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LPLA - Q1 2019 LPL Financial Holdings Inc Earnings Call

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PRESENTATION

Operator

Good afternoon, and thank you for joining the first quarter 2019 earnings conference call for LPL Financial Holdings Inc. Joining the call today are our President and Chief Executive Officer, Dan Arnold; and Chief Financial Officer, Matt Audette. Dan and Matt will offer introductory remarks and then the call will be opened for questions. (Operator Instructions) The company has posted its earnings press release and supplementary information on the Investor Relations section of the company's website, investor.lpl.com.

Today's call will include forward-looking statements, including statements about LPL Financial's future financial and operating results, outlook, business strategies and plans as well as other opportunities and potential risks that management foresees. Such forward-looking statements reflect management's current estimates or beliefs and are subject to risks and uncertainties that may cause actual results to differ materially. The company refers listeners to the safe harbor disclosures contained under the caption Forward-Looking Statements in the earnings press release as well as the company's latest SEC filings to appreciate those important factors that may cause actual financial or operating results or the timing of matters to differ from those contemplated in such forward-looking statements.

During the call, the company will also discuss non-GAAP financial measures governed by SEC Regulation G. For a reconciliation of such non-GAAP measures to the comparable GAAP figures, please refer to the company's earnings release, which can be found at investor.lpl.com.

With that, I will now turn the call over to Mr. Arnold.

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Thank you, Carmen, and thank you to everyone for joining today's call. In the first quarter, we remained focused on our strategic priorities of growing our core business and executing with excellence. This focus, combined with strong investor engagement and the support of macro environment, led to another quarter of business and financial growth.

Let's review our first quarter progress, starting with recent feedback from advisers at 2 of our larger conferences. Advisers tell us their experiencing a renewed focus on them and how we are helping to expand their value through new capabilities and the way we're making it easier to do business by taking friction out of the system. They are enthusiastic about our continued focus on these areas and our vision to deliver an experience that is unique in the wealth management space.

Moving to our first quarter financial results, we continue to generate growth as gross profit increased 20% year-over-year. Additionally, while we invested for growth, we stayed disciplined on expenses to drive operating leverage. As a result, first quarter EPS prior to intangibles was $1.93, which was up over 70% from a year ago.

Turning to our first quarter business performance, our brokerage and advisory assets were $684 billion, up 6% year-over-year. This increase was primarily driven by a combination of organic growth and higher equity market levels. Looking more closely at first quarter organic growth, net new assets were $4 billion, which translated to a 2.5% annualized growth rate. Organic growth strengthened throughout the quarter as we move beyond the impact of December volatility. This included positive trends and new store sales as prospective advisers reengaged in recruiting dialogues and in same-store sales as investors move back into the market.

Let's now turn to executing on our strategic priorities, starting with core business growth. We think about that primarily as adding and retaining advisers, helping our advisers grow and driving a better return on assets. To achieve these outcomes, we are investing in capabilities in 3 key areas: digitizing adviser practices, enriching the quality of advice and modernizing practice management. Today, we want to highlight 2 of these areas. First, we continue to see a big opportunity to digitize key workflows that will help advisers transform their business. One of the most important workflows is turning prospects into clients. So in Q1, we introduced new CRM solutions, rolled our goals-based planning and as a results of our acquisition of AdvisoryWorld, integrated our new proposal generation solution. With these separate capabilities integrated into 1 streamline workflow, our advisers can now more efficiently add clients to their practice.

In addition to digitizing workflows, we are investing in new capabilities to enhance the value and flexibility of our advisory platforms. We recently introduced our adviser sleeve solution, which allows advisers to use their own asset allocation models in centrally managed platforms, while outsourcing to us the day-to-day work of portfolio allocation and trading. This gives advisers another way to leverage our centrally managed platforms to meet client needs, while helping them drive efficiency in their practices.

Pricing also remains an important strategic lever to help advisers differentiate and win. Over the past few years, we have developed one of the most robust no transaction fee mutual fund offerings in the marketplace. And we've seen advisers increase their utilization as a result. We now have a similar opportunity with ETFs. In partnership with sponsors, later this year, we plan to reduce transaction charges on select ETFs from $9 to $5, which will provide advisers with simpler and lower advisory pricing for their clients.

Financially, this offering will be roughly neutral for us, as we are in sponsor revenue from ETF manufacturers in place of transaction revenue. We believe our investments and capabilities are helping advisers with what matters most to them, driving growth, creating scalability and lowering their cost. As a result, this makes our platform an increasingly compelling place for existing and prospective advisers to thrive, which in turn benefits our growth.

Let's now turn to our second strategic priority, executing with excellence. We think about this as enhancing ClientWorks, driving continuous improvement, evolving our service model and transforming our culture. We continue to invest in and evolve our ClientWorks technology platform to increase its value and differentiation. In the first quarter, we completed ClientsWorks 1.0, and now we are working to deliver new features as part of ClientsWorks 2.0. The focus of version 2.0 is creating more streamlined and intuitive experiences across core functionality, such as new account opening, cash management and account transfers. Rolling out these enhancements will help advisers save time and increase their capacity to serve clients.

Turning to continuous improvement. One of the most important elements of this initiative is capturing adviser feedback and translating it into insights that we can learn from and effectively apply. In the first quarter, we launched the alpha version of our new transactional survey, that enriches our feedback with real-time data. Now this data will help us accelerate our learning, and thus make us more nimble and agile and continuously improving our operating platform.

More broadly, we're working to transform our service model by moving from a traditional call center to a customer care approach. At a high level, this customer care model has 3 primary elements: providing multiple channels for advisers to engage with us, intelligent routing of their inquiries and case management for complex issues. This model gives advisers simpler access to information and more accurate support without having to navigate a service center. We've seen this model work in other industries and we're excited to bring this solution to our advisers.

And before closing, I want to highlight our ongoing efforts to transform our culture, which is instrumental to executing our strategy. As a reminder, we are taking a structured approach by instilling a client-centric mindset, logic-based thinking and mission-driven alignment. Last quarter, we rolled out a new mission. And this quarter, we are starting to bring the mission to life with a set of new values that will guide our behavior in decision-making in our daily work. Our advisers tell us they're excited about the cultural transformation that is taking hold and see it as a catalyst for continuing positive change in their service and experience.

In summary, we're pleased to deliver another quarter of business and financial growth. We plan to remain focused on our strategic priorities of growing our core business and executing with excellence. We believe this focus positions us well to serve our advisers, drive profitable growth and create long-term shareholder value.

With that, I'll turn the call over to Matt.

Matthew Audette - *LPL Financial Holdings Inc. - CFO*

All right. Thank you, Dan. And I'm glad to speak with everyone on today's call. We started 2019 with another quarter of business and earnings growth. We grew assets and gross profit and invested to drive growth, while still delivering operating leverage. As a result, our Q1 EPS prior to intangibles was $1.93, up 74% from a year ago. We are pleased with these results and we continue to focus on executing our strategy.

Let's now review our Q1 business results in greater depth, starting with total brokerage and advisory assets. We finished the quarter at $684 billion, up 9% sequentially, driven by the rising equity markets and organic growth. Total net new assets for Q1 were $4 billion, which translates to a 2.5% annualized growth rate. Our pace of growth increased throughout the quarter as advisers return to asset gathering and recruiting ramped following the slowdown in December, driven by elevated market volatility.

More specifically, net new assets were $0.7 billion in January, $0.9 billion in February and $2.3 billion in March. We also continue to see positive mix shifts in Q1. Advisory assets increased to 46% of total assets, driven by a 7% organic growth rate. Within advisory, the majority of net new assets were on our corporate platform. And we added $1 billion of inflows to our centrally managed platforms.

Now let's turn to our Q1 financial results, starting with gross profit. It was $556 million, up $48 million or 9% sequentially. Looking at the components of gross profit, commission and advisory fees net of payout were $116 million in Q1, down $35 million from Q4. The decrease was driven by the standard mark-to-market of our adviser deferred commission program, which was $47 million this quarter. As a reminder, this increase has offset entirely in other revenue, so the net effect on gross profit is 0. Prior to deferred commission expense, net commissions and advisory fees increased $12 million sequentially, primarily driven by the seasonal decline in production bonus expense. Looking ahead, as a reminder, our production bonus payout rate increases seasonally from Q1 to Q2. I would also note that we had a $3 million benefit in Q1 related to our 2018 payout, which came in slightly below our expectations.

Turning back to Q1 and asset-based revenues. Sponsor revenues were $123 million, up $5 million from Q4. The increase was primarily driven by a sponsor contract we renegotiated, which included a catch-up payment of $4 million related to 2018 activity.

Moving to cash sweep revenues, they were $173 million, up $25 million or 17% sequentially, primarily driven by higher ICA yields. Cash rebalances were $30.7 billion, down $4.1 billion sequentially from client net buying activity of $13 billion, which was the highest quarterly level we have seen. Additionally, I would highlight that the decline in ICA was from our floating rate balances. So while we did not enter into any new fixed rate agreements this quarter, our mix of fixed rate balances increased to about 40% of the ICA portfolio. As a reminder, we do not have many ICA contracts up for renewal in 2019. So while we expect to increase our fixed rate balances even further over time, we do not have many opportunities to shift additional balances this year.

Turning back to our cash sweep yields for Q1. Our ICA yield was 250 basis points, up 35 basis points from Q4. This increase was primarily driven by the full quarter benefit of the fixed rate contracts we executed in Q4, higher average short-term rates and the higher mix of fixed rate balances.

Looking ahead to Q2, we expect our ICA yield to decline slightly, driven by the full quarter impact of our January increase in client deposit rates and the recent decline in LIBOR. Combining those 2 factors and assuming no further changes in the short-term interest rates, client deposit rates or fixed versus floating mix, we estimate our Q2 ICA yield will be in the mid to upper 240 basis point range.

Let's now move on to Q1 transaction and fee revenues. They were $122 million, up $3 million from Q4. The increase was primarily from seasonally higher IRA fees, partially offset by slightly lower transaction revenue. Looking ahead to Q2, we expect transaction and fee revenues to decline by roughly $6 million, primarily driven by seasonally lower transaction volume.

Now turning to expenses. Core G&A was $213 million in Q1, down $4 million sequentially. This was primarily driven by lower professional fees, partially offset by a seasonal increase in compensation expense.

Looking ahead, we continue to anticipate full year 2019 core G&A to be in a range of $850 million to $875 million. As for the timing of expenses, we expect them to ramp through the year as we continue investing in technology and service to help drive growth.

Moving on to Q1 promotional expenses. They were $51 million, up $6 million or 14% sequentially. This was primarily driven by increases in conference expense and transition assistance as expected, partially offset by seasonally lower marketing expense. Looking ahead, we expect Q2 promotional expense to be roughly in line with Q1.

Moving to share-based compensation expense. It was $8 million in Q1, up from $5 million in Q4. Looking ahead to Q2, we expect share-based compensation expense to be at a similar level to Q1.

Turning to depreciation and amortization. It was $23 million, up $2 million sequentially. We expect depreciation and amortization to rise over time as we continue to invest in technology to drive growth.

Looking at our EBITDA margins relative to our gross profit, it increased to 49.7% in Q1, as we grew gross profit and continue to invest to drive growth, while delivering operating leverage.

Moving on to capital management, our balance sheet remained strong in Q1. Cash available for corporate use was $376 million and our credit agreement net leverage ratio was down slightly to 2.05x.

Turning to capital deployment, our priorities remain investing for organic growth first and foremost. Taking advantage of M&A opportunities if they arise and returning capital to shareholders. Looking at organic growth, our investments are focused on recruiting new advisers, helping existing advisers to grow and enhancing our technology.

In addition to our investments for growth, we returned excess capital to shareholders in Q1. This included $125 million of share repurchases, in line with our plan to complete our $1 billion authorization over roughly 2 years. Looking back over the last year, we repurchased 7.3 million shares or 8% of our total shares outstanding. In Q1, we also returned capital through $21 million of regular quarterly dividends.

In closing, we are pleased to have started 2019 with another quarter of strong business and financial results. We remain focused on growing assets and gross profit, investing to drive organic growth, while staying disciplined on expenses and returning excess capital to shareholders.

With that, operator, please open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Steven Chubak with Wolfe Research.

Steven Joseph Chubak - *Wolfe Research, LLC - Director of Equity Research*

Dan, I wanted to start with a question on some of the drivers of the strong organic growth that you cited and improve momentum again in the quarter, certainly encouraging to hear. Now at the same time, there continues to be a lot of M&A activity in the space. And I was wondering if you could provide some updated thoughts about your appetite for M&A? And separately, can you discuss some of the benefits you're seeing in adviser recruitment as a result of some increased consolidation, much of which has been driven by the thesis?

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Yes, so Steve, there's a lot there. So if I don't get it all, please just follow up. So let me start with maybe your question around how we think about acquisitions versus organic growth. And I think as Matt just said in his remarks, that strategically our first priority remains organic growth, where we return on investment is the highest. That said, I think we always are interested in potentially complementing that organic growth with some M&A opportunity should it occur and should it arise. With that lens that we always share with you, that it's aligned strategically, financially and operationally. And so we do believe there will be ongoing consolidation that will create opportunity for us to do an acquisition that would bring new advisers to the platform and so we will continue to explore those possibilities, again, all with good discipline around how we think about that.

Now when those transactions occur, as you say, it does create recruiting opportunity out in the marketplace. So as we pivot over to how we think about recruiting, if you look at our recruiting over the last several quarters, we've had pretty strong results. In fact, we had a little over $7 billion and recruited AUM in the first quarter. And if you actually look back over the trailing 12 months, we had a little over $30 billion in recruited AUM. It's the first time we've ever had that.

And so I think you begin to sort of peel that back and go, hey, what's happening there, what do you think you're having success there. And there's a couple of things. I think part of that is as I've shared with you, we've been working hard to improve the efficacy of our own teams recruiting capabilities and business development capabilities. And we've continued to evolve and transform how that group and unit works. And it's really encouraging to see the progress they're making, whether it be new sales processes and structures, new ways of which to use data and digital to better target the marketplace for opportunities.

So we're seeing them continue to grow a healthier and healthier pipeline and do a better job of pulling through those prospects once they're in the pipeline. You match that up with where we aligned our transition assistance with financial returns, and we think those 2 things bode well for our continued ability to recruit going forward, but also a more reflective of the success that we've had in the past other than any sort of circumstance out in the marketplace like a transaction that created a short run more episodic opportunity. And again, I think that's what we're trying to do is build the fundamentals and foundation, so they're more repeatable and sustainable predictor of your outcome versus just relying on some market circumstance.

That said, we don't ignore. If there's an opportunity out in the marketplace that comes, we certainly try to allocate resources to those opportunities. So hopefully that gives you a little answer of how we think about both M&A with -- M&A specifically focused on adviser acquisition and then how we're thinking about recruiting. Let me pause there. You may have had a question about organic growth, but I'll let you follow up if you want me to drill down on that.

Steven Joseph Chubak - *Wolfe Research, LLC - Director of Equity Research*

Nice, it's really helpful color, Dan. I really wanted to focus on the M&A side. So I appreciate all that context. Matt, just a question for you. Given the macro backdrop has been quite volatile over the past 6 months, I was hoping to hear your perspective on how you're feeling at this point in the year? And how it's going to impact your thoughts specifically around the areas like expanding capital management? Do you still feel good about the core G&A outlook and ongoing repurchases? And more specifically, was your original guidance dependent on continued rate hikes in '19.

Matthew Audette - *LPL Financial Holdings Inc. - CFO*

Yes. So we -- so I feel good. And I think we're well positioned, especially given our business models get natural macro hedges built into it, as equity markets and cash rebalances tend to move in opposite directions. So maybe a little bit reminder, the sensitivity there, every 100-point move in the S&P is about a $25 million impact for us. And every $1 billion change in cash rebalances is about a $20 million impact, right? So if you just look at the last 2 quarters, I think to the point of your question, when we look at Q4, we saw the S&P go down by about 300 points, but our cash balance has increased meaningfully, $5 billion just in the month of December, over $6 billion for the quarter. And then when you look at this quarter Q1, you saw the markets recover and they were up almost in equal and offsetting amount at about 300 points and then cash rebalances went back into market declined by a little over $4 billion. So just looking at those moves over the last couple of quarters, you can see they roughly offset each other. So I think getting to the core of your question from a strategic perspective for us, these natural hedges, combined with where we have the balance sheet positioned which is a really strong position, I think, allows us to consistently focus on our clients and what's best for them. So investing in capabilities, investing in technology, investing in service, all things are going to improve their experience and we think drive growth over the long term. So we think it's really good. It's real differentiator for us and really a driver of growth over the long term. And I'd say the same thing plays through on the capital allocation side, whether it be share repurchases or as Dan was just discussing, M&A if it comes up, I think, we positioned ourselves well even with an environment like we saw over the last 6 months to be able to be consistent in a steady deployer of capital in all those areas.

Operator

And our next question is from Bill Katz with Citi.

William R. Katz - *Citigroup Inc, Research Division - MD*

So just in terms of your opening commentary, Dan, it certainly seems like there's a lot of traction and new asset growth. How much of the investment spending and some of these technology enhancements you're making today, which sort of puts you in front of competition rather than sort of playing catch up, if you will?

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Bill, I think, look, we're beginning on a journey from an investment standpoint, and you kind of look at that over a multi-year period of the time, right? It starts with your strategic framework and then how you think about allocating those resources. And I think certainly, we think we have good solid strengths out in the marketplace and we continue to try to invest in those, such that they further help us differentiate and create more appeal in the model. There's other places, where I think we acknowledged we had work to do, and we tend to run right at that and take that on and challenge ourselves to say how are we going to improve and enhance those capabilities, such that not only do we just catch up in that area or fill the gap but we continue then to push it on forward in order to create a differentiated experience. So if I summarize that, then we tend to start with our strategy, which is focused on creating capabilities for our advisers to help them differentiate and win. We absolutely want to be a leader in that area. And then secondly, we've been focused on how do we improve that adviser experience in the form of technology processes' capabilities, and we want to be a leader in that area. And so to the extent that we look at our opportunities to invest, we start there with the mindset being what's that journey to ultimately be the best. And so that's kind of how we frame up and think about allocating our capital and human resources towards those efforts. I hope I answered your question.

William R. Katz - *Citigroup Inc, Research Division - MD*

That's helpful. And just my follow-up, just in terms of where are we in terms of the IFP exposure? And then is there any way to sort of think about what kind of trends we're seeing into April and May? And related to them, I was a little surprised I didn't see a better commissions per adviser metric given the elevated buying. So was there any sort of adverse mix shift here? Was that maybe a part of the pricing change you made?

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Yes. Let me start with IFP, and then we'll try to walk those down. So with respect to your IFP question, I think, in short we -- as sort of we closed that effort out, we'll end up retaining roughly 2/3 of the assets. So let me give you a little color as to how we walk down and get to that place. So if you remember, if you look at the assets that IFP started with, it was about $12 billion of brokerage and advisory assets on our platform. Roughly, retaining 2/3 of those is $8 billion that will stay on our platform, which means roughly $4 billion will transition off. About $0.5 billion of that left in Q1, which means the remaining $3.5 billion will come out in Q2, probably more specifically in the May and June periods of time, associated with their transition date.

If you look at that through slightly different metrics, perhaps on an adviser basis, we retained a little more than 50% of the advisers, which would suggest we retained on balance the more productive advisers. So we think, all-in, that's a pretty good outcome. Hopefully, that answers your IFP question.

With respect to your organic growth question and sort of how are we thinking about things as we move into second quarter, I think, again, Q1 was pretty strong. We had $4 billion of net new assets roughly annualized, 2.5% growth. As we move into second quarter, we saw strengthening in Q1, which certainly takes momentum -- takes us with momentum going into Q2. We delivered a number of capabilities in Q1 and early Q2, which certainly will support and enhance the appeal of the platform. You continue the good strong work of our organizations from an efficacy standpoint and their sales efforts. So we feel good about the prospects for organic growth in the second quarter. There are a couple of items that I would call out that are just things to remember. One would be IFP and the $3.5 billion that will come out associated with that. And then as always, we have that seasonal tax period, where people are paying their taxes, and so you typically see the first half of April where people will be using some cash in their accounts to pay their taxes. So that's something to think about in Q2. I hope that answers your questions on Q2. Matt, I'll let you take the third question, which is around adviser productivity.

Matthew Audette - *LPL Financial Holdings Inc. - CFO*

Yes. So Bill on commission advisory fees, I'll just highlight a couple of things. One, on the sales commission side, there's just 2 less trading days in the quarter than the prior quarter. And then just a reminder on the advisory fee side, that's -- the fees in Q1 are primarily driven on where assets ended the fourth quarter. So what you see this quarter is the flow-through effect of the decline in the market in Q4, which all else being equal, you would see that we recover when you see results in Q2. So those are the 2 things that, I think, make that trend a little bit counterintuitive.

Operator

And our next question comes from Alex Blostein with Goldman Sachs.

Alexander Blostein - *Goldman Sachs Group Inc., Research Division - Lead Capital Markets Analyst*

So just -- Dan, just a follow-up on your point around some of the seasonal factors in April, maybe just an update on where cash balances stand with you guys currently on the back of the tax season? And obviously, the markets have been reasonably robust, so presumably there has been more kind of deployment back in the market.

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Yes. So if I just drill down on April a bit, knowing that we'll give you our monthly metrics here in a couple of weeks. So let me give you a directional sense of how we think about April as context. As you say, you've got the tech seasonality going on in the height of the paying of those taxes in the first half of April, certainly the equity markets moved up, which all in all is a good context for activity. So I would say, given those 2 things, we saw what we would have expected in April. Asset levels moving up consistent with equity markets and good activity associated with investor reengagement or strengthening investor engagement. We certainly saw cash balances decrease in the month, given both tax payments and solid investor engagement. And then finally, the pace of NNA was solid in the second half of the month past tax season. So hopefully, that gives you, Alex, a little sense of some of the color around April.

Alexander Blostein - *Goldman Sachs Group Inc., Research Division - Lead Capital Markets Analyst*

Great. No, that's definitely helpful. And then slightly bigger picture question. On the metric that you guys disclosed around recruited assets, did the pace that you alluded to on a net new asset recruiting kind of short up there as well, meaning that just kind of really accelerated towards the end of the quarter. And as we think about the next couple quarters, should we anticipate the recruited asset level kind of return to the run rate we saw in the back half of last year kind of $8 billion to $9 billion range?

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Yes. So we did see a pickup as we move through the quarter as you get further away from the volatility and advisers logically would reengage in those recruiting discussions and dialogue. That said, I never would suggest that 1 quarter would be predictive of another. I think with respect to recruiting rights, it's hard to define it within a 90-day period of time. And that said, I would say our aspirations for working on new store sales and driving our recruiting efforts definitely have a desire to continue to increase them and our work is pointed towards continuing to improve that trend over time. That said, it's just hard to predict quarter-to-quarter.

Operator

And our next question comes from Craig Siegenthaler with Crédit Suisse.

Craig William Siegenthaler - *Crédit Suisse AG, Research Division - MD*

So we understand that 1Q was somewhat of an anomaly with the decline in client cash, just given the high starting point in December. But how should we think about further downside decline in cash and incremental sorting if the risk on backdrop here continues?

Matthew Audette - *LPL Financial Holdings Inc. - CFO*

Yes, Craig, I'll take that one. I mean, I think when you think about where cash can go from here, I mean, I think history is best guide and it's really market driven, right? When markets are increasing and growing like we're seeing right now, cash tends to get deployed in the market. And you've seen us kind of hover in that 4%, 4.5% range. And then when you have periods of volatility like we -- clients typically hold more cash like we just saw happen in December, where cash went from about 4.5% of AUM to 5.6 or a full percentage point in just 1 month. So I think those trends are probably the best way to -- best thing to think about or look at from cash level standpoint. I would highlight that clients typically maintain some amount of cash in their accounts, just to facilitate trading and rebalancing and the paying of fees or chewing up cash to take disbursements. So if you look at our lowest level of cash balances, you go back to Q3 of last year, they were in the low 4% range, almost right at 4%. And I'd say that fell pretty close to the minimum level you would hold for those factors. So that's probably the best thing I can point to and give you some context there.

Craig William Siegenthaler - *Crédit Suisse AG, Research Division - MD*

And so Matt, I know you won't add LPLA in the last cycle. But if you -- I don't know if you have the data, but if you think about 2006 and 2007, do you guys recall where client cash sweep bottomed? And if it was higher than current levels, which, I think, it probably. Do you think the relationship here has changed? Or is it just a function of a tenurable market?

Matthew Audette - *LPL Financial Holdings Inc. - CFO*

Yes. I think the general performance of sweep accounts is pretty similar across our space. And I think where the lowest we've really gotten is what I just referenced last -- from a percent of AUM was last year. On the other end of that, the highest cash ever got as a percent of AUM was just under 10% when markets -- when volatility peaked at the end of the last cycle. So those are probably the 2 bookends I would think about on where cash could go.

Operator

Our next question is from Chris Harris with Wells Fargo.

Christopher Meo Harris - *Wells Fargo Securities, LLC, Research Division - Director and Senior Equity Research Analyst*

Sorry if I missed it, but what drove the pretty large step-up in the DCA fee rate in the quarter, was that all attributable to the move in interest rates?

Matthew Audette - *LPL Financial Holdings Inc. - CFO*

Yes, I mean...

Christopher Meo Harris - *Wells Fargo Securities, LLC, Research Division - Director and Senior Equity Research Analyst*

It seems like a large move.

Matthew Audette - *LPL Financial Holdings Inc. - CFO*

Yes. I mean, DCA has got 2 things. It always makes the moves in a short period of time, a little bit noisy. One, remember, it's -- the fees are a fee per account. So we quoted in basis points, but they're actually charged as a fee per account and balance has moved and went down. So you get a little bit of noise of that and the timing with which the fee change gets made following a rate hike that we had at the end of the fourth quarter. So it's those 2 things that make it a little bit noisy. But at it's core, it's the rates went up and balances went down. So those are the 2 things that drove that up.

Christopher Meo Harris - *Wells Fargo Securities, LLC, Research Division - Director and Senior Equity Research Analyst*

Okay. In terms of your production expense, the production-based bonuses was actually a bit lower than we thought and kind of flattish year-on-year. But I thought there was a pricing increase that supposed to flow through there that which was going to push it up. So what was the offsetting factor there?

Matthew Audette - *LPL Financial Holdings Inc. - CFO*

Yes, Chris, so that was the $3 million benefit that I referred to in the prepared remarks. We ended up -- our 2018 payout ended up being a little bit less than we had estimated. So you see that correction or that benefit coming through in that line. Without that, it would have been an increase as you suspected due to the pricing change because that -- it does show up in that line item. So you'll see that increase next quarter.

Operator

Our next question is from Devin Ryan with JMP Securities.

Devin Patrick Ryan - *JMP Securities LLC, Research Division - MD and Senior Research Analyst*

Just another one here on cash and, I guess, yield expectations. I always appreciate the outlook. If the Fed is on pause for a while, do you see room to maybe bring down the cash pay rates? Or is there something you maybe look at for certain clients of segments that are less sensitive?

Matthew Audette - *LPL Financial Holdings Inc. - CFO*

Yes, Devin, I think, our view on pricing deposits is unchanged even if the Fed is on hold for a while, right, which is first and foremost, we always look at the competitive set and on what our competitors are paying and what make sense for that product. I think generally when you think about our product set, especially ICA and DCA, those are largely small balances that are operational cash that are not rate sensitive. And when we think about the pricing coefficients that we talked about for a while in that 25% to 50% range, I think that's the best way to think about it. And if the Fed is not moving and the market is not moving, I wouldn't anticipate that we would be moving either.

Devin Patrick Ryan - *JMP Securities LLC, Research Division - MD and Senior Research Analyst*

Got it. Okay. Very helpful. And then with respect to employee headcount, obviously, continues to expand. I think that's consistent with all the comments on investing, and I think that's a good thing. When you look at kind of hiring moving forward, where are you guys, I guess, really most focuses it, areas of adviser, service or technology or somewhere else? And then should we think about kind of the pace of headcount expansion from here more trending with adviser headcount? Or is there still a little bit of catch-up as you're just continuing to put a lot of investment into the system right now?

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Yes, it's a good question. And I think to answer your first question, you would continue to see investment in the areas of technology and service in terms of human capital and that obviously is consistent and aligned with our priorities. That said, the pace of the increasing of the headcount would be, I think, a mix of both investing into opportunities, which would drive some increase in that headcount. Though there is offset as we pull through efficiencies from some of that technology that would enable us to automate things that may have been a manual process or you began to use robotics and machine learning, et cetera, that are bigger leverage points with respect to certain of your predictable and repeatable type of processes. So in that spirit, we would expect our headcount trajectory to be at a lower trajectory than our adviser headcount growth.

Operator

Our next question comes from Michael Cyprys with Morgan Stanley.

Michael J. Cyprys - *Morgan Stanley, Research Division - Executive Director and Senior Research Analyst*

Just wanted to ask about the flows in hybrid adviser channel. Looks like the flowed have continued to slow a little bit. Just wanted to take your updated thoughts around that and expectations as we look forward from here?

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Yes. No, again, we're very committed to offering both the corporate RIA -- and the hybrid models. We think they're important with respect to ensuring that we have the versatility to meet the different preferences of advisers out in the marketplace and continue to invest in both. I think you actually are beginning to see strengthening and growth returning to our hybrid model, which is a combination of both the investments that we're making in the platform and system as well as, I think, where we didn't have necessarily strategic alignment with certain clients. And as you saw that pull-through mainly through the balance of last year, you're seeing less noisier environment and our investments in our platform will, we believe, support growth going forward in that channel.

Michael J. Cyprys - *Morgan Stanley, Research Division - Executive Director and Senior Research Analyst*

Got it. Okay. And then just a follow-up question on the centrally managed assets. I think you said about $1 billion flows into that. It's a little bit below $1.5 billion to $2 billion range, and I think, we've seen in recent quarters. So I just wondering what was driving the slowdown? And what sort of actions could you take to reaccelerate that growth?

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Yes. So first of all, we believe the centrally managed solutions deliver meaningful value for our advisers and their clients. And so as you said, we've increased the investment in that area over the last couple of years and you've seen actually movement from outflows to inflows on our centrally managed platform, which is certainly encouraging. In fact, in the last year, centrally managed platforms made up about 30% of our net new assets in advisory, which Q1 actually wasn't far off from that overall target -- sorry, certain level of performance. So Q1 is not as big of an anomaly. I think you perhaps have other factors like just lower NNA in Q1, and so consequently the managed platforms saw some sort of correlation of adjustment there. That said, I think we see them as an opportunity of further growth and continue to invest in them. A great example would be in April, we just introduced our adviser sleeve solution, which I referred to in my remarks. We also created a new conversion tool, which makes it simpler for advisers to move accounts to our centrally managed platforms. And -- so we think this ongoing innovation and investment in support of those platforms will continue to drive the appeal of them and higher utilization by advisers.

Operator

And our next question is from Ken Worthington with JPMorgan.

Kenneth Brooks Worthington - *JP Morgan Chase & Co, Research Division - MD*

Maybe first, the asset management industry has gotten approval for the nontransparent ETFs. Maybe what are your thoughts here on broker or adviser adoption? And if it does become popular, what might this mean for LPL?

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Yes. So we do think that the product category likely has some future, but that evolution won't happen overnight just like any other product. I think it requires extensive diligence and education to ensure that the industry gets it right in terms of optimally serving investors. So that will take some time to work through. That said, we certainly are already a large distributor of ETFs, especially on our advisory platforms and have working relationship with these products, right? So we're actively engaged with them and how do we think through innovating around these types of solutions. And we would look at this opportunity as a similar way to work with them on making sure that we position it as an appealing opportunity for advisers to use. So we see it as an opportunity for innovation and continuing to expand the value proposition of our advisers.

Michael J. Cyprys - *Morgan Stanley, Research Division - Executive Director and Senior Research Analyst*

And then net new advisers were up 80. How did the terrible 4Q and maybe contrasting the great 1Q influence the recruiting? And I think you guys mentioned that the cadence of that new assets was heavily weighted towards March, kind of building from January to February to March. Is that sort of the cadence you saw in recruitment as well as there are stories here about recruitment kind of accelerating through the quarter?

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Yes. So recruiting definitely accelerated through the quarter as you said. The further you got away from the volatility in December, we saw more engagement in recruiting, discussions and dialogue. And certainly in a more normalized environment, as I said earlier, we feel good about the work that the leadership team is doing with our recruiting and business development teams in terms of improving the efficacy of their performance. Since we've aligned our TA with financial returns, we think those 2 dynamics create much more of a reputable and sustainable way to think about levels of recruiting. So I think those are the ways that, we believe, will drive our performance aside from some big swing in volatility. So I think your thinking is right.

Operator

And this ends our Q&A session. I would like to turn the call back to Dan Arnold for his final remarks.

Dan Arnold - *LPL Financial Holdings Inc. - President, CEO & Director*

Yes. So thank you, and thanks everyone for taking time to join us this afternoon. Just as a reminder, we are holding our Investor and Analyst Day in New York on May 22. So we look forward to speaking with you then, as we'll discuss our business in greater depth. We hope you can make it. Thanks, everyone.

Operator

And with that, ladies and gentlemen, thank you for participating in today's conference. This concludes the program and you may all disconnect. Have a wonderful day.
