SVB Financial Group Q2 2019 Financial Highlights

Record Quarterly Earnings and Profitability

July 25, 2019

To our Stakeholders:

We are pleased to report outstanding second quarter results, with **Earnings per Share of $6.08, Net Income of $318 million and an industry-leading Return on Equity of 23 percent**. This performance is the result of healthy markets for our clients and continued effective execution against our strategy. Our results reflect exceptional warrant and investment gains; robust balance sheet growth; healthy net interest income growth, despite net interest margin pressures; solid core fee income; stable credit and well-managed expenses.

The power of the SVB platform to drive growth

Our continued strong performance demonstrates the power of SVB's place at the center of the innovation ecosystem and the ways in which our strategy and values reinforce the foundation we've laid for long-term growth. Our long-term commitment to innovators and investors enables us to understand their businesses, give advice and solve their problems to improve the probability of their success. The networks and deep relationships we've cultivated globally over decades allow us to make meaningful connections for our clients and provide value well beyond the capabilities of a typical bank. Our strategy has enabled us to outperform peers over the long term and we believe it will contribute to continued outperformance in the future.

Q2: Focus on what matters

Several key themes capture what we believe is most important about the quarter and the market environment:

1. Healthy markets and strong execution on our strategy setting the stage for continued growth;
2. Strong balance sheet growth driving net interest income growth, with NIM headwinds;
3. Our proactive strategy to manage the impact of a declining rate environment;
4. The power of our liquidity franchise as the engine for NII growth;
5. Stable credit with an improving risk profile;
6. Levers to drive long-term profitability; and
7. Continued execution on our strategy through investment in growth and operating leverage.

Healthy markets and strong execution set the stage for continued growth

Venture Capital investment retained its momentum in the second quarter with $33 billion invested in more than 3,000 companies. Our new client acquisition remained strong, with more than 1,200 core commercial clients added during the quarter, continuing the robust client acquisition trend of the last five years and resulting in net client growth of 63 percent since 2015. Our access to and ability to work with clients at these earliest stages, and to keep them as they grow, remains a key part of our strategy.

A flood of long-awaited **IPOs helped drive Q2 exits of $138 billion**, the highest quarterly VC-backed exit values in history. IPOs made up 95 percent of this activity and 69 percent of the venture backed companies that went public during the quarter were SVB Clients. While big technology IPOs got most of the headlines, our Life Science and Healthcare clients accounted for nearly half of these IPOs. Our clients' IPO activity during the quarter resulted in exceptional warrant and investment gains of $77 million.

VC fundraising rebounded somewhat in the second quarter and remains on a healthy trajectory relative to the past five years, with $21 billion raised so far in 2019. The current robust exit activity is likely to support continued fundraising and investment, as a portion of those cash flows is reallocated back into new investments. Strong VC numbers tell only part of the story, however, given the increasing amounts of capital for investment available from PE investors, hedge funds, corporate VCs, family offices and traditional asset managers.

US private equity investment improved in the second quarter following a slow Q1, with first half deal values of approximately $300 billion, on pace with the first six months of 2018. PE fundraising showed even greater improvement, surpassing the first six months of 2018 with $102 billion raised year to date.

This healthy market activity provided the right environment for our strong performance. Against this backdrop, we continued to execute on our strategy of enhancing client experience, improving employee enablement, enhancing risk management, and driving revenues and scalable, long-term growth.

Strong balance sheet growth drives NII growth, with NIM headwinds

We saw superior balance sheet growth in the second quarter driven by exceptional client liquidity, with robust increases in both loans and client funds. These increases helped drive healthy NII growth, although market rates on investments and deposits, as well as competition for loans, impacted overall yields and provided headwinds to net interest margin.

Assets

Average loans grew by 3.6 percent to $29.4 billion, driven primarily by capital call lending, which now constitutes 50 percent of the loan portfolio, and by record growth in our Private Bank lending. While commitments to our technology and life science clients grew slightly, lending remained flat as those clients continued to enjoy ample market liquidity.

Average fixed income investment securities increased by 4.7 percent to $23.1 billion, although yields were slightly lower at 2.57 percent. New purchases totaled $2.6 billion at 2.79 percent, versus maturity yields of 2.25 percent. As a result of changes in market rates, we have lowered our assumptions on new purchase yields for the rest of 2019 by 40 basis points. We expect average tax-effected purchase yields between 2.30 and 2.40 percent and overall investment portfolio yields will remain flat or increase slightly for the remainder of 2019.

Client funds

Average total client funds increased by 4 percent to $142.6 billion, primarily as a result of healthy client funding and exit markets for our technology and life science clients.

- **Average on-balance sheet deposits increased by 6.5 percent to $53.0 billion,** primarily driven by funds from our technology and life science clients, and partially offset by lower balances from our Asia clients.
- **Average interest-bearing deposit growth of 29 percent to $14.8 billion** exceeded our growth expectations, due to the success of new products related to our deposit growth initiative. Interest bearing deposits now constitute 28 percent of total deposits (up from 23 percent in Q1). Our total deposit costs increased by 13 basis points due to strong interest-bearing deposit growth during the quarter but remained very low at just 36 basis points.

We are increasing our full-year deposit outlook to growth in the low double digits, as a result of our better-than-forecast deposit growth and the momentum created by our deposit growth initiatives. We expect the majority of 2019 deposit growth to occur in interest-bearing products.

Net Interest Income and NIM

Net interest income increased by 3.2 percent to $532.3 million. This increase was driven by higher interest income from higher loan, fixed-income investment and cash balances, which were partially offset by a $19.2 million increase in interest expense related to our successful deposit growth initiatives.

Net Interest margin declined by 13 basis points to 3.68 percent. This was due to several factors:

- Higher deposit costs of $19.2 million (13 bps) related to our successful deposit initiative.
- An increase of 2 basis points in total loan yields, driven by an increase in loan fee yields due to higher loan prepayments. This was offset by lower gross loan yields related to competition and growth from our lower-yielding Private Equity and Private Bank portfolios.

We are reducing our full year 2019 outlooks for NII and NIM due to strong interest-bearing deposit growth and our expectations for lower fixed-income reinvestment rates, continued intense pricing competition for loans and deposits, and growth in lower-yielding Private Equity loans.

- **We expect Net Interest Income growth in the low teens**, versus our prior outlook of the mid-teens.
- **We expect NIM of 3.60% to 3.70%**, a decline of 10 basis points from our prior outlook of 3.70% to 3.80%. This reflects our expectations for lower gross loan yields and higher full-year deposit costs of between 30 and 40 basis points.
- If we were to see the two 25 basis point Fed Funds decreases in July and September implied by the forward curve, we would expect to revise our NII expectations for 2019 down to the low double digits and NIM expectations to between 3.50 % and 3.60%.

Noninterest Expense

Noninterest Expense increased by 2.1 percent to $243.2 million. This increase was driven by higher compensation and benefits expense primarily from higher salaries and wages related to merit increases, as well as an increase in the number of average full-time equivalent employees. For the remainder of 2019, we plan to continue investing in our initiatives, which you will see reflected mainly in higher professional services costs. We expect to end the year at the lower end of our expense outlook range.

We are proactively managing the impact of a declining rate environment

We continue to work toward our goal of managing the impact of rate decreases on our net interest income sensitivity to less than 10% in a 100 basis point shock scenario. We have a variety of strategies underlying this effort, but the primary ones are interest rate swaps, continued extension of our fixed-income securities portfolio, and adapting our deposit pricing to market rates.

Taking into account our expectations for the impact of our balance sheet strategies through the rest of 2019, we are forecasting a $40 to $50 million annualized, pre-tax reduction in NII for each 25 basis point Fed Funds decrease, which equates to approximately 2 percent of our net interest income. This estimate assumes deposit beta between 50 and 70 percent and continued deposit growth primarily in interest-bearing accounts.

Our actual results will be impacted by a variety of factors, including future demand for interest-bearing deposit products; the impact of competition on loan yields; and whether we expect to continue growing on-balance sheet deposits, which depends in large part on the velocity of deposit flows, particularly continued distributions by Private Equity firms.

Power of our liquidity franchise provides the engine for Net Interest Income growth

Our balance sheet strategy remains our most powerful tool for driving net interest income growth in a declining rate environment. Our deep relationships with clients generate a continuous stream of low-cost client liquidity, providing ample funding for growth in high-quality loans and investments and cash to manage our day-to-day liquidity. We have demonstrated our ability to offer clients the right mix of products that meet their needs while enabling us to drive funding on or off the balance sheet to optimize our deposit mix, and we will use this approach to manage to our long-term ROE and EPS growth targets.

Stable credit with an improving risk profile

Credit quality, remained solid in the second quarter, with strong underlying metrics and no change in our outlook for 2019. Our credit performance reflects continued growth in high-quality loan categories, such as Private Equity and Private Bank, as well as the gradual improvement of our risk profile over the years, as early stage loans, which tend to have higher loss rates, have become a much smaller portion of our overall mix.

Our provision for credit losses was $24 million in the second quarter, a decrease from the first quarter, and in line with recent quarters. Our allowance for loan losses remained stable at 1.03%, reflecting an increase in performing reserves and a decrease in reserves for non-performing loans due primarily to the overall growth in loans during the quarter and the continued change in mix of our overall loan portfolio. Charge-offs of $26 million were partially offset by strong recoveries of $10 million. Non-performing loans decreased by 29 percent to $97 million, following the successful resolution of several large non-performing loans, including full repayment of our two largest non-performing loans.

Levers to drive profitable growth in a changing rate environment

Looking forward, we believe we can continue to drive profitable growth and operating efficiency in a declining rate environment.

- We continue to invest in geographic expansion, domestically and globally; digital enhancements to improve client acquisition and retention as well as the client experience; and diversification of our business into complementary areas that increase our value to clients, as with our acquisition of SVB Leerink.
- We have the ability, through products and pricing, to reprice and reposition excess deposits on or off the balance sheet over time.
- Our capital and liquidity remain very strong and we continue to accrete capital, which gives us the power to invest as necessary in our business or return capital to investors, under the right circumstances.
- Finally, we continue investing in our business to take advantage of the growth opportunities we see and drive growth, efficiency and scalability over the long term.

Continued execution on our strategy through investment in growth and operating leverage

To that end, we remain focused on our efforts to drive revenue growth and transform our business while making it more efficient through investments in client experience, employee engagement, risk management, scalability and revenue growth.

Many of the investments we're making will improve our operating leverage and efficiency over the long term, and we are already seeing some of those benefits from initiatives that are well underway, such as our client and loan onboarding.

Our efforts to drive revenue growth through expanded product offerings, improved penetration and extension of our platform globally are also gaining traction. We recently unveiled a new Private Bank/Wealth Management client portal that gives our Private clients access to their accounts, advisors and financial services from any device. At the same time, we've been developing new lending solutions for these clients customized to their needs and liquidity profiles. In a similar vein, we rolled out our new SVB Gateway initiative to early stage clients. The SVB Gateway gives clients a single digital entry point to all of their accounts and the entire SVB platform and, over the next year, we expect to phase the gateway in for all clients. The Private Bank portal and SVB Gateway are both examples that will enable us to grow by serving clients at scale, improving and deepening engagement, while achieving the optimal balance of self-service and high-touch.

While we expect to continue investing throughout the coming rate cycle while keeping expense growth well managed, we also have the flexibility to manage the timing and impact of our investments to reduce our expense growth trajectory, should the environment worsen notably.

We believe our investments in growth and scalability now will enable us to capture market share and build our market position around the world in the years to come.

Q2 summary: Continued strong performance, positive outlook and long-term growth catalysts

Our strong performance in the second quarter, healthy markets and exceptional client liquidity make us optimistic about our business and our growth prospects. While declining rates are a concern, they are a near-term concern. Our long-term growth strategy has never hinged on interest rates. Instead, it depends on our continued ability to prove our value to innovators and their investors, to capture the lion's share of new companies year after year, and to forge deep and lasting bonds with our clients as they grow. This not only leads to better product penetration and larger, more profitable relationships, but to a continuous cycle of successful exits and liquidity events, which, in turn, drives more new company formation and continues to expand the opportunity. We believe our continued focus on our clients' success; and our ongoing investments in clients, employees, products and revenue growth will enable us to make the most of this cycle, to get even better and more efficient at serving our clients, and to further strengthen our position as the bank of the global innovation economy.



Greg Becker
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