

LPL Financial Holdings

4Q23E: '23 capital deployment levels not sustainable while NNAs remain strong

Maintain Rating: NEUTRAL | PO: 285.00 USD | Price: 255.27 USD

Core profit beat & strong organic growth continued

LPLA reported better than expected 4Q23 financial results including an EPS beat (\$3.51 vs. \$3.38 BofA / \$3.36 consensus) driven by brokerage commissions (annuities +10% q/q) along with other asset-based revenues; tax rate also came in lower. NNAs remained strong at +8% (ann.) despite no enterprise onboarding and were in its 7-12% target range. LPLA provided new 2024 targets and these metrics generally were favorable versus our expectations (including core G&A at \$1.455-\$1.490B x-PRU and 1Q24 payout ratio of 86.5%).

2023 buyback, liquidity/succession & TA not sustainable

In 2023, LPLA returned \$1.2B of capital to shareholders via buybacks and dividends which was 101% of its adjusted earnings. Additionally, LPLA grew its advisor loan balances by \$357M which includes loans to advisors for transition assistance (estimate 75% from 10-K). This was larger than its TA loan amortization (in promotional expenses) and also excludes \$100M q/q outflow for liquidity & succession. We note that this level of capital return (plus a one-time \$470M tax payment), which is supporting LPLA's strong NNAs and EPS growth, is not sustainable and we model less buybacks in 2024 (\$800M vs. \$1.1B in 2023).

Raising LT EPS & PO to \$285; Implies 18% total return

We raised our 1Q24/2025/2026 EPS estimates to \$4.23/\$21.73/\$25.93 from \$3.89/\$20.92/\$25.12 driven by adjustments to client cash revenues and expenses (following new guidance). We apply a 11x multiple on 2026 EPS to arrive at our \$285 PO (previously \$276) which implies +18% total return potential. LPLA historically traded at between a range of 10-17.5x EPS while its closest public comps (RJF, SF) currently trade at 8-11x.

Reiterate Neutral but forecast upside to '25 consensus

In our view, LPLA offers an attractive EPS algorithm that includes 8-10% organic growth + 6% beta with both combining to 15% revenue growth. If one were to apply operating leverage and capital management (including M&A potential), it would imply LPLA could generate annualized EPS growth of 20% or even higher in active deployment years. What is most important relative to peers is LPLA's stable ROCA trajectory, as its economics (x-cash sweep) have demonstrated resiliency over the last few years. However, LPLA remains one of the most sensitive names to Fed rate cuts in our coverage and appears to be a crowded long based on our investor conversations and ownership data.

Estimates (Dec) (US\$)	2021A	2022A	2023E	2024E	2025E
EPS	7.32	11.53	15.19	16.83	21.73
EPS Change (YoY)	10.4%	57.5%	31.7%	10.8%	29.1%
Consensus EPS (Bloomberg)			15.44	16.25	19.58
DPS	0.99	0.98	1.19	1.48	1.83
Valuation (Dec)					
P/E	32.8x	20.9x	15.8x	14.3x	11.1x
Dividend Yield	0.4%	0.4%	0.5%	0.6%	0.8%

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Timestamp: 02 February 2024 12:13PM EST

02 February 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	276.00	285.00
2023E Rev (m)	4,114.6	4,132.9
2024E Rev (m)	4,455.4	4,526.6
2025E Rev (m)	5,032.9	5,111.0
2023E EPS	15.07	15.19
2024E EPS	15.99	16.83
2025E EPS	20.92	21.73
2023E DPS	1.18	1.19

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Stock Data

Price	255.27 USD
Price Objective	285.00 USD
Date Established	2-Feb-2024
Investment Opinion	B-2-7
52-Week Range	179.00 USD -257.65 USD
Mkt Val / Shares Out (mn)	19,304 USD / 75.6
Free Float	98.6%
Average Daily Value	141.99 USD
BofA Ticker / Exchange	LPLA / NAS
Bloomberg / Reuters	LPLA US / LPLA.OQ
ROE (2023E)	0%
ESGMeter™	High

Please refer to "BofA ESGMeter Methodology".

NNA – net new assets
TA – transition assistance
RJF – Raymond James Financial
SF – Stifel Financial
ROCA – Revenue on client assets

iQprofileSM LPL Financial Holdings

Income Statement Data (Dec)	2021A	2022A	2023E	2024E	2025E
(US\$ Millions)					
Net Revenues	2,541	3,276	4,133	4,527	5,111
Compensation & Benefits	(1,494)	(1,665)	(2,041)	(2,388)	(2,516)
% of Net Revenue	58.8%	50.8%	49.4%	52.7%	49.2%
Non-Compensation Expenses	(421)	(500)	(647)	(829)	(876)
Net Income to Ordinary Shareholders	484	846	1,066	969	1,272

Balance Sheet Data (Dec)	2021A	2022A	2023E	2024E	2025E
(US\$ Millions)					
Total Assets	7,992	9,482	10,385	10,401	10,749
Deposits	NA	NA	NA	NA	NA
Long Term Debt	2,814	2,717	3,734	3,734	3,734
Total Equity	1,671	2,168	2,079	1,749	1,749

Sector Metrics (Dec)	2021A	2022A	2023E	2024E	2025E
(US\$ Millions)					
DARTs	NA	NA	NA	NA	NA
Net Interest Margin	NA	NA	NA	NA	NA
Interest Earning Assets	49	66	50	52	60
Net New Assets	0	0	0	0	0
Growth	0%	0%	0%	0%	0%
Total Client Assets	1,206	1,111	1,354	1,585	1,796

Performance Metrics (Dec)	2021A	2022A	2023E	2024E	2025E
(US\$ Millions)					
Operating Margin	24.6%	33.9%	35.0%	28.9%	33.6%
Net Profit Margin	23.5%	28.6%	28.6%	27.8%	30.8%
Comp Expense/Revenue	58.8%	50.8%	49.4%	52.7%	49.2%
Non-Comp Expense / Revenue	16.6%	15.3%	15.7%	18.3%	17.1%
Net Revenue Growth	16.8%	28.9%	26.2%	9.5%	12.9%

Company Sector

Asset Management

Company Description

LPLA is the largest independent broker-dealer in the United States with \$1.2Tn in client assets. The firm supports more than 22,000 financial advisors nationwide, through a number of services including brokerage & advisory, investment solutions, technology and cybersecurity platforms, operational support and compliance oversight.

Investment Rationale

LPLA operates a high-growth and capital-light business model and has continued to expand the capabilities that it provides its advisors. We believe LPLA's current organic growth rate is sustainable longer-term with the firm expanding into higher growth segments (pure RIA) and has used M&A to accelerate its growth/competitive positioning. LPLA is sensitive to interest rates and Fed rate cuts could trigger negative EPS revisions.

Quarterly Earnings Estimates

	2022	2023
Q1	1.95A	4.49A
Q2	2.24A	3.94E
Q3	3.13A	3.74E
Q4	4.21A	3.51E

Additional information

ICA 2H24 reinvestments should help offset Fed rate cuts

LPL has \$6.5B of fixed rate ICA balances maturing in 2024 (\$0.5B in 1Q24) yielding 250bps. Today, LPLA could reinvest at 400-420bps (3-5Y swap curve at 370-390bps + 30bps spread) which would support a \$100M increase in gross profit and help to mitigate the impact of Fed rate cuts on its floating rate contracts. LPL's variable contracts are especially susceptible to sorting as they are most easily accessible source of liquidity while simultaneously having the highest yields (5.43-5.48% yield near current Fed Funds rate).

Cash sorting & cash allocation declines both continued

LPLA's client cash allocations continued to grind lower in 4Q23 (3.6% vs. 3.8% in 3Q23, 4.0% in 2Q23, 4.6% in 1Q23). This was despite the seasonal cash builds from rebalancings, tax-loss harvesting and distributions (mostly in December). Additionally, we expect these seasonal trends to reverse in January and February as clients reinvest. Management commented that cash balances overall were down \$1.2B for the month in January. Sorting continues (evidenced by strong net buying activity) but is well below the levels of 1H23.



Price objective basis & risk

LPL Financial Holdings (LPLA)

Our price objective (PO) for LPLA is \$285 and is derived from a price to earnings method. We apply a 11x multiple to our 2026E to obtain our PO. Its closest public comps currently trade at 8-11x consensus EPS, but we think that LPLA offers a higher growth trajectory and its business model is less capital intensive.

Risks to our PO are sustainability of its long-term growth, revenue pressure from maturing fixed contracts, soft deposit demand from third party banks, risk of Fed rate cuts, and elevated financial leverage.

Analyst Certification

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US - Brokers, Asset Managers, & Exchanges Coverage Cluster

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	Ameriprise Financial	AMP	AMP US	Craig Siegenthaler, CFA
	Ares Management Corp	ARES	ARES US	Craig Siegenthaler, CFA
	BlackRock, Inc.	BLK	BLK US	Craig Siegenthaler, CFA
	Blackstone	BX	BX US	Craig Siegenthaler, CFA
	Blue Owl Capital	OWL	OWL US	Craig Siegenthaler, CFA
	Cboe Global Markets	CBOE	CBOE US	Craig Siegenthaler, CFA
	Interactive Brokers	IBKR	IBKR US	Craig Siegenthaler, CFA
	Intercontinental Exchange	ICE	ICE US	Craig Siegenthaler, CFA
	KKR & Co. Inc.	KKR	KKR US	Craig Siegenthaler, CFA
	Raymond James Financial	RJF	RJF US	Mark McLaughlin, CFA
	TPG Inc	TPG	TPG US	Craig Siegenthaler, CFA
	Tradeweb Markets Inc.	TW	TW US	Craig Siegenthaler, CFA
	Victory Capital Holdings, Inc.	VCTR	VCTR US	Craig Siegenthaler, CFA
	Virtu Financial	VIRT	VIRT US	Craig Siegenthaler, CFA
NEUTRAL				
	Affiliated Managers Group	AMG	AMG US	Craig Siegenthaler, CFA
	Apollo Global Management	APO	APO US	Craig Siegenthaler, CFA
	Brookfield Asset Management	BAM	BAM US	Craig Siegenthaler, CFA
	CME Group Inc	CME	CME US	Craig Siegenthaler, CFA
	Invesco	IVZ	IVZ US	Craig Siegenthaler, CFA
	Janus Henderson Group	JHG	JHG US	Craig Siegenthaler, CFA
	LPL Financial Holdings	LPLA	LPLA US	Craig Siegenthaler, CFA
	Patria	PAX	PAX US	Craig Siegenthaler, CFA
UNDERPERFORM				
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	Franklin Resources	BEN	BEN US	Craig Siegenthaler, CFA
	Nasdaq	NDAQ	NDAQ US	Craig Siegenthaler, CFA
	Robinhood Markets	HOOD	HOOD US	Craig Siegenthaler, CFA
	T. Rowe Price	TROW	TROW US	Craig Siegenthaler, CFA
	The Carlyle Group	CG	CG US	Craig Siegenthaler, CFA

iQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

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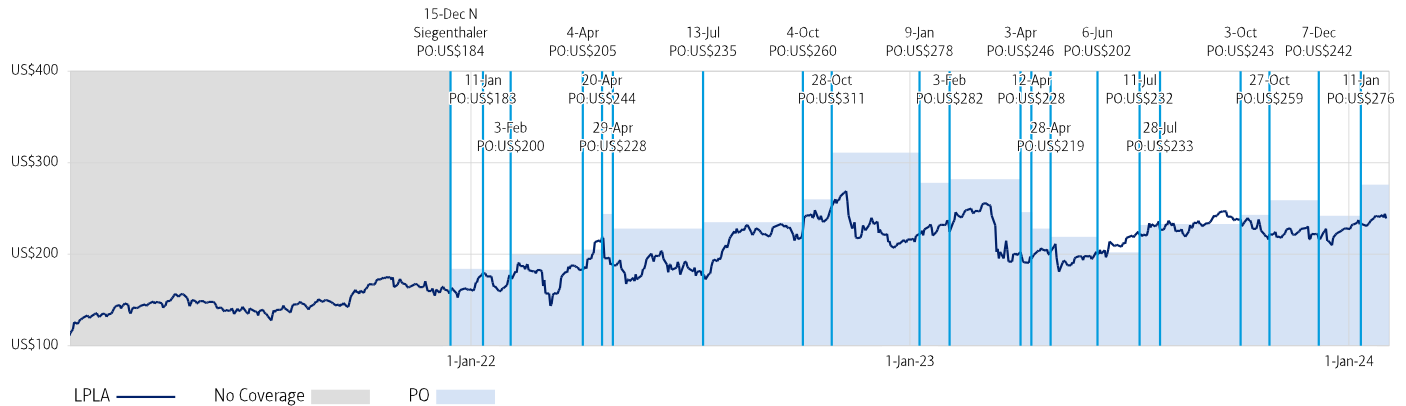
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LPL Financial (LPLA) Price Chart



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Equity Investment Rating Distribution: Financial Services Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	156	53.79%	Buy	94	60.26%
Hold	72	24.83%	Hold	48	66.67%
Sell	62	21.38%	Sell	35	56.45%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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