BNY MELLON | PERSHING

Win. Grow. Retain.

How to enrich your business with smart liability management

As a trusted advisor, you help clients articulate their goals, design comprehensive financial plans and invest their assets appropriately. But what about the other side of their balance sheet?

Strategic use of credit is an important, but often overlooked, aspect of wealth management. While some advisors may be hesitant to introduce lending capabilities, the fact is that many clients can benefit from incorporating smart liability management into their financial picture.

For advisors, expanding your offering to include lending can attract prospects, capture additional assets from current clients and extend relationships to the next generation (beneficiaries of $30 trillion wealth transfer). For clients, securities-based lending allows them to easily meet business and personal needs without interrupting their long-term investment strategy.

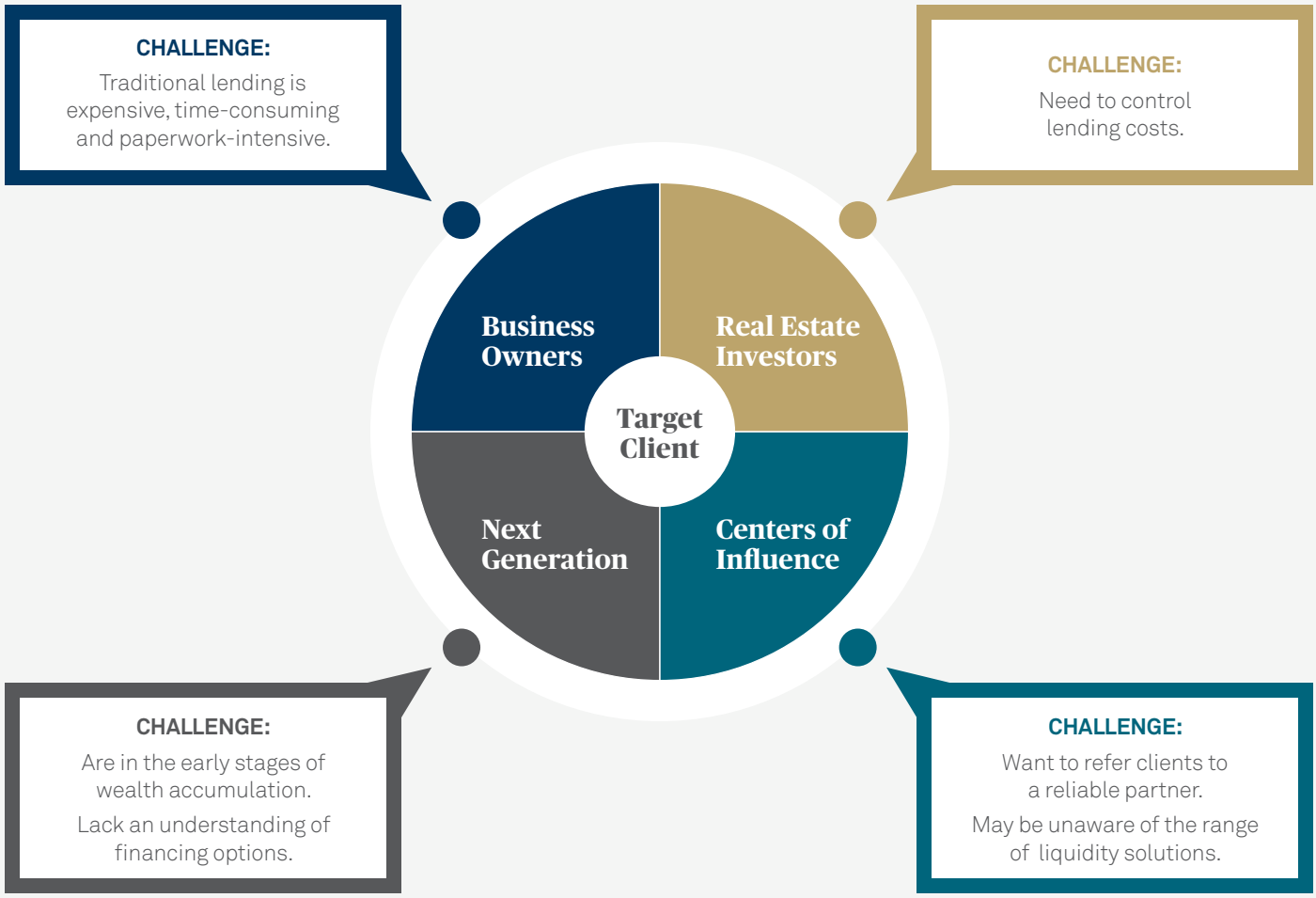
≈$200 BILLION*

TOTAL SECURITIES-BASED LENDING BALANCES

> "Incorporating liquidity into client conversations allows you to deepen relationships with your current prospects, clients — and with the next generation."
>
> — KATIE SWAIN, DIRECTOR, GLOBAL STRATEGY & PRODUCT MANAGEMENT | PERSHING

*Source: WealthManagement.com, "When Is Securities-Based Lending Right for Clients?" Zohar Swaine, Sept. 14, 2017.

WHO NEEDS LIQUIDITY?
EVERYONE.



Cementing assets and relationships

By definition, high-net-worth (HNW) and ultra-high-net-worth (UHNW) clients have sufficient assets to fund their lifestyle and meet their financial goals. If they need to make a large purchase, pay a capital gains tax bill or invest in their business, they may think liquidating a portion of their portfolio is their best option.

However, this may not be the most efficient way to meet their needs. Selling investments can interfere with the integrity of their wealth management plan. It may also carry unintended consequences, such as taxes and opportunity costs.

You can provide a more effective approach: securities-based lending. This strategy enables clients to seize opportunities and make their money work harder.

WIN NEW CLIENTS

Offering securities-based lending is a smart way to enhance your value proposition and turn prospects into clients. Serving as a resource for their credit needs can help you differentiate yourself from advisors who focus solely on the asset side of the balance sheet.

Centers of influence (COIs) such as CPAs, estate attorneys and divorce attorneys may be more willing to refer clients to you if they know you can help with liability management. Many of their clients need ready access to financing for items such as a tax bill, a divorce settlement or a real estate bridge loan.

CLIENTS MAY NOT KNOW THAT THEY CAN USE NON-PURPOSE LENDING TO:

- Purchase residential or commercial real estate
- Renovate a home
- Expand their business
- Enhance working capital
- Fund major milestones
- Pay for medical needs and elder care
- Make a luxury purchase
- Implement wealth transfer strategies

GROW ASSETS AND ENHANCE CLIENT RELATIONSHIPS

The larger the balance in a non-retirement brokerage account, the more a client can borrow — and the lower the interest rate is likely to be. Discussing securities-based lending with an existing client who needs liquidity may encourage him or her to consolidate assets held away in order to qualify for a larger line of credit.

When you talk to clients about lending, you have the opportunity to learn more about them, deepening your existing relationships. Ask them what they would do if they had additional liquidity, or how they are paying for a major purchase. You could gain new insights into their short-term needs as well as their long-term goals.

Securities-based lending can be a tool to forge relationships with your clients' children or grandchildren. A client can use the proceeds to fund college tuition or help with a down payment on a home. Lending could also start conversations about philanthropy, business needs, existing liabilities and other important aspects of a client's financial life.

START THE CONVERSATION

Asking these questions will help you start the conversation with your clients.

"Do you have a plan in place to deal with significant unexpected expenses?"

"Does your business have a working capital line of credit in place?"

"Do you anticipate a large tax bill from capital gains or investment income?"

"Are you planning to make any major purchases or expenses in the next year?"

"Are you paying for a child's education?"

"Are you planning a business acquisition or expansion?"

"If you have an outstanding mortgage or variable rate debt, do you have a plan for rising interest rates?"

RETAIN CLIENTS AND ASSETS UNDER MANAGEMENT

The extension of credit is increasing rapidly as financial entities try to cope with fee compression. In fact, it is highly likely that your clients have already been approached about lending by a banker, an online lender or another advisor.

Research firm Aite Group notes that, "Lending relationships, regardless of the amount loaned, are a primary cross-sell channel for noncredit products."[1] When clients borrow elsewhere, it can bring them closer to your competition by exposing them to the cross-selling of other financial solutions, including investments, insurance and even financial planning.

The credit relationship is detailed and intimate. Offering securities-based lending can help you protect clients from forming relationships with other advisors.

It is estimated that for every dollar lent, two are retained. Providing an alternate source of liquidity to your clients can prevent them from selling part of their investment balances. In addition, assets tend to be stickier when tied to a loan. Collateralizing assets as in securities-based lending makes them more difficult to unwind.

> "Wealthy individuals need more than financial planning and asset management. They need a source of liquidity for their business and personal needs, from an advisor who understands their entire financial situation."
>
> — EVGENIA VOLKONITSKAYA, VICE PRESIDENT, GLOBAL STRATEGY & PRODUCT MANAGEMENT | PERSHING

HOW TO INCORPORATE LIABILITY MANAGEMENT INTO YOUR BUSINESS

1 Profile your top clients

Target sophisticated clients with non-retirement assets

2 Conduct relationship reviews with your clients

Identify existing debt, pricing and use of proceeds

Determine potential liquidity or long-term capital needs (real estate, luxury purchase, business capital needs, estate planning, tax obligations)

3 Ask why clients are liquidating investments

Is lending a viable option?

Do they have non-qualified investable assets?

4 Focus on top prospects and Centers of Influence (COIs)

Look for prospects with complex capital needs — business owners, real estate investors, private equity and venture capital investors

Identify key COIs to call on

Host educational seminars about the benefits of a ready source of liquidity

[1] Aite Group, *"Profiling Innovations in Business Lending,"* August 2018.

Liability management is good for your clients

There are many situations in which clients can benefit from securities-based lending, even if they have sufficient personal resources to meet their liquidity needs.

Borrowing can enhance a client's wealth management plan and investment strategy by reducing transaction costs, avoiding capital gains taxes and eliminating the need to sell in a down market.

CLIENTS CAN TAKE ADVANTAGE OF OPPORTUNITIES AND MEET UNEXPECTED NEEDS

Many wealthy individuals are business owners, corporate executives, or hedge fund or private equity partners. As such, they may need a source of liquidity for working capital, investment opportunities or unforeseen expenses.

A securities-based line of credit can help smooth out lumpy cash flows, provide a bridge loan for a real estate purchase, and serve as an estate planning tool. The sophisticated needs of HNW and UHNW clients require the ready access to capital that securities-based lending can deliver.

CASE STUDY

Buying a dream home for cash

Jennifer, an UHNW client, had long admired a large historic home in her neighborhood.

Driving by one day, she saw that it had a "For Sale" sign on the lawn. She decided to seize the opportunity, but wasn't sure how to fund it while she waited to sell her home. Anne, her advisor, suggested that she borrow against her $10 million portfolio to make a cash offer.

Jennifer qualified for a $4 million line of credit. She offered $3 million to the seller, who had received another bid that was slightly higher but involved a mortgage. The seller decided to take the less-complicated cash offer, and the sale closed in five weeks. Jennifer listed her current home for sale and moved into her new one. The line of credit gave her time to shop around for a mortgage for her dream home after she had sold the old one.

BORROWING ALLOWS CLIENTS TO KEEP THEIR LONG-TERM INVESTMENT STRATEGY INTACT

Selling investments to generate liquidity is costly, both in terms of expenses and missed opportunities. These include paying capital gains taxes and trading costs, as well as missing out on potential future growth and income.

In contrast, securities-based lending allows the client to remain invested and continue to participate in the markets. In fact, capital appreciation from a portfolio that remains fully invested could help offset the interest expense of a securities-based line of credit.

CASE STUDY

Funding long-term care when needed

Fran, a 75-year-old client in need of continuing care, was relocating to be near Sarah, her only daughter.

Immediately after listing her home for sale, an opening became available at a long-term care facility within miles of Sarah's home. To secure a spot, Fran had to make an initial deposit within seven days and final payment two months later.

Dennis, Fran's advisor, helped her establish a securities-based line of credit in just a few days. Fran wired funds directly to the facility in order to secure the room. She avoided unnecessary tax consequences from liquidating any investments, and eliminated the pressure to sell her home too quickly. Sarah had peace of mind knowing her mother would move closer and receive the care she needed.

SECURITIES-BASED LENDING OFFERS QUICK AND EASY ACCESS TO LIQUIDITY

Unlike other forms of secured and unsecured debt, securities-based lending is flexible, cost-effective and convenient. Because the client's securities serve as collateral, the interest rates tend to be competitive relative to standard bank loans or credit card advance rates.

Securities-based lending is responsive to the rapidly changing needs of affluent clients. It typically takes only a few days to open a line of credit, versus three to four weeks for bank lending. It also offers easy access to funds, which can be transferred to a client's checking account or wired to an external account with a simple phone call.

In order to give clients ready access to liquidity, experts recommend opening a securities-based line of credit before a need arises. This can position clients to quickly seize opportunities or cover expenses.

CASE STUDY

Funding business growth

Mark, an entrepreneur with a $20 million portfolio, owned a controlling interest in a company that makes audio components.

He wanted to acquire a company in a complementary business that makes hardware. When he considered liquidating assets to buy the company outright for cash, he found that he would face a large capital gains tax bill. Mark also worried about the opportunity cost of being out of the stock market.

If the business borrowed money to make the acquisition, there would be other hurdles. Because its assets are less diversified than an individual's portfolio — in this case Mark's — the company would likely pay a higher interest rate for the loan. It would also face costly legal and accounting fees to complete the transaction.

Instead, Mark's advisor Sheila recommended a securities-based loan. Mark qualified for the line of credit and loaned the proceeds to his company, which used the funds to acquire the target firm. His business is on track for future growth. And, because he remained fully invested, he was able to participate in market gains he otherwise would have missed.

Enhance your value proposition and your clients' financial situation with smart liability management

Expanding your wealth management services to include lending can make your business more comprehensive and competitive. Many clients can benefit from a trusted advisor who focuses on both sides of their balance sheet. Securities-based lending allows clients to pursue a wide range of goals while offering you the opportunity to build your business and connect with the next generation of clients.

To learn more about how liability management can help you and your clients, visit our Lending Solutions page on pershing.com.

"By including lending solutions in your offering, you can address the complex needs of HNW and UHNW clients, and provide a more comprehensive approach to wealth management."

— ROBERT LARUE, NATIONAL DIRECTOR, PRIVATE BANKING | BNY MELLON

IS SECURITIES-BASED LENDING RIGHT FOR YOUR CLIENTS?

Securities-based lending may not be appropriate for all investors. Clients should be sophisticated enough to understand the benefits and risks. When considering whether a client could benefit from securities-based lending, be sure to carefully evaluate their individual situation and discuss the risks with them. This solution may be better suited to clients with well-diversified portfolios of non-qualified assets.

ABOUT BNY MELLON'S PERSHING

BNY Mellon's Pershing and its affiliates provide a comprehensive network of global financial business solutions to advisors, broker-dealers, family offices, hedge fund and '40 Act fund managers, registered investment advisor firms and wealth managers. Many of the world's most sophisticated and successful financial services firms rely on Pershing for clearing and custody; investment, wealth and retirement solutions; technology and enterprise data management; trading services; prime brokerage and business consulting. Pershing helps clients improve profitability and drive growth, create capacity and efficiency, attract and retain talent, and manage risk and regulation. With a network of offices worldwide, Pershing provides business-to-business solutions to clients representing approximately 7 million investor accounts globally. Pershing LLC (member FINRA, NYSE, SIPC) is a BNY Mellon company.

Additional information is available on pershing.com, or follow us on Twitter @Pershing.

IMPORTANT LEGAL INFORMATION — PLEASE READ THE DISCLAIMER BEFORE PROCEEDING.

- Please read these terms and conditions carefully. By continuing any further, you agree to be bound by the terms and conditions described below.
- This paper has been designed for informational purposes only. The services and information referenced are for investment professional use only and not intended for personal individual use. Pershing LLC and its affiliates do not intend to provide investment advice through this paper and do not represent that the services discussed are suitable for any particular purpose. Pershing and its affiliates do not, and the information contained herein does not, intend to render tax or legal advice.

WARRANTY AND LIMITATION OF LIABILITY

- The accuracy, completeness and timeliness of the information contained herein cannot be guaranteed. Pershing and its affiliates do not warranty, guarantee or make any representations, or make any implied or express warranty or assume any liability with regard to the use of the information contained herein.
- Pershing and its affiliates are not liable for any harm caused by the transmission, through accessing the services or information contained herein.
- Pershing and its affiliates have no duty, responsibility or obligation to update or correct any information contained herein.

BNY MELLON | PERSHING

pershing.com

One Pershing Plaza, Jersey City, NJ 07399

WP_PER_HNW_LA_6_19