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Lending Earnings Insights

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Where are we in the credit cycle? Earnings calls indicate CEOs/CFOs are constructive on the health of the US consumer and see a tax reform as improving consumers' disposable income. However, an increasing supply for credit and demand for credit, as well as re-normalization trends and increased competition are leading to higher charge-offs.

Credit re-normalization continues across all major lending groups. Credit performance this quarter is mixed. We observe improvements, and record low delinquencies from ONDK, OMF, and FinTechs in particular. LendingClub expects 31 bps lower charge-offs going forward due to tighter credit standards. At Discover – a bellwether for personal loan performance – the net charge off rate jumped 92 bps YOY to 3.62% - the largest increase in several years.

Card issuers are increasing loan loss reserves at a higher rate than loan growth, indicating expectations of higher losses going forward. American Express increased loan loss provisions 33% although loan growth was only 14%.

GS & Morgan Stanley remain comparable in market cap, revenues, and margins – are focused on lending to improve ROE. MS is doubling the size of its warehouse lending footprint. GS continues to invest in Marcus and aggressively pursue M&A. If GS executes on its strategic plan of generating, in 5 years we should observe a growth in ROE from their consumer lending activities.

Bank FinTech partnerships, and M&A continues. Banks are either partnering with FinTechs or investing in beefing up their technology capabilities in payments, lending, digital banking and wealth management. Banks like JP are partnering with Amazon by rolling out co-branded checking accounts and credit cards. A specter is haunting financial services – the specter of Amazon.

Lenders are taking actions to pass rising rates on to borrowers to protect margins and investor returns. Lenders are also trying to reduce all-in funding costs by reducing the credit spreads on their securitizations.

Where are we in the credit cycle?

Overall, lenders thought that the US consumer was healthy and should benefit from tax reform, although they acknowledged that credit re-normalization trends are still underway:

Discover (CEO, David Nelms)	• “The increasing supply of credit from lenders and greater demand for credit from consumers have contributed to rising debt levels and larger losses when a customer defaults. Consumer debt service burdens while rising are still near historic lows, while consumers are re-leveraging both creditors and borrowers are still generally behaving responsibly.”
Citi (CEO, Michael Corbat)	• “The U.S. consumer should also benefit as higher take-home pay could drive either increased discretionary spending or the acceleration of payment of existing debt, each a potential positive outcome from the reduction in tax rates.”
JP Morgan (CFO, Marianne Lake)	• “Whether you're talking about consumers or whether you're talking about small businesses, think about the small business environment, [the tax cut] was quite positive for them, so they're going to see higher profitability, higher free cash flow, and to all intents and purposes, the equivalent of an upgrade. So, we would be hopeful that, much like the commercial space, that could be the catalyst to see them spend money and hire. And we'll be focusing on that as we think about programs to help. So, I think in general, it's going to mean that the already very good credit trends we're seeing will be good for longer.”
Capital One (CEO, Richard Fairbank)	• “I think the consumer is in a pretty good place. Consumer confidence is high. I think consumers have been appropriately cautious over time. They are stepping up to take on more debt, and we have a careful eye on that. But generally, I think the consumer and the credit marketplace in which we play, I think, is at a place that I would describe as the middle of the credit cycle. I think the tax benefit is going to be a near-term positive to an already fairly confident consumer. I think this is almost certainly going to be a good. From a lenders point of view, the one caution I have about the tax windfall, if you will, is will it lead to a wave of greater competitive response, more supply, more competition, more investment such that the inevitable sort of credit effects happen over time.”
OnDeck (CEO, Noah Breslow)	• “We also expect to benefit from the broader economic environment. The economy and employment continue to be robust, and small business confidence is at its highest level in years. And the recent tax reform will be good for OnDeck’s customers as small business owners see their tax bills reduce and their businesses benefit from consumers having additional discretionary income.”

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Technology & Innovation Driving Performance

Lenders are focusing on technology to deliver a better customer experience and grow revenues:

OneMain (CEO, Jay Levine)	• "So, we are investing in the technology that supports both our branches and our online capabilities. We also plan to invest in our post charge-off strategies. We believe we can improve future recoveries by collecting a larger portion of charged off accounts internally."
Citi (CEO, Michael Corbat)	• "I think there's nothing really outside of what we've described, but a big emphasis towards digital, towards technology, towards new and smart banking as we go forward and then, obviously, continued investments in place like our TTS businesses and all the things that we've talked about."
Goldman Sachs (CFO, Marty Chavez)	• "So, the first is [technology] investments in Marcus, something that we've talked a fair bit about, huge and important and exciting area of growth for us and one of the pillars of our growth plan."
Capital One (CEO, Richard Fairbank)	• "I think the technology that I am bullish about being very helpful to us is actually the consumer facing technology of online banking and being able to have a great online experience combined with and build on the shoulders of an infrastructure that we spent years investing in to modernize and integrate from our direct bank and our local bank to modernize and integrate and in a sense rebuild the full technology stack to be able to really credibly offer online banking backed by a thin physical distribution and be able to compete against some of the really great established players."
Square (CFO, Sarah Friar)	• "We've utilized direct mail, utilized TV. In those channels, it's where you'll see us put a lot of machine learning muscle to work. So that we're optimizing those go-to-market avenues and really getting strong ROI"

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Sector Performance

Stock price performance has generally been positive year-to-date, even with the bout of volatility seen in February. With the S&P 500 barely positive for the year, FinTechs with the exception of LC and ONDK, and banks with the exception of WFC and C are positive for the year. Credit card issuers haven't fared as well.

Enova and Square, tech-enabled small business lenders, have delivered the best stock performance this year. Bulge bracket banks have seen only a small rally in their stock prices this year as ROE hasn't lived up to market expectations, especially with lackluster performance in the trading divisions. Card issuers have seen stock price drops, even in a benign credit environment.

Year-to-Date Stock Performance

FinTech & Non-Banks

	Stock Price Performance (%)		
	YTD	QTD	Earnings
ENVA	47%	47%	13%
LC	(7%)	(7%)	(1%)
OMF	22%	22%	5%
ONDK	(9%)	(9%)	14%
PYPL	7%	7%	(6%)
SQ	45%	45%	(1%)

Bulge Bracket Banks

	Stock Price Performance (%)		
	YTD	QTD	Earnings
BAC	9%	9%	1%
C	0%	0%	1%
GS	3%	3%	(3%)
JPM	8%	8%	1%
MS	6%	6%	4%
WFC	(5%)	(5%)	(1%)

Credit Card Issuers

	Stock Price Performance (%)		
	YTD	QTD	Earnings
AXP	(3%)	(3%)	(3%)
COF	(2%)	(2%)	(0%)
DFS	0%	0%	2%
SYF	(6%)	(6%)	6%

Source: Bloomberg, PeerIQ. Note: Earnings price change is the percentage change in closing price before and after earnings update

Impact of the Tax Reform Act

Tax reform has significantly affected revenues for 4Q2017 as banks and card issuers take one-time charges to their deferred tax assets, but are also looking forward to lower tax rates in the future. The lower tax rate in the future will boost ROE, with most banks promising a 1-3% increase in ROE when the new tax rates become effective, a net positive for the sector. In the table below, we summarize the one-time tax impact and expected future tax rates.

Highlights that drive stock price performance

Stocks like ONDK and ENVA that have delivered loan growth and low charge-offs with a focus on risk management have seen strong performance. BAC and SQ are building digital banking capabilities to grow revenues.

- BAC is focused on digital banking, digital wealth management clients and is now rolling out digital shopping for home improvement and auto loans. Consumer NPLs also declined to $5.2 Bn, the lowest since 2008.
- JPM's loan portfolios are growing 8% and charge-offs have been in-line with expectations at 2.95%.
- ONDK delivered its first net profit with lowest ever quarterly provision rate of 6.4% as they see stabilizing credit performance. OnDeck is also focusing on its Software-as-a-Service partnership with JPM as a big driver of future revenue growth.
- ENVA reported its highest revenues at $240 Mn, had lower net charge-offs and is seeing improving credit performance and regulatory backdrop due to a weaker CFPB.
- SQ's is integrating its small business and consumer platforms to create an ecosystem for omnichannel commerce, which is paying off with 7 Mn users for its Cash app.

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FinTech & Non-Bank Lenders

Of the three sectors we look at, FinTech and Non-Bank is the most diverse: LC and ONDK are pure FinTech lenders, PYPL and SQ are payment processors who lend to existing customers as a secondary business, and OMF and ENVA are technology enabled non-bank lenders. FinTech and Non-Banks overall posted good revenue growth in the range of 7% to 25% and most expressed optimism about the exceedingly good credit environment we find ourselves in. ENVA, OMF and ONDK saw some of the lowest charge-offs and provisions, with LC indicating that expected charge-offs across grades would be up to 31 bps lower. OMF sees strong borrower performance as a result of their high-touch lending model, a very healthy borrower and potential positive cashflow for borrowers due to tax cuts.

LC indicated that rising interest rates would need to be passed on to borrowers. Rising interest rates would potentially push more borrowers to refinance their revolving credit card loans, a net positive for the sector.

Financial Highlights – Q4 2017

	Price		ROE (%)		Interest Income		Interest Expense		NIM (%)		Loss Reserve	
	3/5/18	YTD	2017 Q4	% Change	2017 Q4	% Change	2017 Q4	% Change	2017 Q4	Change	2017 Q4	% Change
ENVA	**$22.30**	47%	11.2	(28%)								
LC	**$3.83**	(7%)	-16.2	12%	$141	(15%)	$142	(14%)	0.5	0.4		
OMF	**$31.64**	22%	5.8	(21%)	$857	12%	$204	1%	67.1	6.3	$963	6%
ONDK	**$5.25**	(9%)	-4.4	(84%)	$87	9%	$11	13%	29.7	-0.2	$953	765%
PYPL	**$79.07**	7%	11.7	19%								
SQ	**$50.42**	45%	-9.2	(71%)								

	Outstanding Loans		Reserve as a % of Loans		Net Charge-Off Rate (%)	
	2017 Q4	% Change	2017 Q4	Change	2017 Q4	Change
ENVA						
LC	$3,294	-24%				
OMF	$14,800	10%	6.5%	-0.002	6.4	-1.1
ONDK	$953	-5%	3.6%	-0.019	12.9	-1.2
PYPL						
SQ						

Source: PeerIQ, Bloomberg, Capital IQ. All dollar values are in millions except Price; Change shows the value in % difference since Q4 2016.

Summary Insights

- LendingClub deployed its latest credit model in September and is seeing lower early delinquencies.
- OneMain and OnDeck saw strong credit performance and expect it to continue with tax cuts adding to consumer income.

- **LendingClub** delivered another quarter with record revenue. Originations were slightly below those in 3Q2017. LC deployed its latest credit model in September and is seeing lower early stage delinquencies.
- **OnDeck** delivered its first quarterly profit of $5 Mn and achieved lowest quarterly levels in 2017 for their provision rate at 6.4%, 15-plus-day delinquency ratio at 6.7% and their net charge-off rate at 12.9%.
- **Enova's** originations grew by 19% YoY and their loan book grew by 24% YoY, with net charge-offs slightly lower at 13.4%.
- **OneMain** grew its loan portfolio by 10% YoY to $14.8 Bn with a greater emphasis on secured lending. Net charge-offs were 6.4% and OMF expects 2018 charge-offs below 7%.

- PayPal sold its consumer loans portfolio to Synchrony and will focus on payments.
- Square is building an omnichannel ecosystem for borrowers and sellers to interact using its platform and apps.

- **PayPal** sold its consumer loan portfolio to Synchrony Financial for $6 Bn. PayPal's Credit arm will lend through Synchrony and the deal frees up $1 Bn in annual free cash-flow which PayPal will invest in higher yielding initiatives. PayPal's revenue grew by 26% YoY and continues to focus on its payments platform in the US and abroad.

- **Square** continues to pursue a Utah ILC banking charter as they look to bring lending capabilities typically offered by a bank in-house. Square Capital loans grew by 26% YoY in 4Q cumulatively to $2.5 Bn. Square Cash, an online wallet and payment transfer app, has 7 Mn users now and is expected to be a major revenue driver.

OnDeck

Ticker:	NYSE: ONDK
Close:	$5.25
Mkt Cap:	$388 Mn
4Q Revenue:	$88 Mn

Senior Management
Noah Breslow, CEO
Howard Katzenberg, CFO

Other Information
Headquarters: New York, NY
Year Founded: 2006
Employees: ~500

Major Shareholders

RRE Ventures	11.7%
EJF Capital	9.0%
Sapphire Ventures	7.7%
Inst. Venture Mgt. XII	5.5%
Inst. Venture Mgt. IX	5.5%

Highlights

OnDeck delivered its first quarterly net profit of $5 Mn, up $40 Mn YoY. Gross revenue increased 7% YoY to $88 Mn, which was slightly above expectations, and was driven primarily by higher interest income which was up 10% YoY. 4Q Opex was $38 Mn, only slightly higher than that in 3Q, and was down 28% YOY.

Originations grew in 4Q to $546 Mn, and for 2017, ONDK originated $2.1 Bn. Cost of funds increased to 6.5% in 4Q, up slightly over 3Q, driven by the Fed raising short-term rates. To counter this, ONDK will actively tighten its borrowing spreads by refinancing higher-cost securitizations. ONDK, once again, achieved record origination on the JPM program which recently entered a new four-year agreement. To-date, loans have only been available to a select portion of existing Chase business checking account customers and those will soon be expanded to Chase prospects and customers.

Credit Performance

Effective interest yield (EIY), was 35.6% in the quarter, up 202 bps YoY and up from 33.4% in 3Q. Management guided EIY to between 35% - 36% in 2018. Provision rate was 6.4% for the quarter and the 15-day delinquency rate was 6.7%. The provision rate was down substantially from 7.5% in 3Q and reflected the improved credit performance of recent originations, and strong collections' execution. Net charge-off rate was 12.9%, down from 16.9% in 3Q and reflected nearly $10 Mn of lower gross charge-offs, and over $5 Mn of recoveries. Management expects net charge-off rates to be between 13% to 15% going forward.

Outlook

Noah Breslow, CEO: "Looking ahead to 2018, we expect to drive double-digit loan growth due to strong customer demand, our disciplined risk management, and our focus on scaling responsibly. With improved credit performance and loan yields, our realigned cost structure and the secured funding base, our lending business is well-positioned to continue margin expansion and profit growth."

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LendingClub

Ticker:	NYSE: LC
Close:	$3.83
Mkt Cap:	$1.6 Bn
4Q Revenue:	$156.5 Mn

Senior Management

Scott Sanborn, CEO
Thomas Casey, CFO

Other Information

Headquarters: San Francisco
Year Founded: 2006
Employees: ~1,500

Major Shareholders

Shanda	23.4%
Vanguard	7.4%
Nikko Asset Mgt.	6.8%
Blackrock	5.3%
Deutsche Bank	4.5%

Highlights

LendingClub, once again, delivered its strongest revenue in company history, $156.5 Mn up 20% increase YOY, an up marginally QoQ. Total originations for the quarter were flat at $2.4 Bn. Revenue from Q4 securitization activities was up slightly to $2.8 Mn. Revenue growth was flat QoQ as interest income and transaction fee revenues were partially offset by fair value adjustments of $18.9 Mn. Fair value adjustments increased by $10.6 Mn QoQ reflecting charges related to a selloff in interest rates and the performance on the suspended F and G loans.

Credit Performance

The company announced a next-generation credit model using the latest machine learning techniques in 3Q, and has been deploying it in 4Q. LC sees better early delinquency performance using this model, but it is too early to say whether this model will meaningfully affect credit performance.

LendingClub indicated that expected charge-offs across grades would be up to 31 bps lower going forward, which should also improve expected portfolio returns.

Capital and Liquidity

LendingClub ended the quarter with $762 Mn of cash and equivalents and no debt. LendingClub held about $361 Mn in loans on the balance sheet, most of which will be used future securitization programs.

LendingClub completed 2 securitizations in 4Q, a prime and a near-prime deal totaling $580 Mn. Both deals were sponsored by LendingClub using loans originated on the LendingClub platform as part of their Prime and Near-Prime programs.

Shanda has increased its stake in LC stock by over 10% QoQ.

Outlook

Scott Sanborn, CEO: "As we enter 2018, our core business will continue to grow, and we will be focused on the operational efficiencies to drive our profitability, while making the right investments for our future. We are eager to execute and deliver."

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OneMain

Ticker:	NYSE: OMF
Close:	$31.64
Mkt Cap:	$4.3 Bn
4Q Revenue:	$568 Mn

Senior Management
Jay Levine, CEO
Scott Parker, CFO
David Schultz, Treasurer
CRO

Other Information
Headquarters: Evansville, IN
Year Founded: 1912
Employees: ~10,00

Major Shareholders

Fortress Investment	40.51%
FMR	9.0%
Vanguard	4.2%
Alliance Bernstein	3.0%
Wellington	2.9%

Highlights

OneMain beat revenue and earnings expectations this quarter driven by interest income that increased by 7% YoY. Revenue increased by 24% YoY to $568 Mn, and net income increased by 44% YoY to $39 Mn. 4Q Opex was $299 Mn, $26 Mn lower YoY.

Originations grew in 4Q to $3.1 Bn, up 34% YoY. On the funding side, OneMain issued $875 Mn in 5-year unsecured debt at 5.6%, $600 Mn in 1-year revolving direct auto ABS at 2.6%, and retired $700 Mn of 6.75% unsecured debt. On the liquidity side, the company had $5 Bn of unencumbered consumer loans and over $5 Bn of undrawn conduit capacity.

Fortress also recently sold its stake in OneMain to Apollo and Varde for between $1.5 – 2 Bn, pending regulatory approval.

Credit Performance

30 to 89-day delinquencies were 2.4%, 90+ delinquencies were 2.3% and net charge-offs were 6.4% for 4Q and 7% for 2018. Loan loss reserves increased by $9 Mn to $724 million, 4.9% of outstanding receivables. Management expects 2018 credit losses to come in below 7% but the loan loss reserves would increase based on asset growth.

Outlook

Jay Levine, CEO: **"**We expect 2018 to be a year in which OneMain drives our momentum and strategic priorities forward. We will stick to what we do best, providing our customers with the right products to improve their financial standing and flexibility. As we continue to build value for our customers, we will enhance the fundamental trends in our businesses that drive the long-term value creation for all shareholders."

Large Banks

Boosting ROE remains the theme across banks earnings. With trading revenues falling post-crisis, banks are looking at new channels for growth. Goldman Sachs' Marcus is a major new firm initiative, and Goldman is building Marcus into a digital bank.[1] Citigroup may soon follow suit, and Amazon looks likely to ink a partnership with JPM to offer checking accounts to its customers.

Banks have also been investing in technology to enable digital solutions and partnering with FinTechs on initiatives ranging from payment processing to lending. Bank of America, Wells Fargo and JP Morgan have been promoting Zelle as an easy way to transfer money between personal bank accounts for no fee. BBVA Compass launched its online Personal Express Loan which offers same-day funding and a fully digital application process. Santander and TD Auto Finance are joining forces with AutoGravity to speed up the car shopping and financing process by moving it online.

We expect large banks to acquire or partner with FinTechs to maintain competitiveness. Bank and FinTech combinations continue, with Goldman's acquisition of personal-finance startup Clarity Money and credit card startup Final.

We also expect banks with an unsecured lending capability to partner with "BigTech" firms to combine their deposits and risk management with captive customer channels and data. Bank of America is partnering with Amazon on small business lending. JPM is reportedly offering a co-branded checking account and personal card. See our analysis of AMZN's lending and banking ambitions here for more.

NIMs were slightly under pressure in 4Q as the curve flattened aggressively but should recover as the long-end has sold-off in 2018. Banks like Citigroup and Wells-Fargo with the largest consumer credit exposures and deposit bases continue to show the highest NIM. Morgan Stanley's focus on wealth management continues with $1 Tr in fee-paying accounts at the end of the year.

Consumer credit growth has been predominantly in mortgage and credit cards with banks being cautious extending auto credit, especially to subprime consumers.

Financial Highlights – Q4 2017

	Price		ROE (%)		Interest Income		Interest Expense		NIM (%)		Loss Reserve	
	3/5/18	YTD	2017 Q4	% Change	2017 Q4	% Change	2017 Q4	% Change	2017 Q4	Change	2017 Q4	% Change
BAC	**$32.13**	9%	6.8	0%	$11,215	18%	$3,604	40%	2.6	0.1	$10,393	(8%)
C	**$74.42**	0%	-3.9	(159%)	$15,759	9%	$4,536	38%	2.7	-0.2	$12,355	2%
GS	**$263.12**	3%	10.6	13%	$3,736	54%	$2,838	36%	0.3	-0.1	$509	-
JPM	**$115.06**	8%	9.9	(3%)	$12,655	20%	$3,966	46%	2.3	0.1	$13,604	(1%)
MS	**$55.49**	6%	9.5	17%	$2,586	38%	$1,591	62%	0.4	-0.1	$274	-
WFC	**$57.59**	(5%)	11.4	(3%)	$11,270	7%	$2,645	60%	2.9	0.0	$11,004	(4%)

Source: PeerIQ, Bloomberg, Capital IQ. All dollar values are in millions except Price; Change shows the value in % difference since Q4 2016.

[1] See our GS Teardown to learn more about GS lending strategy. Also see our timeline of GS M&A.

Summary Insights

- Bank ROE remains low and they continue to pivot to lending activities.
- JPM charge-offs are in line with expectations, while Citi charge-offs increased by 7%.
- Revenue growth at MS was driven by the Wealth and Investment Management.
- Wells Fargo saw growth in its loan portfolio.

- Banks stocks are up modestly in 2018 with only WFC lower year-to-date as it struggles with the regulatory fallout.

- **JP Morgan's** Consumer and Community Banking business generated $2.6 Bn in net income and an impressive ROE of 19% vs. 10% for the firm overall.
  - Core loan portfolio grew by 8% and deposits grew by 7% YoY.
  - JPM added $200 Mn in card reserves driven by lending growth. Net charge-offs on credit cards were in line with expectations at 2.95%.
  - JPM sees the auto industry on a solid footing and released $35 Mn in reserves held for auto loans.

- **Citibank's** North American consumer banking business delivered net income of $0.8 Bn.
  - Net charge-offs increased by 7% YoY and loan loss reserves increased by $151 Mn, reflecting volume growth and portfolio seasoning.
  - Citi expects $80 Mn increase in interest revenue for every 25bp hike in the Fed Funds rate.

- **Morgan Stanley's** focus on wealth management continues and the division delivered a 25.5% pre-tax margin in 2017.
  - Revenue growth was driven by the Wealth and Investment Management businesses.
  - Lending under Wealth Management grew to $68 Bn in 2017 with $41 Bn under Securities-Based Lending. MS is ramping up mortgage lending as well.
  - Areas for technology investment are digital banking and advisory, and cash management, lending and deposit platforms.

- **Wells Fargo** reported weaker than expected earnings this quarter with continued pressure on the bank due to legal issues.
  - Loan growth returned this quarter as loans grew by $5 Bn QoQ but are still down by $11 Bn YoY. The drop in loan volumes came from auto loans and junior mortgage liens.
  - Credit losses (including mortgage) remain low at 31 bps, and NPLs dropped to 1% of loans outstanding.
  - Auto loans outstanding were down $2.1 Bn QoQ due to tighter underwriting, and WFC expects a continued decline in outstanding loans through late 2018.
  - Outstanding credit card balances increased by $1.7 Bn and the bank's deposit base grew to its highest ever at $1.31 Tr.

- **Bank of America's** Consumer Banking and Wealth Management experienced loan growth of 9% QoQ and deposit growth of 8% QoQ.
  - Consumer charge-offs increased slightly to 68 bps and NPLs decreased by 18 bps YoY to 1.14%.

  - Average loans and leases increased by 9% YoY to $276 Bn, driven by growth in residential mortgage, credit card and auto lending.
  - BAC has 35 Mn active digital banking users. 23% of all deposits transactions were on mobile devices and BAC processed 23.1 Mn online P2P payments in 2017.

- **Goldman Sachs** beat earnings expectations driven by the Investing and Lending business, but trading revenue was down by 34% YoY.
  - Goldman is building Marcus into a digital bank and expects to generate double-digit ROE through the credit cycle on this business, with revenues of $2 Bn over 3 years.
  - The recent expansion of "lending activities positions the firm with $2 Bn run-rate net interest income as we start 2018.". Lending includes secured and unsecured lending (personal loans, home improvement, fix-and-flip, GS Select, etc.)
  - GS consolidated Lending and Deposits under the Marcus brand. Marcus loans grew to $2.3 Bn and online deposits grew to $17 Bn, part of Goldman's total deposit base of $124 Bn. GS launched securities-based lending and extended $3 Bn in collateralized loans in 2017.
  - Marty Chavez: "Marcus is a huge and important and exciting area of growth for us and one of the core pillars of our growth plan."

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Card Issuers

Card issuers generally saw the US consumer to be in a good place, with a potential for income gains with tax reforms. Credit normalization continues, and card issuers are increasing provisions to cover any uptick in losses, although provisions are growing slower than income is.

Financial Highlights – Q4 2017

	Price		ROE (%)		Interest Income		Interest Expense		NIM (%)		Loss Reserve	
	3/5/18	YTD	2017 Q4	% Change	2017 Q4	% Change	2017 Q4	% Change	2017 Q4	Change	2017 Q4	% Change
AXP	**$96.66**	(3%)	13.5	(47%)	$2,316	27%	$580	40%	8.7	0.0	$833	33%
COF	**$97.90**	(2%)	3.9	(52%)	$6,173	10%	$791	41%	6.9	0.2	$7,502	15%
DFS	**$77.07**	0%	19.3	(12%)	$2,549	13%	$436	19%	9.7	0.4	$2,621	21%
SYF	**$36.23**	(6%)	13.6	(19%)	$4,233	8%	$375	18%	17.9	0.2	$5,574	28%

	Outstanding Loans		Reserve as a % of Loans		Net Charge-Off Rate (%)	
	2017 Q4	% Change	2017 Q4	Change	2017 Q4	Change
AXP	$76,006	14%	1.1%	0.002	1.8	0.2
COF	$255,444	4%	0.8%	0.000	2.7	0.5
DFS	$84,248	9%	0.8%	0.001	2.9	0.5
SYF	$81,947	7%	1.7%	0.002	5.8	1.2

Source: PeerIQ, Bloomberg, Capital IQ. All dollar values are in millions except Price; Change shows the value in % difference since Q4 2016.

Summary Insights

- Overall credit card issuers see the US consumer in a good place and expect an income boost from the tax reform.
- Credit normalization continues with loan loss provisions increasing at most issuers.
- Discover's loan portfolio grew by 14% YoY, while Capital One's loan portfolio only grew by 3% YoY.
- Synchrony purchased PayPal's consumer loan portfolio and will now issue loans under the PayPal Credit brand as well.

- **American Express** has a new CEO, Steve Squeri. AmEx saw loan growth of 14% YoY and charge-offs came in at 1.8%, 20bp higher YoY. Loan loss provisions increased 33% YoY to $833 Mn driven by loan growth and portfolio seasoning. AmEx's deposit funding costs go up by between 35-70% of the increase in the Fed Funds rate and rising interest rates have put pressure on overall funding costs.

- **Capital One's** earnings disappointed once again due to impacts from the tax reform act and other one-time items. The credit card portfolio grew by 8% YoY, but the consumer loan portfolio only grew by 4%. The net charge-off rate increased slightly to 2.9% and provisions increased to 2.95%. Capital One sees the US consumer in a very good place but also sees higher competition for the customer going forward.

- **Discover's** loan portfolio grew by 9% YoY, driven in part by 12% growth in student loans – a record $1.6 Bn in new loans. Discover is now the second largest student lender in the country. Net charge-offs rose by 54 bps YoY to 2.7% driven by supply driven credit normalization along with the seasoning of loans. Credit card net charge-off rate rose by 56 bps YoY and private student loan net charge-off rate rose by 3 bps YoY. Personal loan net charge-off rate increased by 92 bps YoY to 3.62%. Discover expects growth to slow due to tightening credit standards. Discover is seeing pressure on borrower performance due to personal loans which are indebting borrowers further,

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instead of consolidating their debt. Although Discover is profitable on personal loans, they will keep an eye on loan performance.

- **Synchrony** purchased PayPal's $6Bn consumer loan portfolio and will now issue loans under the PayPal Credit brand as well. The partnership will focus on the consumer value proposition, merchant differentiation and world-class digital customer experience to support ongoing engagement within the digital payments channel. Synchrony's net charge-off rate was 5.8% driven by credit normalization. The loan loss provision grew 111 bps to 6.8% of outstanding receivables, but Synchrony expects the charge-off rate to average between 5.5-5.8% going forward.

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