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PRESENTATION

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

Okay. So we'll start with our next session. Up next, it's my pleasure to welcome Dan Arnold, President and CEO of LPL Financial. With over $1.2 trillion in client assets, 22,000 financial advisors and a high single-digit organic growth, LPL remains one of the fastest-growing companies in the wealth management industry.

Over the last few years, the company has meaningfully expanded its capabilities and affiliation options, creating a much larger addressable market and a path to sustainable organic growth. Coupled with increasing capital deployment opportunities, LPL remains well positioned to drive robust EPS growth over the next coming years. So thank you for being here. Always good to host you at our conference. Thank you for the time.

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

Great to be here. Thanks for the opportunity.

QUESTIONS AND ANSWERS

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

Great. So why don't we start with organic growth. It's always an important topic that's usually how we start these conversations with you. So look, LPL is on track, I think, to do 9% organic growth over the last 4 quarters, 11%, I think, in the most recent quarter, in the third quarter. But importantly, it seems like the breadth of organic growth continues to expand quite a lot and you guys obviously made a lot of investments into various affiliation options.

So as you look forward into 2024, what are the expectations for net new asset growth and importantly, what channels do you think will contribute more to that than what we've maybe seen over the last couple of years?

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

So I always love to start with this topic. And maybe just as a little context before we get specifically to 2024, look, organic growth, as you know, is one of the key tenets of our overall strategy. And that is steeped in the opportunity around what is 3 really durable structural trends, right? You have this ongoing demand for advice, you have the ongoing preference to receive that advice from a financial advisor and then finally, you have this trend towards doing this type of business in the independent model.

And we sit at the intersection of all those, and we believe in a rather unique place. So that fuels that strategy to invest back into our platform to create capabilities necessary to help these advisors differentiate and win and run thriving businesses, and to ultimately create the flexibility of affiliation models so that we could potentially serve any of the potential 300,000 advisors that are out there. We won't win them all. We'll keep trying to, but we should be in those conversations.

So that expansion of those affiliation models, you'll hear us refer to that as our horizontal growth strategy or horizontal strategy, horizontal expansion strategy. And then our capability set is this concept of vertical integration where we create that end-to-end capability set to help advisors win. And so as we think about that and we reflect on the outcome, if you look over the last 4 years, you said it, we've been able to deliver using those 2 primary components of the strategy, somewhere at a minimum around a high single-digit growth rate in the last 12 months, it's been 9%, as you mentioned now.

And look, as we go forward, we believe that given our positioning in the marketplace as an industry leader, the IP and the insight around this business matched with a platform that has the capabilities and services and technology to be differentiating and then finally, with this commitment and capacity to invest continually back into the program to continue to help it evolve that we can further differentiate our model, which ultimately creates more and more durability around the growth and so when you look out over the long term that creates this ongoing ability to create outsized share gains from that.

Now you get to 2024, as you said, and how do we think about that? Well, if you look across all of our affiliation models, we've got really solid momentum in all of them as we enter 2024. In our traditional core markets, you see us with earning higher and higher win rates, which has driven record recruiting in the last 12 months associated with that channel. You look at our new affiliation models, we have accelerating growth in those as those models season in that has created record recruiting in those models in the last 12 months.

And then, of course, on the enterprise business, you see us consistently producing wins. And certainly, the Prudential win we announced is a nice tailwind of growth for 2024. So you take that opportunity and then you match it with the high retention rates that we have, the ongoing same-store sales work that we're doing, and we're set up, we think, really well for growth in 2024.

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

Great. I would love to hit on some of the competitive dynamics as well. You spoke a lot about not just today, but really over the course of several years, around the enhanced capabilities that LPL has put out into the marketplace. But it is a competitive market, as you said, there's a lot of financial advisors, a lot of folks competing for those financial advisors. There's been a lot of volatility this year, clearly, and that put pressure on cash balances across the industry. And obviously, that's an important source of economics for a lot of other advisory platforms.

And at the same time, higher interest rates probably put some pressure on some of the financial kind of engineering models and some of the good roll-up strategy. So are you seeing a change in the competitive dynamics that also helps your ability to recruit from those forces?

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

Yes. And we always start there, trying to be great students of the marketplace and really understanding the competitive landscape. So on a broad sense, if you look across the landscape, we haven't seen any significant big changes in terms of the players that we typically would see out there or their positioning in the marketplace. And we haven't seen any new innovation around what we might call a tactical strategy in the marketplace.

I think I've highlighted the most significant change over the last couple of years, it's the one that you were referring to, where we've seen the emergence of these aggregators in the marketplace that many times are backed by private equity capital. And they're trying to do 2 things, right? Take a -- especially in the RIA-only marketplace, where they take a large number of small advisors that lack the scale and provide them some structure. And then just as importantly, provide them a succession strategy. So they're trying to solve for those 2 things.

The emergence of that competitive set 2 years ago was one of the primary catalysts for us, pivoting and innovating and recognizing that we needed to do a better job of solving for that question around 1/3 of the advisors retiring over the next 10 years. And seeing that competitive threat emerging was the catalyst to build our liquidity and succession program that we did. And we rolled that out roughly a little over a year ago. And we've seen great success in appeal with that solution as we're able to do some unique things inside that model that others can't.

Primarily, we're able to -- when the aggregators come in, they will many times create a proposal that flips that independent model more to an employee-based model. We're actually able to create a model that maintains an independent model, creates a bridge for the original entrepreneur to sunset off, think over a 3- to 5-year period of time, where they're able to maintain an independent practice, they're able to continue to serve and support their clients like they're used to. We even put growth incentives in place such that we've seen growth rates emerge at a faster pace than pre-the-transaction.

And then the second half of the bridge is then we're able to bring in a new entrepreneur to then take over that practice over the long haul and give them a chance to buy that in a way that they can have access to capital, where they couldn't have if they had to pay at all upfront in a transaction. And so we're able to create sort of this 10-year bridge that is a really interesting and appealing solution that we think is quite differentiated and that's been kind of a cool innovation around your question around the competitive set.

We've used it really well with our existing advisors and we just took it to the external marketplace because we realized the appeal of it, and we think it also will complement growth as we go forward. So maybe that's where competitive landscape has led to us continuing to try to innovate.

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

Just to build on that, I'd imagine that LPL has a lower cost of capital than some of the financial sponsors that were engaged in this part of the market. Does that give you also a competitive advantage to build this succession planning business in sort of outside of the LPL network. So when you go to an affiliated folks and you say, like, look, you might be able to offer a better transaction now given the difference in capital costs?

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

Yes. I think one is capital cost. I think two is we monetize in a more vertically integrated way. And then three, a nonfinancial metric that's just as important as we're able to create a better solution for that advisor for the stakeholders that matter most to them, which is, of course, them, but it's also their teams and their clients. And if those potentially are going to be disrupted in that other model, then that's the intangible piece that is also a differentiator.

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

I got you. All right. Let's pivot away from individual advisor business and talk about the enterprise channel. It's a place where you've seen substantial amount of growth as well over the years. And to your point earlier, you signed a deal with Prudential. It's your first insurance and proprietary product institution, which kind of further expands your footprint and your TAM outside of the traditional kind of bank kind of channel.

So let's talk a little bit about the level of engagement you're seeing with other perhaps larger enterprises. And maybe a couple of comments on what your pipeline in this channel looks like into '24?

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

Yes. So if you take the whole channel across the board, and I remind you, it's been a kind of a cool place of innovation, we kind of broke through with an outsourcing model at this sort of larger end of this segment of the marketplace. And if you remember, back in 2021 and specifically focused on banks, so that's when BMO and M&T joined our platform. And that was sort of a breakthrough event that created or expanded this new market.

We've had success at bringing on roughly $85 billion in assets subsequent to then. That total market for just the bank space is $1 trillion in assets. And then we were able to take the learnings and insights and capabilities from the platform that we had built for banks, and we were able to make some incremental investments in capabilities, some personalization options that banks weren't interested in, but other companies like an insurance or a product manufacturer might be and leverage that core platform, create a slightly different version of it and obviously, take that to the marketplace, and that's where we made the announcement for Prudential.

Now that part of the market is $1.5 trillion in assets. So you've got some expanding TAM there as well as -- so a different flavor of this enterprise model, which gives us a lot of flexibility in how we position them in the marketplace. As you would expect, with the announcement of Prudential, you get that initial wave of, hey, what are they doing? And why are they doing it? And why am I not doing it? And how do I learn more about that? And so we do believe that both the bank space and this insurance product manufacturer space will be long-term contributors to growth as -- like in the bank space, we create a consistent series of wins. We think if we onboard the Prudential program successfully, then that will create opportunities that will follow it.

So again, I think you've got a good pipeline for the bank space as we think about '24. We've got good tailwind in the insurance space with Prudential onboarding second half of next year. And then we're having good dialogue with other companies about this concept of what we've done with Prudential and we think as that builds, that pipeline will deepen as well.

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

Great. Let's talk about some of the newer things you guys have done recently. You recently rolled out a new affiliation option, focusing on the high net worth part of the business, I think you're just calling it private wealth. What competitive advantages, I guess, does LPL bring to this marketplace? Obviously, it's a place where a lot of folks would like to compete in. And what are the kind of other recruiting goals that you have for yourself in this channel?

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

Yes. So this is another example of horizontal expansion, right? And again, how do we ultimately position ourselves to have a discussion for any of the 300,000 licensed advisors that are out in the marketplace. And we think we've delivered a novel or new sort of solution to the marketplace in that we've taken the capabilities that a high net worth advisor would want. So think about $5 million and up in a retail investor.

And the capabilities that an advisor would need to serve or support that type of client, but then we've taken those capabilities and we've put them into an independent model that preserves those principles of independence. So think about important things like branding, think about important things like ownership of the client and the economics that the advisor gets paid for the value that they provide in the ecosystem.

So when putting it inside that independent wrapper, that's what makes it really differentiated and novel. Up to this point, if you were a high net worth advisor, meaning I focus on high net worth clients, I'd be limited to making more of a kind of a wire-to-wire type of move if I wanted to move or if I wanted to go independent, I kind of had to go figure it out myself, and I could cobble together different resources to support me and help me but it was up to me to do it.

And in this case, we've created a much more turnkey solution that makes that pathway much easier for them, much more predictable for them. And ultimately, we believe gives them the right leverage point so that they can focus on what they do best, which is take care of those high net worth clients. And then the other benefits of client ownership, economics, autonomy and how they run their businesses. So we think it's, again, a differentiated solution that fits a really interesting sort of overlook place inside the high net worth space.

So we think it's a model that will work and that we can win with it. And certainly, this marketplace, as you guys know as well as I do, it's a $15 trillion size market with great growth characteristics. So a place that we think creates an interesting contribution to growth as we season it in. And we'll season it in like we did those other new affiliation models, right? We've taken it to the marketplace. We announced that. And then we've got to build our credibility and demonstrate that it works. And then I think you'll see that growth rate ramp from there.

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

What kind of response are you guys hearing from the marketplace so far?

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

Very positive. We actually launched it with an initial client that we had onboarded. And I think because of the differentiated concept, it's generating a lot of discussion throughout the industry.

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

Got it. Great. Let's talk about some of the other services that you provide. We and I think investors will have definitely been focused on LPL services group kind of suite of services that you rolled out. I think the name has changed a little bit over the years. But effectively, it's a various financial advisor solutions. You recently added CFO option on top of that. I think it brings a total number of offerings to 13. What's your vision for this suite of products internally and externally when it comes to LPL? I know we talked about white-labeling that and maybe updating that progress and wrapping it around, what kind of revenue growth do you expect the collection of these platforms to provide to you guys?

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

Yes. This is a really kind of cool area of innovation. And it sits right in the sweet spot of that vertical integration concept. It was one of the things that we recognized probably 5 years ago that there wasn't enough value that I would call at the point of sale or inside the advisor's offices in the independent model. We stopped sort of midway through the value chain. And advisors needed these leverage points and resources to help them do 2 things, again, be a great advisor, how do I differentiate and win and service my clients really well; and b, how do I run a thriving practice?

Individually, those are hard. You put them together, it's real hard. So it's a relevant thing to solve for, right? And our initial concept that we started with was one of kind of a gig economy concept. Let's go provide them some roles like a role or an expertise they don't have. So think of something like a Chief Marketing Officer, a CFO, an admin, a paraplanner, something that is an ongoing role. They need ongoing support and insight. They don't necessarily have access to in their practice. So maybe they outsource it and don't get much quality and overpay for it. Or even worse, they try to do it themselves and muscle through that, right, which isn't a great use of time.

And so we've seen great success with that first entry. We're up to 13 different services within the portfolio today. Now the uptake or the appeal has been mainly to larger practices that are a bit more complex. And you'll see we've got, I think, 3,700 different advisors that are using these services today. The growth rate in the last year has been 25-plus percent year-on-year. So good growth but begs the question, wow, we still got 22,000 to 23,000 advisors out there. That's a runway for growth. How do we expand that opportunity and really step into that additional available market, and that's the next source of wave of innovation.

So we're working right now on innovation work that will roughly double that portfolio of 13 services over the directionally next 2-plus years, not to be overly precise, but just the pace of what we're trying to do. And we see a number of different opportunities, but maybe 2 that are -- can help me sort of frame that opportunity. One would be this concept of still gig economy solutions. But tweaking that original version or first generation of solutions so that we might make them a bit simpler for a smaller practice at a lower price point, if you will.

And that's where we just announced the CFO Essentials, which is a different version of the CFO solution or where we introduced bookkeeping as a specific smaller, simpler service than a CFO offering. So that's where we're innovating that we think gig economy support still makes sense, but let's get it to the rest of our practices, a concept that's affordable for them and that works for them given their -- the more simplicity of their practice. That's one wave of innovation. A second one is around this concept of solving for something that is more a moment in time need.

So think about our assurance plan, think about partial book sales, think about tax planning. This is where I have a specific need, and I need it solved for in a moment in time versus an ongoing role or an ongoing access to expertise, if you will. And so that's another area that we're innovating in. And we think with those 2 complementing the first wave that we have, that we ultimately have a portfolio that will help us ramp into that solution that potentially could be relevant for any of the 22,000, 23,000 advisors and growing that we have today.

Now we haven't ruled out the external market, as you mentioned. Our focus has just been internally because there's so much opportunity there. But as you would guess, the 300,000 advisors that sit outside our platform have similar needs as to the ones that are in the LPL platform today. So we know these solutions are relevant. Our liquidity and succession solution that I mentioned earlier, it's the first one that we've begun to experiment to the external market.

So that creates a learning ground for us as we understand how to provide that type of service to the external marketplace. I think then we can ask better questions around hey, with the other rest of our portfolio that we're innovating on, how might we apply it externally. So that's kind of how that comes together. But it's secondary to really trying to provide those services to focus on our platform today.

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

Yes. No, clearly, long runway there. Okay. Let's shift gears a little bit. I would love to hit on regulation. We've seen Department of Labor roll out their updated fiduciary rule, the good news for us and perhaps for you as well. The hysteria that was around this rule back in 2016, was a lot more subdued this time around, but what did come out of the original proposal is that it really sort of catalyzed a move towards larger platforms. So I would love your perspective on kind of the initial response you're seeing from the marketplace and look, who knows whether or not this is going to go through as proposed. But if it does, should we think about this being another catalyst of consolidation, which you guys were a bigger winner of -- in the last go around?

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

Yes. It's a great question and I love the context of the question. Maybe just to fill in some of the elements before you get to that specific question. If you think about process and where we are, as you all know, they proposed the rule at beginning of November, there's a 60-day comment period. So in early January, the industry has to respond. It's likely that the rule, if it does become effective, there will be an attempt to make it effective in late spring and then there will be an implementation period of which then the industry works to comply with the new rules and regs.

And they'll likely take that approach to try to avoid it getting caught up in the election process. It's reasonable to believe that there will be litigation along the way that may change that path from a timing and/or ultimately whether the rule ultimately becomes effective. So there's a lot of game left to play and uncertainty around that. That said, we're preparing as if the rule is going to be effective. If you look at the rule itself, it's very similar to the version in 2016. It tries to fill in some of the gaps that Reg BI necessarily didn't capture.

And so because of that, we did a lot of innovation in preparation for the proposed rule in 2016. And then when it got struck down in the courts, we ultimately didn't use some of that innovation and automation that was built. So we still have that and can leverage some of that. And then with respect to this rule, it's a little early, but based on what we know about it so far, we'll likely make some small incremental investments around the edges and certain things just to improve the efficiency and efficacy of which we would comply with the rule.

So we feel good about our ability to pivot and adjust to the rule, should it become effective. That said, if you then take that one step further and say, well, what are the strategic implications of this, which I think, Alex, is the root of your question, there's probably 3 that come to mind initially. And I suspect there's other opportunities that sit underneath this.

First and foremost, I think it's easier for larger players to pivot, to make the necessary investments, to comply with the rule, to accept the shift in the risk profile associated with this. And so I think you'll see a wave of consolidation because of those 2 things, which certainly how we're positioned in the marketplace, we would look to participate in that consolidation. And I think it's logical to believe that other larger players would as well. Hence, your point earlier where that's an advantage to larger players.

I think secondly, we'll see an ongoing acceleration of shift from brokerage to advisory because of it. We've already seen significant shifts in the qualified or retirement assets. We think that's only a catalyst for that shift to continue. Again, an advantage for larger players like ourselves, who have vertically integrated advisory platform systems and solutions that makes it easier for us to help the advisor and ultimately deploy assets on the advisory platforms across a variety of different solutions as well as ultimately help them shift assets from brokerage to advisory in a more integrated, simpler, better experience for the client way.

And so again, advantage is for larger players. I think the third place which is probably, again, an advantage for larger players is specifically where we're able to go in some of those incremental investments that I was talking about, where we can pivot better and create a better solution going forward. If you create a better solution to help me process the business within this new rule that as an advisor, that's going to be appealing to me. So take fixed annuities as an example which currently do not fit within Reg BI's oversight. Now this rule would propose that they would and sit inside this higher standard, if you will, under the DOL's rule.

So because of the way that we process business and we have an integrated solution to process business, we already treat fixed annuities like we do other Reg BI services, and we process and supervise them and support them in a very similar way. So that pivot is much easier for us. And let's say we do make some incremental investments around that just to improve the efficacy of doing that. So we're going to have a big advantage over a firm that doesn't do that work like we do today, doesn't have the capacity to adjust.

So our solutions are going to be more attractive and let's say, it makes up 10% of an advisor's business. That's meaningful reason to think, wow, I may not be able to do that where I am today, I can do that much better in your place. I'm going to have a dialogue with you. The other thing that about fixed annuities is interesting or all fixed insurance. A lot of that business in the independent space, not in the enterprises, but in the independent space in the advisors don't necessarily do through us because it's not a security. They have to do variable and index to us, but not necessarily a pure fixed annuity.

So if you're an advisor who can't comply with the rule or don't want to take on that risk, that really challenges you to reimagine, hey, I'll just do that business through my partner, in this case, LPL. And so that also creates opportunity for us. And I think you will see some participants in the industry might conclude that all fixed annuities just have to be done through them. Because even if the advisor is doing it on their own, but they did something they had unintended consequences that might fly back to their partner, the partners are going to try to mitigate that risk by requiring the fixed annuities to be done through them. So again, this is another place that I think strategically, it's a benefit to larger players.

At the end of the day, from principle standpoint, we have -- we think choice is in the best interest of the investor always, and it's really important, we believe, to maintain the availability of both advisory and brokerage. We think some of the advocates of this rule are sort of missing or losing sight of that fundamental principle. I think secondary to that, we also think the standard of care is really important for the reputation of this industry. But we think Reg BI got that right. It improved the standard of care. And we think that we should let that play out and see ultimately whether it truly achieves what it's intended to do.

And then finally, we think the SEC is the best regulator to oversee this, not the DOL because you didn't have inconsistency across qualified and nonqualified assets. And so from a principle standpoint, you could see where we would be advocating for a different outcome. But I do think strategically, there's opportunity for a larger play, right?

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

Well, yes, certainly, it will be fascinating to see how this unfolds. Let's shift down the P&L a little bit. I want to spend a minute or 2 on margins. Now LPL has made increased investment over the course of this year as we've seen. And while this is clearly supporting industry-leading organic growth, its weighed on operating margins over the course of the last couple of quarters. So as you move forward, help us think about the trade-off between kind of organic growth and operating leverage and kind of how do you think about operating margins from here?

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

Yes. So maybe just to give you a simple headline, nothing's changed with our cost strategy. So let me just give you some color on that. I think first and foremost, we're always focused on delivering operating leverage in our core business. Second, we're looking at investing in opportunities that drive growth but at the same time, trying to pull through efficiency and productivity. And then we'll tend to look at our -- the trajectory of our cost and we can adjust that given kind of the opportunities in the macro.

And so those are the fundamental principles we use that sit underneath that cost strategy. So if you apply them to this year as a reference point, right? So 2023, you would -- where we targeted about a 13% to 15% core G&A growth, clearly, a higher number than you would typically see. Well, 4% to 5% of that was because the macro was set up with some tailwinds around the interest rate environment. And so we were able to take that and accelerate some investments in order to try to capitalize on that.

In future years, if the set-up in the macro wasn't as positive or it wasn't as conducive for that, then we can make adjustments and pivot. We likely don't have that type of macro as an example, going into 2024. And so we can adjust and pull back from that. I think if you look at then the remaining 8% to 10% of the core G&A growth in 2023, roughly half of that goes towards supporting the growth of the core business and the other half goes to investing in what I'll call some of these new markets, new capabilities, new solutions that will drive future growth.

So that's a way to think about the cost structure. The point on it, that's probably the most important is we can be flexible in adjusting that spend around the macro as well as just how we think about the growth opportunity that sits in front of us. So given the changing landscape in either one of those, our ability to pivot and adjust and strike that balance between the opportunity set and the macro that's in the short run, but also making long-term investments that are going to drive growth is, I think, the right way to think about the balance.

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

Great. Well, unfortunately, I think we're at time. So Dan, thanks so much for being here. Appreciate it. Thank you.

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

Thanks, Alex.
