



# 2020 and 4Q20 Financial Results

January 20, 2021

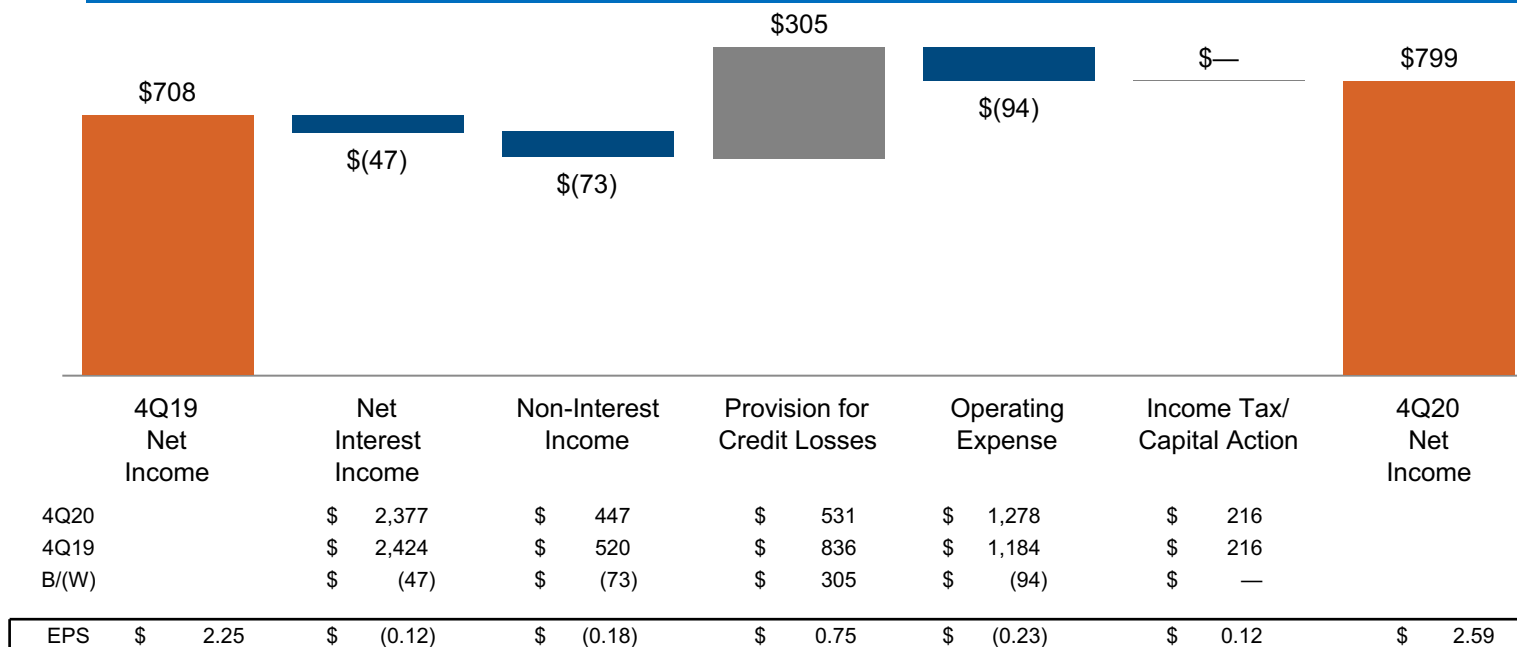
The following slides are part of a presentation by Discover Financial Services (the "Company") in connection with reporting quarterly financial results and are intended to be viewed as part of that presentation. No representation is made that the information in these slides is complete. For additional 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, 2019, "Risk Factors" 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 March 31, 2020, June 30, 2020, and September 30 2020 which is filed with the SEC and available at the SEC's website ([www.sec.gov](http://www.sec.gov)) and subsequent reports on Forms 8-K and 10-Q, including the Company's Current Report on Form 8-K filed today with the SEC. The Company does not undertake to update or revise forward-looking statements as more information becomes available.

- The challenges of 2020 highlighted the strength of our digital banking business model; our effective execution on several initiatives protected employees, supported customers and strengthened the Discover franchise
- Strong credit performance aided by history of conservative credit management and actions taken early in the pandemic
  - Tightened underwriting criteria on new accounts
  - Pulled back on promotional rate offers
  - Proactive credit line management
- Delivered \$400MM in planned expense reductions
  - Committed to disciplined expense management
  - Continuing to invest in core capabilities to drive long-term growth and efficiency gains
- Well-positioned for growth as U.S. economy moves into recovery
- Remain committed to returning capital to shareholders; recent Board approval for new \$1.1 billion share repurchase program
- 2020 Net Income of \$1.1Bn; diluted EPS of \$3.60; 4Q20 Net Income of \$799MM; diluted EPS of \$2.59

# DISCOVER® | 4Q20 Summary Financial Results

## Year-Over-Year Net Income & EPS (\$MM, except EPS)



## Key Points

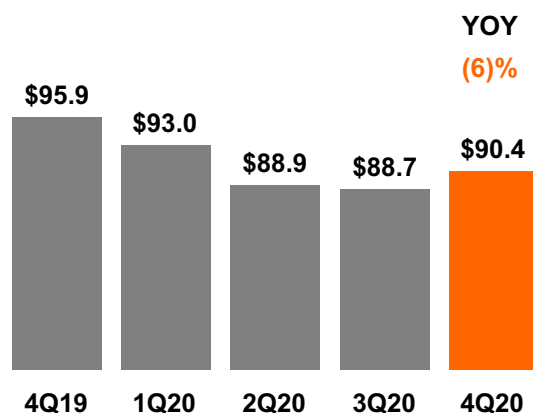
- Revenue net of interest expense was \$2.8Bn, down 4%, driven by lower net interest income and lower net discount and interchange revenue
- Net interest margin was 10.63%, up 34 bps as lower funding costs were partially offset by lower loan yields driven by prime rate decreases
- Provision for credit losses decreased by \$305MM driven by lower net charge-offs; there was no change in reserves in 4Q20
- Expenses were up 8% reflecting one-time items; excluding these items, expenses were down 4% as reductions in marketing and professional fees were partially offset by higher compensation <sup>(1)</sup>

### Note(s)

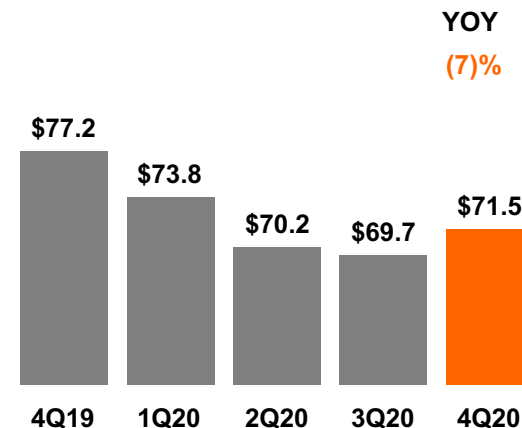
1. Operating expense adjusted for one-time items is a non-GAAP measure. Management believes providing expenses excluding one-time items helps investors understand the impact of activities that are not expected to continue and provides investors with a useful metric to evaluate the company's operating performance; see appendix for a reconciliation

# DISCOVER® | 4Q20 Loan Growth (\$Bn)

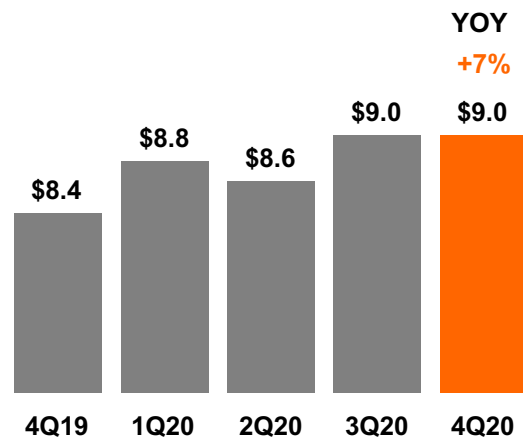
## Total



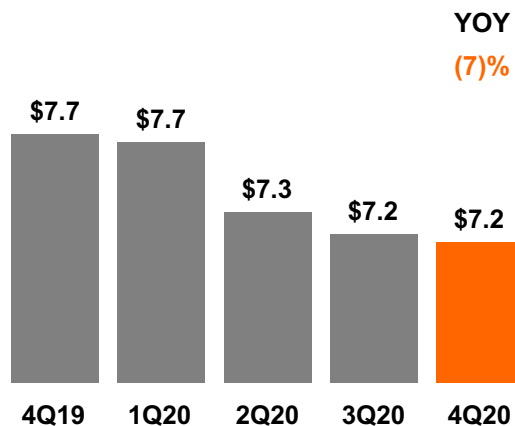
## Card



## Organic Student



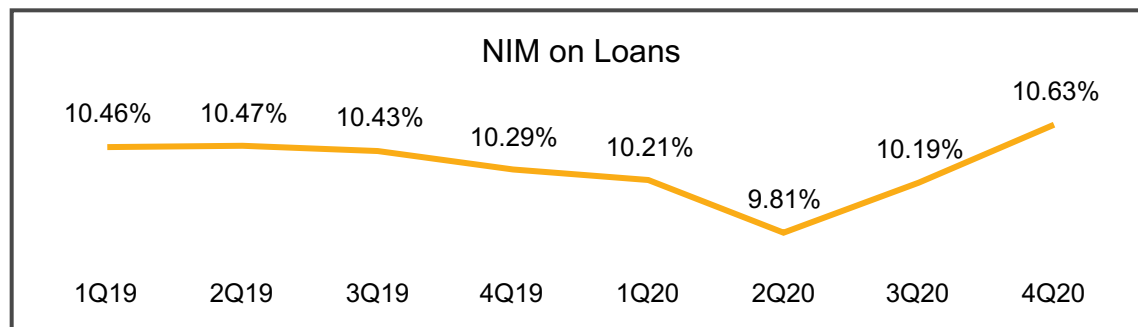
## Personal



## Key Points

- Card receivables down 7% YOY driven by increased payment rates and lower BT/ promo activity; up 3% QOQ driven by seasonal activity
- Organic student loans up 7% YOY reflecting market share gain through 2020 peak season
- Personal loans decreased 7% YOY reflecting increased payments and actions taken to mitigate credit risk

# DISCOVER® | 4Q20 Net Interest Margin



(%)				Change	
	4Q20	3Q20	4Q19	QOQ	YOY
Total Interest Yield on Loans	11.96 %	11.78 %	12.52 %	18bps	-56bps
NIM on Loans	10.63 %	10.19 %	10.29 %	44bps	34bps
NIM on Interest-Earning Assets	7.93 %	7.70 %	8.66 %	23bps	-73bps

Interest-Earning Assets (\$Bn)	4Q20		3Q20		4Q19	
	Avg Bal	Yield	Avg Bal	Yield	Avg Bal	Yield
Total Loans	\$89.0	11.96 %	\$88.4	11.78 %	\$93.4	12.52 %
Other Interest-Earning Assets	30.3	1.13 %	28.6	0.88 %	17.7	2.05 %
Total Interest-Earning Assets	\$119.3	9.20 %	\$117.0	9.11 %	\$111.1	10.86 %

Interest-Bearing Liabilities (\$Bn)	4Q20		3Q20		4Q19	
	Avg Bal	Rate	Avg Bal	Rate	Avg Bal	Rate
Direct to Consumer Deposits <sup>(1)</sup>	\$62.5	0.94 %	\$61.6	1.25 %	\$53.0	2.03 %
Brokered Deposits and Other	13.7	2.38 %	15.3	2.47 %	17.9	2.72 %
Interest Bearing-Deposits	76.2	1.20 %	76.8	1.49 %	70.9	2.20 %
Borrowings	25.1	2.42 %	22.9	2.23 %	25.1	3.50 %
Total Interest-Bearing Liabilities	\$101.3	1.50 %	\$99.7	1.66 %	\$96.0	2.54 %

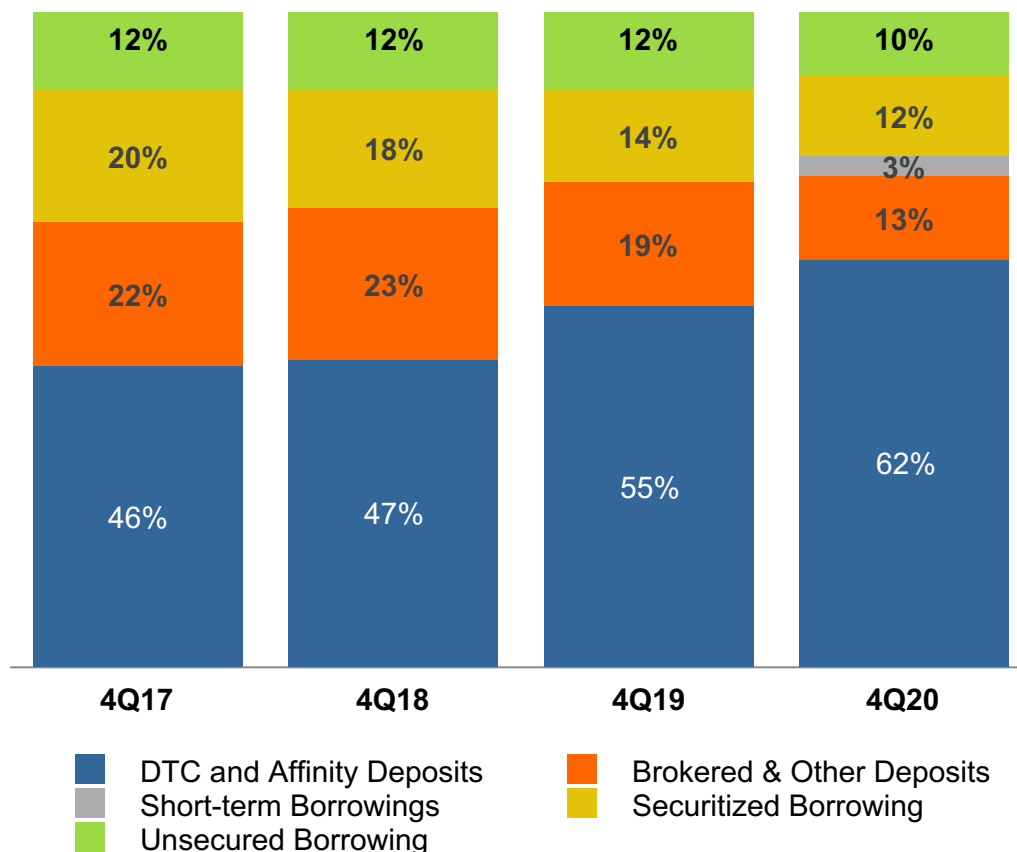
## Note(s)

1. Includes Affinity relationships

## Key Points

- NIM on loans was 10.63%, up 44bps QOQ driven by favorable deposit pricing
- Total loan yield of 11.96% down 56bps YOY reflecting the impact of prime rate decreases partially offset by favorable portfolio mix and lower interest charge-offs; up 18bps QOQ driven by favorable portfolio mix and lower interest charge-offs
- Average consumer deposits of \$62.5Bn grew 18% YOY and were up 1.0Bn QOQ; consumer deposits composed 62% of total funding
- Rate on average interest-bearing liabilities of 1.50%, down 104bps YOY and 16bps QOQ, driven by lower deposit pricing

## Funding Mix (%), Average Balance



## Maturities

Maturity profile provides opportunity to continue optimizing funding costs

Maturities (\$Bn)	FY20	FY21	FY22
Brokered & Other Deposits	\$ 19.0	\$ 17.9	\$ 4.5
Securitized Borrowing	\$ 3.0	\$ 3.4	\$ 4.4
Unsecured Borrowings	\$ 1.8	\$ 0.8	\$ 0.8
<b>Total</b>	<b>\$ 23.8</b>	<b>\$ 22.0</b>	<b>\$ 9.7</b>

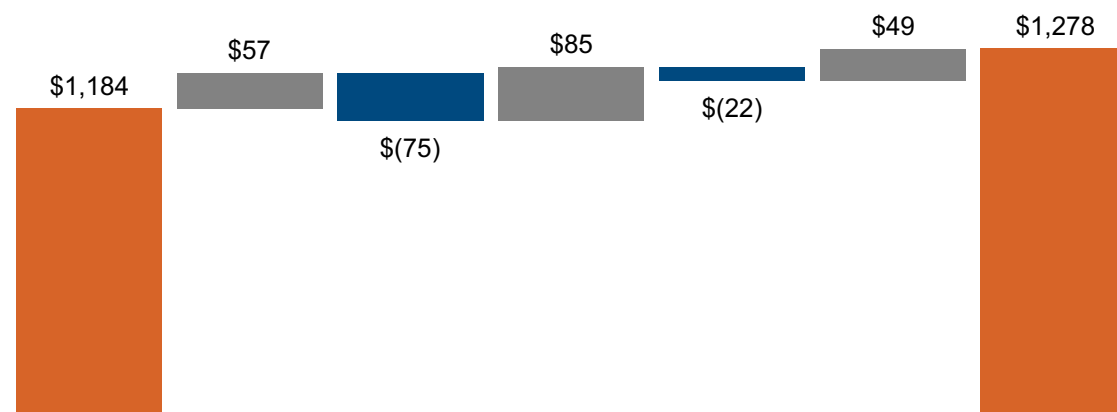
Average Maturity Rate (%) <sup>(1)</sup>	FY20	FY21	FY22
Brokered & Other Deposits	2.34 %	1.81 %	2.21 %
Securitized Borrowing	0.63 %	0.47 %	0.70 %
Unsecured Borrowings	4.21 %	1.93 %	4.35 %
<b>Total</b>	<b>2.26 %</b>	<b>1.61 %</b>	<b>1.72 %</b>

### Note(s)

1. Effective cost net of hedge impact

# DISCOVER® | 4Q20 Operating Expense

## Year-Over-Year Expense (\$MM)



4Q19 Expense	Employee Comp	Marketing	Info Process	Prof Fees	All Other	4Q20 Expense
(\$MM)						
				4Q20	4Q19	Inc / (Dec)
				\$		%
Employee Compensation and Benefits				\$504	\$447	\$57 13%
Marketing and Business Development				159	234	(75) (32%)
Information Processing & Communications				198	113	85 75%
Professional Fees				192	214	(22) (10%)
Premises and Equipment				30	27	3 11%
Other Expense				195	149	46 31%
Total Operating Expense				\$1,278	\$1,184	\$94 8%
Total Operating Expense ex one-time items <sup>(1)</sup>				\$1,141	\$1,184	(\$43) (4%)
Operating Efficiency <sup>(2)</sup>				45.2 %	40.2 %	500 bps

### Note(s)

- Operating expense adjusted for one-time items is a non-GAAP measure. Management believes providing expenses excluding one-time items helps investors understand the impact of activities that are not expected to continue and provides investors with a useful metric to evaluate the company's operating performance; see appendix for a reconciliation
- Defined as reported total operating expense divided by revenue net of interest expense

## Key Points

One-time items in the quarter included:

(\$MM)

Information Processing	\$77	Software write-offs
Compensation & Benefits	\$26	Voluntary early retirement program
Other Expense	\$27	Penalties and restitution
Premise & Equipment	\$7	Accelerated lease depreciation

Excluding one-time items, expenses were down 4% and included:

- Increased employee compensation reflecting higher average salaries and increased headcount
- Lower marketing expense as we aligned costs with the economic environment; reductions primarily in brand and acquisition marketing
- Decreased professional fees primarily driven by lower collection fees

	4Q19	3Q20	4Q20	Change	
				QOQ	YOY
<b>Credit Card Loans</b>					
Ending Loan Balance (\$MM)	\$77,181	\$69,656	\$71,472	2.6%	(7.4)%
Net Principal Charge-off Rate	3.41%	3.45%	2.63%	(82) bps	(78) bps
30-Day Delinquency Rate	2.62%	1.91%	2.07%	16 bps	(55) bps
<b>Private Student Loans</b>					
Ending Loan Balance (\$MM)	\$9,653	\$10,016	\$9,954	(0.6)%	3.1%
Net Principal Charge-off Rate	1.02%	0.58%	0.71%	13 bps	(31) bps
30-Day Delinquency Rate <sup>(1)</sup>	1.72%	1.41%	1.32%	(9) bps	(40) bps
<b>Personal Loans</b>					
Ending Loan Balance (\$MM)	\$7,687	\$7,211	\$7,177	(0.5)%	(6.6)%
Net Principal Charge-off Rate	4.26%	2.69%	2.79%	10 bps	(147) bps
30-Day Delinquency Rate	1.37%	1.10%	1.08%	(2) bps	(29) bps
<b>Total Loans</b>					
Ending Loan Balance (\$MM)	\$95,894	\$88,660	\$90,449	2.0%	(5.7)%
Net Principal Charge-off Rate	3.19%	3.00%	2.38%	(62) bps	(81) bps
30-Day Delinquency Rate <sup>(1)</sup>	2.40%	1.76%	1.88%	12 bps	(52) bps

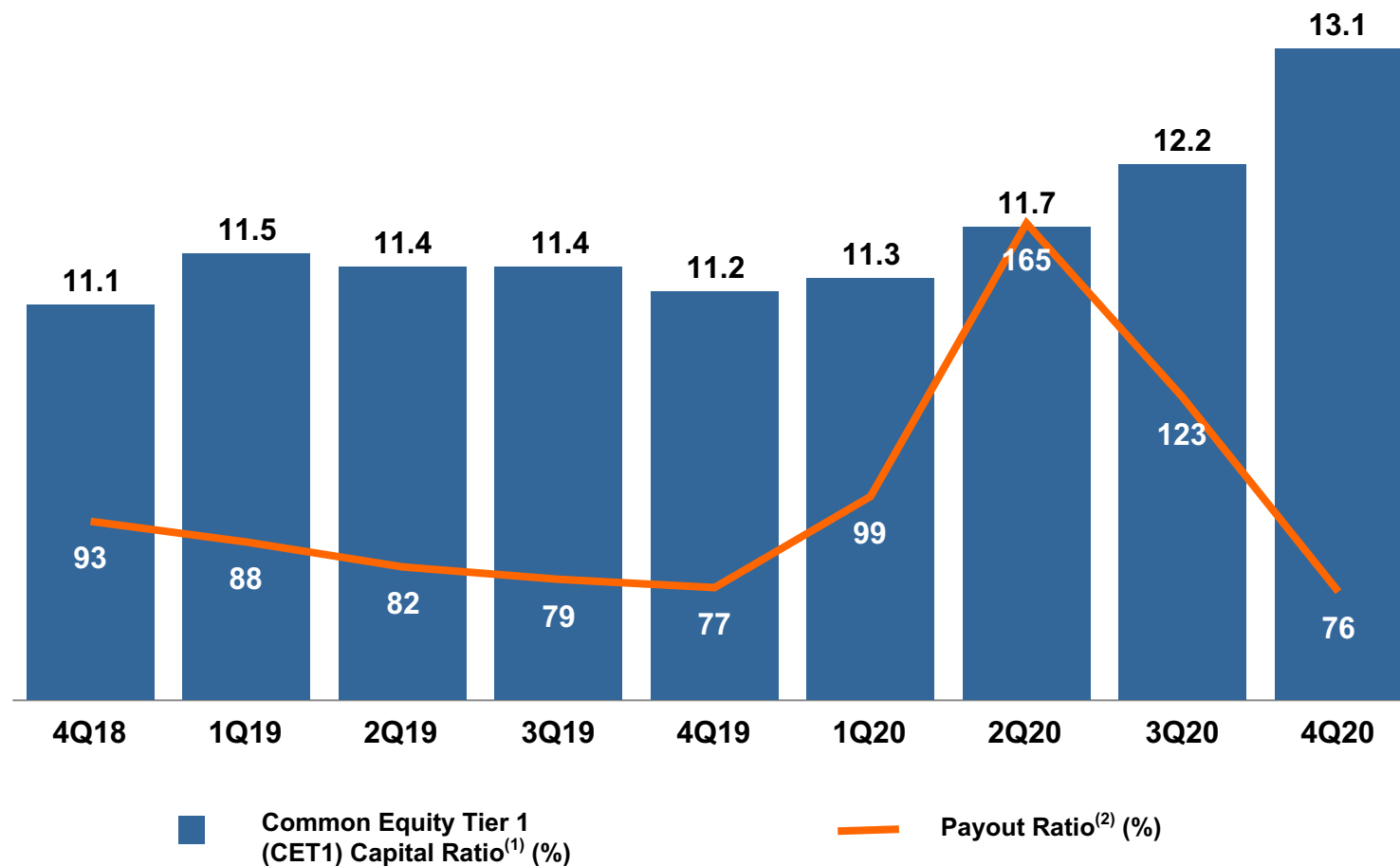
**Note(s)**

1. 30-Day Delinquency Rate excludes purchased loans

## Key Points

- Credit card net charge-off rate decreased 78 bps YOY while 30-Day delinquency decreased 55bps YOY reflecting strong credit performance
- Student loan credit performance remains stable
- Personal loan net charge-offs improved 147bps YOY reflecting underwriting enhancements and consumer liquidity

(\$MM)	Credit Card	Student Loans	Personal Loans	Other	Total Loans
<b>Balance at January 1, 2020</b>	4,550	653	613	28	5,844
Reserve rate	5.90 %	6.76 %	7.97 %	N/A	6.09 %
<b>Balance at March 31, 2020</b>	5,306	765	807	35	6,913
Reserve rate	7.19 %	7.68 %	10.55 %	N/A	7.44 %
<b>Balance at June 30, 2020</b>	6,491	799	857	37	8,184
Reserve rate	9.25 %	8.21 %	11.71 %	N/A	9.2 %
<b>Balance at September 30, 2020</b>	<u>\$6,491</u>	<u>\$840</u>	<u>\$857</u>	<u>\$38</u>	<u>\$8,226</u>
Reserve rate	9.32 %	8.38 %	11.89 %	N/A	9.28 %
Provision for credit losses	463	18	50	—	531
Net Charge-offs	(463)	(18)	(50)	—	(531)
<b>Balance at December 31, 2020</b>	<u>\$6,491</u>	<u>\$840</u>	<u>\$857</u>	<u>\$38</u>	<u>\$8,226</u>
Reserve rate	9.08 %	8.43 %	11.94 %	N/A	9.09 %



**Note(s)**

1. Based on the final rule published September 30, 2020. Capital ratios reflect delay in the recognition of the impact of CECL reserves on regulatory capital for two years in accordance with the final rule
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

## Loan Growth

- Modestly positive, subject to payment rate trends and economic conditions

## Net Interest Margin

- Decline in funding costs provides tailwind

## Operating Expense

- Focus on disciplined expense management
- Investments in marketing, technology capabilities, and automation

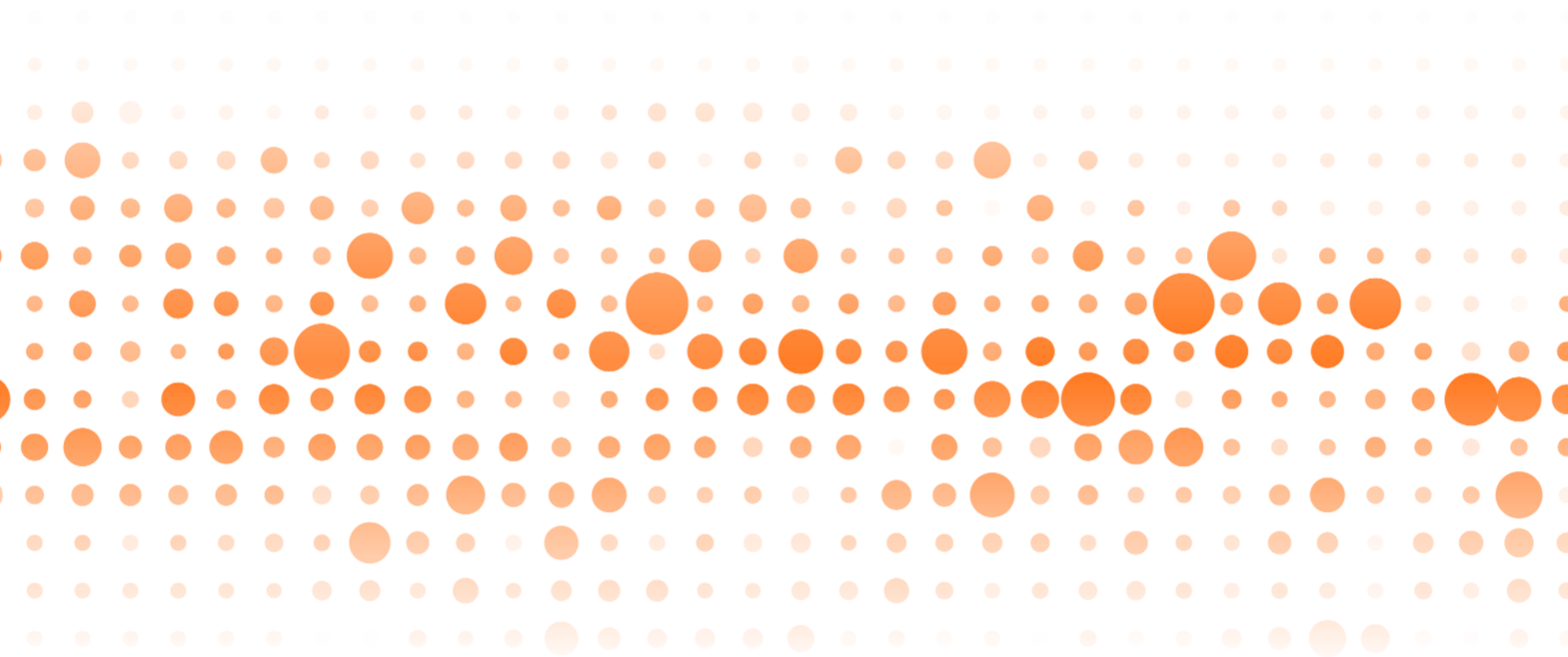
## Net Charge-offs

- Losses expected to increase in 2H21
- Likely to remain elevated into 2022

## Capital Management

- Priorities for capital return remain unchanged
- Approved up to \$1.1Bn in share repurchases

# Appendix



(\$MM)	4Q20	4Q19	Inc / (Dec)	
			\$	%
Net Interest Income	2,377	2,424	(47)	(2%)
Net Discount/Interchange Revenue	242	281	(39)	(14%)
Protection Products Revenue	45	48	(3)	(6%)
Loan Fee Income	110	123	(13)	(11%)
Transaction Processing Revenue	52	51	1	2%
Other Income	(2)	17	(19)	(112%)
Total Non-Interest Income	447	520	(73)	(14%)
Revenue Net of Interest Expense	<u>\$2,824</u>	<u>\$2,944</u>	<u>\$(120)</u>	<u>(4%)</u>

	4Q20	4Q19	Change	
			QOQ	YOY
Discover Card Sales Volume (\$MM)	\$40,957	\$39,188	10 %	5 %
Rewards Rate <sup>(1)</sup>	1.38 %	1.32 %	—bps	6bps
NIM on Loans	10.63 %	10.29 %	44bps	34bps

**Note(s)**

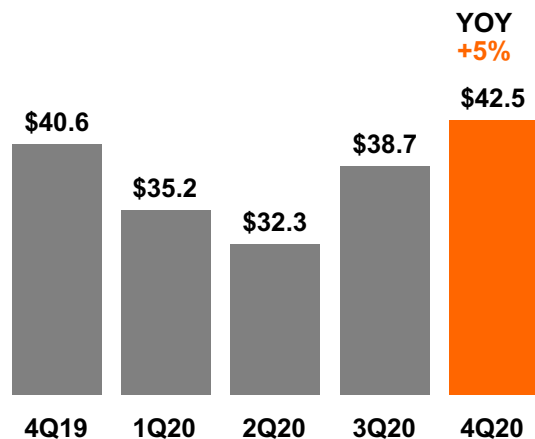
1. Rewards cost divided by Discover card sales volume

## Key Points

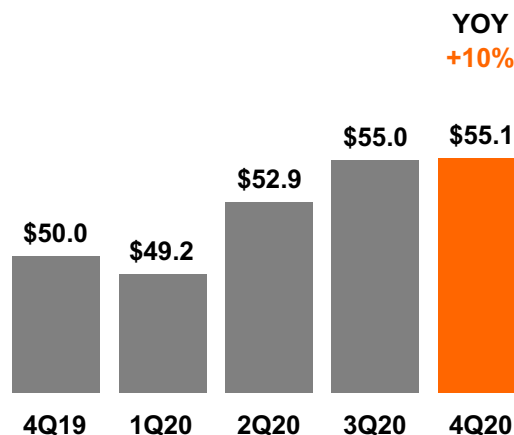
- Net interest income decreased 2% primarily due to lower average receivables
- Net discount and interchange revenue down 14% driven by higher rewards cost
- Rewards rate was 6bps higher YOY primarily driven by increased sales in 5% categories, particularly due to growth in online spending

# DISCOVER® | 4Q20 Payments Volume (\$Bn)

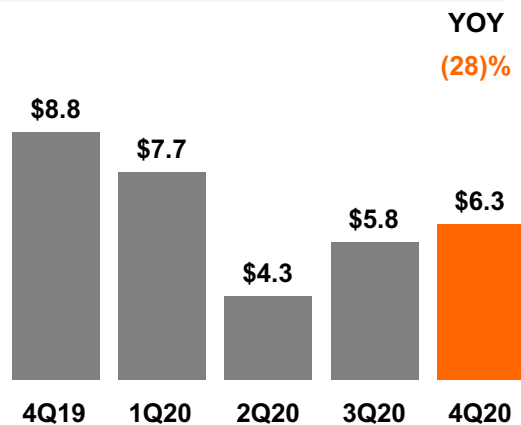
## Discover Network



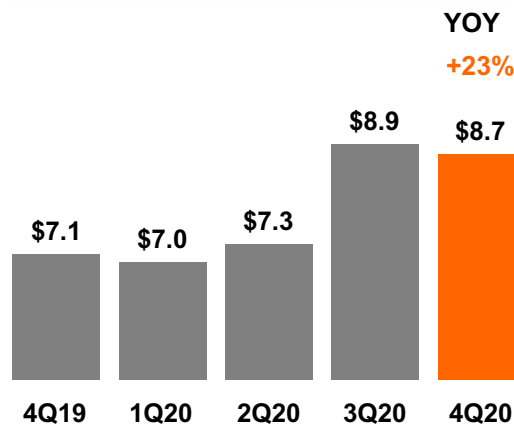
## PULSE



## Diners <sup>(1)</sup>



## Network Partners



Total Network Volume up 6% YOY

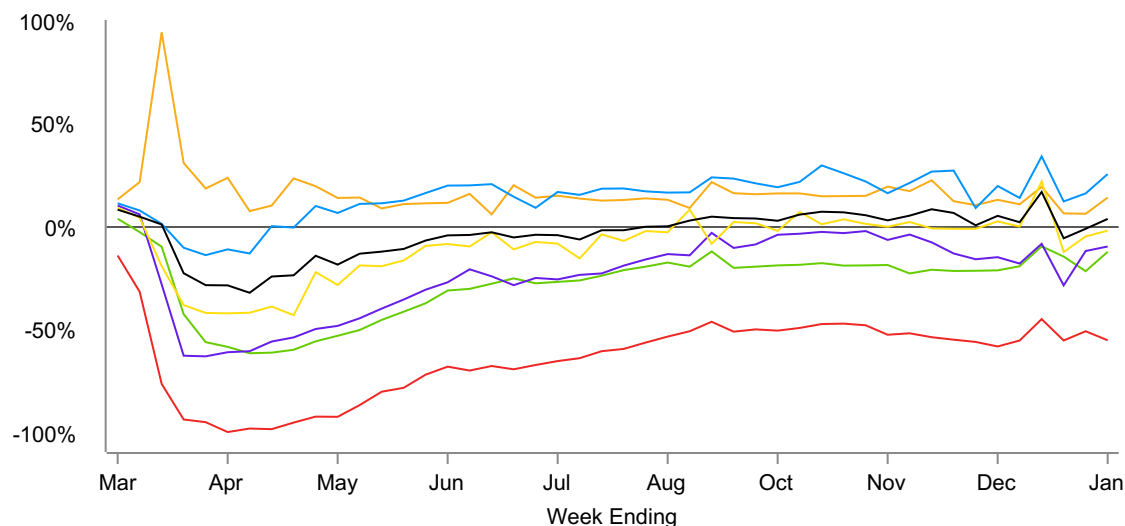
## Key Points

- Discover Network volume was up 5% reflecting the increase in Discover card sales volume
- PULSE volume up 10% YOY driven by higher average spend per transaction, increased spend at grocery and home improvement and higher ATM volume
- Diners Club volume down 28% from the prior year reflecting the impact of the global pandemic on T&E spending
- Network Partners higher 23% driven by higher AribaPay volume

### Note(s)

- 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

## Weekly Sales Volume Trend (%)



Gas (green line)  
 Restaurants (purple line)  
 Total Sales Volume (black line)  
 Groceries (orange line)  
 Services (yellow line)  
 Retail (blue line)  
 Travel (red line)

## Year-Over-Year Sales Volume Trend (%)

	FY19 Sales Mix	FY20 Sales Mix	1Q20	2Q20	3Q20	4Q20
Gas	6%	4%	—%	(48)%	(23)%	(20)%
Grocery	9%	11%	14%	14%	13%	14%
Retail	35%	40%	6%	7%	18%	20%
Restaurants	8%	7%	(2)%	(43)%	(18)%	(10)%
Services	19%	18%	(1)%	(25)%	(4)%	1%
Travel	8%	4%	(20)%	(85)%	(59)%	(53)%
All Other	16%	16%	6%	(6)%	4%	4%
<b>Total Sales Volume</b>	<b>100%</b>	<b>100%</b>	<b>3%</b>	<b>(16)%</b>	<b>(1)%</b>	<b>5%</b>

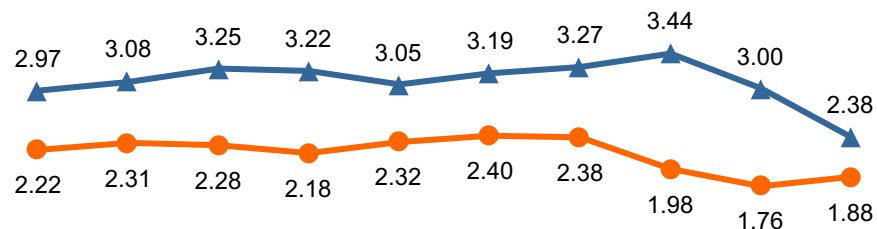
### Category Definitions

- Services includes entertainment, auto, education, medical, and other service providers
- All Other includes discount stores, drug stores, wholesale clubs, telecommunication, utilities, insurance, financial services and government

## Key Points

- 4Q20 sales volume up 5% YOY with trends improving across all categories
- Sales mix shifted to a higher concentration from retail and grocery which are now over half of total sales
- Significant YOY increase in online sales volume
- Travel, restaurants, and gas have improved significantly; headwinds remain due to the pandemic

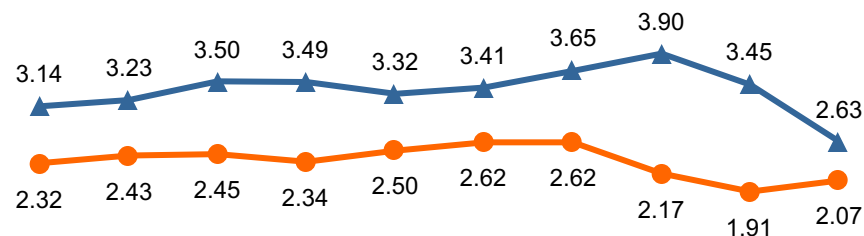
## Total Company Loans



3Q18 4Q18 1Q19 2Q19 3Q19 4Q19 1Q20 2Q20 3Q20 4Q20

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

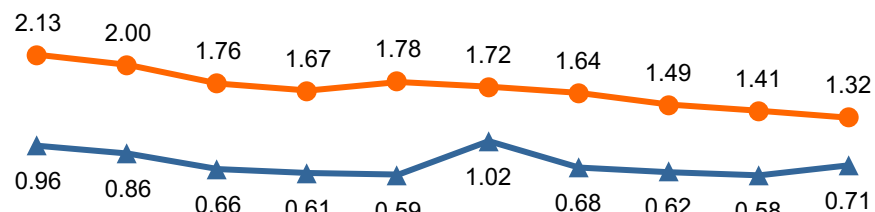
## Credit Card Loans



3Q18 4Q18 1Q19 2Q19 3Q19 4Q19 1Q20 2Q20 3Q20 4Q20

▲ NCO rate (%) ● 30+ day DQ rate (%)

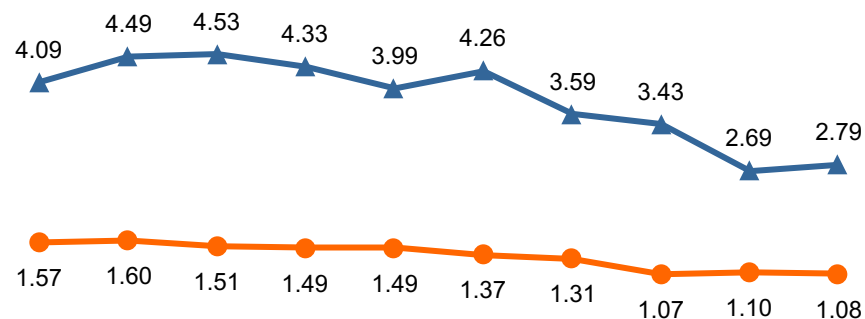
## Private Student Loans



3Q18 4Q18 1Q19 2Q19 3Q19 4Q19 1Q20 2Q20 3Q20 4Q20

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

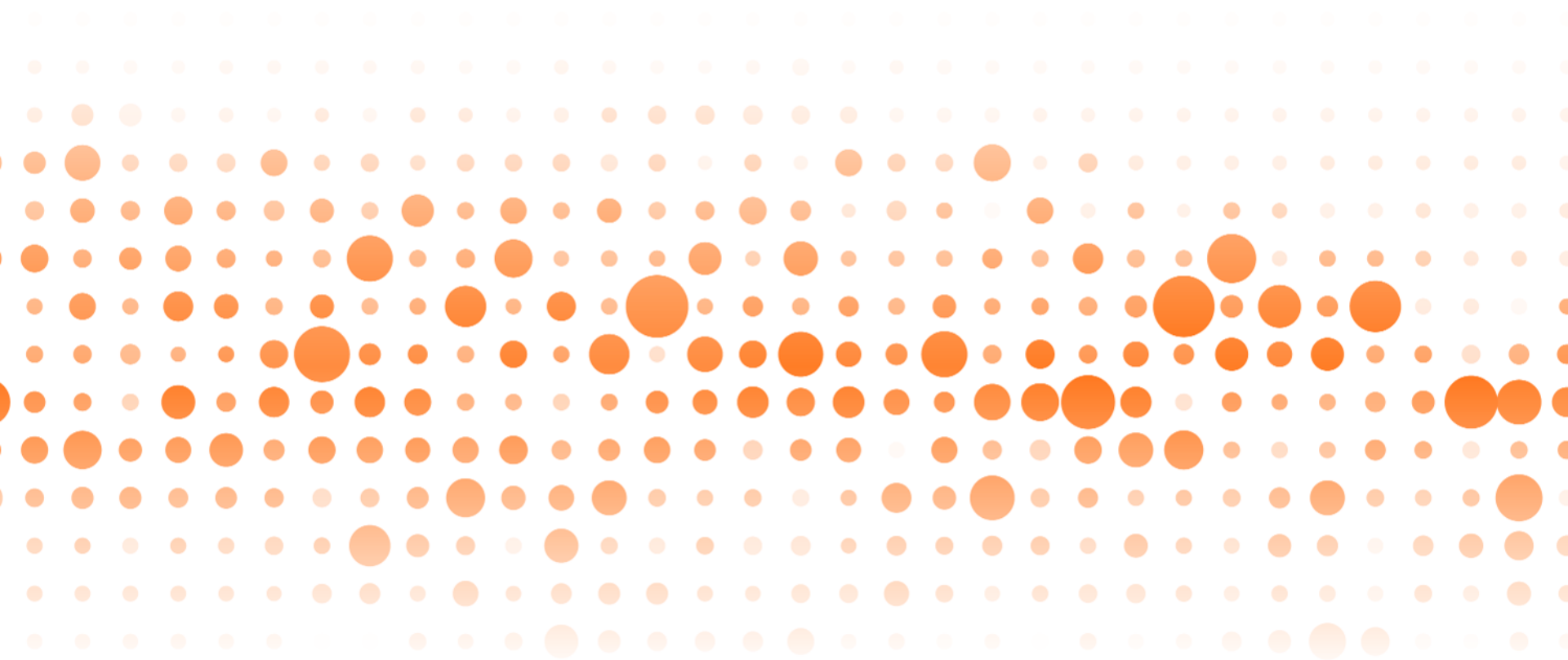
## Personal Loans



3Q18 4Q18 1Q19 2Q19 3Q19 4Q19 1Q20 2Q20 3Q20 4Q20

▲ NCO rate (%) ● 30+ day DQ rate (%)

(\$MM)	<u>4Q20</u>
Total operating expense	\$ 1,278
One-time expenses related to software write-offs, penalties and restitution, voluntary early retirement program, accelerated lease depreciation	<u>\$ (137)</u>
Operating expense ex one-time items	<u><u>\$ 1,141</u></u>



**DISCOVER<sup>®</sup>**