Forbes.com

April 17, 2009

Citi Profits, For Now
By Liz Moyer

Funny how when Citigroup announced its first profit in 18 months Friday morning, no one asked if it was ready to repay its government bailout money.

Thanks to strong fixed-income trading activity and favorable tax and other one-time items, the bank had profits of $1.6 billion. But it didn't include the effect of a dividend payment on preferred stock held by the government.

Adding in that cost, the first-quarter loss was $966 million, or 18 cents a share, which is not good, but not as bad as everyone expected.

That doesn't dissipate the dark clouds, though. **It"'s the triumph of hope over fundamentals," says Dan Alpert of Westwood Capital regarding a rise in the Citi shares Friday morning, which later faded.**

Citi, while viewed as in a weaker position than Goldman Sachs, JPMorgan Chase and Wells Fargo, all three of which also surpassed expectations, tracks the same industry trends. Big gains in credit and interest-rate trading at all the banks and better margins from wide credit spreads helped to mask weakness elsewhere.

Revenues in three of Citi's main businesses were down. Card revenues fell 10%, consumer banking 18% and wealth management 20%.

Only corporate and investment banking results rose, to $9.5 billion, compared with a loss last year and last quarter. Delinquencies are rising significantly, 3.62% of managed loans compared to 1.9% in the first quarter last year. It had $3.7 billion in loan losses in the quarter and added $2.7 billion to reserves.

The fear is that the first-quarter trading gains aren't sustainable, and with rising unemployment and rising loan defaults, banks are going to have to come up with another way to earn their way out of problems.

Banks are also awaiting the results of the Treasury Department's stress testing, which are expected to be revealed May 4. Citi has received $45 billion in government money through the Troubled Asset Relief Program, along with guarantees on $300 billion in assets, and yet it is seen as potentially needing more capital.

Other banks are rushing to repay their portion of TARP funds. Goldman sold $5 billion worth of stock this week to repay its $10 billion, and JPMorgan said on Thursday it would jump to repay its $25 billion and wouldn't have to raise capital to do so.

Nevertheless, JPMorgan sold $3 billion of bonds Thursday not backed by the Federal Deposit Insurance Corp., a sign, says Alpert, that private investors are willing to put money into at least a few major banks.

Banks and other financial institutions have offered $238 billion in debt under the FDIC's guarantee program since last fall and $33 billion in non-guaranteed debt, according to Dealogic.

Citi delayed its conversion of $25 billion of preferred to common shares until after the stress tests are revealed. After the conversion, the government will own a 36% stake, and Citi's tangible common equity, which is a cushion against losses, would increase from $30 billion to $81 billion.

Still, the quarter's showing is good news for Chief Executive Vikram Pandit, who has presided over $20 billion of losses since taking over in late 2007. He vowed to take only $1 in salary until the bank returns to profitability. Pandit wasn't on the conference call with analysts Friday morning, a curious absence given the high degree of investor interest in Citi's progress. Newly installed Chief Financial Officer Ned Kelly told one analyst not to read anything into it.