



## 3Q19 Financial Results

October 22, 2019

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 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, 2018, and "Management's Discussion & Analysis of Financial Condition and Results of Operations" in the company's Quarterly Report on Form 10-Q for the quarters ended June 30, 2019, and March 31, 2019, 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 \$770MM, diluted EPS of \$2.36; return on equity of 26%
- Total loan growth of 6% led by an 7% increase in credit card loans; revenue growth of 6% and NIM of 10.43%
- Strong credit performance reflecting disciplined underwriting and continued investments in servicing and collection capabilities
- Payment Services continued to drive strong network volume growth (up 7%)
- Returned \$540MM of capital through dividends and share repurchases

**Note(s)**

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

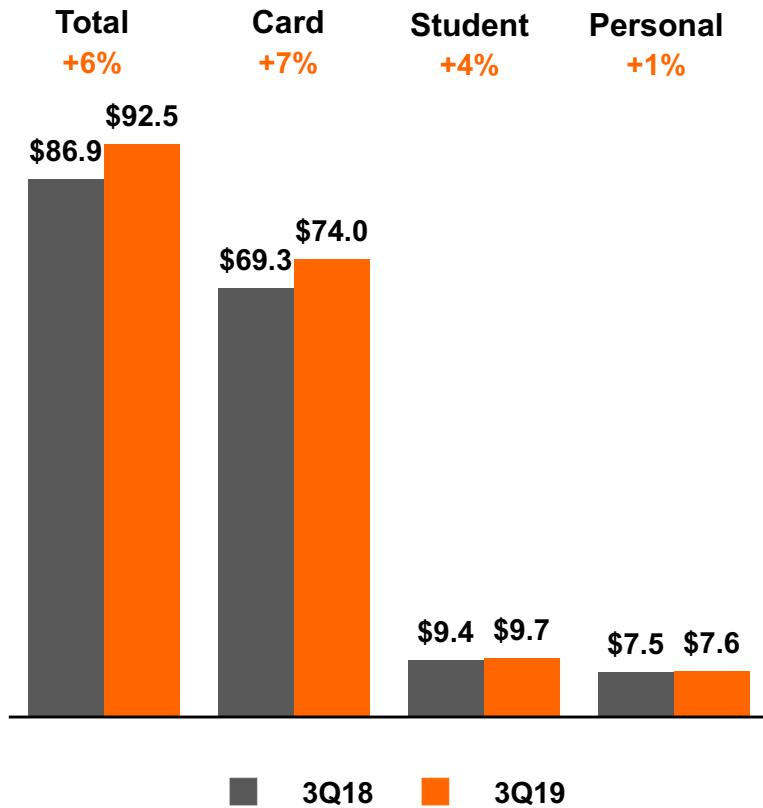
(\$MM, except per share data)	3Q19	3Q18	Inc / (Dec)	
			\$	%
Revenue Net of Interest Expense	\$2,900	\$2,724	\$176	6%
Net Principal Charge-off	702	642	60	9%
Reserve Change	97	100	(3)	(3%)
Provision for Loan Losses	799	742	57	8%
Operating Expense	1,107	1,015	92	9%
Total Pre-Tax Income	994	967	27	3%
Income Tax Expense	224	247	(23)	(9%)
Net Income	\$770	\$720	\$50	7%
<u>Segment Pre-Tax Income</u>				
Direct Banking	\$943	\$923	\$20	2%
Payment Services	51	44	7	16%
Total Pre-Tax Income	\$994	\$967	\$27	3%

<b>ROE</b>	<b>26%</b>	<b>26%</b>		
<b>Diluted EPS</b>	<b>\$2.36</b>	<b>\$2.05</b>	<b>\$0.31</b>	<b>15%</b>

## Highlights

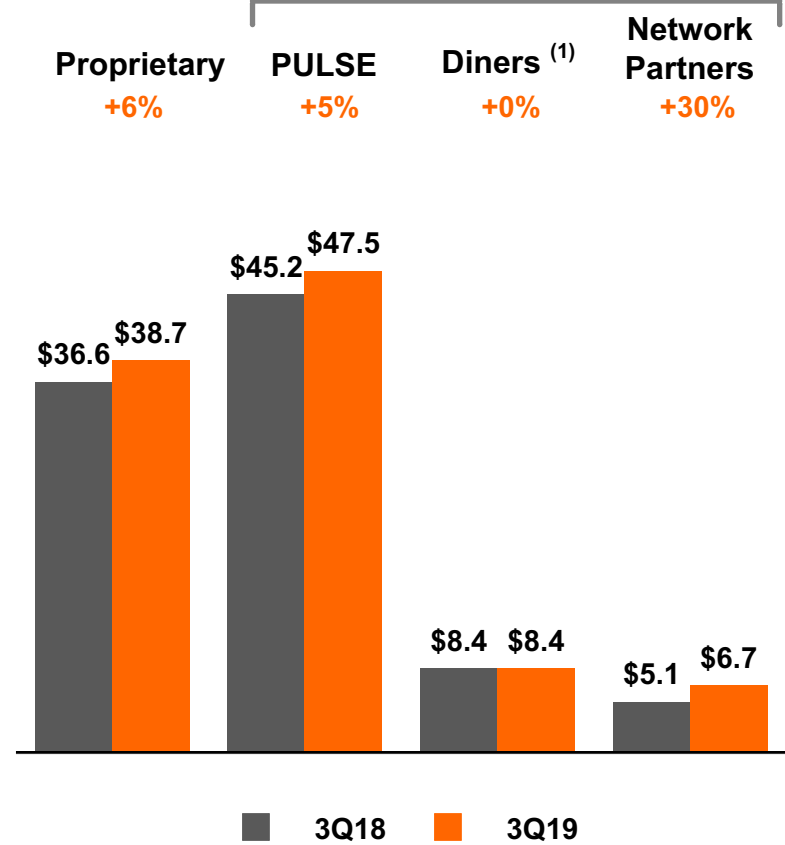
- Revenue net of interest expense of \$2.9Bn, up 6%, driven by higher net interest income
- Provision for loan losses increased \$57MM, or 8%, on higher net charge-offs, slightly offset by a lower reserve build
- Expenses rose 9%, primarily driven by higher compensation expense, as well as investments to support growth and new capabilities
- Diluted EPS of \$2.36, up 15%

## Ending Loans (\$Bn)



## Volume (\$Bn)

### Payment Services



Total Network Volume up 6% 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)	3Q19	3Q18	Inc / (Dec)	
			\$	%
Interest Income	\$3,040	\$2,781	\$259	9%
Interest Expense	638	558	80	14%
Net Interest Income	2,402	2,223	179	8%
Discount/Interchange Revenue	775	753	22	3%
Rewards Cost	520	473	47	10%
Net Discount/Interchange Revenue	255	280	(25)	(9%)
Protection Products Revenue	48	51	(3)	(6%)
Loan Fee Income	120	103	17	17%
Transaction Processing Revenue	52	47	5	11%
Other Income	23	20	3	15%
Total Non-Interest Income	498	501	(3)	(1%)
Revenue Net of Interest Expense	\$2,900	\$2,724	\$176	6%
<u>Segment Revenue Net of Interest Expense</u>				
Direct Banking	\$2,811	\$2,644	\$167	6%
Payment Services	89	80	9	11%
Revenue Net of Interest Expense	\$2,900	\$2,724	\$176	6%

(\$MM)	3Q19	3Q18	Change	
			QOQ	YOY
Discover Card Sales Volume	\$37,432	\$35,896	2%	4%
Rewards Rate <sup>(1)</sup>	1.38%	1.31%	13 bps	7 bps

**Note(s)**

1. Rewards cost divided by Discover card sales volume

## Highlights

- Loan growth and higher net interest margin drove 8% increase in net interest income
- Net discount and interchange revenue decreased 9% driven by increased rewards cost
- Loan fee income increased due to higher late fees
- Rewards rate up 7 bps YOY driven primarily by the addition of PayPal to the 5% category in 2019

Interest-Earning Assets (\$MM)	3Q19		3Q18	
	Average Balance	Yield	Average Balance	Yield
Credit Card	\$73,248	13.35%	\$68,613	13.06%
Private Student	9,459	8.54%	9,158	8.19%
Personal	7,522	13.17%	7,460	12.66%
Other	1,116	6.72%	624	6.38%
Total Loans	91,345	12.76%	85,855	12.45%
Other Interest-Earning Assets	17,952	2.25%	17,112	2.00%
Total Interest-Earning Assets	<u>\$109,297</u>	<u>11.03%</u>	<u>\$102,967</u>	<u>10.72%</u>

Interest-Earning Liabilities (\$MM)	3Q19		3Q18	
	Average Balance	Rate	Average Balance	Rate
Direct to Consumer and Affinity	\$50,497	2.16%	\$42,498	1.88%
Brokered Deposits and Other	19,132	2.73%	19,939	2.51%
Interest Bearing Deposits	69,629	2.32%	62,437	2.08%
Borrowings	24,767	3.70%	26,495	3.43%
Total Interest-Bearing Liabilities	<u>\$94,396</u>	<u>2.68%</u>	<u>\$88,932</u>	<u>2.49%</u>

(% )	Change		
	3Q19	QOQ	YOY
Total Interest Yield on Loans	12.76%	-6bps	31bps
NIM on Loans	10.43%	-4bps	15bps
NIM on Interest-Earning Assets	8.72%	15bps	15bps

## Highlights

- Net interest margin on loans up 15 bps as higher loan yields were partially offset by higher funding costs
- Credit card yield increased 29 bps due to prime rate increases in 2018 and favorable portfolio mix, partially offset by higher interest charge-offs and recent prime rate decreases
- Average consumer deposits grew 19% and composed 53% of total funding
- Funding costs on interest-bearing liabilities increased 19 bps, primarily driven by higher market rates

(\$MM)	3Q19	3Q18	Inc / (Dec)	
			\$	%
Employee Compensation and Benefits	\$439	\$408	\$31	8%
Marketing and Business Development	230	218	12	6%
Information Processing & Communications	96	89	7	8%
Professional Fees	189	166	23	14%
Premises and Equipment	26	26	0	—%
Other Expense	127	108	19	18%
<b>Total Operating Expense</b>	<b>\$1,107</b>	<b>\$1,015</b>	<b>\$92</b>	<b>9%</b>

#### Segment Operating Expense

Direct Banking	1,069	979	\$90	9%
Payment Services	38	36	2	6%
<b>Total Operating Expense</b>	<b>\$1,107</b>	<b>\$1,015</b>	<b>\$92</b>	<b>9%</b>

**Operating Efficiency<sup>(1)</sup>**                      **38.2%**    **37.2%**                      **(100) bps**

#### Note(s)

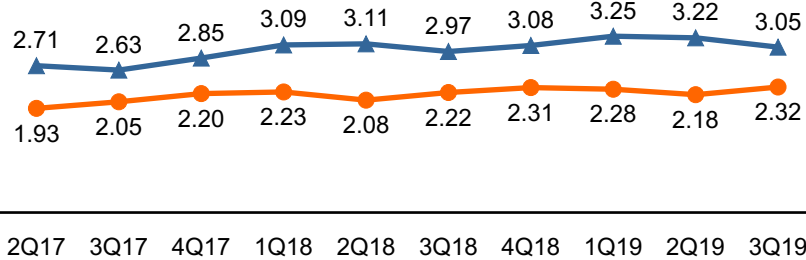
1. Defined as reported total operating expense divided by revenue net of interest expense

## Highlights

- Employee compensation and benefits up 8%, primarily due to higher average salaries and benefits
- Marketing up 6% as a result of higher investments in new account acquisition
- Professional fees up 14%, primarily related to achieving a higher level of recoveries

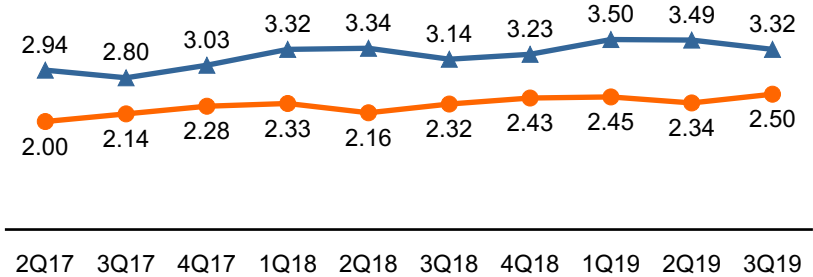


## Total Company Loans



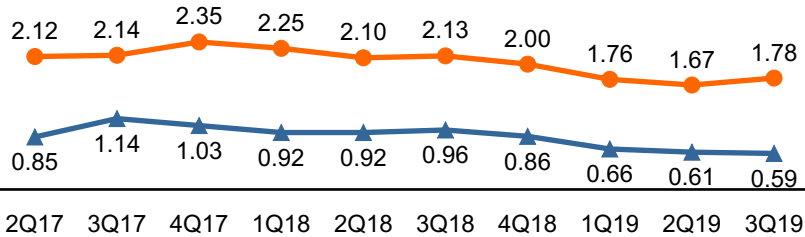
▲ NCO rate (%)      ● 30+ day DQ rate ex-PCI (%)

## Credit Card Loans



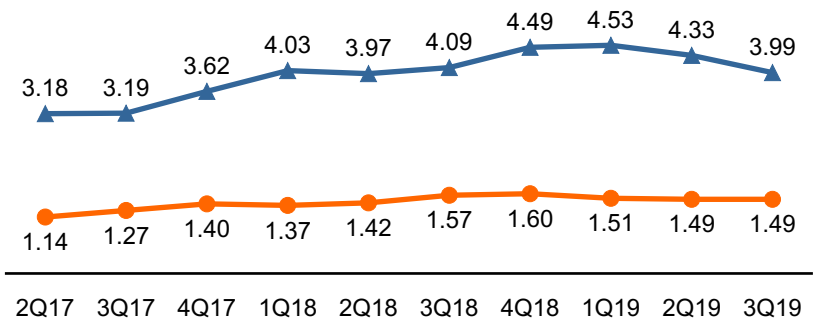
▲ NCO rate (%)      ● 30+ day DQ rate (%)

## Private Student Loans

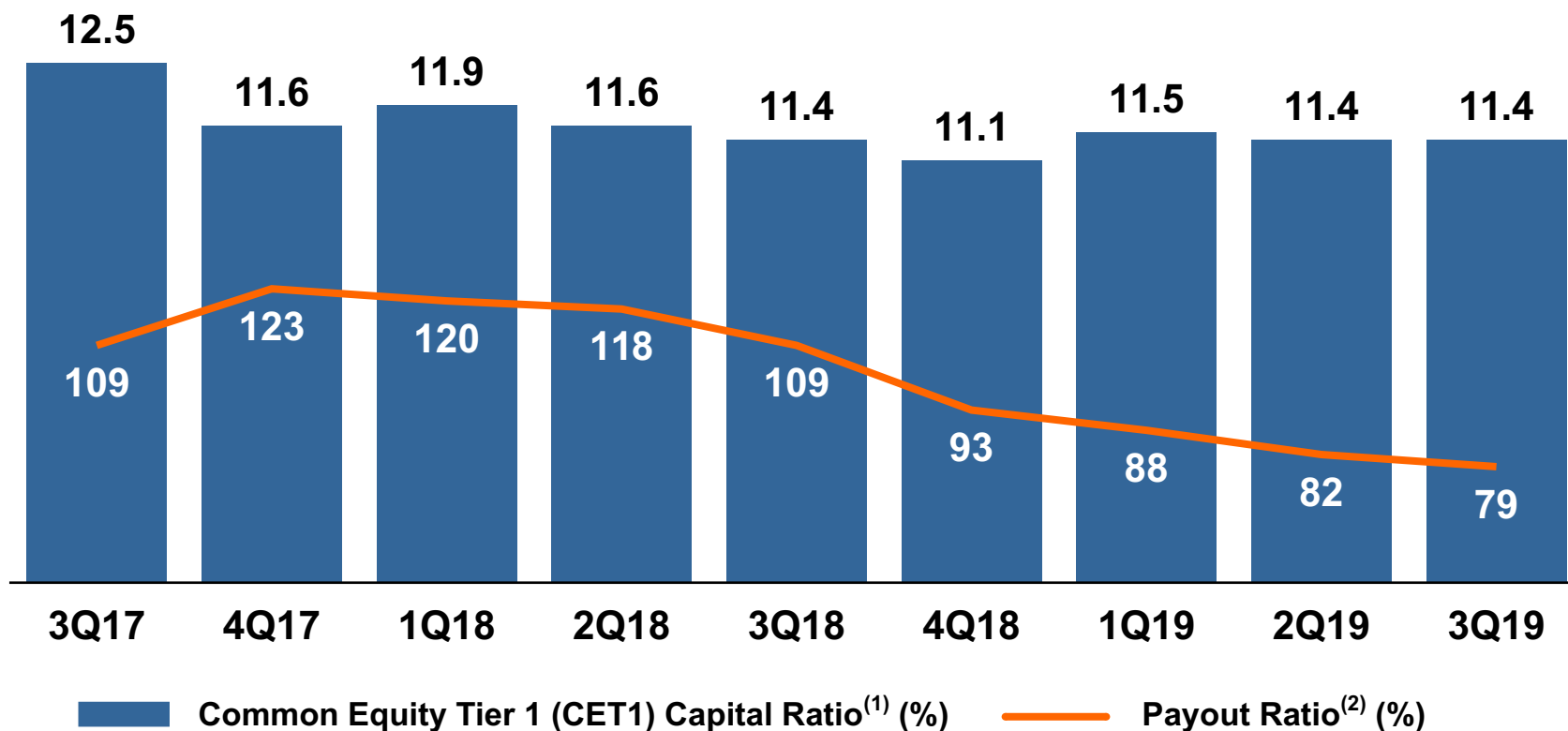


▲ NCO rate (%)      ● 30+ day DQ rate ex-PCI (%)

## Personal Loans



▲ NCO rate (%)      ● 30+ day DQ rate (%)



**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 6% (\$5.6Bn) YOY
- Credit card loans grew 7% (\$4.7Bn) YOY as sales volume increased 4%
- Average consumer deposits grew 19% (\$8.0Bn) YOY, while deposit rates increased 28 bps

## Credit and Capital

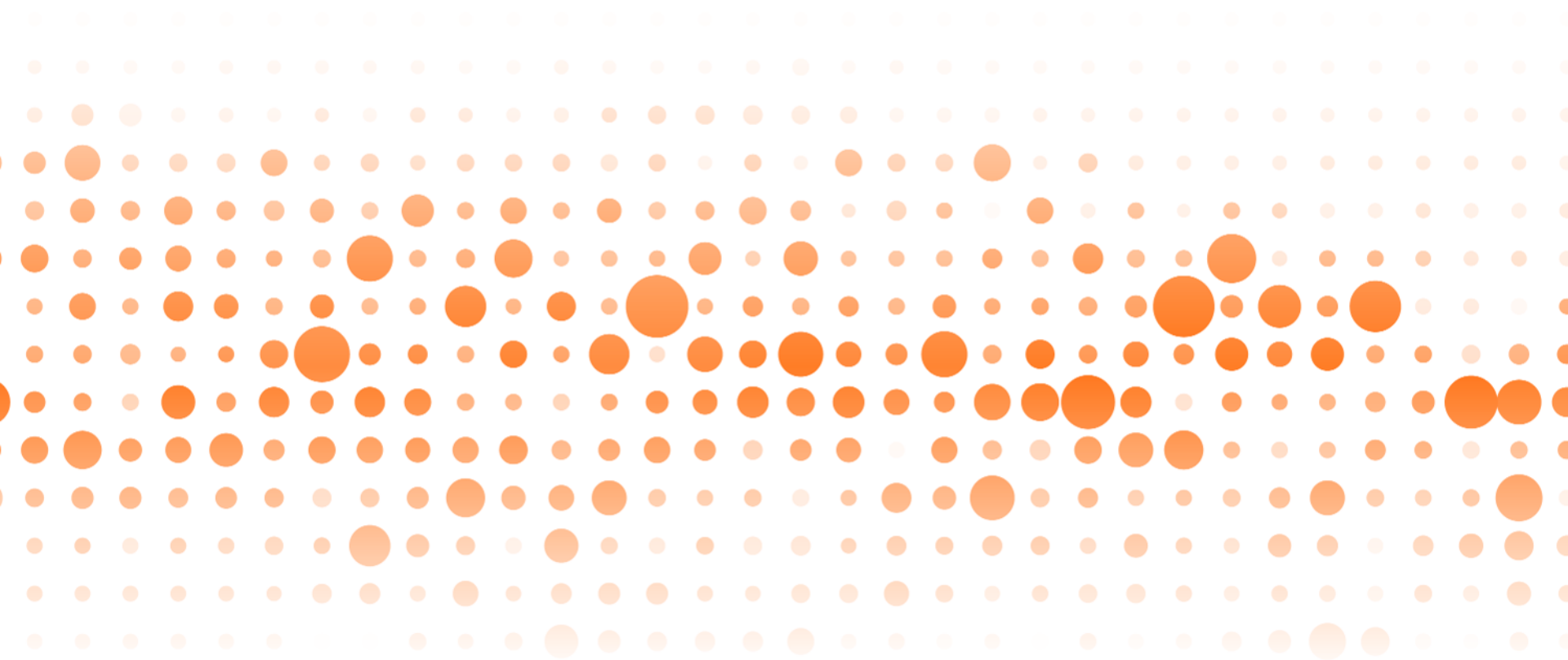
- Total NCO rate of 3.05%, up 8 bps YOY
  - Reflects loan seasoning and supply-driven credit normalization
- Capital return
  - Repurchased 5.1MM shares of common stock for \$419MM
  - CET1 capital ratio<sup>(1)</sup> of 11.4% flat to prior year and prior quarter

## Profitability

- Net income of \$770MM and diluted EPS of \$2.36
- Revenue growth of 6% on higher net interest income
- NIM of 10.43%, up 15 bps YOY
- Strong return on equity at 26%

### Note(s)

1. Basel III Transition



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