THE VIEW FROM THE BRIDGE

Conversations with three CEOs who were at the precipice of the unparalleled banking crisis

Richard Kovacevich, Sheila Bair and Richard Parsons occupied powerful vantage points during the financial crisis. In these interviews, they discuss the causes of the crisis, reforms that have been put in place and the future of the banking industry. ■ Kovacevich dissects how U.S. government actions drove a run on investment banks. His provocative insights challenge what is becoming conventional thinking about what it will take to spur the economy. He also offers insights into the business strategies that have made Wells Fargo a $1.2 trillion financial powerhouse. ■ Parsons was leading a mega bank that was on the brink of nationalization. He steered it through the crisis, and ultimately, graded the U.S. government B+ for its efforts in navigating the disaster. Having emerged from the shallows, he articulates Citigroup's role in the global financial system. ■ When Bair took the reins at the Federal Deposit Insurance Corp. (FDIC) in 2006, the organization was aware of what was going on, but few listened. In the aftermath, Bair raises concerns about community banks. They can play a huge role in economic growth, but they might be stymied by regulatory burdens. She also discusses the Dodd-Frank reform legislation and how she hopes it will lessen the risk of future crises. ■ These interviews were conducted by William M. Isaac, Senior Managing Director and Global Head of Financial Institutions of FTI Consulting. Isaac was chairman of the FDIC during the banking crisis of the 1980s. He also serves as chairman of Fifth Third Bancorp.

PHOTO ILLUSTRATIONS BY SEAN McCABE

CHALLENGING SACRED COWS

RICHARD KOVACEVICH

Wells Fargo famously navigated the financial crisis better than most of its peers. Now the man who led the bank through the crisis to the high ground, former Wells Fargo chairman and CEO Richard Kovacevich, challenges what is becoming conventional wisdom about what drove the financial crisis.

Kovacevich argues that a bank's risk has nothing to do with its size — banks fail because their risk is too concentrated. He firmly believes that TARP, stress tests and mark-to-market accounting did not stem the crisis; they made it worse by creating panic. Legally combining commercial and investing banking didn't fuel the crisis — this particular crisis would not have occurred had the Glass-Steagall Act not separated the two industries in 1934. And the Dodd-Frank Act absolutely does not end "too big to fail." Kovacevich also brings his experience to bear on the vexing challenge of emerging from the crisis and spurring U.S. economic growth.

The following are excerpts from the interview conducted by William M. Isaac, Senior Managing Director and Global Head of Financial Institutions at FTI Consulting. He is the former chairman of the Federal Deposit Insurance Corp. Isaac also serves as chairman of Fifth Third Bancorp.

The complete interview is available at fticonsulting.com/critical-thinking. It further illuminates the dangers still inherent in the financial system and is a must-read for all who work in, regulate and analyze the banking industry — or, like most, simply rely on its health.

WILLIAM M. ISAAC: **What event or events do you think turned the recent crisis into a panic?**

RICHARD KOVACEVICH: One of the most critical was the process of bailing out Bear Stearns and then days later not bailing out Lehman. The biggest mistake was not, as most people think, failing to bail out Lehman. The mistake was bailing out Bear Stearns and then not bailing out Lehman. The investors just said: "We have no idea what's going on. We don't know what's happening next. We are getting out of the market."

And for the Fed and [former Treasury Secretary Henry] Paulson to say, as they have, that they had no authority to bail out Lehman is simply not true. How can they say they had the authority to bail out AIG but they had no authority to bail out Lehman?

In my opinion, we should not have bailed out Bear Stearns, which was much smaller and much less risky than Lehman. It could have been handled more easily.

If that had happened, there was no question in my mind that Dick Fuld [CEO of Lehman] would have said "Uh-oh, game's up. I'd better sell this thing right away at whatever price I can get." He may have been able to sell it. I'm told it was close many times. And if Lehman could have been sold, then you may not have had the run on the other investment banks.

ISAAC: **You're arguing that they should have let Bear Stearns go and then Lehman would have taken care of itself.**

KOVACEVICH: Because if they bailed out Bear Stearns and also Lehman, everyone would know that every financial institution was going to be bailed out. Then you're back to too big to fail, squared. I think the reason Lehman was allowed to go bankrupt, and I know Hank [Paulson] pretty well, I think he said to himself, "Well, if we rescue Lehman, then we have to do it for everybody. And we don't have enough money or political will to bail out everyone."

When they let Lehman go down, and the markets all crashed and liquidity dried up, they then realized the world was coming to an end. They ran to Congress to get the $700 billion to purchase toxic assets under the TARP program. Then they realized that the $700 billion for assets would not even put a dent in the problem, so they ended up bailing out everybody by supplying capital.

To cover their mistakes, they claimed they had no authority to bail out Lehman and, with a straight face, bailed out AIG a few days later. Chaos occurs when people don't think in terms of what's the next step if we do such and such now.

Mark-to-market accounting eviscerated equity and caused markets to cease functioning. Mark-to-market accounting establishes a "fair value" for an asset or liability based on current market prices versus historical cost accounting, which bases value on amortized cost.

ISAAC: **You and I are probably the two people in the world who hate mark-to-market [MTM] accounting the most. What role did it play in the crisis?**

KOVACEVICH: A huge role. People thought the world was coming to an end because everyone was reporting huge book but not actual losses because of MTM accounting.

We had to write off $900 million on a prime mortgage portfolio that we thought had a maximum loss exposure of $100 million. Our current loss estimate for that portfolio is now just $35 million. But we had to report nearly a billion-dollar loss that never came to fruition. And that was just one relatively small portfolio. I could give you many more examples.

Also, we wanted to purchase some assets because we knew they were undervalued. We were very reluctant to be a purchaser, however, because we would have to take an MTM loss if the asset went down further, even though we knew over the cycle it would be profitable.

This caused the markets to cease functioning. It destroyed a lot of companies and ultimately forced the Fed to intervene with trillions of dollars and be the buyer of last resort. Mark-to-market accounting was a huge culprit in the financial crisis and caused unnecessarily massive damage to the economy, and to housing in particular.

Kovacevich argues that riskiness in banking has little to do with the size of a bank. More small banks fail than do large ones. The problem is risk that is too highly concentrated.

KOVACEVICH: I quickly learned that the riskiest part of the banking business is lending. If your loan risks become concentrated, whether geographically, by borrower or by industry, a bank's total risk becomes excessive, even if you've underwritten those loans well. Banks fail due to concentrated risk. Risk has little to do with the size of the bank.... In fact, more small banks fail than big banks because they are generally more concentrated geographically, by product and by industry. Now if a big bank is concentrated, then obviously it is a higher risk.

Even if you underwrite well, when real estate goes to hell or the economy

slows significantly, you're going to get hammered. So you must underwrite well. But then to mitigate the macro factors you can't control, you have to spread the risk. Risk management in banking should be more like it is in an insurance company. There you spread and diversify the risk.

I believe that the chance of Wells Fargo's failing today at $1.2 trillion in assets is less likely than when I joined Norwest. It was a $20 billion company with a narrow product line concentrated in the upper Midwest and in agriculture-related lending.

ISAAC: **I've noted that the five largest institutions control more than 50% of the financial system and that is an undue concentration. Do you agree with that?**

KOVACEVICH: I don't. Five or fewer companies control more than 50% in every industry, from cereal to automobiles. Five banks control more than 50% of their industry in about every country in the world.

ISAAC: **You don't believe banking is different or special compared with, say, the beer or cereal industry?**

KOVACEVICH: No. In any given product line or geography the largest bank has, on average, 15% of the business. Some banks are big only because they have product and geographic diversity. That reduces the concentration of risk. If U.S. banks had been allowed to bank nationally from the get-go, as was the case in most other countries, few would even question their market share today. Texas banks in the 1990s were small by today's standards. But they all failed because they were not allowed to bank outside of Texas. Savings and loans in the 1980s, individually, were not big. But they were excessively concentrated and required hundreds of billions of dollars of taxpayer money to be resolved. In the recent crisis, the taxpayer is unlikely to pay a dime for bank failures.

When we acquired Wachovia, it doubled our size but reduced our risk because it doubled the geography in which we operate. I believe that deal reduced risk for the system — as it increased our ability to serve more customers, with more products and in more geographies — and is absolutely positive for the economy.

The Dodd-Frank Act "absolutely" does not end too big to fail.

ISAAC: **Do you believe that we have, through the Dodd-Frank Act, ended too big to fail?**

KOVACEVICH: Absolutely not. But too big to fail must be stopped. No bank, none whatsoever, should be too big to fail. I worked on this issue with the

Minneapolis Fed 20 years ago. Gary Stern [former president of the Federal Reserve Bank of Minneapolis] has been writing books and papers about this for two decades. It's very simple — the only way we can solve too big to fail is when it's clear that everybody that supplies capital to a failed bank, except insured depositors, is going to take a haircut [absorb losses] in a failure. That includes the failure of a $300 million bank or a $1 trillion bank. Until we force haircuts on all suppliers of capital to failed banks, we will be living with too big to fail.

Administering haircuts requires a huge liquidity fund from the Fed or from the FDIC because it could take months to fully wind down the bank, and there's not going to be enough liquidity to do that without the government supplying the temporary funding. But banks should be able to be wound down at no cost to the insurance fund or taxpayers. The cost will be borne by the debt holders, the uninsured depositors, and the common and preferred stockholders. I believe that haircuts will cause those who provide capital to banks to be more disciplined about determining to whom and how much will be provided. Capital suppliers will monitor a bank's risk appetite more closely, and will restrict additional capital when the risk grows too large and banks become too concentrated. In fact, I believe self-interested vigilance on the part of capital suppliers will be more effective in reducing bank failures than our regulators have been.

Kovacevich recounts a disturbing conversation he had with the Federal Reserve during the crisis that underscores the potential perils of placing the banking industry under a single regulatory body.

KOVACEVICH: The Fed called us after they completed our stress test and said we needed to raise something like $15 billion in additional capital. I was shocked. I said: "How did you get $15 billion?" They had reduced our earnings forecast. There was very little difference in projected credit losses. In fact, the Fed actually had our credit losses a few million less than ours really were. Where you would expect there might be differences, such as operating expenses, there were no differences. Instead the Fed had reduced our revenue forecast by more than 30%, which was the sole reason they had reduced our earnings forecast. I said: "What?" Just making sure I understood.

ISAAC: **Something tells me you didn't just say "What?"**

KOVACEVICH: "So you are saying that between May and November,

our revenue is going to decline by 30%?" The answer: "Yes, that's what our model shows." I said: "That's mathematically impossible. I couldn't do it even if I tried. Let me see your model." And they said: "We're not going to show it to you." How's that for transparency in prudential regulation?

I pushed back: "How can I accept needing $15 billion in capital when it is based on a revenue assumption that is mathematically impossible?" "That's it," they said. "You need $15 billion." As we stated in our earnings press releases in subsequent quarters, our actual revenue turned out to be even higher than our own forecast. So the Fed's 30% revenue reduction and $15 billion capital raise as a consequence of that were totally wrong.

Now that's what happens when you have a strong single regulator.

The U.S. Congress repealed the Glass-Steagall Act in 1999, eliminating the separation of commercial from investment banking. Many believe the repeal stoked the crisis. But Kovacevich argues that it actually forced investment banks into high-risk activity.

ISAAC: **Do you believe that the repeal of the Glass-Steagall Act helped lead to the crisis in 2008 and 2009?**

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KOVACEVICH: Not at all. In fact, if we had eliminated Glass-Steagall 40 years ago instead of nearly 15 years ago, this crisis is unlikely to have happened. The biggest problem of this crisis was the nonregulated investment banks that grew to an enormous size and with substantial and concentrated risks under the protection from competition by the Glass-Steagall Act.

One reason why this particular crisis will not happen again is because there aren't many of these bad guys left. The ones that survived are regulated by the Fed, and therefore there is less chance that they will make these obviously bad decisions of high leverage, liquidity issues and concentrated risk that the SEC totally ignored.

Wells Fargo can now do investment banking, such as underwriting debt and equity and doing customer hedges. We don't have to originate risky structured products or take proprietary trading risk. We have 95 other businesses from which to make profits. There's no way investment banks can make attractive returns, in my opinion, with their limited product line and their lack of a deposit base, without taking excessive risks and crossing the line of ethical behavior. That's why we were never in that business, in a major way, prior to the crises. ■

The entire interview is available at fticonsulting.com/critical-thinking. In it, Isaac and Kovacevich also tackle the challenge of how to emerge from the crisis and spur U.S. economic growth, along with many other important subjects.

the WELLS FARGO WAY

The benefits of cross-selling in financial services

KOVACEVICH: If you're only a lender, the only way you grow is by making more loans. But as you do that, you are increasing your risk and your concentration.

The loan is the hook — that's what customers want the most. So you have to give them the loan and hopefully some deposits will come in return. But customers buy 14 products from financial institutions — both consumers and businesses — and the majority of those products don't entail credit risk. They might involve operational risk, but it's a different type of risk. So you can grow your bank while reducing and diversifying your risk.

Now if you do that, three other things that you haven't thought of turn out to be true. The cost of selling an incremental product to an existing customer is about 10% of the cost of selling that same product to a new customer. You don't open up a new account. You don't advertise. You don't take other risks.

You can say to the customer, if you bring over your treasury management product, your business or personal insurance, your credit card, your 401(k) or whatever, I'm going to give you a better deal than the competitor who is selling you only one product because of the 10% cost versus that 100% cost. You give a better deal to your customer, and they want to buy more. You benefit because you're making more profits. You benefit from lower risk, and then finally you have the phenomenon that the more products that customer has with you, the longer they stay with you.

So it's magic. We reduce cost, increase revenue, make higher profits, have less risk, and the customer gets a better deal. This is a business model for financial services that is far superior to any other one that I am aware of.

EXECUTION

KOVACEVICH: Let me ask you, is this easy to do or hard to do?

ISAAC: **Well, I think it's easier relative to the other approaches because you can sleep better at night.**

KOVACEVICH: No, it's harder, much harder, because you need to manage hundreds of businesses and products. Systems have to be capable of aggregating products and profitability by customer so you know what more to sell them and what better deals you can give them to incent them to give you more business. You need to be geographically dispersed. We have 100 different businesses out there doing some very complex things that are difficult operationally, and yet they have to work together as if we are one business from the customer standpoint. And that's why most people don't do it.

RELEVANCE TO MANAGEMENT OF RISK

KOVACEVICH: Wells Fargo can now do investment banking, such as underwriting debt and equity and doing customer hedges and all the standard investment banking activities. We don't have to originate risky structured products or take proprietary trading risk and so on because we have 95 other businesses to make profits from. There's no way that an investment bank can make attractive returns, in my opinion, with their limited product line and their lack of a deposit base, without taking excessive risks and crossing the line of ethical behavior. That's why we were never in that business, in a major way, prior to the crises.

ISAAC: **So you're saying that you believe affirmatively that investment banking and commercial banking need to be mixed together?**

KOVACEVICH: Absolutely, for diversity of risk. And what got us into trouble was they weren't. I'm telling you that as bad as Citicorp was, if we didn't have Bear Stearns, Lehman Brothers, Merrill Lynch, Morgan Stanley, and Goldman Sachs, this crisis would never have reached the level it did. Citicorp survived this crisis, despite doing most of the same things as the investment banks that failed, because it was more diversified, including a deposit base.

THE PATH TO THE PRECIPICE

SHEILA BAIR

When Sheila Bair became chairman of the U.S. Federal Deposit Insurance Corp. in 2006, the housing market was faltering and subprime delinquencies were on the rise. But even so, analysts were predicting only an 8% drop in home prices and a 15% loss rate in subprime mortgages. No one was taking precautionary action. Within two years, regulators were scrambling to avert the collapse of the banking system.

The following are excerpts from an interview of Chairman Bair by William M. Isaac, Bair's predecessor at the FDIC under Presidents Carter and Reagan, and currently Senior Managing Director and Global Head of Financial Institutions at FTI Consulting. Bair gives a unique behind-the-scenes view of how the FDIC came to terms with the scope of the crisis and how improvements in transparency can prevent one in the future. She also voices a strong concern for the vibrancy of community banks and the regulatory demands that could stifle their role in economic growth.

As a financial crisis silently loomed in 2006, the FDIC was among the first to see the early warning signs.

WILLIAM M. ISAAC: **How did you come to realize, so early, that the banking system was in grave danger?**

SHEILA BAIR: To the credit of the FDIC staff, on the day of my arrival they were talking about the deterioration in mortgage lending standards. We were seeing a marked increase in subprime delinquencies, even in 2006. We bought private data on mortgage-backed securities to try to get a better handle on what was going on. As you know, most of this information was not on the bank balance sheets and therefore not reported to us. What we saw was pretty frightening.


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There was already an effort under way to tighten standards for nontraditional mortgages, which are basically the negative amortization products like option ARMs [adjustable rate mortgages]. There were clearly some problems there. Subprime mortgages were deteriorating. So we pushed very hard to tighten lending standards for subprime mortgages and to get the states involved because they had the authority over the nonbank mortgage originators.

I was somewhat in tune with these issues from my days at Treasury, but I credit the FDIC staff for identifying the problems early on. Congress had bills pending to deal with subprime lending issues, but those bills weren't going anywhere. Ironically, the Federal Reserve had authority to set lending standards across the board for bank and nonbank mortgage originators. But it had decided not to use it.

People said we were being alarmist, and the problem was contained. In researching my book, I've gone back to look at the financial market commentary during late 2006 and 2007. Analysts were saying, "Oh, it's going to be maybe an 8% decline in home prices over a couple of years and maybe a 15% loss rate on subprime mortgages." That was in line with the groupthink back then. Everybody said housing was going to correct a bit, but it would just be ones with subprime mortgages. The losses would be manageable. So I credit the FDIC staff with being on top of that early and understanding it could affect the insured banks as well. However, nobody, including people at the FDIC, thought it was going to get as bad as it did.

Bair examines the critical issue of transparency in financial institutions and how it has affected the past and future of the ability to deal with a crisis.

BAIR: You know, we had one hand behind our back. We had no information on anything outside of the insured bank. Getting the living will authority [which requires systemically significant banks to report to the FDIC and other parties how they would conduct an orderly resolution of their businesses in the event of a financial crisis] was crucial to ending too big to fail. I know you don't think it has done it, but I think it has the potential to do it — and it is critical in terms of our ability to deal with a crisis.

ISAAC: Let's dig into that a little bit so people can understand from the FDIC's perspective what it was dealing with.

BAIR: We don't have the staff to provide hundreds of examiners at each of these large banks. So, to a significant degree, you have to rely on the primary regulators [the state banking departments and the comptroller of the currency]. The information was better in the bank than in the holding company, but even there it was opaque.

And I must say, for the Office of the Comptroller of the Currency and

In the full interview at fticonsulting.com/critical-thinking Isaac and Bair also confront the controversies still swirling around Freddie Mac and Fannie Mae, too-big-to-fail financial institutions, the Dodd-Frank reform legislation and the dangers to the banking system if the FDIC's political independence is diminished.

the Federal Reserve, there were things going on inside the insured banks that they could have had more information about. There are robust efforts to improve that monitoring capability now.

A lot of that will be contained in the living wills and resolution plans. The critical exposure reports, if properly implemented, could be a huge boon. A key bit of information that we were missing: If a financial institution goes into an FDIC resolution process, or if a nonbank goes into a bankruptcy, what's going to be the impact? Who's going to take the losses? We just didn't have that information. We didn't know who the counterparties were. We didn't know who the bondholders were. It was very, very difficult. And so the credit exposure reports now put the onus on the institution to basically tell the regulators: If they fail, who else could be materially affected? Or, if some other institution fails, will it have a material impact on the bank or its holding company? I think that's huge.

Community banks can play a pivotal role in boosting lending. Will new banking regulations stifle their role in growing the U.S. economy?

ISAAC: **A lot of people are concerned that we're going to lose a large part of our community banking system.**

BAIR: I believe community banks should be strengthened by recent events. People are not angry at them. People want the high-touch banking that they can provide. Though we had a fair number of small bank failures, on a percentage basis the amount of distress in the smaller banks was significantly lower than it was with the large institutions.

Small banks weathered the crisis pretty well. The big issue is regulatory burden. I'm a regulator. But I believe in common sense and efficient regulation. A lot of the reforms are targeted toward practices that you find in larger institutions. If we just layer lots of new regulations on everyone, even though they don't really have anything to do with what small banks do, we are going to hurt the community banking sector.

So before I left the FDIC, I started a community bank impact analysis of any proposal that we were going to move forward. We did a community bank impact statement once a rule or proposal went out.

I hope the new consumer protection agency in particular will be sensitive to this issue, because many consumer compliance rules can be quite daunting to a smaller bank. A lot of smaller banks would like to do more in the consumer banking space, but they are reluctant because of the expense. There is some valid concern there.

At the same time, we need to simplify the rules because, frankly, one of the reasons consumer regulation has been weak is that it's so complex. Consumers can't understand what their rights are, much less the products. So simplification could really help the community banks and consumers. ■

RESTORING A SHAKEN CITI

RICHARD PARSONS

When Richard Parsons was named chairman of Citigroup Inc. in January 2009, the bank had just announced an $8 billion quarterly loss. It was on the brink of being nationalized.

Parsons sat down with William M. Isaac, Senior Managing Director and Global Head of Financial Institutions at FTI Consulting, to recount the harrowing experience of preventing one of the world's largest banks from collapsing. To Parsons, the government played a major role, and he is less critical of its actions than many of his peers. He argues, for example, that TARP [Troubled Asset Relief Program] and its follow-on measures helped restore confidence in the banking system.

Fast-forward to the present: Citi posted profits of $10.6 billion in 2010 and $6.2 billion in the first half of 2011. Having brought Citi back to life, Parsons articulates the bank's leadership role going forward, including its commitment to housing finance.

The following are excerpts from the interview.

As the financial crisis hit, Citibank teetered on the edge of implosion. The decision to keep it from going down wasn't straightforward.

WILLIAM M. ISAAC: **What was it like being at the top of Citi during that period?**

RICHARD PARSONS: Citi was perceived to be the worst of the worst of the big guys. So trying to navigate that was a challenge. In my view, and I'm certain that it was the view of Tim Geithner [then president of the Federal Reserve Bank of New York] and every thoughtful person in Washington, we just couldn't let Citi go down. The federal regulatory

establishment was committed to the general proposition that we had to figure out how to get this big bank through this crisis — and in a way that was defensible given the toxicity of the environment. We had to figure it out and try to avoid making a mistake that could cause the bank to implode.

It was dicey because it's all about confidence — whether it's depositor confidence or counterparty confidence. One of Citi's issues was that a huge part of its balance sheet and operations was funded in the wholesale markets. If those markets were closed to you, or if investors got spooked, your funding might disappear overnight. So we had to make sure we were doing the things needed to keep the markets calm. Then there was the heat of the battle in Washington. Every bank and all the bankers had become pariahs to many of my good friends and colleagues in the Washington establishment. Bank bashing and fat cat bashing were in vogue.

Shortly after Lehman Brothers failed, global interbank trading ceased. Parsons credits U.S. government actions for preventing total chaos.

ISAAC: **How do you view the way the government handled the crisis? How would you grade its effort?**

PARSONS: B+. I'm talking about how the government handled the crisis once it was on us. I really do think the system could have melted down. I was told by the Treasury Department that there was about an hour on the Tuesday after Lehman collapsed when interbank trading around the world stopped. Nobody would clear anything. It just halted.

The financial world could have been thrown into total chaos. The government's response, putting TARP in place and the follow-on measures thereafter, salvaged at least some confidence in the system. The bottom line is we worked through the crisis.

ISAAC: **But Lehman is part of that story in terms of the government's actions, right?**

PARSONS: Certainly, it started off badly. But even if Lehman had been bailed out the way Bear Stearns had been, then the next one would pop up. There could have been more forethought to the handling of Lehman. But I've heard people argue that Lehman had to happen, so the sooner the better.

From the failure of Lehman forward, the government's response was pretty good. But neither our government nor the industry did a good job of communicating why the financial system is different from other privately held industries, and the

The full interview is available online at fticonsulting.com/critical-thinking. In it, Parsons discusses how he came to be named chairman of Citigroup and delves into his experience leading AOL–Time Warner and The Dime Savings Bank and how that experience prepared him to prevent what could have been one of the largest banking catastrophes of all time. He also discusses a variety of other important topics, such as mark-to-market accounting, in candid fashion.

consequence of letting the financial system slip into chaos. So the angst and the anger caused by the crisis and the government's response to it were higher than they needed to be. The situation was not helped by the handling of AIG — how we dealt with credit-default swaps and who was made whole without participating in any of the pain. In hindsight, I'm sure people would look at that and say we could have done a better job.

Citi is a mega bank with a global footprint. But it has had to reassess its leadership role in the banking industry.

ISAAC: **What is Citi's future?**

PARSONS: Here's the way I think of it. Citi right now thinks of itself as being in three businesses: institutional or wholesale banking, retail banking, and global transaction services. GTS operates in about 96 countries but serves clients in 140 countries around the world. We have by far the biggest global footprint of any U.S. bank. HSBC is a distant second to Citi in terms of its global footprint.

I think of this GTS system as a circulatory system of the corporate body. It doesn't have the highest amount of reported net income, although it's highly profitable. But it connects all the other parts, both in country and across borders. We have a new tagline at Citi, which hasn't actually been publicly promulgated yet: "America's Global Bank." Citi is going to continue to provide connectivity for its largest institutional clients and particularly for the top 5,000 corporations in the world.

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ISAAC: **You said that the GTS is not the most profitable part of Citi. What is?**

PARSONS: It will bounce back and forth between the securities and banking business and the retail business and cards. Credit cards for a long, long time were a quarter of Citi's earnings.

ISAAC: **Is there a future for housing finance at Citi?**

PARSONS: Yes, there has to be. The most stable and therefore valuable source of funding is deposits. If you're going to be in that business, you're going to be dealing with retail customers. You have to have a full suite of products and services to keep them there. You can't just say, "Look, we want to take your deposits, but we don't do anything else."

There will continue to be a significant residential and commercial real estate component to Citi here in North America. But the old business of having a whole network of mortgage brokers out there so that you can get the mortgages and run them through the warehouse, package them up and sell them off as securities — that's gone. ■