

CITIGROUP'S GLOBAL TRANSACTION SERVICES BUSINESS IS POSTING STRONG GROWTH DESPITE ITS PARENT'S BANKING WOES. NOW CEO VIKRAM PANDIT WANTS THE UNIT TO HELP POWER A BROADER REVIVAL.

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Global Transaction Services boss Francesco Vanni d'Archirafi says the financial crisis has been a boon for the unit, which helps companies manage their cash

SECURITIES SERVICES



AS HE LOOKS TO GET CITIGROUP BACK ON TRACK AFTER

record losses and multiple government bailouts, CEO Vikram Pandit could do with more businesses like the bank's Global Transaction Services unit.

GTS may lack the excitement and star power of Citi's investment banking and global retail banking subsidiaries, but it has something that the group sorely needs: consistently strong profitability. Even in the midst of a deep recession, companies need to manage their cash, process transactions, pay vendors and account for their securities holdings. Citi's GTS unit is only too happy to oblige—and to charge a fee for each one of these tasks.

Now Pandit is looking to this unglamorous back-office business to drive growth throughout the group. The CEO is asking clients to meet with GTS executives before discussing loans or other banking services. The thinking is that if Citi is going to lend money and take on risk, it wants a long-term relationship when it comes to transaction services—one that won't disappear the next time the markets slow down.

"GTS is a key driver of financial performance, for our clients and for the new Citi," Francesco Vanni d'Archirafi, the recently promoted boss of GTS, tells *Institutional Investor*. "We've only just scratched the surface of the market. The liquidity crisis has been a powerful catalyst for change, compelling our clients across corporate, financial and public sectors to find more-efficient ways of using capital and running their businesses. The crisis is making our business all the more valuable."

The credit crisis has indeed underscored the value of GTS's high-margin, low-risk business, which derives its competitive edge from Citi's global scale and technology rather than big trading bets. Although massive subprime write-downs and mounting losses on everything from credit cards to commercial real estate caused Citi to post a record loss of \$18.7 billion last year, its GTS unit boosted revenue by 22 percent, to \$9.6 billion, and increased net income by 34 percent, to \$3 billion. Revenue grew at an average annual rate of 25 percent from 2005 to 2008, outpacing growth at the services units of rivals such as State Street Corp. (up 24.9 percent annually), Bank of New York Mellon Corp. (17 percent), JPMorgan Chase & Co. (14 percent) and Bank of America Corp. (9 percent). GTS's pretax operating profit margin of 45 percent last year was second only to BofA's 55 percent, according to industry sources, but BofA includes foreign exchange payment processing in its business, which GTS doesn't.

The sharp decline in global equity markets has taken a toll on the Citi unit lately. Assets under custody were down 20 percent in the first

quarter of this year from the same period a year earlier; GTS's overall revenue dipped 1 percent in the quarter, to \$2.3 billion. Still, cost-cutting and foreign exchange translation gains helped net income rise 15 percent, to \$843 million—more than half of Citi's overall earnings of \$1.6 billion for the quarter. By comparison, JPMorgan's Treasury and Securities Services unit had net income of \$308 million for the same period.

Vanni d'Archirafi wants to keep growth going by roughly doubling GTS's market share, to about 10 percent, by 2015 from just below 5 percent last year, which would imply annual revenue of about \$20 billion. The recent slowdown may force Citi to extend that timetable, he acknowledges, but the executive insists that Citi's scale should enable it to achieve the kind of market share that leaders in other sectors have attained. Bank of America and JPMorgan each have about 10 percent of U.S. bank deposits, for example, while Bank of America-Merrill Lynch had 9.6 percent of global investment banking revenues last year and JPMorgan had 8.6 percent, according to data provider Dealogic.

Citi enjoys several advantages that could help it reach its goal. The bank has a physical presence in 104 countries around the world, compared with 33 for JPMorgan Chase. That network enables GTS to help multinational companies manage their working capital, trade and payments more efficiently around the world. Eighty percent of GTS revenues come from outside the U.S. HSBC Holdings rivals Citi's global reach, but it operates treasury services as a local business in each market rather than as a fully integrated global product, according to custody sources. Other competitors tend to have a regional rather than global presence, with Deutsche Bank strong in Europe, for instance, and Standard Chartered active in Asia.

Citi's scale and clout have allowed GTS to continue to grow despite the blows its parent has suffered to its balance sheet and reputation during the crisis. "GTS's capabilities are undiminished



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by problems within Citi's other divisions," notes Ian Johnson, the London-based senior director of global cash management at Merck & Co. The pharmaceuticals company had about 100 banks handling its cash in more than 70 countries before signing on with Citi in 2007 to consolidate its cash management. "Now we're importing bank statement information in real time for more than 330 bank accounts in all countries and regions in the world," Johnson says. Merck has managed to reduce its idle-cash balances from \$450 million to \$220 million. "We either invest that [spare cash], deploy it to somebody who needs it or use it to expand the business," he explains.

GTS should be able to meet its growth targets, provided that the bank continues to invest in technology, asserts Larry Tabb, founder and CEO of the TABB Group, a financial markets research and strate-



Vanni d'Archirafi's focus on resilient services like working capital are boosting GTS's profit margins

gic advisory firm in Westborough, Massachusetts. Custody and cash management contracts are extremely “sticky” businesses that most clients think hard about before changing, he says. The fallout from the giant fraud at Bernard L. Madoff Investment Securities should also bolster the asset servicing business, as more hedge funds turn to outside administrators and valuation experts. Seeking to capitalize on that trend, GTS last month launched Hedge Fund Middle Office services, which provides daily operations for hedge funds, including reconciled profit and loss reports, trade capture, pricing and corporate action processing. The new service also double-checks margin calculations received from prime brokers, a service that grew out of the credit crisis and the increasingly high price of financing.

Citi GTS spends about \$1 billion a year on technology, both on direct investment in its global network and on acquisitions. In 2007 the bank acquired Ecount, a corporate prepaid-cards business that provides cards for unemployment-benefits recipients in Kansas and Maryland; last year it acquired PayQuik, a platform that facilitates payments, including helping companies comply with anti-money-laundering rules. The bank didn't disclose the terms of those deals. GTS also develops technology internally. The unit plans to roll out, later this year, a mobile treasury system that will allow corporate treasurers to authorize wire transfers by using a smart card and a BlackBerry.

Established in 2002, GTS is a relatively new division at Citi, although the underlying business has been around for decades. The bank traditionally offered cash management, securities services and trade services as local products that were managed separately in each country. It began integrating those activities in 2002 under

Frank Bisignano, then head of operations and technology, who left the bank in 2005 to become JPMorgan's chief administrative officer. To spearhead the effort, Bisignano recruited Paul Galant to integrate Citi's cash management offering. Galant is a technology buff who had been head of e-commerce and financial engineering in debt capital markets at Donaldson, Lufkin & Jenrette before Michael Carpenter, then head of Citi's investment bank, hired him in 2000 to oversee e-commerce and market data strategy for the corporate investment bank.

“At the time we kicked off the overhaul, it was a struggle,” Galant tells *II*. “This was not the attention getter. This was neither sexy, nor was it well understood.” Galant saw the need for a unified global technology platform that would enable clients to do business the same way in every country. He also reorganized sales and marketing along specific industry lines, such as banks and financial firms, power, energy and mining companies and public sector institutions. And Galant decided to focus on the top 3,000 companies only, determining that it was too labor-intensive to court and service smaller clients. Instead, he built a white-label business through which GTS offered its infrastructure to small and regional banks to market to their clients.

Galant, who was promoted to head of GTS in 2007, gave a big boost to the division's securities and fund services business that year by acquiring Roseland, New Jersey-based Bisys Fund Services for \$800 million. Bisys put Citi on the map when it came to transfer agency, mutual fund servicing, fund accounting and hedge fund and private equity servicing. The bank now ranks fourth by assets among U.S. providers in mutual fund accounting, up from 15th in 2006, and jumped to first place as a transfer agent, from fifth in 2006. GTS has also moved up to fourth place globally in single hedge fund administration, from 26th in 2006.

His record at GTS made Galant such a rising star that Pandit tapped him in April to take charge of Citi's giant credit card business. Galant leaves GTS with a strong management team led by Vanni d'Archirafi, a 25-year Citi veteran who worked for years in the bank's European investment banking arm before joining GTS as regional head for Europe, the Middle East and Africa in 2003. In January 2008, Vanni d'Archirafi merged cash and trade services into Treasury and Trade Solutions, a unit that generates two thirds of GTS's revenues.

Notwithstanding GTS's strong growth, Galant and Vanni d'Archirafi saw economic headwinds building early in 2008 and reacted. They started cutting costs, bringing systems online to reengineer the business and focusing on services that do well in recession, such as working capital. “That has translated into huge operating leverage for the business,” says Vanni d'Archirafi. Indeed, in the first quarter of 2009, GTS's operating profit margin rose by seven percentage points, to 52 percent.

With results like that, it's no surprise that Citi's top executives are counting on the division to drive growth and help lead an overall turnaround at the bank.

As John Havens, Pandit's top deputy and head of the investment bank, puts it, “If you look at the model that we have here at Citi, which is to bring local access to global companies and to bring the global platform to local champions, GTS fits right in the middle of that.” ●●