LIVE OAK BANCSHARES

CFO Highlights: Q4 2019

January 23, 2020

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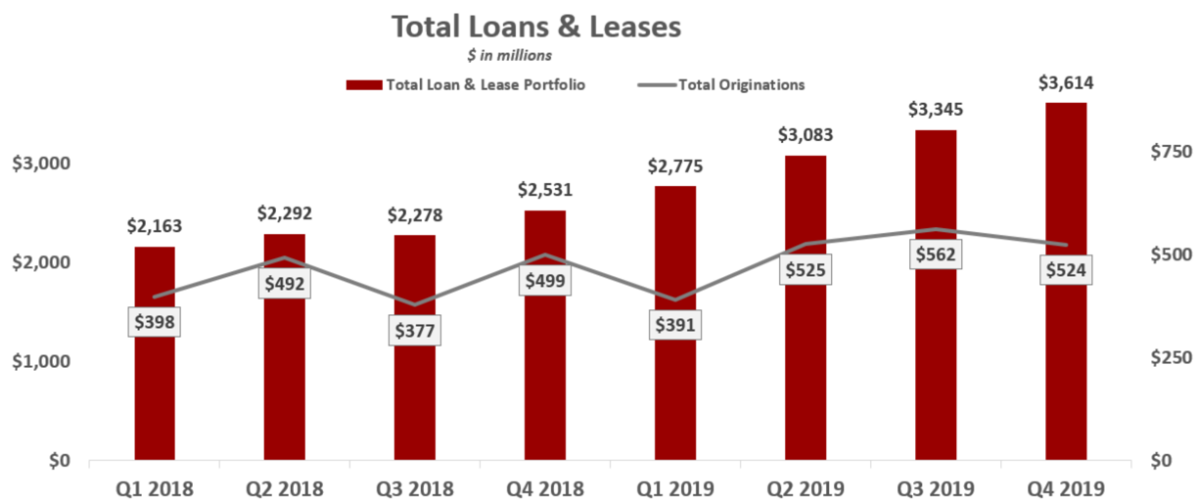
Our net income in the fourth quarter of 2019 totaled $6.8 million, or $0.17 per diluted share. For the full year of 2019, our net income totaled $18.0 million or $0.44 per diluted share. The year demonstrated the strength of our strategic pivot with sustained growth and improvement in balance sheet levels, recurring revenues, and loan and deposit originations.

SUCCESS OF REVISED BALANCE SHEET STRATEGY

Our performance for the full year illustrated the continued success of our business model pivot intended to maximize long-term profitability. Our total portfolio of loans and leases held for investment and held for sale of $3.61 billion increased by $1.08 billion, or 42.8%, over the same quarter a year ago and by $268.7 million, or 8.0%, compared to the prior quarter. Our recurring revenue, consisting of net interest income and servicing revenue, rose to $44.7 million for the fourth quarter of 2019, which comprised 75.2% of our total revenue for the quarter. The meaningful increase in recurring revenue was driven by our consistent focus on loan retention during 2019. For the year, $972.2 million of guaranteed loans became eligible for sale and $340.4 million were sold, a 65.0% retention rate and in line with our expectations for 2019. Further enhancing earnings stability, the strategic decision to sell fewer loans has contributed to significant reductions in our historically volatile servicing asset and related valuations.

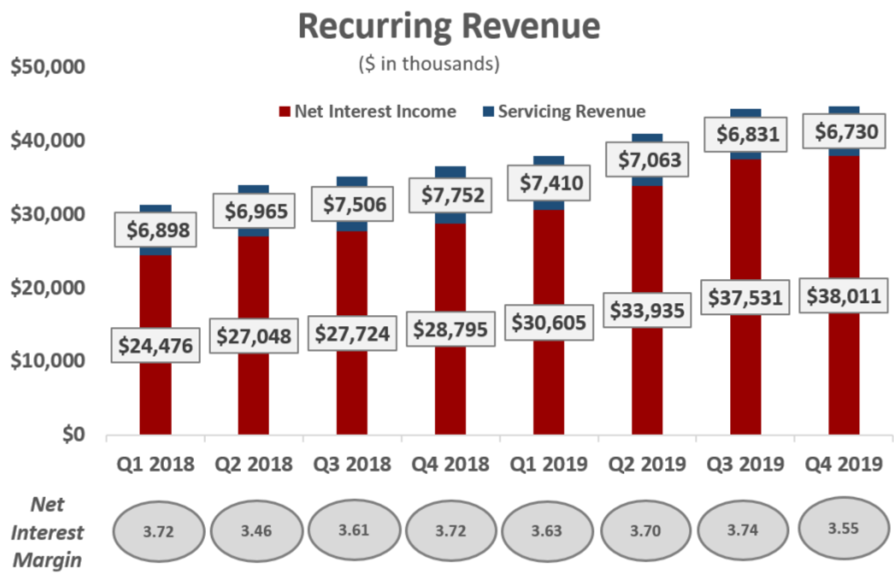
LOAN & LEASE PORTFOLIO



Loan originations for 2019 increased to $2.00 billion from $1.77 billion in 2018 with originations of $523.7 million during the fourth quarter of 2019. The success of many of our legacy and emerging industry verticals along with the investment in experienced SBA lending generalists is evidenced by the 13.4% growth in loan and lease originations from 2018 to 2019.

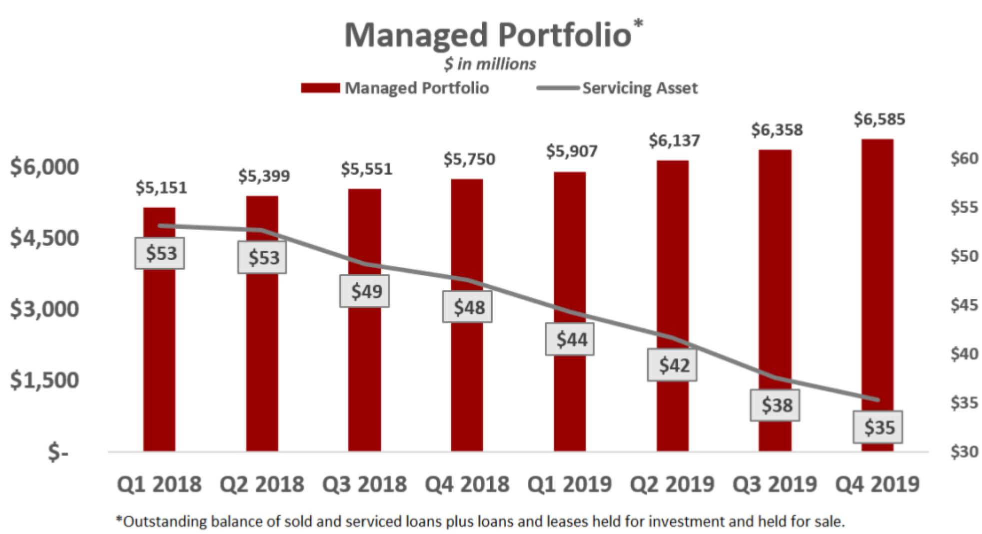
SUSTAINED RECURRING REVENUE

The recurring revenue streams of net interest income and servicing revenue grew to $44.7 million for the fourth quarter of 2019, a 22.4% increase compared to the fourth quarter of 2018. Recurring revenue streams for the full year of 2019 totaled $168.1 million compared to $137.2 million for the full year of 2018, a 22.6% increase.



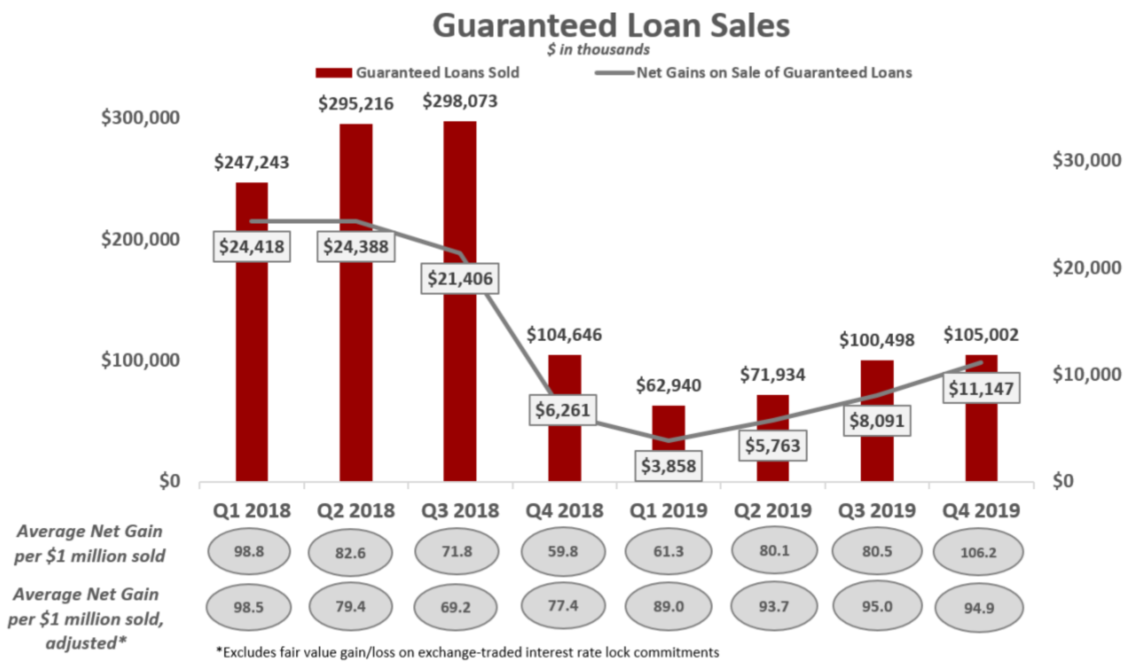
Net interest income for the year 2019 increased to $140.1 million, a 29.7% increase over net interest income during the year 2018 attributable to higher interest earning asset levels. During the fourth quarter of 2019, net interest income increased to $38.0 million, a 32.0% increase over the fourth quarter of 2018. On a linked quarter basis, the net interest margin declined 19 basis points to 3.55%, reflecting the impact of variable rate loans repricing at a faster pace than interest-bearing liabilities, following a total of 50 basis points of rate cuts by the Federal Reserve during the third quarter which became effective in the fourth quarter. As a result of this repricing timing, the yield on interest earnings assets decreased 31-basis points to 5.77% while the cost of interest-bearing liabilities decreased 12-basis points during the fourth quarter. Servicing revenue on our sold and serviced loan portfolio amounted to $6.7 million during the fourth quarter of 2019, a decrease of 13.2% over the fourth quarter of 2018 and 1.5% over the linked quarter, as the amortization of the serviced portfolio outpaced the addition of new loans to that portfolio driven by our strategic decision to sell fewer loans. Servicing revenue for the year 2019 decreased 3.7% to $28.0 million compared to the year 2018.

The managed portfolio, consisting of the outstanding balance of sold and serviced loans plus loans and leases held for investment and held for sale, at December 31, 2019, totaled $6.6 billion, a 14.5% increase over its level a year ago.



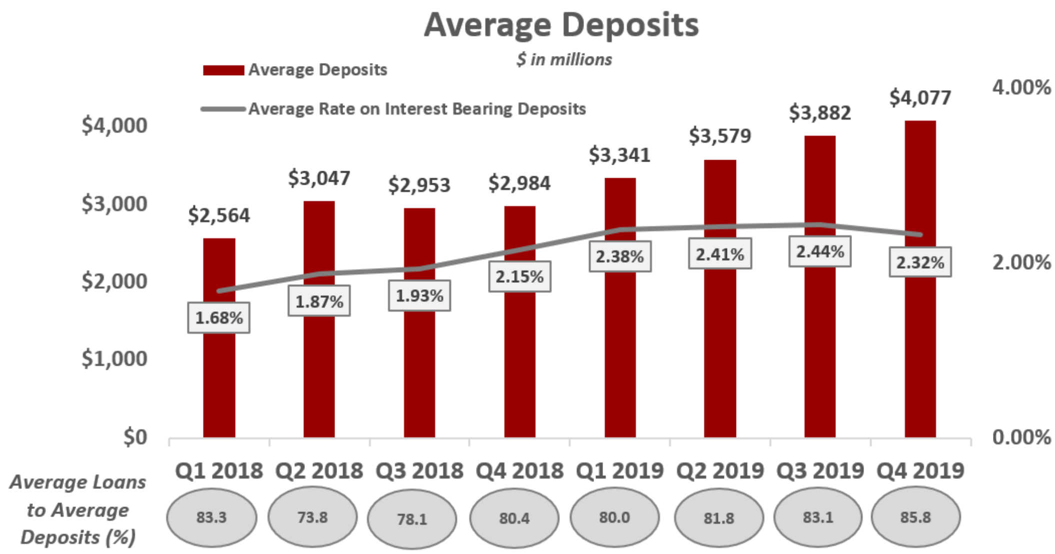
At the end of the fourth quarter of 2019, the carrying value of the servicing asset declined 25.8% over the past year to $35.4 million, representing 6.6% of our total equity, a downward trend from 9.7% a year ago. The net loss arising from the revaluation of the loan servicing asset amounted to $1.3 million in the fourth quarter of 2019 compared to net losses of $627 thousand in the fourth quarter of 2018 and $859 thousand in the linked quarter and was primarily attributable to amortization of the serviced portfolio.

SECONDARY MARKET SALES



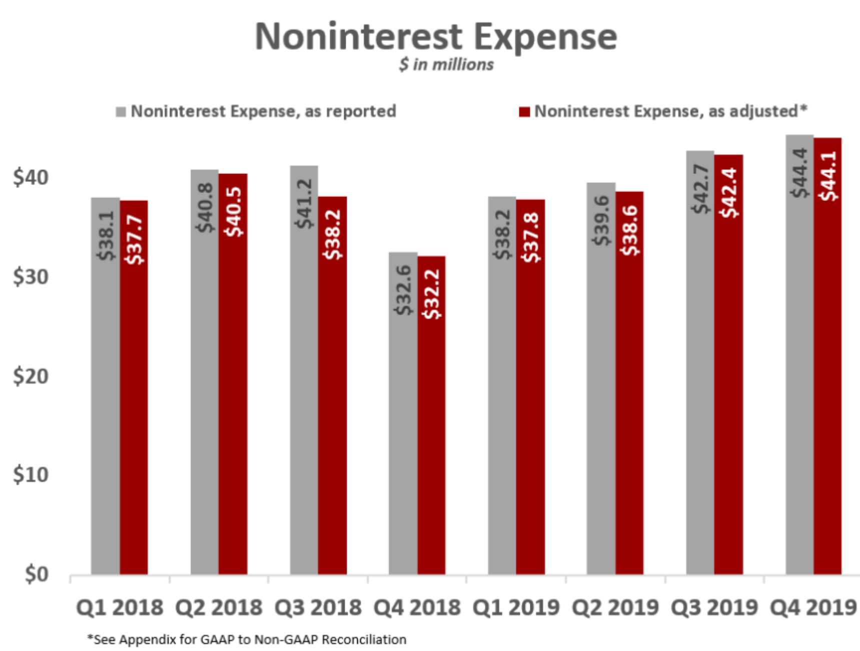
Loan sale volumes in the fourth quarter of 2019 were similar to the prior year as we continued to execute our strategy of loan retention. However, gain on sale revenue from the sale of guaranteed loans for the fourth quarter of 2019 increased $4.9 million to $11.1 million compared to the fourth quarter of 2018 reflecting continued strength of the secondary market. The average net gain per $1 million sold, excluding the fair value adjustment for exchange-traded interest rate lock commitments of $1.2 million, was $94.9 thousand for the fourth quarter of 2019 compared to $77.4 thousand for the fourth quarter of 2018 and $95.0 thousand for the third quarter of 2019.

FUNDING OUR STRATEGY



Our deposit funding model is successfully supporting the strategic repositioning to hold more loans on balance sheet. Deposit balances grew $1.08 billion, or 34.3%, to $4.23 billion at December 31, 2019, compared to the prior year end. The average balance of deposits increased $195.6 million, or 5.0%, during the fourth quarter of 2019 compared to the linked quarter. We continue to operate what we believe is an efficient branchless model for deposit gathering, at an incremental cost of 12 basis points for the full year of 2019, which allows us to offer competitive rates. The average rate on interest bearing deposits decreased by 12 basis points from the prior quarter.

SCALING THE PLATFORM



Our non-GAAP noninterest expense, as adjusted, totaled $44.1 million for the fourth quarter of 2019, an increase of $1.7 million, or 3.9%, over the prior quarter. The main contributors to the increase in noninterest expense from the prior quarter are increases of $1.9 million in FDIC insurance and $1.4 million in salaries and benefits as we continued to invest in our workforce to support the Company's growth and initiatives. These increases were offset by reductions in expenses associated with professional services, data processing, and loan related expenses compared to the prior quarter. For the year, our non-GAAP noninterest expense totaled $162.9 million in 2019, a $14.3 million increase from the full year 2018. Of note, incentive compensation for 2019 increased $6.6 million over 2018 due to the Company's reversal of accrued incentive compensation in the fourth quarter of 2018. The year-to-year increase is largely attributable to the continued investments in people, facilities, and initiatives that complement the Company's long-term strategic plan covering core banking activities and innovative solutions for the industry. Compared to the $14.3 million previously mentioned increase in noninterest expense, net interest income in 2019 increased $32.0 million from the prior year demonstrating the operating leverage of the business. See Appendix for reconciliation of non-GAAP noninterest expense, as adjusted, to noninterest expense, as reported.

CREDIT QUALITY

Our net charge-offs during the fourth quarter of 2019 declined to $905 thousand compared to $2.3 million in the prior quarter. Net charge-offs as a percentage of average held for investment loans and leases, annualized, for the fourth quarter of 2019 was 0.14% compared to 0.39% for the third quarter of 2019. Net charge-offs for the year ended December 31, 2019 totaled $3.8 million compared to $4.8 million for the prior year, or 0.17% and 0.31% of average held for investment loans and leases, respectively. The unguaranteed exposure of nonperforming loans and leases decreased to $17.9 million, or 0.91% of total unguaranteed exposure, during the fourth quarter of 2019 compared to $19.8 million, or 1.08%, for the prior quarter.

Provision expense of $6.2 million decreased $952 thousand compared to the previous quarter which was primarily attributable to growth in the loan and lease portfolio combined with ongoing changes in net charge-offs and criticized and classified loans and leases. The ratio of allowance for loans and lease losses to loans and leases held for investment was 1.82% as of December 31, 2019, compared to 1.76% for the prior quarter.

The Company's methodology for estimating credit losses changed on January 1, 2020, upon adoption of the current expected credit losses methodology (CECL) for estimating allowances for credit losses.

INCOME TAX EXPENSE

We incurred a net income tax expense of $2.1 million, which equates to an effective rate of 23.4%, in the fourth quarter of 2019 compared to a net income tax benefit of $3.0 million in the fourth quarter of 2018 and a net income tax expense of $2.4 million for the linked quarter, resulting in effective tax rates of (40.2)% and 37.8%, respectively. Our effective tax rate is heavily influenced by our leasing volume of renewable energy assets which generate investment tax credits.

APPENDIX
GAAP TO NON-GAAP RECONCILIATION

	Three Months Ended							
	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	Q3 2019	Q4 2019
Noninterest expense, as reported	$ 38,072	$ 40,830	$ 41,244	$ 32,558	$ 38,201	$ 39,576	$ 42,737	$ 44,410
Stock based compensation expense	(352)	(357)	(360)	(360)	(352)	(357)	(360)	(360)
Impairment expense on goodwill other intangible, net	-	-	(2,680)	-	-	-	-	-
Renewable energy tax credit investment impairment	-	-	-	-	-	(602)	-	-
Noninterest Expense, as adjusted	$ 37,720	$ 40,473	$ 38,204	$ 32,198	$ 37,849	$ 38,617	$ 42,377	$ 44,050
Less: Reversal of Incentive Compensation	-	-	-	4,457	-	-	-	-
Noninterest expense, as modified	$ 37,720	$ 40,473	$ 38,204	$ 36,655	$ 37,849	$ 38,617	$ 42,377	$ 44,050

Deposits Direct Cost of Funds

	YTD December 31, 2019 (Dollars in Thousands)
Interest	$ 87,897
Personnel	2,123
Travel & Entertainment	33
Fraud Expense	199
Marketing Expense	961
Technology Expense	894
Other Expense	441
Total Direct Deposit Expenses	**$ 92,548**
Average Deposit Balances for Twelve Months Ended December 31, 2019	**3,684,761**

	Cost of Funds (YTD December 31, 2019 expense)
Interest	2.30%
Personnel	0.06%
Travel & Entertainment	0.00%
Fraud Expense	0.00%
Marketing Expense	0.03%
Technology Expense	0.02%
Other Expense	0.01%
Cost of Funds % including Deposits Department	**2.43%**
Direct Noninterest Cost of Funds	0.12%

FORWARD-LOOKING STATEMENTS

Information in this document may contain “forward-looking statements” within the Private Securities Litigation Reform Act of 1995. These statements generally relate to our financial condition, results of operations, plans, objectives, future performance or business and usually can be identified by the use of forward-looking terminology such as “may,” “will,” “would,” “should,” “could,” “expect,” “anticipate,” “estimate,” “believe,” “plan,” “intend,” “project,” “goals,” “outlook,” or “continue,” or the negative thereof or other variations thereof or comparable terminology. These statements represent our judgment concerning the future and are subject to business, economic and other risks and uncertainties, both known and unknown. These statements are based on current expectations, estimates and projections about our business, management’s beliefs and assumptions made by management. These statements are not guarantees of our future performance and involve certain risks and uncertainties, which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in the forward-looking statements. These risks, uncertainties and assumptions include, without limitation:

- deterioration in the financial condition of borrowers resulting in significant increases in our loan and lease losses and provisions for those losses and other adverse impacts to results of operations and financial condition;
- changes in SBA rules, regulations and loan products, including specifically the Section 7(a) program, changes in SBA standard operating procedures or changes to Live Oak Banking Company’s status as an SBA Preferred Lender;
- changes in rules, regulations or procedures for other government loan programs, including those of the United States Department of Agriculture;
- changes in interest rates that affect the level and composition of deposits, loan demand and the values of loan collateral, securities, and interest sensitive assets and liabilities;
- the failure of assumptions underlying the establishment of reserves for possible loan and lease losses;
- changes in loan underwriting, credit review or loss reserve policies associated with economic conditions, examination conclusions, or regulatory developments;
- a reduction in or the termination of our ability to use the technology-based platform that is critical to the success of our business model, including a failure in or a breach of our operational or security systems or those of its third party service providers;
- changes in financial market conditions, either internationally, nationally or locally in areas in which we conduct operations, including reductions in rates of business formation and growth, demand for our products and services, commercial and residential real estate development and prices, premiums paid in the secondary market for the sale of loans, and valuation of servicing rights;
- changes in accounting principles, policies, and guidelines applicable to bank holding companies and banking;
- fluctuations in markets for equity, fixed-income, commercial paper and other securities, which could affect availability, market liquidity levels, and pricing;
- the effects of competition from other commercial banks, non-bank lenders, consumer finance companies, credit unions, securities brokerage firms, insurance companies, money market and mutual funds, and other financial institutions operating in our market area and elsewhere, including institutions operating regionally, nationally and internationally, together with such competitors offering banking products and services by mail, telephone and the Internet;
- our ability to attract and retain key personnel;
- changes in governmental monetary and fiscal policies as well as other legislative and regulatory changes, including with respect to SBA lending programs and investment tax credits;
- changes in political and economic conditions;
- the impact of heightened regulatory scrutiny of financial products and services, primarily led by the Consumer Financial Protection Bureau;
- our ability to comply with any requirements imposed on us by our regulators, and the potential negative consequences that may result;
- operational, compliance and other factors, including conditions in local areas in which we conduct business such as inclement weather or a reduction in the availability of services or products for which loan proceeds will be used, that could prevent or delay closing and funding loans before they can be sold in the secondary market;
- the effect of any mergers, acquisitions or other transactions, to which we may from time to time be a party, including management’s ability to successfully integrate any businesses that we acquire;
- other risk factors listed from time to time in reports that we file with the SEC, including in our Annual Report on Form 10-K; and
- our success at managing the risks involved in the foregoing.

Given these risks, uncertainties and other factors, you should not place undue reliance on these forward-looking statements. Moreover, these forward-looking statements speak only as of the date they are made and based only on information actually known to us at the time. We undertake no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise. Except as otherwise disclosed, forward-looking statements do not reflect: (i) the effect of any acquisitions, divestitures or similar transactions that have not been previously disclosed; (ii) any changes in laws, regulations or regulatory interpretations; or (iii) any change in current dividend or repurchase strategies, in each case after the date as of which such statements are made.