



## 2Q18 Financial Results

July 26, 2018

The following slides are part of a presentation by Discover Financial Services (the "Company") in connection with reporting quarterly financial results and are intended to be viewed as part of that presentation. No representation is made that the information in these slides is complete. For additional financial, statistical, and business related information, as well as information regarding business and segment trends, see the earnings release and financial supplement included as exhibits to the Company's Current Report on Form 8-K filed today and available on the Company's website ([www.discover.com](http://www.discover.com)) and the SEC's website ([www.sec.gov](http://www.sec.gov)).

The information provided herein includes certain non-GAAP financial measures. The reconciliations of such measures to the comparable GAAP figures are included at the end of this presentation, which is available on the Company's website and the SEC's website.

The presentation contains forward-looking statements. You are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date on which they are made, which reflect management's estimates, projections, expectations or beliefs at that time, and which are subject to risks and uncertainties that may cause actual results to differ materially. For a discussion of certain risks and uncertainties that may affect the future results of the Company, please see "Special Note Regarding Forward-Looking Statements," "Risk Factors," "Business – Competition," "Business – Supervision and Regulation" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Company's Annual Report on Form 10-K for the year ended December 31, 2017, and "Management's Discussion & Analysis of Financial Condition and Results of Operations" in the company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2018, which are filed with the SEC and available at the SEC's website ([www.sec.gov](http://www.sec.gov)). The Company does not undertake to update or revise forward-looking statements as more information becomes available.

- Net income of \$669MM, diluted EPS of \$1.91; return on equity of 25%
- Total loan growth of 9% led by a 10% increase in credit card loans; revenue growth of 8%
- Strong credit performance as a result of disciplined underwriting and investments in credit risk management initiatives, even as normalization continued; credit environment remains constructive
- Payment Services continues to drive strong network volume growth (up 14%)
- Returned \$656MM of capital through dividends and share repurchases and received a non-objection from the Federal Reserve for 2018-2019 capital plan

**Note(s)**

(1) All comparisons stated on a year-over-year basis

# DISCOVER® | 2Q18 Summary Financial Results

(\$MM, except per share data)	2Q18	2Q17	B / (W)	
			\$ Δ	% Δ
Revenue Net of Interest Expense	\$2,603	\$2,419	\$184	8%
Net Principal Charge-off	649	520	(129)	(25%)
Reserve Change build/(release)	93	120	27	23%
Provision for Loan Losses	742	640	(102)	(16%)
Operating Expense	984	912	(72)	(8%)
Direct Banking	837	831	6	1%
Payment Services	40	36	4	11%
Total Pre-Tax Income	877	867	10	1%
Income Tax Expense	208	321	113	35%
Net Income	\$669	\$546	\$123	23%
<b>ROE</b>	<b>25%</b>	<b>19%</b>		
<b>Diluted EPS</b>	<b>\$1.91</b>	<b>\$1.40</b>	<b>\$0.51</b>	<b>36%</b>
Pre-Tax, Pre-Provision Income <sup>(1)</sup>	\$1,619	\$1,507	\$112	7%

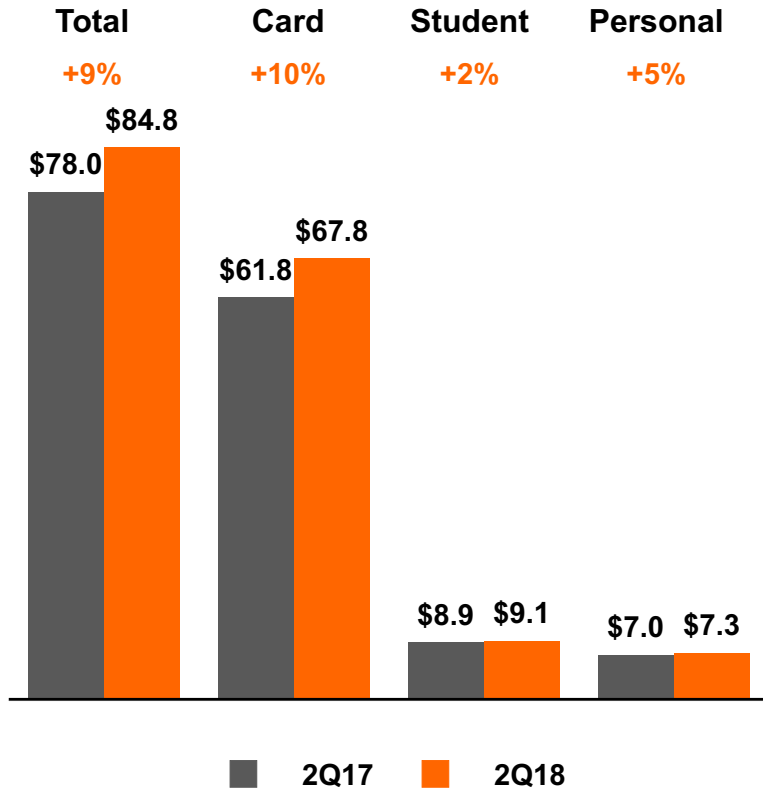
## Highlights

- Diluted EPS of \$1.91, up 36%
- Revenue net of interest expense of \$2.6Bn, up 8%, driven by higher net interest income
- Provision for loan losses increased \$102MM, or 16%, on higher net charge-offs, partially offset by a lower reserve build
- Expenses rose 8%, primarily driven by investments to support growth and new capabilities

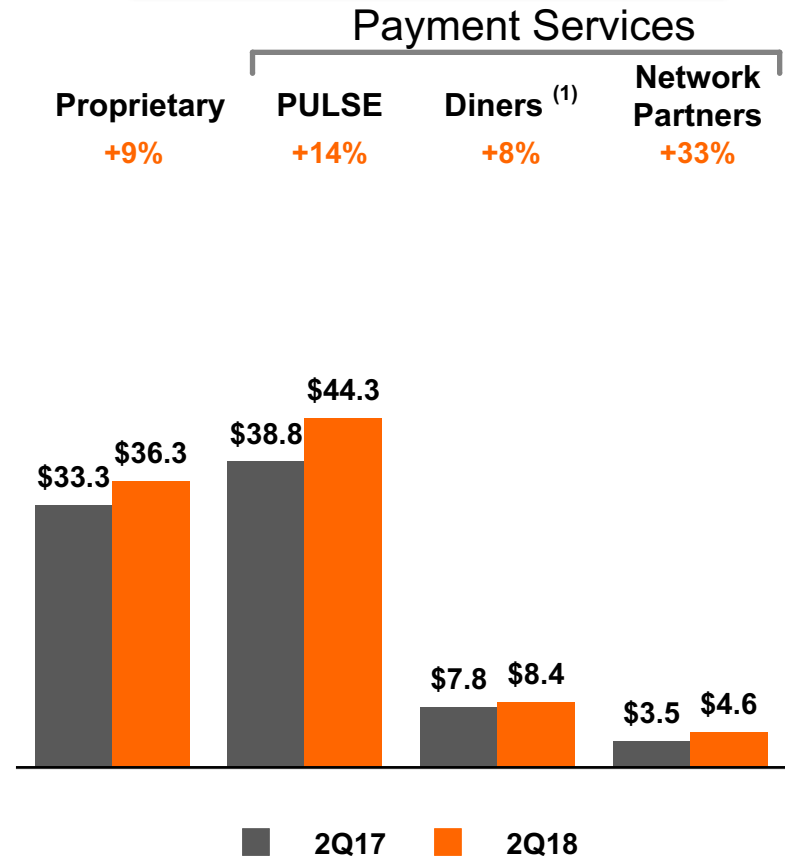
### Note(s)

1. Pre-tax, pre-provision income, which is derived by adding provision for loan losses to pre-tax income, is a non-GAAP financial measure which should be viewed in addition to, and not as a substitute for, the Company's reported results. Management believes this information helps investors understand the effect of provision for loan losses on reported results and provides an alternate presentation of the Company's performance; see appendix for a reconciliation

## Ending Loans (\$Bn)



## Volume (\$Bn)



Total Network Volume up 12% YOY

**Note(s)**

1. Volume is derived from data provided by licensees for Diners Club branded cards issued outside of North America and is subject to subsequent revision or amendment

(\$MM)	2Q18	2Q17	B / (W)	
			\$ Δ	% Δ
Interest Income	\$2,636	\$2,338	\$298	13%
Interest Expense	507	400	(107)	(27%)
Net Interest Income	2,129	1,938	191	10%
Discount/Interchange Revenue	724	666	58	9%
Rewards Cost	461	388	(73)	(19%)
Net Discount/Interchange Revenue	263	278	(15)	(5%)
Protection Products Revenue	50	56	(6)	(11%)
Loan Fee Income	95	83	12	14%
Transaction Processing Revenue	42	42	0	—%
Other Income	24	22	2	9%
Total Non-Interest Income	474	481	(7)	(1%)
Revenue Net of Interest Expense	<u>\$2,603</u>	<u>\$2,419</u>	<u>\$184</u>	<u>8%</u>
Direct Banking	\$2,527	\$2,346	\$181	8%
Payment Services	76	73	3	4%
Revenue Net of Interest Expense	<u>\$2,603</u>	<u>\$2,419</u>	<u>\$184</u>	<u>8%</u>

(\$MM)	2Q18	2Q17	Change	
			QOQ	YOY
Discover Card Sales Volume	\$35,077	\$32,172	14%	9%
Rewards Rate <sup>(1)</sup>	1.31%	1.20%	4 bps	11 bps

**Note(s)**

1. Rewards cost divided by Discover card sales volume

## Highlights

- Loan growth and margin expansion drove 10% increase in net interest income
- Net discount and interchange revenue decreased \$15MM driven by higher promotional rewards cost
- Rewards rate increased 11 bps YOY due to greater customer engagement in rotating 5% categories

(\$MM)	2Q18		2Q17	
	Average Balance	Rate	Average Balance	Rate
Credit Card	\$66,594	12.88%	\$60,700	12.66%
Private Student	9,219	8.05%	9,020	7.45%
Personal	7,304	12.55%	6,820	12.22%
Other	531	6.02%	314	5.59%
Total Loans	83,648	12.28%	76,854	11.98%
Other Interest-Earning Assets	16,861	1.81%	15,175	1.10%
Total Interest-Earning Assets	<u>\$100,509</u>	10.52%	<u>\$92,029</u>	10.19%
Direct to Consumer and Affinity	\$41,459	1.71%	\$36,956	1.29%
Brokered Deposits and Other	19,166	2.33%	15,600	2.07%
Interest Bearing Deposits	60,625	1.90%	52,556	1.52%
Borrowings	25,988	3.39%	26,122	3.09%
Total Interest-Bearing Liabilities	<u>\$86,613</u>	2.35%	<u>\$78,678</u>	2.04%

(% )	Change		
	2Q18	QOQ	YOY
Total Interest Yield on Loans	12.28%	7bps	30bps
NIM on Loans	10.21%	-2bps	10bps
NIM on Interest-Earning Assets	8.50%	-9bps	6bps

## Highlights

- Net interest margin on loans increased 10 bps driven by higher loan yields, partially offset by higher funding costs
- Credit card yield increased 22 bps as increases in the prime rate were partially offset by portfolio mix and higher interest charge-offs
- Average consumer deposits grew 12% and composed 48% of total average funding
- Funding costs on interest-bearing liabilities increased 31 bps, driven by higher market rates partially offset by favorable shifts in funding mix

# DISCOVER® | 2Q18 Operating Expense Detail

(\$MM)	2Q18	2Q17	B / (W)	
			\$ Δ	% Δ
Employee Compensation and Benefits	\$400	\$367	(\$33)	(9%)
Marketing and Business Development	224	192	(32)	(17%)
Information Processing & Communications	86	77	(9)	(12%)
Professional Fees	161	156	(5)	(3%)
Premises and Equipment	24	23	(1)	(4%)
Other Expense	89	97	8	8%
<b>Total Operating Expense</b>	<b>\$984</b>	<b>\$912</b>	<b>(\$72)</b>	<b>(8%)</b>
Direct Banking	948	876	(\$72)	(8%)
Payment Services	36	36	0	—%
<b>Total Operating Expense</b>	<b>\$984</b>	<b>\$912</b>	<b>(\$72)</b>	<b>(8%)</b>
<b>Operating Efficiency<sup>(1)</sup></b>	<b>37.8%</b>	<b>37.7%</b>		<b>(10) bps</b>

## Highlights

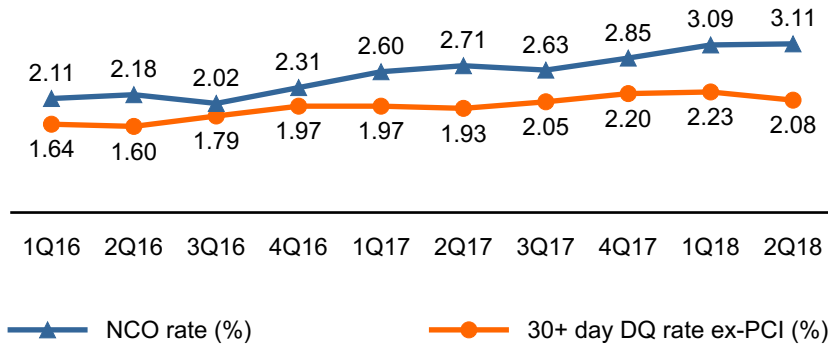
- Employee compensation and benefits up 9%, primarily on higher staffing levels, as well as higher average salaries
- Marketing up 17% as a result of higher investment in new account acquisition and brand advertising
- Information processing up 12% due to investments in infrastructure and analytic capabilities

### Note(s)

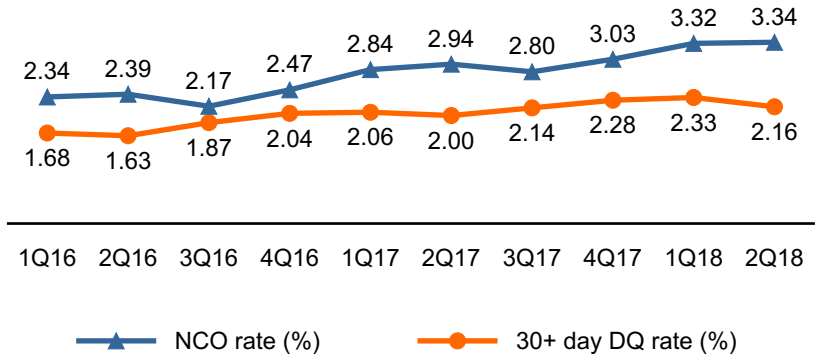
1. Defined as reported total operating expense divided by revenue net of interest expense



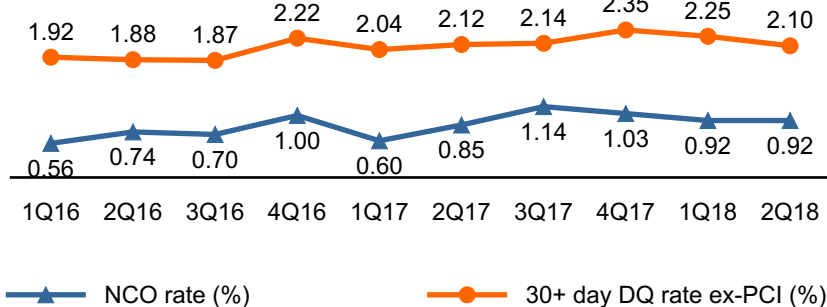
## Total Company Loans



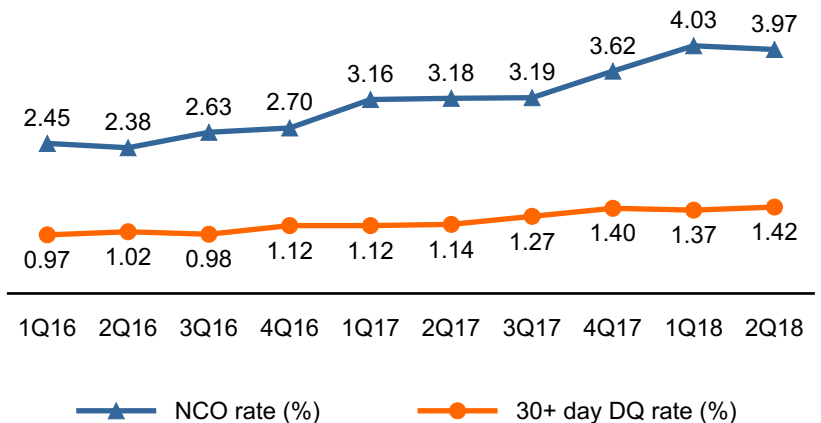
## Credit Card Loans

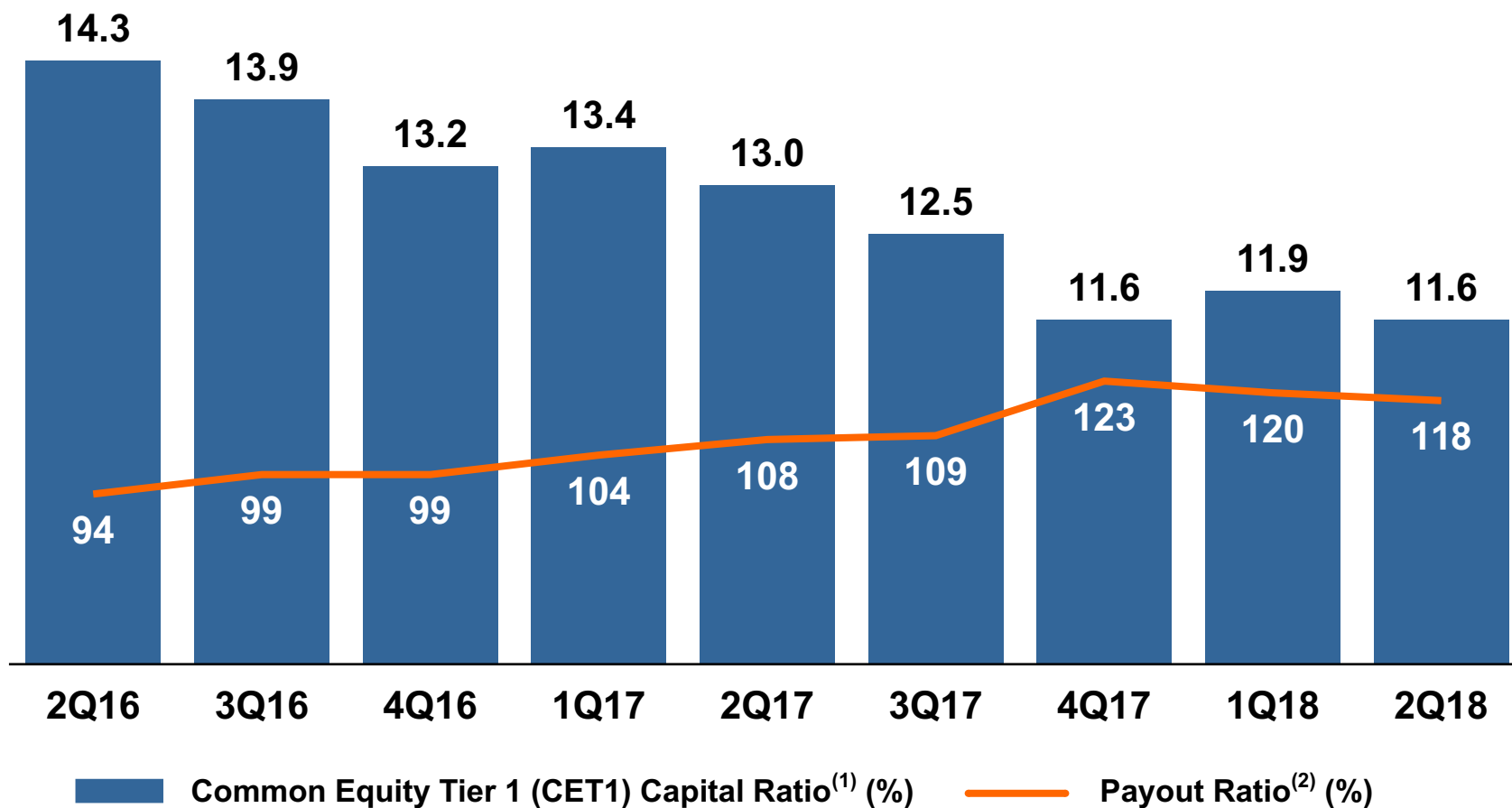


## Private Student Loans



## Personal Loans





**Note(s)**

1. Common Equity Tier 1 Capital Ratio (Basel III Transition)
2. Payout Ratio is displayed on a trailing twelve month basis. This represents the trailing twelve months' Capital Return to Common Stockholders divided by the trailing twelve months' Net Income Allocated to Common Stockholders

## Balance Sheet

- Total loans grew 9% (\$6.8Bn) YOY
- Credit card loans grew 10% (\$6.0Bn) YOY as sales volume increased 9%
- Average consumer deposits grew 12% (\$4.5Bn) YOY, while deposit rates increased 42 bps

## Credit and Capital

- Total NCO rate of 3.11%, up 40 bps YOY
  - Driven by supply-induced credit normalization and loan seasoning
- Capital return
  - Raised quarterly common dividend \$0.05 to \$0.40/share
  - Planned gross share repurchases of \$1.85Bn
  - CET1 capital ratio<sup>(1)</sup> of 11.6% down 140 bps YOY

## Profitability

- Net income of \$669MM and diluted EPS of \$1.91
- Revenue growth of 8% on higher net interest income
- NIM of 10.21%, up 10 bps YOY
- Strong return on equity at 25%

### Note(s)

1. Basel III Transition

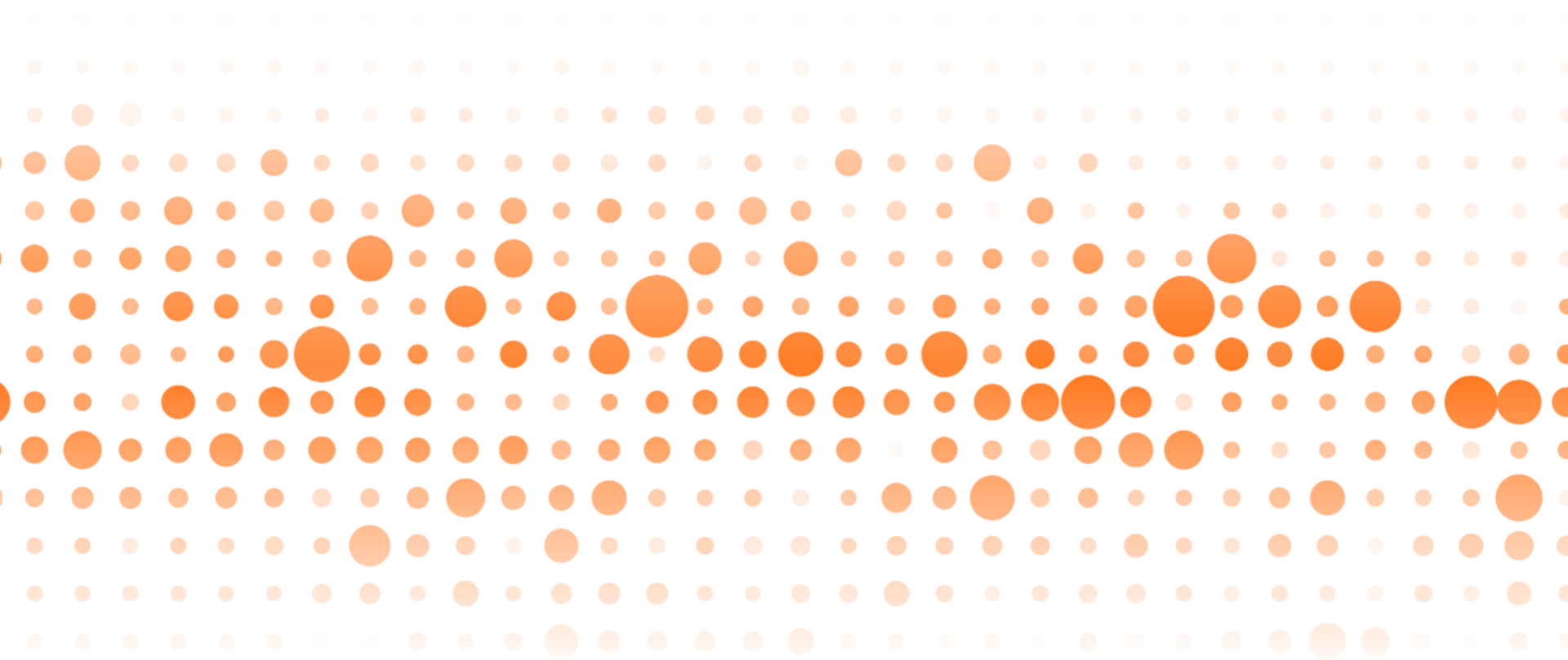
Reconciliation of GAAP to Non-GAAP Data

(unaudited, \$MM)

	2Q18	2Q17
Provision for loan losses	\$742	\$640
Income before income taxes	877	867
<b>Pre-tax, pre-provision income<sup>(1)</sup></b>	<b><u>\$1,619</u></b>	<b><u>\$1,507</u></b>

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