

Xencor Inc
Form 10-Q
August 07, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2017

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number: 001-36182

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Xencor, Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware 20-1622502
(State or Other Jurisdiction of Incorporation (I.R.S. Employer Identification No.)

or Organization)

111 West Lemon Avenue, Monrovia, CA 91016
(Address of Principal Executive Offices) (Zip Code)

(626) 305-5900

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer a smaller reporting company or an emerging growth company. See definitions of "large accelerated filer", "accelerated filer" "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company Emerging growth company

If an emerging growth company, indicate by checkmark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13 (a) of the Exchange Act.

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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act of 1934). Yes No

Indicate the number of shares of each of the issuer's classes of common stock, as of the latest practicable date:

| Class | Outstanding at August 1, 2017 |
|--------------------------------|-------------------------------|
| Common stock, \$0.01 par value | 46,926,340 |

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Xencor, Inc.

Quarterly Report on FORM 10-Q for the quarter ended June 30, 2017

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In this report, unless otherwise stated or the context otherwise indicates, references to "Xencor," "the Company," "we," "us," "our" and similar references refer to Xencor, Inc. The Xencor logo is a registered trademark of Xencor, Inc. This report also contains registered marks, trademarks and trade names of other companies. All other trademarks, registered marks and trade names appearing in this report are the property of their respective holders.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of federal securities laws. Forward-looking statements include statements that may relate to our plans, objectives, goals, strategies, future events, future revenues or performance, capital expenditures, financing needs and other information that is not historical information. Many of these statements appear, in particular, under the headings “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations”. Forward-looking statements can often be identified by the use of terminology such as “subject to”, “believe”, “anticipate”, “plan”, “expect”, “intend”, “estimate”, “project”, “may”, “will”, “should”, “would”, “could”, “can”, the negatives thereof, variations thereon and similar expressions, discussions of strategy.

All forward-looking statements, including, without limitation, our examination of historical operating trends, are based upon our current expectations and various assumptions. We believe there is a reasonable basis for our expectations and beliefs, but they are inherently uncertain. We may not realize our expectations, and our beliefs may not prove correct. Actual results could differ materially from those described or implied by such forward-looking statements. The following uncertainties and factors, among others (including those set forth under “Risk Factors”), could affect future performance and cause actual results to differ materially from those matters expressed in or implied by forward-looking statements:

- our plans to research, develop and commercialize our product candidates;
- our ongoing and planned clinical trials;
- the timing of and our ability to obtain and maintain regulatory approvals for our product candidates;
- our estimates regarding expenses, future revenue, capital requirements and needs for additional financing;
- our ability to identify additional products or product candidates with significant commercial potential that are consistent with our business objectives;
- the rate and degree of market acceptance and clinical utility of our products;
- the capabilities and strategy of our suppliers and vendors including key manufacturers of our clinical drug supplies;
- significant competition in our industry;

- costs of litigation and the failure to successfully defend lawsuits and other claims against us;
- our partners' ability to advance drug candidates into, and successfully complete, clinical trials;
- our ability to receive research funding and achieve anticipated milestones under our collaborations;
- our intellectual property position;
- loss or retirement of key members of management;
- costs of compliance and our failure to comply with new and existing governmental regulations;
- failure to successfully execute our growth strategy, including any delays in our planned future growth; and
- our failure to maintain effective internal controls.

The factors, risks and uncertainties referred to above and others are more fully described under the heading "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2016 and subsequent Quarterly Reports on Form 10-Q. Forward-looking statements should be regarded solely as our current plans, estimates and beliefs. You should not place undue reliance on forward-looking statements. We cannot guarantee future results, events, levels of activity, performance or achievements. We do not undertake and specifically decline any obligation to update, republish or revise forward-looking statements to reflect future events or circumstances or to reflect the occurrences of unanticipated events.

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

Xencor, Inc.

Balance Sheets

(In thousands, except share amounts)

| | June 30, 2017 (unaudited) | December 31, 2016 |
|--|---------------------------------|----------------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$ 11,220 | \$ 14,528 |
| Marketable securities | 177,269 | 115,608 |
| Accounts receivable | 14,876 | 8,616 |
| Prepaid expenses and other current assets | 7,617 | 2,901 |
| Total current assets | 210,982 | 141,653 |
| Property and equipment, net | 3,861 | 3,105 |
| Patents, licenses, and other intangible assets, net | 10,865 | 10,362 |
| Marketable securities - long term | 190,242 | 273,340 |
| Other assets | 214 | 103 |
| Total assets | \$ 416,164 | \$ 428,563 |
| Liabilities and stockholders' equity | | |
| Current liabilities | | |
| Accounts payable | \$ 7,379 | \$ 3,880 |
| Accrued expenses | 3,984 | 6,692 |
| Current portion of deferred rent | — | 128 |
| Current portion of deferred revenue | 95,613 | 95,521 |
| Income taxes | 455 | 65 |
| Total current liabilities | 107,431 | 106,286 |
| Deferred rent, less current portion | 614 | 397 |
| Deferred revenue, less current portion | 6,754 | 7,926 |
| Total liabilities | 114,799 | 114,609 |
| Commitments and contingencies | | |
| Stockholders' equity | | |
| Preferred stock, \$0.01 par value: 10,000,000 authorized shares; -0- issued and outstanding shares at June 30, 2017 and December 31, 2016 | — | — |
| Common stock, \$0.01 par value: 200,000,000 authorized shares at June 30, 2017 and December 31, 2016; 46,854,762 issued and outstanding at June 30, 2017 and | 468 | 466 |

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46,567,978 issued and outstanding at December 31, 2016

| | | |
|--|------------|------------|
| Additional paid-in capital | 562,017 | 553,290 |
| Accumulated other comprehensive loss | (1,240) | (1,441) |
| Accumulated deficit | (259,880) | (238,361) |
| Total stockholders' equity | 301,365 | 313,954 |
| Total liabilities and stockholders' equity | \$ 416,164 | \$ 428,563 |

See accompanying notes.

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Xencor, Inc.

Statements of Comprehensive Income (Loss)

(unaudited)

(In thousands, except share and per share data)

| | Three Months Ended | | Six Months Ended | |
|---|--------------------|------------|------------------|------------|
| | June 30, | | June 30, | |
| | 2017 | 2016 | 2017 | 2016 |
| Revenue | | | | |
| Collaborations, licenses and milestones | \$ 13,340 | \$ 66,007 | \$ 17,681 | \$ 73,259 |
| Operating expenses | | | | |
| Research and development | 16,919 | 14,408 | 31,967 | 24,443 |
| General and administrative | 4,091 | 3,043 | 8,903 | 6,993 |
| Total operating expenses | 21,010 | 17,451 | 40,870 | 31,436 |
| Income (loss) from operations | (7,670) | 48,556 | (23,189) | 41,823 |
| Other income (expenses) | | | | |
| Interest income | 1,038 | 368 | 2,095 | 726 |
| Interest expense | (3) | (10) | (5) | (37) |
| Other income | 30 | — | 30 | 4 |
| Total other income, net | 1,065 | 358 | 2,120 | 693 |
| Income (loss) before income tax expense | (6,605) | 48,914 | (21,069) | 42,516 |
| Income tax expense | 280 | 1,749 | 450 | 1,749 |
| Net income (loss) | (6,885) | 47,165 | (21,519) | 40,767 |
| Other comprehensive income (loss) | | | | |
| Net unrealized gain (loss) on marketable securities | (44) | 113 | 201 | 732 |
| Comprehensive income (loss) | \$ (6,929) | \$ 47,278 | \$ (21,318) | \$ 41,499 |
| Basic net income (loss) per common share | \$ (0.15) | \$ 1.16 | \$ \$ (0.46) | \$ 1.00 |
| Diluted net income (loss) per common share | \$ (0.15) | \$ 1.13 | \$ \$ (0.46) | \$ 0.98 |
| Basic weighted average common shares outstanding | 46,767,759 | 40,800,586 | 46,683,744 | 40,703,688 |
| Diluted weighted average common shares outstanding | 46,767,759 | 41,738,460 | 46,683,744 | 41,701,262 |

See accompanying notes.

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Xencor, Inc.

Statement of Stockholders' Equity

(in thousands, except share data)

| Stockholders' Equity | Common Stock Shares | Common Stock Amount | Additional Paid in-Capital | Accumulated Other Comprehensive Loss | Accumulated Deficit | Total Stockholders' Equity |
|--|------------------------|------------------------|----------------------------------|---|------------------------|----------------------------------|
| Balance, December 31, 2016 as originally reported | 46,567,978 | \$ 466 | \$ 552,889 | \$ (1,441) | \$ (237,960) | \$ 313,954 |
| Adoption of ASU 2016-09 (see note 1) | — | — | 401 | — | (401) | — |
| Balance December 31, 2016 as restated | 46,567,978 | 466 | 553,290 | (1,441) | (238,361) | 313,954 |
| Issuance of common stock upon exercise and vesting of stock awards | 252,278 | 2 | 1,678 | — | — | 1,680 |
| Issuance of common stock under the Employee Stock Purchase Plan | 34,506 | — | 442 | — | — | 442 |
| Comprehensive income (loss) | — | — | — | 201 | (21,519) | (21,318) |
| Stock-based compensation | — | — | 6,607 | — | — | 6,607 |
| Balance, June 30, 2017 (unaudited) | 46,854,762 | \$ 468 | \$ 562,017 | \$ (1,240) | \$ (259,880) | \$ 301,365 |

See accompanying notes.

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Xencor, Inc.

Statements of Cash Flows

(unaudited)

(in thousands)

| | Six Months Ended | |
|--|------------------|-----------|
| | June 30, | |
| | 2017 | 2016 |
| Cash flows from operating activities | | |
| Net income (loss) | \$ (21,519) | \$ 40,767 |
| Adjustments to reconcile net income (loss) to net cash used in operating activities: | | |
| Depreciation and amortization | 864 | 628 |
| Amortization of premium on marketable securities | 1,356 | 876 |
| Stock-based compensation | 6,607 | 3,993 |
| Abandonment of capitalized intangible assets | 225 | 45 |
| Gain on sale of marketable securities available for sale | — | (3) |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (6,260) | (150,310) |
| Interest receivable | (144) | 160 |
| Prepaid expenses and other assets | (4,727) | (1,031) |
| Accounts payable | 3,500 | 1,294 |
| Accrued expenses | (2,708) | (357) |
| Income taxes | 390 | 1,781 |
| Deferred rent | (12) | (53) |
| Deferred revenue | (1,080) | 78,541 |
| Net cash used in operating activities | (23,508) | (23,669) |
| Cash flows from investing activities | | |
| Purchase of marketable securities | (33,440) | (7,123) |
| Purchase of intangible assets | (1,092) | (761) |
| Purchase of property and equipment | (1,256) | (493) |
| Proceeds from sale and maturities of marketable securities | 53,866 | 26,660 |
| Net cash provided by investing activities | 18,078 | 18,283 |
| Cash flows from financing activities | | |
| Proceeds from issuance of common stock upon exercise of stock awards | 1,680 | 447 |
| Proceeds from issuance of common stock under the Employee Stock Purchase Plan | 442 | 226 |
| Net cash provided by financing activities | 2,122 | 673 |
| Net decrease in cash and cash equivalents | (3,308) | (4,713) |
| Cash and cash equivalents, beginning of period | 14,528 | 12,590 |
| Cash and cash equivalents, end of period | \$ 11,220 | \$ 7,877 |

Supplemental disclosure of cash flow information

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Cash paid during the period for:

| | | |
|---|--------|--------|
| Interest | \$ 5 | \$ — |
| Income taxes | \$ 60 | \$ — |
| Supplemental disclosures of non-cash investing activities | | |
| Unrealized gain on marketable securities, net of tax | \$ 201 | \$ 732 |

See accompanying notes.

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Xencor, Inc.

Notes to Financial Statements

(unaudited)

June 30, 2017

1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited interim financial statements for Xencor, Inc. (the Company) have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information. The financial statements include all adjustments (consisting only of normal recurring adjustments) that the management of the Company believes are necessary for a fair presentation of the periods presented. The preparation of interim financial statements requires the use of management's estimates and assumptions that affect reported amounts of assets and liabilities at the date of the interim financial statements and the reported revenues and expenditures during the reported periods. These interim financial results are not necessarily indicative of the results expected for the full fiscal year or for any subsequent interim period.

The accompanying unaudited interim financial statements and related notes should be read in conjunction with the audited financial statements and notes thereto included in the Company's 2016 Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC) on March 1, 2017.

Marketable Securities

The Company has an investment policy that includes guidelines on acceptable investment securities, minimum credit quality, maturity parameters and concentration and diversification. The Company invests its excess cash primarily in marketable securities issued by investment grade institutions.

The Company considers its marketable securities to be available-for-sale. These assets are carried at fair value and the unrealized gains and losses are included in accumulated other comprehensive income (loss). Accrued interest on marketable securities is included in marketable securities. If a decline in the value of a marketable security in the Company's investment portfolio is deemed to be other-than-temporary, the Company writes down the security to its current fair value and recognizes a loss as a charge against income. The Company reviews its portfolio of marketable securities, using both quantitative and qualitative factors, to determine if declines in fair value below cost are other-than-temporary.

Recent Accounting Pronouncements

Pronouncements Adopted in 2017

In March 2016, the FASB issued ASU No. 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting, which amends the current stock compensation guidance. The amendments simplify the accounting for the taxes related to stock based compensation, including adjustments to how excess tax benefits and a company's payments for tax withholdings should be classified. In addition, the standard allows an entity-wide accounting policy election to either estimate the number of awards that are expected to vest, as currently required, or account for forfeitures of awards in the period that they occur. We adopted the new standard on January 1, 2017 and established an accounting policy election to account for forfeitures when they occur. We applied the modified retrospective approach which resulted in a cumulative-effect adjustment of a decrease of \$0.4 million to retained earnings and additional paid-in capital. The adoption will result in periodic adjustments in the recognition of stock compensation expense associated with forfeitures in the period in which they occur. The remaining aspects of adopting ASU 2016-09 did not have a material impact on our financial statement position or results from operations.

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Pronouncements Not Yet Effective

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, as a new Topic, Accounting Standards Codification Topic 606 (ASU 2014-09). The new revenue recognition standard provides a five-step analysis of transactions to determine when and how revenue is recognized. The core principle is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In March 2016, the FASB issued ASU No. 2016-08, Revenue from Contracts with Customer Topic 606, Principal versus Agent Considerations, which clarifies the implementation guidance on principal versus agent considerations. In April 2016, the FASB issued ASU 2016-10, Revenue from Contracts with Customers Topic 606, Identifying Performance Obligations and Licensing, which clarifies certain aspects of identifying performance obligations and licensing implementation guidance. In May 2016, the FASB issued ASU 2016-12, Revenue from Contracts with Customers Topic 606, Narrow-Scope Improvements and Practical Expedients, related to disclosures of remaining performance obligations, as well as other amendments to guidance on collectability, non-cash consideration and the presentation of sales and other similar taxes collected from customers. In December 2016, the FASB issued ASU No. 2016-20, Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers, which amends certain narrow aspects of the guidance issued in ASU 2014-09 including guidance related to the disclosure of remaining performance obligations and prior-period performance obligations, as well as other amendments to the guidance on loan guarantee fees, contract costs, refund liabilities, advertising costs and the clarification of certain examples. These ASUs are effective for public entities for interim and annual reporting periods beginning after December 15, 2017, including interim periods within that year, which for us is the period beginning January 1, 2018.

The Company has reviewed the new standard and its current and prior revenue arrangements and determined that there are several provisions in the new standard that will affect its revenue recognition related to such arrangements. Many of the Company's collaboration arrangements include licensing or intellectual property for rights to certain of its technologies or drug candidates. Additionally, many of these arrangements include upfront payments and potential future payments from partners for future development, regulatory and sales milestones and royalties on sales of approved products. The new standard makes changes to both revenue recognition for licensing of intellectual property and potential milestone revenue for future payments.

We believe that these provisions will have the following impact on contract revenues from our collaboration and license agreements:

- 1) changes in the model for licensing of intellectual property that are functional and distinct performance obligations that may result in a timing difference of revenue recognition. While revenue from these contracts was recognized over the contract term under the revenue recognition guidance in place at the contract's inception, revenue recognition under the new guidance may be recognized at a point in time. This could change the period of time that we have recognized revenue related to the licensing of our intellectual property.
- 2) milestone payments that are directly linked to events under the Company's control will result in variable consideration when determining the contract price under the new guidance and may be recognized earlier when it is probable that the milestone will be achieved without a significant future reversal of cumulative revenue expected. Under current accounting guidance the Company has applied the milestone method of accounting for recognizing such revenue or contingent payments. The new standard may change the period in which such revenue from these arrangements is recognized.

The Company is still in the process of completing its review and has not concluded on the impact on the revenue recognized in periods prior to the required adoption date, January 1, 2018. The Company expects to adopt the full retrospective method of implementation which will require the Company to restate its revenue and earnings for the

2016 and 2017 periods. Management will adopt the new standard effective January 1, 2018 and will continue to monitor additional changes, clarifications or interpretations being undertaken by the FASB which may impact management's implementation approach.

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, which amends the guidance on reporting credit losses for assets

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held at amortized cost basis and available for sale debt securities. Credit losses relating to available-for-sale debt securities will be recorded through an allowance for credit losses rather than as a direct write-down to the security. Credit losses on available-for-sale securities will be required when the amortized cost is below the fair market value. The amendment is effective for fiscal years beginning after December 15, 2019 including interim periods within those fiscal years. We will apply the standard's provision as a cumulative effect adjustment to retained earnings as of the beginning of the first effective reporting period. We do not expect the adoption to have a material impact on our results of operations or financial position.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, which addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. The standard clarifies when cash receipts and cash payments have aspects of more than one class of cash flows and cannot be separated, classification will depend on the predominant source or use. The amendment is effective for fiscal years beginning after December 15, 2017 with early adoption permitted. We continue to review the requirements of this standard and any potential impact it may have on our cash flow statement.

In March 2017, the FASB issued ASU No. 2017-08, Receivables – Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities, which amends the guidance on the amortization period of premiums on certain purchased callable debt securities by shortening the amortization period of premiums to the earliest call date. The amendment affects all entities that hold investments in callable debt securities that have an amortized cost basis in excess of the amount that is repayable by the issuer at the earliest call date. The amendment is effective for fiscal years beginning after December 31, 2018 with early adoption permitted. The Company will review the requirements of the standard but does not anticipate it will have a significant impact on our financial statements.

In May 2017, the FASB issued ASU No. 2017-09, Compensation – Stock Compensation (Topic 718): Scope of Modification Accounting. The standard applies when a company changes the terms of a stock compensation award previously granted to an employee where modification accounting applies. According to the standard, modification accounting is not required if (1) the fair value of the modified award (or the award's calculated value or intrinsic value as appropriate) is the same as the value immediately prior to its modification, (2) the vesting conditions of the modified award are the same as the vesting conditions of the award immediately prior to its modification; and (3) the award's classification as an equity or liability is the same after the modification as it was immediately prior to its modification. The new standard is effective for annual periods beginning after December 15, 2017 including interim periods within those years. The Company will review the requirements of the standard but does not anticipate it will have a significant impact on our financial statements.

There have been no other material changes to the significant accounting policies previously disclosed in the Company's 2016 Annual Report on Form 10-K.

2. Fair Value of Financial Instruments

Financial instruments included in the financial statements include cash equivalents, marketable securities, accounts receivable, accounts payable and accrued expenses. Marketable securities and cash equivalents are carried at fair value. The fair value of the other financial instruments closely approximates their fair value due to their short maturities.

The Company accounts for recurring and non-recurring fair value measurements in accordance with FASB Accounting Standards Codification (ASC) 820, Fair Value Measurements and Disclosures. ASC 820 defines fair

value, establishes a fair value hierarchy for assets and liabilities measured at fair value, and requires expanded disclosure about fair value measurements. The ASC 820 hierarchy ranks the quality of reliable inputs, or assumptions, used in the determination of fair value and requires assets and liabilities carried at fair value to be classified and disclosed in one of the following three categories:

Level 1—Fair Value is determined by using unadjusted quoted prices that are available in active markets for identical assets or liabilities.

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Level 2—Fair Value is determined by using inputs other than Level 1 quoted prices that are directly or indirectly observable. Inputs can include quoted prices for similar assets or liabilities in active markets or quoted prices for identical assets or liabilities in markets that are not active. Related inputs can also include those used in valuation or other pricing models, such as interest rates and yield curves that can be corroborated by observable market data.

Level 3—Fair value is determined by inputs that are unobservable and not corroborated by market data. Use of these inputs involves significant and subjective judgments to be made by the reporting entity –e.g. determining an appropriate discount factor for illiquidity associated with a given security.

The Company measures the fair value of financial assets using the highest level of inputs that are reasonably available as of the measurement date. The assets recorded at fair value are classified within the hierarchy as follows for the periods reported (in thousands):

| | June 30, 2017 | | | December 31, 2016 | | |
|-----------------------|---------------------|-----------|------------|---------------------|-----------|------------|
| | Total Fair Value | Level 1 | Level 2 | Total Fair Value | Level 1 | Level 2 |
| Money Market Funds | \$ 10,063 | \$ 10,063 | \$ — | \$ 12,137 | \$ 12,137 | \$ — |
| Corporate Securities | 154,098 | — | 154,098 | 181,483 | — | 181,483 |
| Government Securities | 213,413 | — | 213,413 | 207,465 | — | 207,465 |
| | \$ 377,574 | \$ 10,063 | \$ 367,511 | \$ 401,085 | \$ 12,137 | \$ 388,948 |

Our policy is to record transfers of assets between Level 1 and Level 2 at their fair values as of the end of each reporting period, consistent with the date of the determination of fair value. During the three and six months ended June 30, 2017, there were no transfers between Level 1 and Level 2. The Company does not have any Level 3 assets or liabilities.

3. Net Income (Loss) Per Share

We compute net income (loss) per common share by dividing the net income (loss) attributable to common stockholders by the weighted-average number of common shares outstanding during the period without consideration of common stock equivalents. Diluted loss per share is computed by dividing the net income (loss) attributable to common stockholders by the weighted-average number of common stock equivalents outstanding for the period. The treasury stock method is used to determine the dilutive effect of the Company's stock option grants. Potentially dilutive securities consisting of stock issuable under options and our 2013 Employee Stock Purchase Plan (ESPP) are not included in the diluted net loss per common share calculation where the inclusion of such shares would have had an

antidilutive effect.

Basic and diluted net income (loss) per common share is computed as follows (in thousands except share and per share data):

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| | Three Months Ended June 30, 2017 | | Six Months Ended June 30, 2017 | |
|---|--|------------|--------------------------------------|------------|
| | 2016 | 2016 | 2016 | 2016 |
| | (in thousands, except share and per share data) | | | |
| Numerator: | | | | |
| Net income (loss) attributable to common stockholders | \$ (6,885) | \$ 47,165 | \$ (21,519) | \$ 40,767 |
| Denominator: | | | | |
| Weighted-average common shares outstanding, basic | 46,767,759 | 40,800,586 | 46,683,744 | 40,703,688 |
| Dilutive effect of stock options | — | 937,874 | — | 997,574 |
| Weighted average common shares outstanding, diluted | 46,767,759 | 41,738,460 | 46,683,744 | 41,701,262 |
| Net income (loss) per share, basic | \$ (0.15) | \$ 1.16 | \$ (0.46) | \$ 1.00 |
| Net income (loss) per share, diluted | \$ (0.15) | \$ 1.13 | \$ (0.46) | \$ 0.98 |

For the three and six months ended June 30, 2017 all outstanding potentially dilutive securities have been excluded from the calculation of diluted net loss per common share as the effect of including such securities would have been antidilutive. For the three and six months ended June 30, 2016 there were no shares from the Company's employee stock purchase plan that had a dilutive effect on shares outstanding.

4. Comprehensive Income (Loss)

Comprehensive income (loss) is comprised of net income (loss) and other comprehensive income (loss). For the three and six months ended June 30, 2017 and 2016, the only component of other comprehensive income (loss) is net unrealized gains (loss) on marketable securities. There were no material reclassifications out of accumulated other comprehensive income (loss) during the three and six months ended June 30, 2017 and 2016.

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5. Marketable Securities

The Company's marketable securities held as of June 30, 2017 and December 31, 2016 are summarized below:

| June 30, 2017 (in thousands) | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|-------------------------------------|-------------------|------------------------------|-------------------------------|------------|
| Money Market Funds | \$ 10,063 | \$ — | \$ — | \$ 10,063 |
| Corporate Securities | 154,634 | 2 | (538) | 154,098 |
| Government Securities | 214,108 | 7 | (702) | 213,413 |
| | \$ 378,805 | \$ 9 | \$ (1,240) | \$ 377,574 |
| Reported as | | | | |
| Cash and cash equivalents | | | | \$ 10,063 |
| Marketable securities | | | | 367,511 |
| Total investments | | | | \$ 377,574 |
| December 31, 2016 (in thousands) | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| Money Market Funds | \$ 12,137 | \$ — | \$ — | \$ 12,137 |
| Corporate Securities | 182,394 | 6 | (917) | 181,483 |
| Government Securities | 207,986 | 44 | (565) | 207,465 |
| | \$ 402,517 | \$ 50 | \$ (1,482) | \$ 401,085 |
| Reported as | | | | |
| Cash and cash equivalents | | | | \$ 12,137 |
| Marketable securities | | | | 388,948 |
| Total investments | | | | \$ 401,085 |

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The maturities of the Company's marketable securities are as follows:

| June 30, 2017 (in thousands) | Amortized Cost | Estimated Fair Value |
|---------------------------------|-------------------|-------------------------|
| Mature in one year or less | \$ 177,542 | \$ 177,269 |
| Mature after one year | 191,200 | 190,242 |
| | \$ 368,742 | \$ 367,511 |

| December 31, 2016 (in thousands) | Amortized Cost | Estimated Fair Value |
|-------------------------------------|-------------------|-------------------------|
| Mature in one year or less | \$ 115,748 | \$ 115,608 |
| Mature after one year | 274,632 | 273,340 |
| | \$ 390,380 | \$ 388,948 |

The unrealized losses on available-for-sale investments and their related fair values as of June 30, 2017 and December 31, 2016 are as follows:

| June 30, 2017 (in thousands) | Less than 12 months | | 12 months or greater | |
|---------------------------------|---------------------|-------------------|----------------------|-------------------|
| | Fair value | Unrealized losses | Fair value | Unrealized losses |
| Corporate Securities | \$ 92,398 | \$ (155) | \$ 53,027 | \$ (382) |
| Government Securities | 75,803 | (120) | 122,269 | (582) |
| | \$ 168,201 | \$ (275) | \$ 175,296 | \$ (964) |

| December 31, 2016 (in thousands) | Less than 12 months | | 12 months or greater | |
|-------------------------------------|---------------------|-------------------|----------------------|-------------------|
| | Fair value | Unrealized losses | Fair value | Unrealized losses |
| Corporate Securities | \$ 82,215 | \$ (133) | \$ 88,990 | \$ (784) |
| Government Securities | 17,573 | (16) | 149,694 | (549) |
| | \$ 99,787 | \$ (149) | \$ 238,684 | \$ (1,333) |

The unrealized losses from the listed securities are due to a change in the interest rate environment and not a change in the credit quality of the securities.

6. Stock Based Compensation

Our Board of Directors and the requisite stockholders previously approved the 2010 Equity Incentive Plan (the 2010 Plan). In October 2013, our Board of Directors approved the 2013 Equity Incentive Plan (the 2013 Plan) and in November 2013 our stockholders approved the 2013 Plan. The 2013 Plan became effective as of December 3, 2013, the date of the Company's initial public offering (IPO). As of December 2, 2013, we suspended the 2010 Plan and no additional awards may be granted under the 2010 Plan. Any shares of common stock covered by awards granted under

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the 2010 Plan that terminate after December 2, 2013 by expiration, forfeiture, cancellation or other means without the issuance of such shares will be added to the 2013 Plan reserve.

As of June 30, 2017, the total number of shares of common stock available for issuance under the 2013 Plan is 8,637,790, which includes 2,684,456 of common stock that were available for issuance under the 2010 Plan as of the effective date of the 2013 Plan. Unless otherwise determined by the Board, beginning January 1, 2014, and continuing until the expiration of the 2013 Plan, the total number of shares of common stock available for issuance under the 2013 Plan will automatically increase annually on January 1 of each year by 4% of the total number of issued and outstanding shares of common stock as of December 31 of the immediately preceding year. Pursuant to approval by our board on January 1, 2017, the total number of shares of common stock available for issuance under the 2013 Plan was increased by 1,862,719 shares. As of June 30, 2017, a total of 4,790,350 options had been issued under the 2013 Plan.

In November 2013, our Board of Directors and stockholders approved the 2013 Employee Stock Purchase Plan (ESPP), which became effective as of December 5, 2013. We have reserved a total of 581,286 shares of common stock for issuance under the ESPP. Unless otherwise determined by our Board, beginning on January 1, 2014, and continuing until the expiration of the ESPP, the total number of shares of common stock available for issuance under the ESPP will automatically increase annually on January 1 by the lesser of (i) 1% of the total number of issued and outstanding shares of common stock as of December 31 of the immediately preceding year, or (ii) 621,814 shares of common stock. Pursuant to approval by our board, there was no increase in the number of authorized shares in the ESPP in 2017. As of June 30, 2017, we have issued a total of 255,992 shares of common stock under the ESPP.

Total employee, director and non-employee stock-based compensation expense recognized for the three and six months ended June 30, 2017 are as follows (in thousands):

| | Three Months Ended | | Six Months Ended | |
|----------------------------|--------------------|----------|------------------|----------|
| | June 30, 2017 | 2016 | June 30, 2017 | 2016 |
| General and administrative | \$ 1,416 | \$ 874 | \$ 2,884 | \$ 1,826 |
| Research and development | 2,032 | 1,159 | 3,723 | 2,167 |
| | \$ 3,448 | \$ 2,033 | \$ 6,607 | \$ 3,993 |

The following table summarizes option activity under our stock plans and related information:

| | Number of | Weighted Average Exercise | Weighted Average Remaining | Aggregate |
|--|-----------|---------------------------------|----------------------------------|-----------|
|--|-----------|---------------------------------|----------------------------------|-----------|

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| | Shares subject to outstanding options | Price (Per Share) | Contractual Term (in years) | Intrinsic Value (in thousands) |
|-------------------------------|---|-------------------------|-----------------------------------|---|
| Balances at December 31, 2016 | 4,045,801 | \$ 11.95 | 7.82 | |
| Options granted | 1,356,100 | \$ 22.65 | | |
| Options forfeited | (76,606) | \$ 15.60 | | |
| Options exercised | (252,278) | \$ 6.66 | | |
| Balance at June 30, 2017 | 5,073,017 | \$ 15.02 | 7.92 | \$ 33,950 |
| Exercisable | 2,206,587 | \$ 10.22 | 6.60 | \$ 24,051 |

We calculate the intrinsic value as the difference between the exercise price of the options and the closing price of common stock of \$21.11 per share as of June 30, 2017.

Weighted average fair value of options granted during the three-month period ended June 30, 2017 and 2016 was \$16.95 and \$8.45 per share, respectively. There were 1,138,000 options granted during the six-month period ended June 30, 2016. We estimated the fair value of each stock option using the Black-Scholes option-pricing model based on

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the date of grant of such stock option with the following weighted average assumptions for the three and six months ended June 30, 2017 and 2016:

| | Options Three Months Ended June 30, | | Options Six Months Ended June 30, | |
|-------------------------|--|--------|--|--------|
| | 2017 | 2016 | 2017 | 2016 |
| Expected term (years) | 6.1 | 5.9 | 6.1 | 6.1 |
| Expected volatility | 88.9 % | 76.1 % | 89.2 % | 75.8 % |
| Risk-free interest rate | 1.91 % | 1.36 % | 2.04 % | 1.53 % |
| Expected dividend yield | — % | — % | — % | — % |

| | ESPP Three Months Ended June 30, | | ESPP Six Months Ended June 30, | |
|-------------------------|--|---------------|--------------------------------------|---------------|
| | 2017 | 2016 | 2017 | 2016 |
| Expected term (years) | 0.5 - 2.0 | 0.5 - 2.0 | 0.5 - 2.0 | 0.5 - 2.0 |
| Expected volatility | 67.8 - 79.8 % | 67.8 - 79.6 % | 67.8 - 79.8 % | 67.8 - 79.6 % |
| Risk-free interest rate | .47% - 1.09 % | .47% - .93 % | .47% - 1.09 % | .47% - .93 % |
| Expected dividend yield | — % | — % | — % | — % |

As of June 30, 2017 and 2016, the unamortized compensation expense related to unvested stock options was \$35.4 million and \$16.3 million, respectively. The remaining unamortized compensation expense will be recognized over the next three years. As of June 30, 2017 and 2016, the unamortized compensation expense under our ESPP was \$242,305 and \$491,000, respectively. The remaining unamortized expense will be recognized over the next 5.5 months.

7. Commitments and Contingencies

Operating Leases

The Company leases office and laboratory space in Monrovia, CA through June 2020. In July 2017, the Company entered into an amended lease agreement for additional space in the same building. The amended lease provides for additional space with a 64-month term with an option to renew for an additional five years. The lease terms for the original space were not amended.

The Company also leases office space in San Diego, CA through June 2020. In June 2017, the Company entered into a new lease agreement for additional office space in San Diego. The new lease has a 61-month term beginning from the date of occupancy and includes an option to renew for an additional five years.

All leases are accounted for as non-cancellable operating leases and future minimum payments are as follows (in thousands):

| | |
|--------------------------------------|--------|
| Years ending December 31, | |
| For the remainder of the fiscal year | \$ 634 |
| 2018 | 2,546 |
| 2019 | 2,726 |
| 2020 | 2,388 |
| 2021 | 1,980 |
| Thereafter | 1,406 |

Rent expense for the six months ended June 30, 2017 and 2016 was \$453,000 and \$298,000 respectively.

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Contingencies

From time to time, the Company may be subject to various litigation and related matters arising in the ordinary course of business. The Company does not believe it is currently subject to any material matters where there is at least a reasonable possibility that a material loss may be incurred.

On March 3, 2015, a verified class action complaint, captioned DePinto v. John S. Stafford, et al., C.A. No. 10742, was filed in the Court of Chancery of the State of Delaware against certain of the Company's current and former directors alleging cause of action for Breach of Fiduciary Duty and Invalidity of Director and Stockholder Consents. In general, the complaint alleged that the plaintiff and the class he seeks to represent were shareholders of the Company during the recapitalization and certain related transactions that the Company underwent in 2013 and that the defendants breached their fiduciary duties in the course of approving that series of transactions. It also challenged as invalid certain corporate acts taken in the 2013 time period.

The plaintiffs and the Company agreed to separate the litigation into two separate claims; Count I relating to the claim of Breach of Fiduciary Duty by the current and former directors of the Company and, Count II relating to the Invalidity of Director and Stockholder consents.

On December 14, 2015, the Delaware Chancery Court entered an Order and Partial Final Judgment in connection with Count II and approved the settlement of the invalidity claims, validating each corporate act challenged in the complaint, dismissing with prejudice Count II of the complaint (the invalidity claims) and granting plaintiff's counsel a fee award of \$950,000. We have paid the plaintiff's legal award of \$950,000 net of insurance proceeds of \$187,500 which has been reflected as a charge in our 2015 operations.

On September 27, 2016, the parties engaged in voluntary mediation and agreed to settle the complaint's remaining claim, Count II, for a total payment of \$2.375 million to the class certified by the Delaware Court of Chancery. The settlement was reached without any party admitting wrong-doing. Under the terms of the settlement, no payments shall be made to the plaintiffs by the Company or any of the defendants in the lawsuit other than payments covered by the Company's insurance.

On April 4, 2017, the Delaware Court of Chancery approved the Settlement between the parties. On May 1, 2017, the Company's insurance carriers fully funded the settlement account.

We recognized legal costs related to the litigation as incurred and offset any insurance proceeds when approved and issued. At December 31, 2016, we reported the \$2.355 million settlement as a payable and reflected a receivable of

the same amount for the insurance coverage. This amount was paid by the insurance carrier on our behalf in May 2017.

We are obligated to make future payments to third parties under in license agreements, including sublicense fees, royalties, and payments that become due and payable on the achievement of certain development and commercialization milestones. As the amount and timing of sublicense fees and the achievement and timing of these milestones are not probable and estimable, such commitments have not been included on our balance sheet.

8. Collaboration and Licensing Agreements

Following is a summary description of the arrangements that generated revenue in the six months ended June 30, 2017 and 2016.

Novartis

In June 2016, the Company entered into a Collaboration and License Agreement (the Novartis Agreement) with Novartis Institutes for BioMedical Research, Inc., (Novartis), to develop and commercialize bispecific and other Fc

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modulated antibody drug candidates using the Company's proprietary XmAb® technologies and drug candidates. Pursuant to the Novartis Agreement:

- The Company granted Novartis certain exclusive rights to research, develop and commercialize XmAb14045 and XmAb13676, two development stage products that incorporate the Company's bispecific Fc technology,
- The Company will apply its bispecific technology in up to four target pair antibodies identified by Novartis (each a Global Discovery Program) and,
- The Company will provide Novartis with a non-exclusive license to certain of its Fc technologies to apply against up to ten targets identified by Novartis.

The Company received a non-refundable upfront payment under the Novartis Agreement of \$150 million in July 2016 and is eligible to receive up to \$2.4 billion in future development, regulatory and sales milestones in total for all programs that could be developed under the Novartis Agreement.

The Company evaluated the Novartis Agreement and determined that it is a revenue arrangement with multiple deliverables or performance obligations. The Company's substantive performance obligations under the Novartis Agreement include:

- delivery of an exclusive license to commercialize XmAb14045 in worldwide territories outside the U.S., with worldwide co-exclusive rights with Xencor to research, develop and manufacture XmAb14045,
- delivery of an exclusive license to commercialize XmAb13676 in worldwide territories outside the U.S., with worldwide co-exclusive rights with Xencor to research, develop and manufacture XmAb13676,
- application of its bispecific technology to four Novartis selected target pair antibodies and delivery of four bispecific product candidates and,
- delivery of a non-exclusive license to its Fc technologies: Cytotoxic, Xtend and Immune Inhibitor.

The Company determined that the \$150 million upfront payment represents the total initial consideration and was allocated to each of the deliverables using the relative selling price method. The Company determined that each of the development and regulatory milestones is substantive. Although sales milestones are not considered substantive, they are still recognized upon achievement of a milestone. After identifying each of the deliverables included in the arrangement, the Company determined the relative selling price using its best estimate of selling price for each of the deliverables.

The total allocable consideration of \$150 million was allocated to the deliverables based on the relative selling price method as follows:

* \$27.1 million to certain rights to the XmAb14045 Program,

- * \$31.4 million to certain rights to the XmAb13676 Program,
- * \$20.05 million to each of the four Global Discovery Programs, and,
- * \$11.3 million to the Fc licenses

The Company recognized as license revenue the amount of the total allocable consideration allocated to the rights to the XmAb13676 and XmAb14045 Programs upon delivery of the exclusive license to Novartis both of which were transferred as of the effective date of the Novartis Agreement. At the time that each Global Discovery Program is accepted by Novartis, the Company will recognize collaboration revenue of \$20.05 million for each program. Since Novartis has substitution rights for up to four target pair antibodies, revenue recognition may be delayed until the earlier that Novartis has an open IND for a delivered bispecific Discovery Program or the right to substitute the target pair lapses. No bispecific antibodies for Global Discovery Programs have been delivered as of June 30, 2017.

The Company will recognize as licensing revenue the amount of the total consideration allocated to the Fc license over the five-year research term beginning from the effective date of the Novartis Agreement.

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During the three and six months ended June 30, 2017, we recognized \$0.6 million and \$1.1 million respectively. As of June 30, 2017, there is \$89.2 million in deferred revenue related to the arrangement.

Amgen, Inc.

In September 2015, the Company entered into a research and license agreement (the Amgen Agreement) with Amgen, Inc. (Amgen) to develop and commercialize bispecific antibody product candidates using the Company's proprietary XmAb® bispecific Fc technology. Under the Amgen Agreement, the Company granted an exclusive license to Amgen to develop and commercialize bispecific drug candidates from the Company's preclinical program that bind the CD38 antigen and the cytotoxic T-cell binding domain CD3, (the CD38 Program). The Company will also apply its bispecific technology to five previously identified Amgen provided targets (each a Discovery Program). The Company received a \$45.0 million upfront payment from Amgen and is eligible to receive up to \$1.7 billion in future development, regulatory and sales milestones in total for all six programs and is eligible to receive royalties on any global net sales of products.

In the fourth quarter ended December 31, 2015, the Company transferred the research material and data related to its CD38 Program to Amgen. Amgen will assume full responsibility for the further development and commercialization of product candidates under the CD38 Program. Assuming successful development and commercialization of a product, the Company could receive up to \$355 million in milestones payments which include \$55 million in development milestones, \$70 million in regulatory milestones and, \$230 million in sales milestones. If commercialized, the Company is eligible to receive from high single-digit up to low double-digit royalties on global net sales of approved products under the CD38 Program.

Pursuant to the Amgen Agreement, for each of the five Discovery Programs the Company will apply its bispecific technology to antibody molecules provided by Amgen that bind Discovery Program Targets and return the bispecific product candidates to Amgen for further testing, development and commercialization. Subject to approval by Xencor, Amgen has the right to substitute up to three of the previously identified targets during the research term provided that Amgen has not initiated non-human primate studies with the Xencor provided bispecific candidate. The initial research term is three years from the date of the Amgen Agreement but Amgen, at its option, may request an extension of one year if Xencor has not completed delivery of all five Discovery Program bispecific candidates to Amgen.

Amgen will assume full responsibility for development and commercialization of product candidates under each of the Discovery Programs. Assuming successful development and commercialization of each Discovery Program compound, the Company could receive up to \$260.5 million in milestones for each compound which include \$35.5 million in development milestones, \$55.0 million in regulatory milestones and \$170.0 million in sales milestones. If commercialized, the Company is eligible to receive mid to high single-digit royalties on global net sales of approved products.

The Company evaluated the Amgen Agreement and determined that it is a revenue arrangement with multiple deliverables or performance obligations. The Company's substantive performance obligations under the Amgen Agreement include delivery of research material and data related to its CD38 Program and application of its bispecific technology to five Amgen provided targets and delivery of the five bispecific product candidates. The Company evaluated the Amgen Agreement and determined that the CD38 Program and each of the five Discovery Programs represent separate units of accounting.

The \$45 million upfront payment represents the total initial consideration and was allocated to each of the deliverables using the relative selling price method. After identifying each of the deliverables included in the arrangement, the Company determined its best estimate of selling price for each of the deliverables.

The total allocable consideration of \$45 million was allocated to the deliverables based on the relative selling price method as follows:

- \$13.75 million to the CD38 Program and,
- \$6.25 million to each of the five Discovery Programs

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The Company recognized as collaboration revenue the amount of consideration allocated to the CD38 Programs upon delivery of the CD38 research material and data to Amgen in the fourth quarter of 2015.

During 2016, the Company recognized as collaboration revenue the amount of consideration for delivery of three Discovery Programs; the Company delivered bispecific antibody candidates for five Discovery Programs and Amgen elected to substitute one of the originally identified antibody candidates. There were no additional Discovery Programs delivered in the three and six months ended June 30, 2017 there were no additional substitutions of originally identified candidate by Amgen during the three and six months ended June 30, 2017.

During the three and six months ended June 30, 2017 we did not recognize any revenues. During the three and six months ended June 30, 2016, we recognized \$6.2 million and \$12.5 million in revenue under this arrangement, respectively. As of June 30, 2017, there is \$12.5 million in deferred revenue related to the arrangement.

MorphoSys Ag

In June 2010, we entered into a Collaboration and License Agreement with MorphoSys AG (MorphoSys), which we subsequently amended in March 2012. The agreement provided us an upfront payment of \$13.0 million in exchange for an exclusive worldwide license to our patents and know how to research, develop and commercialize our XmAb5574 product candidate (subsequently renamed MOR208) with the right to sublicense under certain conditions. Under the agreement, we agreed to collaborate with MorphoSys to develop and commercialize XmAb5574/MOR208. We determined that the arrangement was one with multiple deliverables and we identified the multiple elements in the agreement as the license of XmAb5574/MOR208 and the research and development services provided by us for the initial Phase 1 clinical trial. If certain developmental, regulatory and sales milestones are achieved, we are eligible to receive future milestone payments and royalties. We determined that the future milestone payments were substantive and contingent and we did not allocate any of the upfront consideration to these milestones. We completed all our responsibility with respect to the collaboration services under the arrangement in 2012 and MorphoSys is responsible for all further development of XmAb5574/MOR208.

In June 2017, MorphoSys initiated a Phase III clinical trial under the arrangement and we received a milestone payment of \$12.5 million. We have recognized the payment as revenue in the period that the milestone event occurred.

During the three and six months ended June 30, 2017 we recognized \$12.5 million under this arrangement. As of June 30, 2017, there is no deferred revenue related to this agreement.

Merck Sharp & Dohme Corporation

In July 2013, we entered into a License Agreement with Merck Sharp & Dohme Corp (Merck). Under the terms of the agreement, we provided Merck with a non-exclusive commercial license to certain patent rights to our Fc domains to

apply to one of their compounds. The agreement provided for an upfront payment of \$1.0 million and annual maintenance fees totaling \$0.5 million. We are also eligible to receive future milestones and royalties as Merck advances the compound into clinical development.

We determined that the deliverables under this agreement were the non-exclusive commercial license and the options. The options are considered substantive and contingent and no amount of the upfront payment was allocated to these options. We also determined that the future milestones and related payments were substantive and contingent and did not allocate any of the upfront payment to the milestones.

During each of the three and six months ended June 30, 2017 and 2016 we recognized \$25,000 and \$50,000 of revenue respectively. As of June 30, 2017, there is \$100,000 of deferred revenue related to this arrangement.

Alexion Pharmaceuticals, Inc.

In January 2013, we entered into an option and license agreement with Alexion Pharmaceuticals, Inc. (Alexion). Under the terms of the agreement, we granted to Alexion an exclusive research license, with limited sublicensing rights, to make and use our Xtend technology to evaluate and advance compounds against six different target programs during a

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five-year research term under the agreement, up to completion of the first multi-dose human clinical trial for each target compound. Alexion may extend the research term for an additional three years upon written notice to us and payment of an extension fee of \$2.0 million. Alexion is responsible for conducting all research and development activities under the agreement at its own expense.

Under the agreement, we received an upfront payment of \$3.0 million. Alexion is also required to pay an annual maintenance fee of \$0.5 million during the research term of the agreement and \$1.0 million during any extension of the research term. We determined that \$2.5 million of the upfront fee was allocated to the license and is being recognized into income over the initial research term of five years.

In the third quarter of 2014, Alexion achieved a clinical development milestone with an undisclosed molecule to be used against an undisclosed target. In the fourth quarter of 2015, Alexion exercised its option to take an exclusive commercial license and achieved a further clinical development milestone.

In December 2016, Alexion achieved a Phase 3 clinical development milestone for an undisclosed target for which we received a \$5 million milestone payment.

During each of the three and six months ended June 30, 2017 and 2016 we recognized \$250,000 and \$500,000 in revenues, respectively. As of June 30, 2017, we have deferred revenue related to this arrangement of \$0.6 million.

Novo Nordisk A/S

In December 2014, we entered into a collaboration and license agreement with Novo Nordisk A/S (Novo). Under the terms of the agreement we granted Novo a research license to use certain Xencor technologies including our bispecific, Fcy-IIb, Xtend and other technologies during a two-year research term. In connection with the agreement we received a \$2.5 million upfront payment and funding for research support during the research term.

We recognized the \$2.5 million upfront payment as income over the two-year research term. The research funding was being recognized into income over the period that the services were being provided. We determined that future milestone payments were substantive and contingent and we did not allocate any of the upfront consideration to these milestones.

During the three and six months ended June 30, 2017 no revenue was recognized. During the three and six months ended June 30, 2016, we recognized \$0.7 million and \$1.4 million of revenue, respectively. As of June 30, 2017, we have no deferred revenue related to this arrangement.

CSL Limited

In February 2009, we entered into a Research License and Commercialization Agreement with CSL Limited (CSL). Under the agreement, we provided CSL with a research license to our Fc Cytotoxic technology and options to non-exclusive commercial licenses. CSL elected to exercise one commercial license for a compound, CSL362.

In 2013 CSL sublicensed CSL362 (now called talacotuzumab) to Janssen Biotech Inc. (Janssen Biotech). In March 2017, CSL, through its sub-licensee, Janssen Biotech, initiated a Phase 3 clinical trial for CSL362. As a result of the Phase 3 clinical trial initiation, we received a milestone payment of \$3.5 million.

During the three and six months ended June 30, 2017 we recognized zero and \$3.5 million of revenue respectively. We did not recognize any revenues in each of the three and six months ended June 30, 2016. As of June 30, 2017, we have no deferred revenue related to this arrangement.

9. Income taxes

The provision for income taxes for the three- and six-month periods ended June 30, 2017 and 2016 represents the interim period tax allocation of the federal and state alternative minimum tax based on the Company's projected year-end effective income tax rates which cannot be offset by the Company's net operating loss carryforwards, The

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Company has deferred tax assets consisting primarily of net operating loss and tax credit carryforwards that have been fully offset by a valuation allowance.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis should be read in conjunction with our financial statements and accompanying notes included in this Quarterly Report on Form 10-Q and the financial statements and accompanying notes thereto for the fiscal year ended December 31, 2016 and the related Management's Discussion and Analysis of Financial Condition and Results of Operations, both of which are contained in our Annual Report on Form 10-K for the year ended December 31, 2016. This Quarterly Report on Form 10-Q may contain "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended, (the Exchange Act). Such forward-looking statements, which represent our intent, belief, or current expectations, involve risks and uncertainties. We use words such as "may," "will," "expect," "anticipate," "estimate," "intend," "plan," "predict," "potential," "believe," "should" and similar expressions to identify forward-looking statements, although not all forward-looking statements contain these identifying words. Such statements may include, but are not limited to, statements concerning: (i) the initiation, cost, timing, progress and results of our research and development activities, preclinical studies and future clinical trials, including our expected timeline for nominating clinical development candidates under our strategic alliances and our expected timeline for filing applications with regulatory authorities;(ii) our ability to obtain and maintain regulatory approval of our future product candidates, and any related restrictions, limitations, and/or warnings in the label of an approved product candidate; (iii) our ability to obtain funding for our operations; (iv) our plans to research, develop and commercialize our future product candidates; (v) our ability to attract collaborators with development, regulatory and commercialization expertise; (vi) our ability to obtain and maintain intellectual property protection for our technology; (vii) the size and growth potential of the markets for our technology and future product candidates, and our ability to serve those markets; (viii) our ability to successfully commercialize our technology and our future product candidates; (ix) our ability to develop sales and marketing capabilities, whether alone or with potential future collaborators; (x) regulatory developments in the United States and foreign countries; and (xi) the performance of our collaboration partners, licensees, third-party suppliers and manufacturers. Although we believe the expectations reflected in these forward-looking statements are reasonable, such statements are inherently subject to risk and we can give no assurances that our expectations will prove to be correct. You should not place undue reliance on these forward-looking statements, which apply only as of the date of this Quarterly Report on Form 10-Q. As a result of many factors, including without limitation those set forth under "Risk Factors" under Item 1A of Part II below, and elsewhere in this Quarterly Report on Form 10-Q, our actual results may differ materially from those anticipated in these forward-looking statements. We undertake no obligation to update these forward-looking statements to reflect events or circumstances after the date of this report or to reflect actual outcomes.

Company Overview

We are a clinical-stage biopharmaceutical company focused on discovering and developing engineered monoclonal antibodies to treat severe and life-threatening diseases with unmet medical needs. We use our proprietary XmAb technology platform to create next-generation antibody product candidates designed to treat autoimmune and allergic diseases, cancer and other conditions. In contrast to conventional approaches to antibody design, which focus on the portion of antibodies that interact with target antigens, we focus on the portion of the antibody that interacts with multiple segments of the immune system. This portion, referred to as the Fc domain, is constant and interchangeable among antibodies. Our engineered Fc domains, the XmAb technology, can be readily substituted for natural Fc domains.

Our business strategy is based on the plug and play nature of the XmAb technology, allowing us to create new antibody drug candidates for our internal development or licensing, or to selectively license access to one or more of our XmAb technologies or product candidates to pharmaceutical or biotechnology companies to use in developing their own proprietary antibodies and drug candidates with improved properties. These licensing transactions provide us with multiple revenue streams that help fund development of our wholly owned product candidates and usually require limited resources or efforts from us. There are currently eleven antibody product candidates in clinical trials that have been engineered with XmAb technology, including seven candidates being advanced by licensees and development partners, three of which are in Phase 3 trials.

Our protein engineering capabilities allow us to continue to expand the functionality of the XmAb technology platform to identify new protein enhancements and create new antibody drug candidates with improved properties. Our bispecific technology, heterodimer Fc domains, enables the creation of bispecific drug candidates, which are antibodies that are engineered to bind two targets simultaneously. The core of our bispecific programs is a novel Fc domain that is a

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robust and portable scaffold for two, or potentially more, different antigen binding domains. Our Fc domain technology is designed to maintain full-length antibody properties in a bispecific antibody, potentially enabling stable molecules with favorable in vivo half-life and allowing for the use of standard antibody production methods. The portability of the bispecific technology, including the ability of bispecific candidates generated from our technology to use standard production methods, allows us to license access to our technology as highlighted in our two bispecific licensing transactions that we entered into with Amgen and Novartis in 2015 and 2016, respectively.

We are also developing a pipeline of drug candidates around our bispecific technology. Within the past year, our two lead bispecific drug candidates entered into the Phase 1 stage of clinical development and we plan to file an IND for our third bispecific clinical candidate by the end of 2017 and enter the clinic in early 2018 with additional candidates entering into clinical development in 2018 and 2019.

In June 2016, we entered into the Novartis Agreement which included a \$150 million upfront payment and up to \$2.4 billion in potential development, regulatory and sales milestones. As part of the Agreement, we will apply our bispecific technology to up to four target pair antibodies selected, available for exclusive license to Novartis and not subject to a Xencor internal program.

We will apply our bispecific technology to generate bispecific antibody candidates from starting target pair antibodies provided by Novartis for each of the four Global Discovery Programs and return the bispecific product candidate to Novartis for further testing, development and commercialization. Assuming successful development and commercialization of each bispecific compound, we could receive up to \$250 million in milestones for each compound which includes \$50 million in development milestones, \$100 million in regulatory milestones and \$100 million in sales milestones. If commercialized, the Company is eligible to receive mid-single digit royalties on global net sales of approved products.

In September 2015, we entered into the Amgen Agreement which included a \$45 million upfront payment and up to \$1.7 billion in future development, regulatory and sales milestones if all programs under the agreement advance into development. In connection with the Amgen Agreement, we are applying our bispecific technology to up to five previously identified molecules identified by Amgen and approved by us. We are applying our bispecific technology to each of the five identified programs and returning the bispecific product candidates to Amgen, who is assuming full responsibility for further testing, development and commercialization. Assuming successful development and commercialization of each bispecific compound, we could receive up to \$260.5 million in milestones which include \$35.5 million in development milestones, \$55 million in regulatory milestones and \$170 million in sales milestones. If commercialized, we are eligible to receive mid to high-single digit royalties on global net sales of approved products. Through June 30, 2017 we have delivered five bispecific product candidates to Amgen under the Agreement.

Since we commenced active operations in 1998, we have devoted substantially all of our resources to staffing our company, business planning, raising capital, developing our technology platforms, identifying potential product candidates, undertaking pre-clinical and IND enabling studies and conducting clinical trials. We have no products

approved for commercial sale and have not generated any revenues from product sales, and we continue to incur significant research and development expenses and other expenses related to our ongoing operations. To date, we have funded our operations primarily through the sale of stock and convertible promissory notes and through payments generated from our product development partnership and licensing arrangements.

As of June 30, 2017, we had an accumulated deficit of \$260 million. Substantially all of our operating losses that we have incurred resulted from expenses incurred in connection with our product candidate development programs, our research activities and general and administrative costs associated with our operations.

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Company Programs

We are developing a pipeline of candidates for clinical development based on our Immune Inhibitor Domain and Bispecific Domain technologies.

Immune Inhibitor Pipeline

XmAb5871 uses our XmAb Immune Inhibitor Fc Domain and targets B cells, an important component of the immune system. We believe that XmAb5871 has the potential to address a key unmet need in autoimmune therapies due to its combination of potent B-cell inhibition without B-cell depletion.

In March 2016, we initiated enrollment for two Phase 2 trials for XmAb5871, one trial in IgG4-Related Disease (IgG4-RD) and a trial in Systemic Lupus Erythematosus (SLE or Lupus). In July 2016 we initiated a Phase 1 trial with a subcutaneous formulation of XmAb5871.

In May 2017, we received Orphan Drug designation from the U.S. Food and Drug Administration for XmAb5871 for the treatment of IgG4-Related Disease.

IgG4-RD: In January 2017 we completed planned enrollment of 15 patients in a Phase 2 open-label pilot study of XmAb5871 for IgG4-RD with scheduled treatment up to 24 weeks. To increase clinical and biomarker data collection, an additional five patients were enrolled beginning in April 2017 and the trial closed by June 2017. The primary objective of the study is to evaluate the effect of every other week IV administration of XmAb5871 using the recently reported IgG4-RD Responder Index in patients with active IgG4-RD. Secondary objectives are to determine the safety and tolerability profile and to characterize the pharmacokinetics (PK) and immunogenicity of every other week IV administration of XmAb5871.

We presented interim data from the Phase 2 trial in June 2017 at the Annual European Congress of Rheumatology for the 15 patients that had been enrolled and were evaluable through April 18, 2017, the date selected for cut-off of the interim data review. The preliminary data indicated that XmAb5871 was well tolerated by patients receiving drug in the study. As of the cut-off date, no serious adverse events (AEs) related to XmAb5871 were reported, with all XmAb5871-related AE's graded as mild or moderate and no AE reported in more than two patients. One patient discontinued the study as the result of an AE. This patient developed a Grade 2 (moderate) hypersensitivity reaction with rash and arthritis, commonly referred to as serum sickness, following the fifth infusion. The event quickly resolved without the need for medical management. This patient was subsequently found to have developed anti-drug antibodies.

Interim efficacy data from the trial was very encouraging. As of the cut-off date, 10 patients have completed the study, three of whom discontinued, and five patients are ongoing. Fourteen of the fifteen patients (93%) dosed with XmAb5871 have had a response to XmAb5871 therapy of greater than or equal to a two-point reduction in the IgG4-RD Responder Index (protocol defined response), 12 of them within two weeks of the first dose. At two weeks following the last dose, five patients had an IgG4-RD Responder Index of zero and were on no corticosteroid therapy between months 2-6 (protocol defined remission). In addition, a sixth patient achieved remission in the post-therapy follow-up period. All five of the patients that either entered the study on corticosteroids or that were administered corticosteroids at the beginning of the study have been able to taper and discontinue corticosteroids within two months of the start of the study.

In addition to the patient with early study termination due to an AE, two other patients have discontinued treatment prior to receipt of all 12 planned infusions. One patient had a response to therapy (IgG4-RD RI reduction of six points), but lost response following the sixth infusion, and one patient had no response to therapy. Neither of these two patients have responded to subsequent rituximab treatment.

We believe that this promising preliminary data from the Phase 2 trial warrants further clinical development of XmAb5871 in treating IgG4-RD and we are planning such development.

We expect to provide top line data from the initially planned 15 patients in this trial in the second half of 2017.

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In October 2016, we also completed a Phase 1 bioequivalence trial for XmAb5871 using a subcutaneous formulation. XmAb5871 was safe and well-tolerated as a subcutaneous injection in this trial. Pharmacokinetics and bioavailability data from the trial support an every other week dosing schedule. Our plan is to conduct further clinical studies with XmAb5871 in a subcutaneous formulation.

SLE: We are also enrolling a Phase 2 randomized, double blinded, placebo-controlled study of XmAb5871 in SLE. This trial is designed to assess the effect of XmAb5871 on SLE disease activity in a shorter timeframe and using fewer patients compared to standard SLE trials, and XmAb5871 is the first newly developed agent being assessed with this novel trial design. The trial design calls for treating patients with moderate to severe, non-organ threatening SLE with XmAb5871 (or placebo) after their lupus disease activity has improved with a short course of intra-muscular (IM) steroid therapy. Background, potentially confounding, immunosuppressant medications will be stopped. In this double-blinded placebo-controlled study, the ability of XmAb5871 to maintain the improvement in disease activity after IM steroid therapy and in the absence of immunosuppressant medication will be assessed. Historically, SLE trial designs generally add new medications to the many already taken by the patient, and hence display a discernible treatment effect only when restricted to the sickest patients. The trial will enroll approximately 90 subjects, 1:1 randomized to XmAb5871 or placebo, for up to 24 weeks. We expect to provide initial data from this trial in late 2018 or early 2019.

XmAb7195 uses our Immune Inhibitor Fc Domain and is being developed for the treatment of severe asthma and allergic diseases. XmAb 7195 is designed to reduce blood serum levels of IgE, which mediates allergic responses and allergic disease. In January 2015, we reported top-line interim data from Part 1 of the Phase 1a trial of XmAb7195, in which healthy volunteers received a single intravenous (IV) dose. In 2015, we continued the Phase 1a trial of XmAb7195, treating subjects with high baseline IgE levels, and in June 2015, we announced an expansion of the trial, adding cohorts of subjects that receive two IV doses of XmAb7195. We announced complete data from these studies in May 2016. In September 2016, we initiated a multi-dose Phase 1b trial for XmAb7195 with a subcutaneous formulation. The first part of this trial is dosing healthy volunteers with a subcutaneous formulation of XmAb7195. The second part of the trial is dosing atopic patients with the subcutaneous formulation of XmAb7195 which we began in October 2016. We expect to provide top line data from this trial in the second half of 2017.

XmAb Bispecific Pipeline

XmAb14045 uses our XmAb bispecific Fc technology that allows us to create dual-antigen targeting molecules. In September 2016, we dosed the first patient in a Phase 1 clinical trial for XmAb14045, our first bispecific oncology candidate, for the treatment of acute myeloid leukemia (AML). XmAb14045 targets CD123, an antigen on AML cells and leukemic stem cells, and CD3, an activating receptor on T cells. The trial is a Phase 1, open-label, multiple-dose, dose escalation study to assess safety, tolerability and preliminary anti-tumor activity in AML.

XmAb13676 is our second bispecific oncology candidate. In February 2017, we dosed the first patient in a Phase 1 clinical trial for XmAb13676. XmAb13676 is a tumor-targeted antibody that contains both a B-cell tumor antigen

binding domain (CD20) and a cytotoxic T-cell binding domain (CD3). The trial is a Phase 1, open-label, multiple-dose, dose escalation study to assess safety, tolerability and preliminary anti-tumor activity in B-cell malignancies.

In connection with the Novartis Agreement we granted Novartis exclusive licenses to commercialize XmAb14045 and XmAb13676 in all worldwide territories outside the U.S., with worldwide co-exclusive rights with us to research, develop and manufacture XmAb14045 and XmAb13676. We continue to retain U.S. rights to both drug candidates and will co-develop worldwide both candidates with Novartis and share development costs equally. Upon successful development of each of XmAb14045 and XmAb13676 we are eligible to receive up to \$325 million in milestones which includes \$90 million in development milestones, \$110 million in regulatory milestones and \$125 million in sales milestones. If commercialized, the Company is eligible to receive tiered low double-digit royalties on net global sales outside the U.S.

XmAb18087 is our third CD3 bispecific oncology candidate and it targets the Somatostatin Receptor 2 (SSTR2) and the cytotoxic T-cell binding domain CD3 for the treatment of neuroendocrine tumors. We plan to file an IND in 2017 and initiate a clinical trial for XmAb18087 in early 2018.

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XmAb20717 is our initial checkpoint inhibitor candidate that is being developed using our bispecific technology platform. XmAb20717 targets PD-1 and CTLA-4 and is being developed for broad oncology indications including solid tumors. We plan to file an IND for this compound in early 2018 and initiate clinical trials in 2018.

Out-Licensed Compounds

In addition to our wholly-owned compounds in clinical development, we have used our XmAb technology to create antibody compounds which have been licensed to other pharmaceutical and biotechnology companies for further development. These licensed compounds do not require additional development effort by us as they advance into development by our partners. If successful, these candidates will generate additional milestone payments and royalties to support our internal development efforts. These include XmAb5574/MOR208 (now MOR208) licensed to MorphoSys, and XmAb13551, a bispecific CD38 x CD3 preclinical candidate, which we developed and licensed to Amgen. In June 2017, MorphoSys commenced a Phase 3 trial for which we recorded \$12.5 million in milestone revenues.

| Program | Target | Fc Domain | Primary Stage of Indication | Development | Partner |
|-----------------|------------|------------|-----------------------------|-------------|-----------|
| XmAb5574/MOR208 | CD19 | Cytotoxic | CLL/NHL/ALL | Phase 3 | Morphosys |
| XmAb13551 | CD38 x CD3 | Bispecific | Myeloma | Preclinical | Amgen |

Our Out-Licensed Technology

We selectively license our XmAb technology to other companies for use in their own internal development candidates and to potentially make next-generation improvements to their marketed products. These licenses generally require little or no development effort by us and provide us with cash to fund our own research and development programs. These agreements typically provide the licensee with specific rights to use one or more of our Fc technologies to be applied to their proprietary antibodies or targets. The licensee is generally responsible for all development, of any resulting product candidate. As part of these agreements, we are generally entitled to receive upfront fees, annual licensing fees, potential milestone payments and royalties on the sales of any resulting products. In connection with our collaboration with Novo Nordisk, we also received research and development funding.

There are currently eight programs in development with our partners. The most advanced programs are with Alexion which started a Phase 3 trial in 2016 and CSL-Janssen Biotech, which entered into Phase 3 clinical trial in March 2017.

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| Licensee | Year | Xencor Technology | Indication | Milestones | Royalties | Current Development Stage |
|----------------------|------|--------------------------------------|---------------------|------------|-----------|-------------------------------------|
| Alexion | 2013 | Xtend | Undisclosed | Yes | Yes | Phase 3 |
| CSL-Janssen Biotech | 2009 | Cytotoxic | Oncology | Yes | Yes | Phase 3 |
| Boehringer Ingelheim | 2007 | Cytotoxic | Oncology | Yes | Yes | Phase 1 (2 candidates) |
| Janssen Biotech | 2009 | Xtend | Autoimmune disease | Yes | Yes | Preclinical |
| NIH (not licensed) | | Xtend | HIV | N/A | N/A | Phase 1 |
| Merck | 2013 | Fc optimization | Autoimmune disease | Yes | Yes | Phase 1 5 Preclinical candidates |
| Amgen | 2015 | Bi-specific Various, including | Oncology/Autoimmune | Yes | Yes | |
| Novartis | 2016 | Bi-specifics | Undisclosed | Yes | Yes | Preclinical |

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Results of Operations

Comparison of the Three Months Ended June 30, 2017 and 2016

The following table summarizes our results of operations for the three months ended June 30, 2017 and 2016 (in millions):

| | Three Months Ended June 30, | | |
|---|--------------------------------|---------|-----------|
| | 2017 | 2016 | Change |
| Revenues: | | | |
| Research collaboration | \$ — | \$ 7.2 | \$ (7.2) |
| Licensing | 0.8 | 58.8 | (58.0) |
| Milestone | 12.5 | — | 12.5 |
| Total revenues | \$ 13.3 | \$ 66.0 | \$ (52.7) |
| Operating expenses: | | | |
| Research and development | 16.9 | 14.4 | 2.5 |
| General and administrative | 4.1 | 3.0 | 1.1 |
| Total operating expenses | 21.0 | 17.5 | 3.6 |
| Other income, net | 1.1 | 0.4 | 0.7 |
| Income (loss) before income tax expense | (6.6) | 48.9 | (55.6) |
| Income tax expense | 0.3 | 1.7 | (1.4) |
| Net income (loss) | \$ (6.9) | \$ 47.2 | \$ (54.2) |

Revenues

Research collaboration revenues decreased by \$7.2 million in the three months ended June 30, 2017 over 2016 amounts primarily due to revenue recognized under the Amgen Agreement in 2016.

Licensing revenues were \$58 million lower during the three months ended June 30, 2017 compared to the same period in 2016 primarily due to revenue recognized under our Novartis Agreement in 2016.

Milestone revenues for three months ended June 30, 2017 were earned from our Morphosys collaboration. There were no milestone revenues for the three months ended June 30, 2016.

Research and Development Expenses

The following table summarizes our research and development expenses for the three months ended June 30, 2017 and 2016 (in millions):

| | Three Months Ended | | |
|---|--------------------|---------|--------|
| | June 30, 2017 | 2016 | Change |
| Product programs: | | | |
| XmAb5871 | \$ 4.7 | \$ 4.5 | \$ 0.2 |
| XmAb7195 | 1.0 | 2.2 | (1.2) |
| Bi-specific | 9.7 | 7.0 | 2.7 |
| Early research and discovery | 1.5 | 0.7 | 0.8 |
| Total research and development expenses | \$ 16.9 | \$ 14.4 | \$ 2.5 |

Research and development expenses increased by \$2.5 million for the three months ended June 30, 2017 over the same period in 2016 as we continue to advance our initial bispecific candidates XmAb14045 and XmAb13676 into clinical development as well as development activities for the next two bispecific candidates XmAb18087 and XmAb20717. Increases in research and development spending on our XmAb5871 and early discovery research programs were offset by reduced spending on our XmAb7195 program.

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General and Administrative Expenses

The following table summarizes our general and administrative expenses for the three months ended June 30, 2017 and 2016 (in millions):

| | Three Months Ended | | |
|----------------------------|--------------------|--------|--------|
| | June 30, | | |
| | 2017 | 2016 | Change |
| General and administrative | \$ 4.1 | \$ 3.0 | \$ 1.1 |

General and administrative expenses increased by \$1.1 million for the three months ended June 30, 2017 over the same period in 2016 primarily due to an increase in stock-based compensation costs offset by reimbursement of legal costs to the litigation described in Part II item 1.

Other Income, Net

Other income, net was \$1.1 million for the three months ended June 30, 2017 compared to \$358,000 for the same period in 2016 reflecting interest income on our investment in marketable securities.

Comparison of the Six Months Ended June 30, 2017 and 2016

The following table summarizes our results of operations for the six months ended June 30, 2017 and 2016 (in millions):

| | Six Months Ended | | |
|------------------------|------------------|---------|-----------|
| | June 30, | | |
| | 2017 | 2016 | Change |
| Revenues: | | | |
| Research collaboration | \$ — | \$ 14.1 | \$ (14.1) |
| Licensing | 1.7 | 59.1 | (57.4) |
| Milestone | 16.0 | — | 16.0 |
| Total revenues | \$ 17.7 | \$ 73.2 | \$ (55.5) |

| | | | |
|----------------------------|-----------|---------|-----------|
| Operating expenses: | | | |
| Research and development | 32.0 | 24.4 | 7.6 |
| General and administrative | 8.9 | 7.0 | 1.9 |
| Total operating expenses | 40.9 | 31.4 | 9.5 |
| Other income, net | 2.1 | 0.7 | 1.4 |
| Income (loss) before taxes | (21.1) | 42.5 | (63.6) |
| Income tax provision | 0.4 | 1.7 | (1.3) |
| Net income (loss) | \$ (21.5) | \$ 40.8 | \$ (62.3) |

Revenues

Research collaboration revenues for the six months ended June 30, 2017 decreased by \$14.1 million compared to the same period in 2016 primarily due to revenue recognized under our Amgen Agreement in 2016.

Licensing revenues for the six months ended June 30, 2017 decreased by \$57.4 million compared to the same period in 2016 primarily due to revenue recognized from our Novartis Agreement in 2016.

Milestone revenues for the six months ended June 30, 2017 were earned from our MorphoSys and CSL collaborations. There were no milestone revenues for the same period in 2016.

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Research and Development Expenses

The following table summarizes our research and development expenses for the six months ended June 30, 2017 and 2016 (in millions):

| | Six Months Ended | | |
|---|------------------|---------|--------|
| | June 30, | | Change |
| | 2017 | 2016 | |
| Product programs: | | | |
| XmAb5871 | \$ 8.2 | \$ 8.0 | \$ 0.2 |
| XmAb7195 | 2.0 | 3.2 | (1.2) |
| Bi-specific | 18.9 | 11.9 | 7.0 |
| Early research and discovery | 2.9 | 1.3 | 1.6 |
| Total research and development expenses | \$ 32.0 | \$ 24.4 | \$ 7.6 |

Research and development expenses increased by \$7.6 million for the six months ended June 30, 2017 over the same period in 2016 as we continue to advance our initial bispecific candidates XmAb14045 and XmAb13676 into clinical development as well as development activities for the next two bispecific candidates XmAb18087 and XmAb20717. Increased spending on our early discovery research programs was offset by reduced spending on our XmAb7195 program

General and Administrative Expenses

The following table summarizes our general and administrative expenses for the six months ended June 30, 2017 and 2016 (in millions):

| | Six Months Ended | | |
|----------------------------|------------------|--------|--------|
| | June 30, | | Change |
| | 2017 | 2016 | |
| General and administrative | \$ 8.9 | \$ 7.0 | \$ 1.9 |

General and administrative expenses increased by \$1.9 million for the six months ended June 30, 2017 over the same period in 2016 primarily due to an increase in stock-based compensation costs offset by reimbursement of legal costs to the litigation described in Part II item 1.

Other Income, Net

Other income, net was \$2.1 million for the six months ended June 30, 2017 compared to \$693,000 for the same period in 2016 reflecting interest income on our investment in marketable securities

Cash Flows

The following table sets forth the primary sources and uses of cash for each of the periods presented below (in thousands):

| | Six Months Ended June 30, | | |
|---------------------------------|---------------------------|-------------|----------|
| | 2017 | 2016 | Change |
| Net cash (used in) provided by: | | | |
| Operating activities | \$ (23,508) | \$ (23,669) | \$ 161 |
| Investing activities | 18,078 | 18,283 | (205) |
| Financing activities | 2,122 | 673 | 1,449 |
| Net decrease in cash | \$ (3,308) | \$ (4,713) | \$ 1,405 |

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Operating Activities

Cash used in operating activities for the six months ended June 30, 2017 decreased by \$161,000 over amounts reported for the six months ended June 30, 2016 reflecting lower deferred revenue and accounts receivable in the June 2017 period.

Investing Activities

Investing activities consist primarily of investments in marketable securities available-for-sale, purchases of intangible assets, capitalization of patent and licensing costs and, purchases of property and equipment. Net cash provided by investing activities for the six months ended June 30, 2017 decreased by 205,000 over amounts reported for the period ended and June 30, 2016.

Financing Activities

Net cash provided by financing activities for the six months ended June 30, 2017 increased by \$1.4 million over the same period in 2016 which reflects additional proceeds received from stock option exercises and issuance of common stock pursuant to our Employee Stock Purchase Plan in 2017.

Liquidity and Capital Resources

We have financed our operations primarily through private placements of our equity and convertible notes, the public offerings of our common stock, and payments received under our product development partnerships and licensing arrangements.

On March 3, 2015, we finalized the sale of 8,625,000 shares of common stock at an offering price of \$14.25 per share, resulting in net proceeds of approximately \$115.2 million, after deducting underwriting discounts, commissions and offering expenses. In September 2015, we received a \$45 million upfront payment in connection with the 2015 Amgen Agreement.

In July 2016, we received a \$150 million upfront payment in connection with the Novartis Agreement.

On September 19, 2016, we entered into an Equity Distribution Agreement (the Distribution Agreement) with Piper Jaffray & Co (Piper Jaffray) pursuant to which we may sell from time to time, at our option, up to an aggregate of \$40 million of common stock through Piper Jaffray as sales agent. The issuance and sale of these shares by Xencor under the Distribution Agreement will be pursuant to our shelf registration statement on Form S-3 (File No.333-213700) declared effective by the SEC on October 5, 2016.

Piper Jaffray may sell the common stock by any method permitted under law deemed to be an “at the market” offering as defined by Rule 15 of the Securities Act of 1933, as amended including without limitation sales made by means of ordinary brokers on the NASDAQ Global market or otherwise at market prices prevailing at the time of sale or as otherwise directed by the Company. Piper Jaffray will use commercially reasonable efforts to sell the common stock from time to time, based on instructions from Xencor. Additionally, under the terms of the Distribution agreement, the Company may sell shares of its common stock through Piper Jaffray on terms agreed upon by both parties.

We are not obligated sell any shares of common stock under the Agreement. The offering of common stock pursuant to the Distribution Agreement will terminate upon the earlier of:

1. the issuance and sale of all of the shares of common stock subject to the Distribution agreement,
2. three years from the Registration effective date, October 5, 2016,
3. the date the Company becomes ineligible to use the Registration statement or,
4. the termination of the Distribution Agreement as provided in the Agreement.

To date, we have not sold any shares under the Distribution Agreement.

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In December 2016, we completed the sale of 5,272,750 shares of common stock which included shares we issued pursuant to our underwriters' exercise of their over-allotment option pursuant to a follow-on financing. We received net proceeds of \$119.3 million, after deducting underwriter discounts and offering expenses.

As of June 30, 2017, we had \$378.7 million of cash, cash equivalents and marketable securities compared to \$168.8 million at June 30, 2016. We expect to continue to receive additional payments from our collaborators for research and development services rendered, additional milestone, contingent payments, opt-in and annual license maintenance payments. Our ability to receive milestone payments and contingent payments from our partners is dependent upon either our ability or our partners' abilities to achieve certain levels of research and development activities and is therefore uncertain at this time.

Funding Requirements

We have not generated any revenue from product sales to date and do not expect to do so until such time as we obtain regulatory approval of and commercialize one or more of our product candidates. As we are currently in clinical stage of development, it will be some time before we expect to achieve this and it is uncertain that we ever will commercialize one or more of our product candidates. We expect that we will continue to increase our operating expenses in connection with ongoing as well as additional clinical and pre-clinical development of product candidates in our pipeline.

Although it is difficult to predict our funding requirements, based upon our current operating plan, we expect that our existing cash, cash equivalents and marketable securities and certain potential milestone payments will fund our operating expenses and capital expenditure requirements beyond 2020. We have based these estimates on assumptions that may prove to be wrong, and we could use our capital resources sooner than we currently expect.

Off-Balance Sheet Arrangements

We did not have during the periods presented, and we do not currently have, any off-balance sheet arrangements.

Contractual Obligations and Commitments

There were no material changes outside the ordinary course of business to our specific contractual obligations during the three and six months ended June 30, 2017.

Critical Accounting Policies

For a discussion on our material changes in critical accounting policies, see “Recent Accounting Pronouncements” in the notes to the financial statements included in this Quarterly Report on Form 10-Q.

ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

Our primary exposure to market risk is interest rate sensitivity, which is affected by changes in the general level of U.S. interest rates. Due to the short-term maturities of our cash equivalents and marketable securities and the low risk profile of our investments, an immediate 10% change in interest rates would not have a material effect on the fair market value of our portfolio. Accordingly, we would not expect our operating results or cash flows to be affected to any significant degree by the effect of a sudden change in market interest rates on our investment portfolio.

We do not believe that our cash and cash equivalents have significant risk of default or illiquidity. While we believe our cash and cash equivalents do not contain excessive risk, we cannot provide absolute assurance that in the future our investments will not be subject to adverse changes in market value. In addition, we maintain significant amounts of cash and cash equivalents at one or more financial institutions that are in excess of federally insured limits.

Inflation generally affects us by increasing our cost of labor and clinical trial costs. We do not believe that inflation has had a material effect on our results of operations during the periods presented.

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ITEM 4. Controls and Procedures

Disclosure Controls and Procedures

Our management, with the supervision of our Chief Executive Officer and Vice President of Finance (our principal executive officer and principal financial officer, respectively), evaluated the effectiveness of our disclosure controls and procedures as of June 30, 2017. Our disclosure controls and procedures are designed to provide reasonable assurance that the information required to be disclosed in this Quarterly Report on Form 10-Q has been appropriately recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our principal executive and principal financial officers, to allow timely decisions regarding required disclosure. Based on that evaluation, our principal executive and principal financial officers have concluded that our disclosure controls and procedures are effective at the reasonable assurance level as of June 30, 2017.

Changes in Internal Control

There have been no changes in our internal control over financial reporting during our most recent fiscal quarter that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

PART II — OTHER INFORMATION

Item 1. Legal Proceedings.

On March 3, 2015, a verified class action complaint, captioned DePinto v. John S. Stafford, et al., C.A. No. 10742, was filed in the Court of Chancery of the State of Delaware against certain of the Company's current and former directors alleging cause of action for Breach of Fiduciary Duty and Invalidity of Director and Stockholder Consents. In general, the complaint alleged that the plaintiff and the class he seeks to represent were shareholders of the Company during the recapitalization and certain related transactions that the Company underwent in 2013 and that the defendants breached their fiduciary duties in the course of approving that series of transactions. It also challenged as invalid certain corporate acts taken in the 2013 time period.

The plaintiffs and the Company agreed to separate the litigation into two separate claims; Count I relating to the claim of Breach of Fiduciary Duty by the current and former directors of the Company and, Count II relating to the

Invalidity of Directors and Stockholders consents.

On December 14, 2015, the Delaware Chancery Court entered an Order and Partial Final Judgment approving the settlement of the invalidity claims, validating each corporate act challenged in the complaint, dismissing with prejudice Count II of the complaint (the invalidity claims) and granting plaintiff's counsel a fee award of \$950,000. We have paid the plaintiff's legal award cost of \$950,000 net of insurance proceeds of \$187,500 which has been reflected as a charge in our 2015 operations.

On September 27, 2016, the parties engaged in voluntary mediation and agreed to settle the complaint's remaining claims, Count II, for a total payment of \$2.375 million to the class certified by the Delaware Court of Chancery. The settlement was reached without any party admitting wrong-doing. Under the terms of the settlement, no payments shall be made to the plaintiffs by the Company or any of the defendants in the lawsuit other than payments covered by the Company's insurance.

On April 4, 2017, the Delaware Chancery Court approved the Settlement between the parties. On May 1, 2017, the Company's insurance carriers fully funded the settlement account.

We recognized legal costs related to the litigation as incurred and offset any insurance proceeds when approved and issued. At December 31, 2016, we reported the outstanding settlement amount of \$2.355 million as a payable and reflected a receivable of the same amount for the insurance coverage that will fund the settlement. This amount was paid by the insurance carrier on our behalf in May 2017.

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Item 1A. Risk Factors

For information regarding certain factors that could materially affect our business, results of operations, financial condition and liquidity, see the risk factor discussion provided under “Risk Factors” in item 1A of our Annual Report on Form 10-K for the year ended December 31, 2016. See also “Special Note Regarding Forward-Looking Statements” included in this Quarterly Report on Form 10-Q. In addition to the risks set forth in our Annual Report on Form 10-K for the year ended December 31, 2016, additional risks and uncertainties not currently known to us or that we currently deem to be immaterial may also materially and adversely affect our business.

Item 6. Exhibits

A list of exhibits filed as part of this Quarterly Report on Form 10-Q is set forth on the Exhibit Index, and is incorporated herein by reference.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

XENCOR, INC.

BY: /s/ BASSIL I. DAHIYAT
Bassil I. Dahiyat, Ph.D.
President and Chief Executive Officer
(Principal Executive Officer)

BY: /s/ JOHN J. KUCH
John J. Kuch
Vice President, Finance
(Principal Financial Officer)

Dated: August 7, 2017

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EXHIBIT INDEX

- 3.1 Amended and Restated Certificate of Incorporation of the Company (incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K, filed with the SEC on December 11, 2013).
- 3.2 Amended and Restated Bylaws of the Company (incorporated by reference to Exhibit 3.2 to the Company's Current Report on Form 8-K, filed with the SEC on December 11, 2013).
- 4.1 Form of Common Stock Certificate of the Company (incorporated by reference to Exhibit 4.1 to the Company's Registration Statement on Form S-1, as amended (File No. 333-191689), originally filed with the SEC on October 25, 2013).
- 4.2* Third Amended and Restated Investor Rights Agreement, dated June 26, 2013, among the Company and certain of its stockholders incorporated by reference to Exhibit 4.2 to the Company's Registration Statement on Form S-1, as amended (File No. 333-191689), originally filed with the SEC on October 11, 2013).

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|---------|---|
| 10.1* | Office Lease dated June 21, 2017 by and among the Company and PRII High Bluffs LLC and Collins Corporate Center Partners, LLC (incorporated by reference to Exhibit 99.1 to the Company's Current Report on Form 8-K filed with the SEC on June 26, 2017). |
| 31.1 | Rule 13a-14(a) Certification of Principal Executive Officer. |
| 31.2 | Rule 13a-14(a) Certification of Principal Financial Officer. |
| 32.1 | Section 1350 Certification of Principal Executive Officer and Principal Financial Officer. |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Schema Document |
| 101.CAL | XBRL Calculation Linkbase Document |
| 101.DEF | XBRL Definition Linkbase Document |
| 101.LAB | XBRL Labels Linkbase Document |
| 101.PRE | XBRL Presentation Linkbase Document |

* Indicates management contract or compensatory plan