal combination of higher cash balances, lower trading NIM and lower loan yields. Looking to the second half of the year, NIM should recover to around 290 basis points or slightly higher, driven by a 3-basis-point improvement from Costco as well as a normalization of average cash balances. This is lower than our prior outlook of around 295 basis points for the remainder of the year, reflecting somewhat lower loan yields as well as the absence of a previously assumed rate increase in the U.S.

On slide 15, we show our key capital metrics. During the quarter, our CET1 capital ratio increased to 12.5%. Our supplementary leverage ratio improved to 7.5% and our tangible book value per share grew by 7% year-over-year to $63.53.

Before I turn it over to questions, let me make a few comments on our outlook for the third quarter. In Consumer Banking, revenues in North America should grow sequentially, driven by branded cards, mostly reflecting the impact of the Costco acquisition, which should generate incremental revenues of roughly $200 million over the second quarter.

International Consumer revenues should grow modestly from the second quarter, resulting in year-over-year improvement in both Asia and Mexico, excluding the gain on the sale of our merchant acquiring business last year.

Turning to the Institutional business, we expect market revenues to reflect a normal seasonal decline from the second quarter, while Investment Banking revenues should be largely stable assuming that market conditions remain favorable. And we expect continued year-over-year growth in our Treasury and Trade Solutions business as we continue to win new mandates and support our clients' day-to-day banking needs around the world.

Finally, to complete the revenue picture in Citicorp, Corp-Other revenues are expected to be close to zero, down from recent levels in the $100 million to $200 million range, driven by lower debt buyback activity and the absence of certain other episodic gains.

Core expenses in Citicorp should be slightly down from the second quarter, reflecting the impact of repositioning savings, partially offset by higher expenses related to Costco and other branded cards investments. And credit costs in Citicorp should be somewhat higher than the second quarter, mostly driven by reserve builds from volume growth and the impact of the Costco portfolio acquisition.

Citi Holdings should be at breakeven for the quarter.

And with that, Mike and I are happy to answer any questions.

## QUESTION AND ANSWER

**OPERATOR:** (Operator Instructions) Your first question comes from the line of Jim Mitchell with Buckingham Research. Please go ahead.

**JIM MITCHELL:** Hey, good afternoon, guys.

**JOHN GERSPACH:** Hey, Jim.

**JIM MITCHELL:** Just a question on the energy credit. I think you said in June, around $1.2 billion of, I think, energy-related credit costs, I think if my math is right, you did about $500 million year-to-date. And now you are saying $300 million to $500 million in the second half. Is that – right so eight – is that kind of the way to think about it, $800 million to $1 billion right now?

**JOHN GERSPACH:** Well, the $1.2 billion, Jim, that was our reference to total ICG cost of credit. That was not specific to energy at that point in time.

**JIM MITCHELL:** Okay. Fair point.

**JIM MITCHELL:** So, is – but it does seem like it's a little bit of a step-down versus expectations, even...

**JOHN GERSPACH:** Well, it's certainly, when you take a look at the first half, which is about a $500 million cost of credit in ICG, and with the second half range of $300 million to $500 million, that gives you your comparison of $800 million to $1 billion against the previous $1.2 billion, so yes, it is a step-down.

**JIM MITCHELL:** And is that just simply the improvement in the capital markets and what you're see in terms of experience with the energy space and them getting capital, is that the big change or is it oil prices or just a combination of both?

**JOHN GERSPACH:** Well, it's a combination of both. It certainly – we're benefiting – that outlook benefits from what we are seeing is a stabilization of energy cost with oil in that $45 a barrel range. But I think it also reflects the overall resiliency in our credit portfolio, which is what we've been talking about. We described to you the quality of our energy exposure in the past. First quarter – even in the first quarter, we said 73% of our energy exposure was to investment grade names. That has continued to remain at 73% in the second quarter. The funded loan book at the first quarter was 63% investment grade, that's actually improved now to 65%. And because we're concentrated in those high-quality names, they do have access to capital markets and therefore are able to strengthen their balance sheets.

**JIM MITCHELL:** Right. And E&P balances were down too. Okay...

**JOHN GERSPACH:** Yeah. I mean, when you take a look at what we've been able to do, we've traded off, we've reduced the high-risk portfolio and remained more concentrated in the high-quality portfolio.

**JIM MITCHELL:** Right. Maybe just one follow-up on Costco. It seems like it's off to a pretty good start. You obviously are going to be building reserves there, do you expect it to be additive to earnings, neutral to earnings, as we think about the combination of expenses, revenues and provision build?

**JOHN GERSPACH:** Yeah, Jim, our view going into the acquisition is that in this first year in 2016, it would likely be neutral to earnings just because of the mechanics behind the reserve build. And so that's our view right now. We'll give you more updates as to how it could impact 2017 certainly as we get later in the year. But for now, I'd say, 2016 on an EBT point of view is basically neutral.

**JIM MITCHELL:** Right. So, still sticking to neutral. Okay. Thanks a lot.

 

**JOHN GERSPACH:** Okay, Jim.

**OPERATOR:** Your next question comes from the line of Glenn Schorr with Evercore ISI. Please go ahead.

**GLENN SCHORR:** Hi, thanks.

**JOHN GERSPACH:** Hey, Glenn.

**GLENN SCHORR:** In cards, when I take a step back and I look at all the – either renewal of rates or the acquisition cost. Cards is a super tough business right now or I should say super competitive business right now. So I heard your comments that the 250 basis point ROA on the retail partner. Could you maybe talk about where the cards' overall ROA and ROTCE is now and where it should be going forward? It kind of follows on, on Jim's question. I'd just like to sort of make sure we're growing profitability here and not just volume – an important business for you, guys.

**JOHN GERSPACH:** No, again, as we said, longer term, our view is from a branded cards portfolio, we want to be running that portfolio at about 225 basis points to 235 basis points, which is consistent with where we were entering into the crisis. So, what you've seen through the crisis is an impact on ROA first with a severe downturn in ROA as everybody built reserves and worked their way through the credit issues. And then coming out, now we've all benefited from reserve releases. So today, we were getting ROA in branded cards something close to 300 basis points, but a lot of that has been fueled by reserve releases. The business that we're building in branded cards is one that is set to yield an ROA of 225 basis points to 235 basis points where we were going into the crisis and with a better, with a higher-quality book of business. And it's the same story with retail services. That 250 basis points is what we think is a realistic long-term return with that business.

**GLENN SCHORR:** Got it. I appreciate that. You mentioned the renewal on American. Most of the channels – I saw that Barclays had gotten – I think it was the airport and on-the-plane, which I'm not sure what that means, but what percentage of the originations in the past came from those channels? Like, do I care?

**JOHN GERSPACH:** Well, I mean, it certainly is a smaller amount of the origination than what we would believe that we are going to be able to achieve through the channels that we retain. The on-airline and in-airport, the – I'd call it the Travel Day type of acquisitions, that was not a particular strength of ours anyway.

**GLENN SCHORR:** Okay. I appreciate that. One last one on – which one to choose? Okay. I saw the commentary on the more preferreds coming. With capital on raise and leverage ratios so strong, like really strong, and a payout ratio still at 70%, I'm just curious where the incremental preferreds, what's their purpose? Where are they going, and why do you need them?

**JOHN GERSPACH:** Glenn, maybe I misspoke, or – but no, we're not signaling that we're issuing more preferreds. We're – we've done our preferred issuance for now. Given the capital stack that we have right now, our preferreds are where they are. But that did – since we now are settled, for a couple of quarters, you're going to see the preferred dividend then increase over where they were prior year. We've given you...

**GLENN SCHORR:** Oh, no problem. I got it.

**JOHN GERSPACH:** Okay. So, if you take a look at slide 32, that just sort of – we just want to level-set your expectations as to where preferred dividends will be reflected. But all these preferred dividends reflect issuances already done.

**GLENN SCHORR:** Totally appreciate it. Thank you. I appreciate it. Thanks.

**JOHN GERSPACH:** Okay, Glenn. Thank you.

 

**GLENN SCHORR:** Bye, John.

**OPERATOR:** Your next question comes from the line of John McDonald with Bernstein. Please go ahead.

**JOHN MCDONALD:** Hi, good morning. As Mike noted, earnings came in nicely; better than the first quarter. Just wondering, John, what are some of the items that got better since the early June guidance that earnings looked kind of flattish with the first quarter.

**JOHN GERSPACH:** Yeah, I'd say several things improved, John. Clearly, Markets revenues were improved. What we found is during the month of June, we were able to engage with our corporate clients. They were seeking advice as to how to handle the volatility both leading up to the UK referendum and then certainly subsequent to the UK referendum, and that gave us a great opportunity.

But at the same point in time, because the capital markets remained open during the month of June, we did benefit from a lot of our energy clients then being able to access the client, so that produced a much lower cost of credit than I think Mike had probably indicated when he spoke at the conference in the early part of June.

And finally, we saw improved momentum in Mexico in the retail bank during the month of June. We noted that overall, consumer revenues in Mexico grew 4% year-over-year. That was higher than what we had thought that was going to be when Mike spoke. So we had – we had momentum building in Mexico, we had good engagement with clients throughout the whole UK referendum, and then we benefited from the lower cost of credit, again, because of the high quality of our book.

**JOHN MCDONALD:** Okay. And you mentioned the corporate credit getting better, and you gave an outlook for the cost of credit for ICG looking ahead. How should we think, John, about the provision trend in cards and overall consumer going forward from here?

**JOHN GERSPACH:** Well, again, that's going to tend to increase for two reasons. One is, as we build additional ANR – and we're definitely in a growth mode when it comes to our branded cards book – we're going to need to build reserves just because of the volume. And then with Costco, again, when you get into purchase accounting, you've got a heavy front-end build on LLR.

**JOHN MCDONALD:** Okay. And then just one final thing on Costco. As you mentioned it, that's starting to grow and you're getting the accounts. There have been some press stories and anecdotal reports of difficulties in the initial rollout. Were there some operational snafus that occurred? Have they been fixed, and is everything running right now? Could you just give us an update on that?

**MIKE CORBAT:** John, it's Mike. I would say that we experienced extremely high calling volumes in the early implementation of it. We put a lot of resources at it. Questions around card activation, questions around statements, questions around where to send payments, and so we're working through that. We're gaining on it. We're very focused on it. We've got a lot of resources deployed against it, and it's something we think we can fix in the short order.

**JOHN MCDONALD:** Okay. But you did mention, John, that the accounts are growing?

**JOHN GERSPACH:** Sign-ups are definitely growing. I mean, 330,000 new card acquisitions just since we took over the book. That far exceeded our expectations by a factor of two, two-and-a-half times. So again, we're really excited about it. I think it speaks to the quality of the value proposition that we put forward with that card in partnership with Costco.

**JOHN MCDONALD:** Right. So it's just dealing with the volume operationally is what you're still working through?

**JOHN GERSPACH:** Yeah. Again, as Mike's mentioned, the call wait times are coming down, but if it's not the largest, it's got to be one of the largest portfolio implementation transfers on a single day that's ever been attempted. And that's not to give us excuses. I mean, we should be performing better than we are, but we're working on that. But again, it's a massive program.

**JOHN MCDONALD:** Okay. Thanks.

**OPERATOR:** Your next question comes from the line of Brennan Hawken with UBS. Please go ahead.

**BRENNAN HAWKEN:** Good morning. Thanks for taking the questions.

**JOHN GERSPACH:** No problem, Brennan.

**BRENNAN HAWKEN:** On card, another one here, the velocity in North America has been really, really good in both purchase volume and ANR. How long should we think about that sustaining? And given some of the deals you've just walked down, from a modeling perspective, how long can that sustain?

**JOHN GERSPACH:** Well, that's a great question. We don't anticipate the same level. Now, you've got two things – two factors. One is, Costco, obviously, is going to benefit us now for the next year. So we're going to get a tremendous pickup from Costco. Absent Costco though, we will begin on an ex-Costco basis, some of that growth – we had 10% growth this quarter in purchase sales year-over-year excluding Costco. That will begin to moderate sometime around – towards the end of this year, the beginning of next year. But again, we still anticipate getting good volume growth, but you're not going to get the same bump that you have when you start an investment program.

**BRENNAN HAWKEN:** Right. Okay. Thanks. We also recently heard about some of your competitors widening out their credit box in card in recent years. Have you guys done that too? Have we seen a shift down within the Citi portfolio, a bit of an expansion as far as credit? Or can you maybe give a little color on that?

**JOHN GERSPACH:** No, we're still focused on the same target client that we had going in. If we've moved by a basis point or two in FICO, that's about it. But when you take a look at where we're focused right now, it's still on the same target client that I described to you in the past. And with the renewals that we've done and with the new partnership with Costco, I think that speaks to the type of client that we're really looking to build on.

**BRENNAN HAWKEN:** Terrific. Just wanted to make sure. And then last one from me, the card trends in Asia, I appreciate your comments on the lower rewards in Australia. But when we look at the loan balances, it doesn't look like Australia is really all that big. Can that really move the needle? Can you help us understand how that would actually drive that – those metrics?

**JOHN GERSPACH:** Again, it's not going to drive in this quarter ANR, but it is going to drive purchase sales. So, we have a lot of usage coming out of Australia, so the drop-down in Australia itself cost us a full percentage point on purchase sale growth year-over-year.

**BRENNAN HAWKEN:** Okay. And then, that'll probably just sustain for a year, that lower volume because it sounds like that's probably pretty structural given the changes in that market.

**JOHN GERSPACH:** Well, what I would actually think is that as the other card issuers in Asia also adjust their rewards programs, what you'll see is less of an impact where people stop using their Citi card and as the programs become more consistent and more competitive with each other, we should get a pickup back again. So I don't think that this is more than a one or two quarter blip-down in purchase sale growth in Asia.

**BRENNAN HAWKEN:** Okay. And have you seen competitors move yet or just – you're just anticipating it?

 

**JOHN GERSPACH:** I don't have anything particular in front of me that would indicate what we've seen yet on behavior. We'll get back to you.

**BRENNAN HAWKEN:** Sounds good. Thanks a lot.

**JOHN GERSPACH:** All right.

**OPERATOR:** Your next question comes from the line of Mike Mayo with CLSA. Please go ahead.

**MIKE MAYO:** Hi. John, you touched on Mexico earlier, but can you talk about Mexico more generally? Where do you see it in its profit cycle in addition to just consumer, which you said is improving? And then a question for Mike. Under what circumstances would you consider a sale of Mexico? I know I've asked that in the past, but your discount to tangible book keeps getting steeper and steeper, especially as your tangible book value continues to climb?

**JOHN GERSPACH:** So, to handle the first part of that question, Mike, we're seeing good momentum throughout our Mexico franchise. We've actually had great momentum in our ICG business in Mexico throughout the past year, year-and-a-half. It's consumer where we had a bit of a slowdown in that momentum which we're now working our way out of, which is why we find getting 4% year-over-year revenue growth to be a nice start. Positive operating leverage this quarter; positive operating leverage in the back half of this year. We anticipate having positive operating leverage coming out of the consumer business in Mexico straight on through 2017. So we've got an improving cards picture. We've got a vibrant retail banking picture going on in Mexico, so we see that as an engine for growth out into the future.

**MIKE CORBAT:** And Mike, from the strategic perspective, it really dovetails off of what John just described. As we've talked about, we like the demographics of Mexico, the growth prospects, where they are now post reforms, the position of Banamex in terms of its retail and consumer franchise, the scale of that, our ability to compete. And so in a world that we see at least for the future ahead of us right now, growth in the world's a pretty tough thing to find. We think Mexico offers that. So based on what we see and what we think the opportunities are in the franchise, we think it's accretive to our shareholders, the returns are solid, and we think we've got the ability to continue to expand those. So right now, I really don't see a scenario where we would contemplate selling it.

**MIKE MAYO:** The spirit behind the question – and I know you understand this. I mean, the tangible book is close to \$64 and the stock price is \$44. And at some point, the best investment is buying back your own stock. And if you created asset sale gains to be allowed to buy back more stock, isn't that something you should consider? And you've made a lot of strides. You've discarded many consumer operations outside the U.S. You've reduced the size of Citi Holdings. And just – can't you reaccelerate some of that restructuring?

**MIKE CORBAT:** Well, if you look, we just announced a pretty meaningful capital return. We're in the market and we'll be buying back \$8.6 billion worth of stock over the next four quarters. As you look at our math and you look at our capital return capacity, we're going to have a lot of ability to buy stock back. And when you think about the trade-offs between the stock buyback and growth, you've got to find the right balance. So again, if we can execute on the things that we want to execute, create the earnings, continue to liberate the DTA, we're going to have a lot of firepower against the stock. And I'd like to keep investing and making sure we're finding and continuing to build on growth.

**MIKE MAYO:** All right. Thank you.

**OPERATOR:** Your next question comes from the line of Erika Najarian with Bank of America. Please go ahead.

**ERIKA NAJARIAN:** Hi. Good morning.

**JOHN GERSPACH:** Hey, good morning.

**ERIKA NAJARIAN:** So because of your capital excess in both CET1 and SLR, your name keeps coming up as someone that can continue to take market share, particularly in ICG. And I'm wondering if there are limitations on growth or balance sheet allocation that we're not thinking about. And I guess the real question here is, where are you in terms of your scoring range on your G-SIB surcharge? And is keeping your surcharge where it is today a bigger priority than potentially growing the balance sheet in a greater way to gain market share, given how volatile that score can be?

**JOHN GERSPACH:** Great question, Erika, and one that we contemplate every day. There is a series of constraining factors that we constantly try to optimize against. G-SIB score is one of them, LCR, CET1, stress test capital, call that CCAR capital, there are just many. And all those ratios on both an advanced approach basis as well as a standardized approach basis, so it's a constant trade-off. But the G-SIB is certainly one of those things that we look at when we're making decisions. And to your point, as was previously disclosed, we got into the 3% bucket last year. We worked to get there and we ended the year, I'd say, in the very high end of that score range. And one of our goals is to remain a 3% G-SIB, in that 3% bucket at year-end this year. And so we're actively managing each of the many elements of the score in order to optimize the returns of the franchise. And you're right. Those indicators can fluctuate quarter to quarter, but it's something that we're trying to actively manage. When I look at the preliminary results that I have for our 6/30 G-SIB score, we come out right at 630. So we're right in that range of where we need to be and we're going to keep on working to make sure that we end the year below that 630 target.

**ERIKA NAJARIAN:** Got it. And just a follow-up question on the margin; appreciate the color that you gave in terms of the puts and takes of Costco for the second half of the year. If the slope of the curve persists, or there is continued pressure on the long end, how should we think about how the margin will progress from that 290 basis points level?

**JOHN GERSPACH:** Well, we're more weighted, especially short term, to the short end of the curve. What we've told you in the past is, if the rates move by 100 basis points, we'll generate an additional, around the world of $1.9 billion of additional net interest income. And most of that $1.9 billion would be concentrated in the U.S., which is at about $1.4 billion, and most of that $1.4 billion is focused on the short end. So the long end of the curve, especially in the near term, the next year, year-and-a-half, doesn't really impact us all that much.

**ERIKA NAJARIAN:** Got it. Thank you.

**JOHN GERSPACH:** Okay. Not a problem.

**OPERATOR:** Your next question comes from the line of Ken Usdin with Jefferies. Please go ahead.

**KEN USDIN:** Thanks a lot. John, we saw a progress this quarter in the efficiency ratio as you mentioned and I was just wondering, is the prior comments you had made about 58% in Corp for the year still relevant given the trends that we've seen? Or is there anything that kind of coming out of the second quarter with the 57% that makes you feel any better about the second half?

**JOHN GERSPACH:** I still feel pretty good about the second half. But what we had said at the end of the first quarter was that our target would be to do 58% efficiency for the full year given the first quarter results, and I'd say that's still where we're targeted. It's at or around that 58% efficiency ratio in Citicorp for the full year.

**KEN USDIN:** Okay. And I know it's hard to talk about seasonality, given the flurry that we just had of activity in the Markets business in June, but how would you characterize how we should think about, quote unquote, seasonality or normal seasonality in the summer for the business? And have you seen any change in activity as things have kind of calmed down post the initial reaction of Brexit?

**JOHN GERSPACH:** Well, we're still very, very, very early in the third quarter. So it's a little hard to comment on activity for an entire quarter after just eight, nine, ten trading days. But the activity levels are fine. I think it's good, and we'll have to see how everything holds up then through the month of August. But again, the beginning part of July looks fine.

**KEN USDIN:** Great. One last little one for me, just in terms of your NIM comments and then just that we know that Costco's got a full quarter in the third, is it pretty good line of sight in terms of being able to grow NII from here?

**JOHN GERSPACH:** I like the prospects of growing NII. I mean, obviously with Costco coming on, that gives us a big boost. I talked about the momentum that we've got for the consumer businesses in Asia, in Latin America, with branded cards. I don't have a prepared comment on guidance on NII. I don't like to give guidance on individual line items of income, but yes, we feel very good about the NII and that's why we feel that the NIM should improve back up to the 290 basis points or maybe a little higher range in the second half of the year.

**KEN USDIN:** Okay. Understood. Thank you.

**OPERATOR:** Your next question comes from the line of Eric Wasserstrom with Guggenheim Securities. Please go ahead.

**ERIC WASSERSTROM:** Thanks. John, a couple of questions. The first is on slide 28 where you have the ICG unfunded corporate energy exposure.

**JOHN GERSPACH:** Yes?

**ERIC WASSERSTROM:** The BB and B component looks like it actually grew by close to $1 billion versus last quarter, and I'm wondering if that's from actual additional exposure or is that from the ratings migration of existing exposures?

**JOHN GERSPACH:** Yeah, some of that is migration. There is a variety of factors that go into that. But there is nothing in there that would indicate that there's something deteriorating or anything else. It's just a series of puts and takes.

**ERIC WASSERSTROM:** Okay. And I think you previously indicated that 65% of the total of about $35 billion is either investment grade or has credit support. Has that figure changed at all?

**JOHN GERSPACH:** I don't have that in front of me, so I apologize for that. We'll have to get back to you. I don't think that there's any big deterioration there, but I just don't have that with me.

**ERIC WASSERSTROM:** Okay. Great. No problem. And then just following up on sort of several of the questions and your response as we think about the back half of this year, it sounds like what you're pointing us towards is balance sheet expansion driving NII growth with perhaps a little bit of a lift also from NIM, continued positive operating leverage from lower repositioning costs, and some improvement in the provision guidance, although still incremental build, but potentially some lesser degree of trading revenue. Is that broadly correct?

**JOHN GERSPACH:** Well, I'm not going to comment on what you might pull out of your own model, but in broad strokes, I would be cautious about thinking that I've guided you to balance sheet expansion. Balance sheet expansion is not really something that we're targeting. As I said, we still believe that we can optimize our balance sheet, so I wouldn't factor in undue expansion of the balance sheet.

 

**ERIC WASSERSTROM:** Okay. Yeah, sorry, I was sort of thinking of within Citicorp rather than broadly. But would Citicorp still be broadly low? I think it was about up about 1% in the period?

**JOHN GERSPACH:** The balance sheet growth?

**ERIC WASSERSTROM:** Yeah.

**JOHN GERSPACH:** I'm not prepared to give forward guidance on the balance sheet. Let's just say that, again, from the overall level of about $1.8 trillion for the overall Citigroup, that's broadly the area that we still believe that we should be operating in.

**ERIC WASSERSTROM:** Great. Thanks very much.

**OPERATOR:** Your next question comes from the line of Steven Chubak with Nomura. Please go ahead.

**STEVEN CHUBAK:** Hi. Good morning.

**JOHN GERSPACH:** Hi.

**STEVEN CHUBAK:** So, John, I had a quick question on CCAR, maybe a bit of a follow-up to Erika's earlier question. The results are priced very positively in the latest round. As you prepare for some of the tougher elements like G-SIB surcharge inclusion, how are you thinking about the capital minimums or target that you need to amass to day-to-day as part of your allocation process? I'm just trying to get a sense as to whether this has changed significantly just given the favorable results that we saw in the latest stress test round.

**JOHN GERSPACH:** Well, first of all, Steven, I wouldn't know what to do about G-SIB surcharge in CCAR because unless something happened this morning while I've been sitting here, we haven't seen any proposed rule yet. So that's something that we're obviously aware of the rhetoric that's out there, but again, we just don't know, so that has not impacted our planning as yet at all.

**STEVEN CHUBAK:** Okay. Got it. And I recognize, John, that you don't want to give explicit guidance on balance sheet growth expectations, but the RWA has come down in the quarter. And given the growth in both loans and assets, I'm just trying to get a better handle as to what was driving that. I know that there was some FX translation impact that could influence the moves in RWA. But given how much Holdings has shrunk, is it reasonable to assume the RWA growth will wrap Citicorp growth going forward.

**JOHN GERSPACH:** Yeah, actually, Steven, if you look, Holdings' RWA declined by about $8 or $9 billion in the quarter. And if you look, our RWA overall dropped by about $8 billion in the quarter.

**STEVEN CHUBAK:** Got it, okay. And one more quick modeling question for me on legal and repositioning costs. You guided to the 225 basis points for Citicorp for the full year. It looks like there's been a higher run rate in those expenses in the first half. What's a reasonable expectation for what we should be modeling for the second half for legal and repositioning?

**JOHN GERSPACH:** I would still say that for the full year, the 225 basis points is still a pretty good number.

**STEVEN CHUBAK:** All right. Perfect. Thank you very much.

**JOHN GERSPACH:** Okay.

**OPERATOR:** Your next question comes from the line of Matt O'Connor with Deutsche Bank. Please go ahead.

**MATT O'CONNOR:** Hello.

**JOHN GERSPACH:** Hi, Matt.

**MATT O'CONNOR:** Just stepping back, bigger picture, you've done a lot of work in the credit card businesses, a lot of upfront investing; obviously, renewal of some contracts, gaining some contracts. So there's still obviously the execution to do, but it seems like the heavy lifting has been done from an investment point of view. If you look at the rest of the franchise across the products and the markets, are there other areas that you want to focus on increasingly so on investment dollars or do we start to see maybe some moderation in some of the spend?

**MIKE CORBAT:** From an investment perspective, Matt, I think we've remained largely consistent to things that we've talked about before. So we've talked about equities and we've talked about what we're trying to do there, the combination of the prime brokerage, the combination of cash, derivative, Delta One and investments in people, balance sheet, et cetera. So those continue. Investments in our network and our cash management business, investments in digital, in our interface on the consumer side, so again, things that we've consistently spoken about, those investments continue.

**MATT O'CONNOR:** Okay. So is it fair – I mean it feels like the credit card and some of it shows up in expenses and some of it's a contra revenue. But it seems like that was a pretty big effort to get behind you. And are these other things more kind of in the run rate or business as usual?

**MIKE CORBAT:** I would say from a technology perspective, we probably need to think of a lot of those investments ongoing as business as usual. I think of the equities investment as probably being slightly different in terms of there is a life to it and there is a set of expectations that we've got to make sure we achieve out of those investments.

**JOHN GERSPACH:** I think, Matt, what you'll see is we'll continue to invest where we have the prospects for growth. So you're likely to see, still, we'll have investment spending in Mexico, but that is captured in the guidance that I gave you as far as our belief of generating positive operating leverage in the second half of this year and positive operating leverage in Consumer in 2017. So that's embedded in that. We'll continue, throughout the U.S., to spend money to enhance our digital capabilities. So we do have investment dollars at play. So I don't want to tell you that we're not going to be investing. Just to keep our TTS network in play, we spend hundreds of millions of dollars a year. That is not going to stop. But I think the spirit that Mike and I are trying to answer your question is we don't see any large lumpy dollar where we're going to tell you that this is going to be some negative impact on our financial performance for the next several quarters.

**MATT O'CONNOR:** Okay. That's what I was getting at. That's helpful. Thank you.

**MIKE CORBAT:** Okay.

**OPERATOR:** Your next question comes from the line of Betsy Graseck with Morgan Stanley. Please go ahead.

**BETSY GRASECK:** Hi. Good afternoon.

**JOHN GERSPACH:** Hi, Betsy.

**BETSY GRASECK:** So, a question on capital creation because clearly, you're creating capital faster than earnings, thanks to things like holdings shrinking and the DTA utilization and all of that. And I'm just wondering, do you get any credit from the regulators for this, in your opinion. And is there an opportunity do you think at some point, maybe it's once we get through the CCAR buffer, for G-SIB that's coming. Do you think there is a point when you'll be able to talk to them about the DTA utilization and the incremental capital from that going towards share repurchase as opposed to factoring into the whole CCAR process?

**MIKE CORBAT:** When we think about capital generation and in particular capital returns, we don't, as you referenced, think of that in terms of earnings because we've got the capacity, and I think slide 33 shows the drivers of capital and DTA. That we've got this ability through the utilization of DTA, and again $10 billion used since it peaked to generate regulatory capital at a pretty significant rate. So we understand that if we're not returning all of that excess capital. And so as we measure ourselves, we measure ourselves against binding capital constraints, and today that would most likely be CCAR. What do we need to run the institution, and what do we need as a buffer, and it's our intention overtime to return all of that excess back to the shareholders that we can't use. And in this environment, that's probably the bulk of earnings and DTA liberalization. And when you think about the difference between our TCE and CE Tier 1, it's largely the $29 billion of disallowed DTA. And so as we liberate that, we'd like to return that. I think as part of that conversation, that's not, nor will be, a perspective conversation, but as we liberate it, we then want the ability to return that in arrears. And we've been in conversations with our regulators about that and that will, I think continue to show itself over time.

**BETSY GRASECK:** So I guess you know is this upcoming rule that we're waiting for from the Fed regarding the G-SIB buffer, G-SIB surcharge increase for the folks like you, that we're waiting for to it get through that and then maybe the ask can go up? I'm just wondering how you think about timing around that?

**MIKE CORBAT:** We've consistently talked about walking the ask up. This year was a tripling of the dividend, a meaningful increase in terms of buyback, and it's our intention around the right operating environment and the right results to continue to do that. And again going back to the knowing that unless we do that and we return or use all of this excess capital, we're going to have a denominator problem. And so, we're committed to doing that.

**BETSY GRASECK:** Okay. Thanks.

**OPERATOR:** Your next question comes from the line of Matt Burnell with Wells Fargo Securities. Please go ahead.

**MATT BURNELL:** Good afternoon. Thanks for taking my question. Just a couple of quick ones. First of all, John, in terms of the DTA utilization you've mentioned a couple of times on the call freeing up that asset. I guess I'm just curious why the pace of the DTA utilization was so much slower in the second quarter than the first quarter given it looks like North American consumer profitability, pre-tax profitability, was roughly similar quarter-over-quarter. And just looking through some the ICG numbers, it appears North American profitability there was also relatively similar quarter-over-quarter?

**JOHN GERSPACH:** Yeah, Matt. If it was very simple to give you the formula as far as how you drive down the DTA, I'd love to lay it out, but it just doesn't work that way. It has to do with certainly where the earnings are generated, importantly how much of that is coming out of current taxes that are due as opposed to how much you can put against your deferral. So it's difficult to give you, well, if earnings are this then the DTA will be that. There's just a lot of other things that go into it. But in general, again, we're focused on driving it down. And, I think as Mike said, we've obviously been able to do that $10 billion of utilization over the last couple of years. And we should be able to continue to utilize it somewhere in the range of $1.5 billion to $2 billion a year. That's going to be the pace.

**MATT BURNELL:** Okay. And then just moving on to page 24 of the supplement. I realize we're looking at end-of-period balances so there may be something skewing this a little bit. But the corporate loans in EMEA grew in the second quarter at a much faster rate than you've seen them grow year-over-year. I'm curious if that is sort of a one quarter blip possibly driven by Brexit or are you really driving market share gains on the lending side partly because of some of the challenges of the European banks?

**JOHN GERSPACH:** Yeah. I don't have a great answer for you on that, Matt. I'm sorry.

**MATT BURNELL:** Okay. And then just finally, John, maybe following up on Betsy's question. Looking really at this CCAR cycle, you've obviously had some good news in terms of the living will, your CCAR proposal was accepted without any change. I guess I'm curious how you're thinking about potentially requesting a de minimis or a further increase in the buyback in this CCAR cycle using the de minimis exception.

**MIKE CORBAT:** Matt, in that, I would say that it's still relatively early in the year. Let's see how the year progresses and where we are and we'll make that judgment or that call later in the year.

**MATT BURNELL:** Okay, thanks very much.

**OPERATOR:** Your next question comes from the line of Brian Kleinhanzl with KBW. Please go ahead.

**BRIAN KLEINHANZL:** Hello, thanks.

**JOHN GERSPACH:** Hey, Brian.

**BRIAN KLEINHANZL:** I have two questions, first on the Costco. You mentioned that the reserving would start in the back half of this year, but do you get from the fair value marks, does that last you the third quarter, so you're not really going to see the reserving start until the fourth quarter? Or does that start as early as the third quarter?

**JOHN GERSPACH:** No. It actually started in the second quarter, but again, we only had the portfolio for 13 days. But if you remember, we kind of went through a similar set of discussions about LLR build when we acquired Best Buy back in 2013. And so as you correctly stated, when we purchase a loan portfolio, we acquire the receivables and they're recorded at fair value so there's no corresponding loan loss reserve. Therefore, as new loans are originated, the LLR is built. Now, if you think about the difference between an acquired portfolio and a mature portfolio, in a mature portfolio, that build would be offset by LLR releases for loans that actually paid off. However, since the acquired loans don't have an LLR, there's no offsetting releases as they pay down. So that means that your rate of build to a, let's call it, normalized LLR for an acquired portfolio is actually dependent on how fast the new loans are created as well as how fast the old loans pay down. So it's the paydown rate, really that's the predominant driver of the pace of the LLR build as the portfolio gets replenished with new spend on existing cards. So since Costco has a high paydown rate, the LLR build on the Costco portfolio is going to be more frontloaded than was the case with Best Buy. So I actually think that what you're going to see in the third quarter could very well be the highest quarterly LLR build that we will see as a result of acquiring the portfolio.

**BRIAN KLEINHANZL:** Okay. Thanks. That's very helpful. And then, also related to Costco, on the purchase, obviously, the intangibles went up. What's the life of those for the amortization schedule? Is it amortized over one year, two years?

**JOHN GERSPACH:** Well, the intangibles were tied back to the contract.

**BRIAN KLEINHANZL:** Okay. And then just lastly, I guess, going back to 2013. I mean, Mike, you provided a nice update as to – back in March of 2013 as to your long-term strategy of where you're going to be investing. Is there any plans to provide another one of those updates and kind of benchmark what you've done over the last three years, because there's a lot that's been done kind of what you're going to do to kind of drive the company forward?

**MIKE CORBAT:** Yeah. We plan on doing that. We haven't set a date in terms of coming out, but probably sometime over this summer or as we get to the end of the third quarter, we'll probably come out with some talk about when we're going to go out more broadly.

**BRIAN KLEINHANZL:** Great. Thanks so much.

**OPERATOR:** Your next question comes from the line of Gerard Cassidy with RBC. Please go ahead.

**GERARD CASSIDY:** Thank you. Good afternoon, guys.

**JOHN GERSPACH:** Hey, Gerard.

**GERARD CASSIDY:** John, you talked about how you had better-than-expected growth in the number of new cards from the Costco – new accounts from the Costco acquisition in these early days. Were the purchase sales as better than expected as the acquisition of the new accounts?

**JOHN GERSPACH:** Purchase sales, I can say, are running roughly in line with what we had anticipated. Maybe a little bit higher but roughly in line.

**GERARD CASSIDY:** Okay. And the two-thirds outside of the store, is that in line with your expectations as well on the purchase sales?

**JOHN GERSPACH:** That's in line.

**GERARD CASSIDY:** Yeah. Is there any way of taking this bigger with your global reach outside the U.S. than what maybe American Express could have done with Costco?

**JOHN GERSPACH:** I'm not prepared to talk about – let's absorb what we've got right now first. Obviously, we're still working through the $11 billion portfolio that we have, 11 million new card members, let's give them a delightful experience first and then we'll think about international.

**GERARD CASSIDY:** Okay. Clearly, you guys have made a commitment to cards with this acquisition and your other acquisitions. Are there any other portfolios that you're aware of that might come up for bidding in the next 12 months or 18 months of meaningful size?

**MIKE CORBAT:** Of meaningful size, there's a couple intermediate-sized bites over the next few years, but there's nothing of any real significance. And obviously, like we have in the past, we'll continue to look at those. And if the numbers and returns work, we'll obviously compete for them, and if not, we won't.

**GERARD CASSIDY:** Okay. There's a lot of moving parts to this question. Obviously, you guys are very well capitalized. The regulators control what you can give back in excess capital, similar to your peers. Is there ever a thought of if you're limited – and we won't know for a couple years that you can only give back what you earn every year and nothing above it. Is there a thought with your investments in the digital consumer capabilities that you're doing, that mobile channel, to pursue a more aggressive consumer business in the United States? Obviously, you don't have a retail branch network, and you probably don't need it in the future like some of your bigger peers, but is there any thought that you guys have as to – your mobile channel is very robust, very strong, can you take that even bigger to grow that faster nationwide?

**JOHN GERSPACH:** Well, I think we have that opportunity whether or not we have the issue that you talked about, which again, I don't think we're going to end up with. But even if we are able to return all the capital that we think we have, I think we still have the opportunity to grow our consumer business in the U.S. as a result between digital and mobile, and those are things that we're definitely focused on.

**GERARD CASSIDY:** Okay. Shifting gears on you, I know you talked about the ICG business, and obviously what went on post-Brexit with the trading. Was there any significant change in the pipeline in Investment Banking activity post-Brexit? I know it's not that long ago, but anything there to talk about?

**MIKE CORBAT:** You know, I think the pipeline remains pretty strong. And actually, on the heels of Brexit, we saw actually quite good deal flow. You saw debt capital markets, you saw equity capital markets, you saw M&A getting executed, getting announced. So I would say that the pipeline for the third quarter remains pretty strong. And provided we get reasonable markets, we've got an environment, which we can continue to get these things done. So it feels pretty good.

**GERARD CASSIDY:** And then just finally, obviously, your credit quality has improved dramatically and it's still very, very strong. But there's always moving parts. And so one of the questions on the moving parts is I think it was on the supplement package on page 33, you give us the breakout of your nonaccrual loans, Corporate and Consumer, I noticed you had some real good improvement in Latin America, they dropped quite a bit, but EMEA jumped up quite a bit in the quarter on non-accrual. Was that an energy-related credit or Brexit-related credit – or credits?

**JOHN GERSPACH:** Two energy-related names in EMEA caused that.

**GERARD CASSIDY:** Okay. Great. And look forward to seeing those, Mike, those new guidelines that you guys are going to hopefully announce later on. And just I would also throw an Investor Day, now that you guys are moving forward, you might want to consider that for 2017, even though Susan's probably not happy about that.

**JOHN GERSPACH:** Susan's thrilled.

**SUSAN KENDALL:** I'm thrilled, Gerard.

**GERARD CASSIDY:** Okay. Thank you.

**MIKE CORBAT:** Thank you.

**OPERATOR:** And we have no further questions in the queue at this time.

**SUSAN KENDALL:** All right. Thank you all for joining us for the call. If you have any follow-up questions, please feel free to reach out to Investor Relations. Thank you.

**OPERATOR:** Thank you. This concludes today's conference call. You may now disconnect.