



Schwab: Business Breakdowns Research

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Research Sources

- Website: [Schwab.com](https://www.schwab.com)
- Social Media: [LinkedIn](#), [Twitter](#), [Facebook](#)
- Podcasts: [Intrinsic assessment of Charles Schwab](#), [The AMM Dividend Growth](#), [Schwab Challenger Mentality](#)
- [Company Financial Statements](#)
- [Case 15 Charles Schwab](#)

Summary

- Charles Schwab Corporation is a financial services company with subsidiaries that provide a wide range of services such as; banking, wealth management, securities brokerage, custody, asset management, and financial advisory management.
- The firm has grown from its beginnings as a simple discount brokerage to provide a full-service investing and banking experience to clients locally and internationally.
- Individual investors who invest on their own or via a workplace-sponsored retirement or equity plan can use Charles Schwab's full-service brokerage platform, which also includes banking through Schwab Bank. The company's client solutions encompass Schwab's third-party mutual fund, ETF and fixed income platforms, managed account solutions, alternative investments, insurance services, and cash and margin lending products.

Company History

- **1963:** Charles Schwab together with 3 other partners launched an investment advisory newsletter, *Investment Indicator*, which grew to have 3,000 subscribers paying an annual subscription fee of \$84.
 - *"If you do the math, the newsletter kicked off maybe a quarter of a million dollars per year in gross revenues, which was not bad considering that the median annual household income in 1965 was \$6,597"* - [Book by John Kador](#)
- **1971:** In April, Schwab set up his own stock brokerage company called First Commander Corporation, to carry out brokerage services and publish the newsletter. Schwab bought out the other partners in 1972 and renamed the company [Charles Schwab & Co](#) the following year.
- **1975:** A major turning point came when the Securities Acts Amendments of 1975 deregulated the securities industry and allowed for negotiated commission rates. Schwab, who had long complained about the lack of focus on the customer, started charging half the fees of what full-service brokers did and the business took off as a result.

- **1980:** In an industry first, the company established the first 24-hour quotation service that would allow customers to place orders from anywhere, at any time.
 - **1981:** Schwab became a member of the [NYSE](#), and the total of client accounts grew to 222,000. The New York Stock Exchange enthusiastically welcomes Chuck.
 - **1982:** Schwab became the first broker to offer 24/7 order entry and quote service. The company opens its first international office in Hong Kong. The IRA account is introduced.
 - **1983:** Stephen McLin purchased the company for \$55 million on behalf of Bank of America. Four years later, Charles Schwab bought the company back from Bank of America for \$280 million. In September of that year, they did their IPO which was followed a month later by the market crash.
 - **1995:** The company acquired [The Hampton Company](#), founded by Walter W. Bettinger, who became CEO of Schwab in 2008. They also launched their first website at [schwab.com](#)
 - **1996:** Their Web trading platform, the country's first, goes live. Online trading grew from zero in 1995 to account for [84% of all stock trades](#) made through Schwab by 2000.
 - **1999:** Schwab launches after-hours trading for Nasdaq and select listed stocks.
 - *Fun fact: "In 1999, the market value of Schwab eclipsed that of Merrill Lynch, the country's largest full-service broker, despite Schwab's revenues being more than 60% lower"*
 - **2000 - 2003:** The firm introduces pre-market trading for most Nasdaq and listed securities and acquired the US Trust. This period was quite challenging for the company as the dot-com bubble burst and the [volume of online trading fell](#) from an average of 204,000 trades a day in 2000 to 112,000 trades a day in 2002. To understand the impact on the [share price](#):
 - *"In 2003 Schwab's revenues and net income fell sharply and the stock price tumbled from a high of \$51.70 a share in 1999 to a low of \$6.30 in early 2003"*
 - **2003:** Charles Schwab stepped down as CEO and handed the role over to Dave Pottruck. He retains the Chairman role. The company's board fired Pottruck only a year later, reinstating Schwab as CEO.
 - **2005:** Schwab eliminates account service and order-handling fees for retail accounts and small business retirement plans.
 - **2008:** Charles Schwab steps down again and Walter W. Bettinger is named Chief Executive. The firm survived the financial crisis of 2008 without needing a government bailout while remaining solidly profitable.
 - **2011:** The company [acquired](#) OptionsXpress, a leading options broker/dealer, and Compliance11, a provider of compliance software.
 - **2019:** Schwab announces zero-commission online trades
- 2020:** Schwab [completed the acquisition](#) of TD Ameritrade for \$26 billion in an all-stock transaction. This acquisition brought 12 million client accounts, \$1.3 trillion in client assets, and \$5 billion in annual revenue to Schwab.

Key People

- **Charles Schwab, Founder, and Chairman**
 - Schwab was born in Sacramento, California. He holds a Master of Business Administration from Stanford Graduate School of Business. He has co-authored numerous successful personal finance and investing books, including [How to Be Your Own Stockbroker](#), [Charles Schwab's Guide to Financial Independence](#), [It Pays To Talk, You're Fifty—Now What?](#) and his most recent book, [Invested: Changing Forever the Way Americans Invest](#) was released in October 2019.
 - *"To say Charles Schwab is an entrepreneur is actually an understatement. He really is a revolutionary."—Phil Knight, co-founder of Nike, author of Shoe Dog*
- **Walt Bettinger II, CEO**
 - Born in 1961, Bettinger has been Chief Executive Officer of the Charles Schwab Corporation since late 2008. Schwab's market capitalization has increased from \$18 billion to a peak of \$180 billion (in January 2022) over

his tenure.

- Bettinger created The Hampton Company, a supplier of retirement plan services to firms and their workers, at the age of 22 in 1983. Hampton was purchased by Schwab in 1995.

Business Model

▷ Value proposition

- The company started off as a traditional brokerage firm but has evolved into a provider of full-service investing and banking experience to clients locally and internationally. The firm has a strong history of creating value for its customers through;
 - **Being a low-cost provider:** The firm pioneered discount brokerage to open up the market to individual investors who didn't have access to Wall Street. The business is built around keeping costs as low as possible which enables the firm to offer competitively priced products and services.
 - **Leveraging tech:** The firm has consistently invested in technology to become more efficient, which allows for low cost and innovative products.
 - **Delivering excellent customer service.** From the very beginning to date, the firm's actions and decisions are driven by the belief that business should focus on service and not sales. Schwab strives to see things through the eyes of their client.
 - "Today's consumers expect great value, a great experience, and a refund if they aren't satisfied. We believe a modern investing experience should deliver on these expectations—period." - Walt Bettinger, CEO, Charles Schwab
- The firm focuses on the **Schwab Way** by asking the question: "Isn't there a better way?". Charles' goal was to build a company that would make investing easier and more accessible to clients. The firm is built around "putting the client first". They take a human approach to financial services and provide better, more intelligent modern ways to build and manage wealth.
- The **Schwab virtuous cycle** ensures that they focus on rewarding and recognizing all relevant stakeholders by providing benefits that encourage them to maintain their relationship with the firm.



Note: All growth metrics are 2021 vs. 2016.
Financial results include TD Ameritrade from October 6, 2020, forward.

- **The firm's products and services include brokerage accounts, mutual funds, exchange-traded funds (ETFs), advice solutions, banking, and Trust. These products and services are provided through investor and advisor services.**
 - **Investor Services:** The company operates in the retail brokerage and banking segments. The services are offered through a multi-channel service delivery model which includes online, mobile, telephone, and branch support. It also offers customized services which include financial planning, managed investing, estate

management, equity compensation, and lending. The company's managed portfolio exclusively invests in mutual funds and Exchange Traded Funds.

- **Advisor Services:** The company also provides recordkeepers and independent retirement advisors with retirement business services. Schwab is one of the largest institutions that provide custodial, trading, banking, and support services to registered investment advisory clients. Other than the platform, Schwab also has thought leadership, educational content, and interactive tools on its website

Economics

Key Metrics:

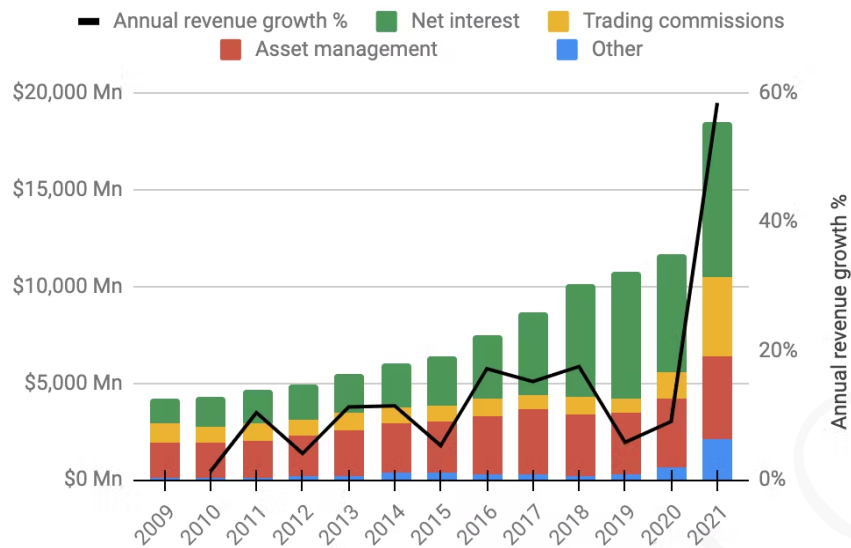
- In October 2004, when Charles Schwab returned to the company, he set some goals for the company, which have stayed with them through the last 2 decades of operations:
 - *"In a small meeting room in the bowels of a downtown Manhattan hotel, I... laid out very specific markers that they could use to measure our success. The markers included increased client satisfaction; growth in new accounts and assets; double-digit revenue growth even in a down market; a pretax margin of greater than 25%; return on equity of 15% or greater; annual revenue per employee of \$300,000; and revenue per dollar of client assets at 0.5%"* - Invested: Changing Forever the Way Americans Invest by [Charles Schwab](#)
- **From the past 5 years, here are the key metrics:**

	2017	2018	2019	2020	2021	5 -Year CAGR
Revenues (\$ Billions)	8.6	10.1	10.7	11.7	18.5	21%
Revenue growth:	15%	17%	6%	9%	58%	
Pretax profits (\$ Billions)	3.7	4.6	4.8	4.3	7.7	21%
Pretax margin	42%	45%	45%	37%	42%	
Net Income (\$ Billions)	2.4	3.5	3.7	3.3	5.9	25%
Net income margin	28%	35%	35%	28%	32%	
Equity	18.5	20.7	21.7	56.1	56.3	32%
ROE	15%	19%	19%	9%	11%	
Client AUM (\$ Trillions)	3.4	3.3	4	6.7	8.1	24%
Revenue per dollar of client assets	0.25%	0.31%	0.27%	0.17%	0.23%	

Revenues:

- The company's total revenues were \$18.5B in 2021 with a 5-year CAGR of 20%. The trajectory of the company's revenue over the past decade is shown below.

Annual Revenue



(Source: Seeking Alpha)

- The company's total revenues can be broken into five segments: *interest revenue, asset management and administration fees, trading fees bank deposits & account fees and others.*

Year Ended December 31,	Growth Rate 2020-2021	2021		2020		2019	
		Amount	% of Total Net Revenues	Amount	% of Total Net Revenues	Amount	% of Total Net Revenues
Net interest revenue							
Interest revenue	30%	\$ 8,506	46%	\$ 6,531	56%	\$ 7,580	71%
Interest expense	14%	(476)	(3)%	(418)	(4)%	(1,064)	(10)%
Net interest revenue	31%	8,030	43%	6,113	52%	6,516	61%
Asset management and administration fees							
Mutual funds, ETFs, and collective trust funds (CTFs)	11%	1,961	11%	1,770	15%	1,747	16%
Advice solutions	38%	1,993	11%	1,443	12%	1,198	11%
Other	22%	320	1%	262	3%	266	3%
Asset management and administration fees	23%	4,274	23%	3,475	30%	3,211	30%
Trading revenue							
Commissions	177%	2,050	11%	739	6%	549	5%
Order flow revenue	N/M	2,053	11%	621	6%	135	1%
Principal transactions	(13)%	49	—	56	—	68	1%
Trading revenue	193%	4,152	22%	1,416	12%	752	7%
Bank deposit account fees	N/M	1,315	7%	355	3%	—	—
Other	126%	749	5%	332	3%	242	2%
Total net revenues	58%	\$ 18,520	100%	\$ 11,691	100%	\$ 10,721	100%

N/M Not meaningful. Percentage changes greater than 200% are presented as not meaningful.

(Source: 2021 Annual Report)

- Net Interest Revenue:** This is the interest earned on loans and margin receivables net of interest expense on funding sources. The company's un-invested client cash balances on the balance sheet remain the primary funding source for interest-earning assets. Their interest-earning assets primarily comprise bank loans, margin loans, and fixed-income securities. Interest revenue, by some margin, is the company's largest source of revenue.
- Asset Management and Administration Fees:** This is their second-largest revenue stream accounting for 23% of total net revenues in 2021 and were up 23% YoY. The company earns fees from managing proprietary money market mutual funds, ETFs, and advisory services in addition to some third-party funds. They also earn management fees for advice solutions.
 - Depending on the type of account and strategy, management fees start at 0.55% to 1.00% with account minimums between \$25,000 to \$1 million.
 - Schwab Asset Management provides a concentrated portfolio of competitively priced mutual funds, ETFs, and individually managed account strategies.

Schwab Assets Under Management (\$)

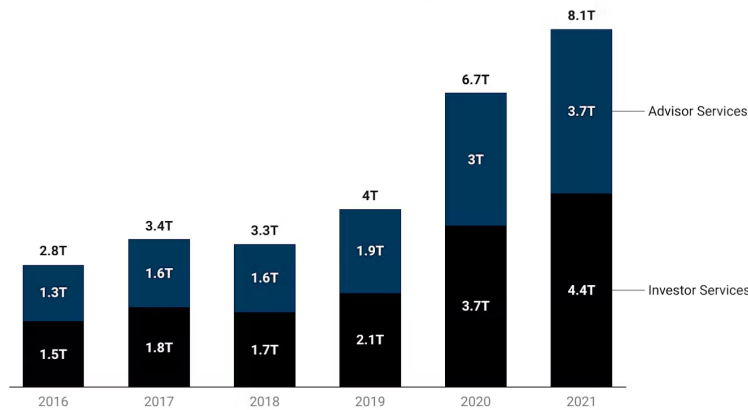


Chart: @ekmokaya • Source: Company Financial Statements • Created with Datawrapper

- **Trading Revenue:** Trading revenues come from Commissions, Order flow revenue, and Principal transaction. It accounted for roughly 22% of the firm's 2021 revenues. These were up a staggering 193% YoY in 2021 and 88% YoY in 2020.
- **Bank Deposit Account Fees:** Accounts for 7% of total revenues. Charles Schwab has a number of [money transfer options](#) all of which are free except for wire transfers.
- **Other Revenues:** Includes order flow income, service fees, software fees, and exchange processing fees. This is responsible for 5% of Schwab's total revenue.

Cost Structures:

- The key cost item for Schwab include compensation and benefits which constitutes 29% of total net revenues and constitute 50% of total expenses in 2021.
- Capex was 6% of net revenues in 2021.

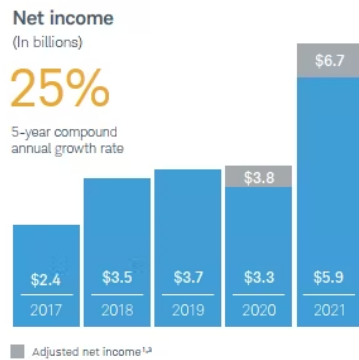
	Growth Rate 2020-2021	2021	2020	2019
Compensation and benefits				
Salaries and wages	31%	\$ 3,161	\$ 2,416	\$ 1,958
Incentive compensation	55%	1,443	932	804
Employee benefits and other	40%	846	606	558
Total compensation and benefits	38%	\$ 5,450	\$ 3,954	\$ 3,320
Professional services	18%	994	843	702
Occupancy and equipment	39%	976	703	559
Advertising and market development	49%	485	326	307
Communications	66%	587	353	253
Depreciation and amortization	33%	549	414	322
Amortization of acquired intangible assets	N/M	615	190	27
Regulatory fees and assessments	69%	275	163	122
Other	97%	876	445	261
Total expenses excluding interest	46%	\$ 10,807	\$ 7,391	\$ 5,873
Expenses as a percentage of total net revenues				
Compensation and benefits		29%	34%	31%
Advertising and market development		3%	3%	3%
Full-time equivalent employees (in thousands)				
At year end	4%	33.4	32.0	19.7
Average	36%	32.5	23.9	20.0

N/M Not meaningful. Percentage changes greater than 200% are presented as not meaningful.

(Source: 2021 Annual Report)

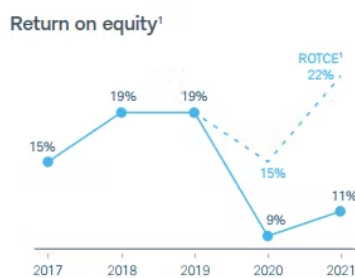
Profitability:

- The company was able to achieve a pre-tax profit margin of 41.6% in 2021. The pre-tax profit margins have been between 37% and 42% in the past 5 years.
- Over the past five years, Schwab has posted increasing revenue (16.5% CAGR) and has equally posted increasing net income (25% CAGR).



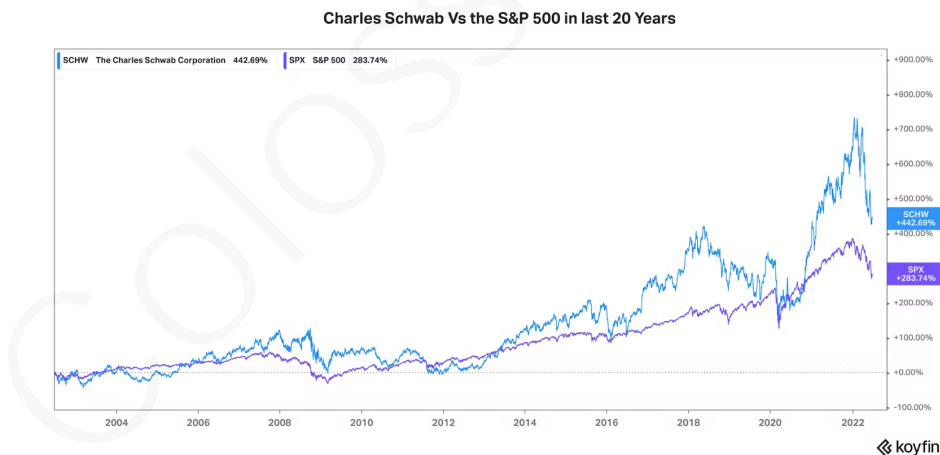
(Source: 2021 Annual Report)

- The return on equity averaged around 14.6% in the last 5 years.



(Source: 2021 Annual Report)

Stock Performance vs. Benchmark (since inception)



Competitive Position

- Traditional financial institutions are looking for ways to accelerate the digital transformation of their wealth management services as emerging fintech firms continue to threaten them. The number of customers using fintech platforms for wealth management is increasing compared to those using traditional financial institutions. These institutions need to provide value-add services and/or compete on price in order to stay relevant.
- Clients' expectations are shifting in regards to the services they receive, how they interact with those services and how well these services can help them achieve their goals. A good number of clients prefer to have their financial activities integrated into one place - a firm that can offer this will have an edge over the rest.

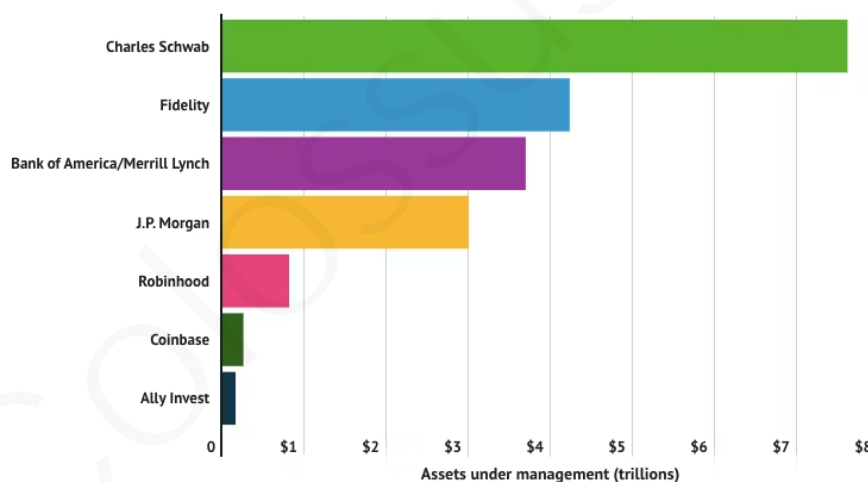
- The firm operates in a highly competitive environment characterized by aggressive price wars. It competes with several firms in retail brokerage services, banking services, and advisory services.
- Some of the competitors include Vanguard, Fidelity, J.P Morgan, Interactive Brokers, Robinhood, Bank of America, Morgan Stanley, Wells Fargo, and Blackrock.

Best Online Stock Brokers 2022: Best Overall Customer Experience	
Broker	Strengths
Fidelity	Fidelity is a perennial leader in our survey, finishing with the top overall rating in six of the past eight years. This year it ranks in the top three in 12 of the 15 performance categories below and earned the top customer rating in seven of them. Its scores for Trade Execution Speed/Price and Website Security set the high marks for customer experience. Read more about Fidelity.
Charles Schwab	Schwab is the only broker to stand among the top three in Overall Customer Experience in all 10 years of our survey. This year it ranks among the leaders in 11 of the 15 performance categories. Its Customer Service rating from its clients was the top score in that category and stood well above the rest of the brokers. Read more about Charles Schwab.
E-Trade	E-Trade broke through to the top three brokers in our survey for the first time. Its best showing was in Trade Ideas, where it earned the second-highest rating. It ranked among the leaders in four other categories: Mobile Trading Platforms, Premarket/Aftermarket Trading, Options Trading Platform and Availability Of Account Types. Read more about E-Trade.

(Source: [Investors.com](https://www.investors.com))

- **Competitors by AUM:** Charles Schwab is the largest brokerage firm with over \$7.6 trillion in assets under management in 2021. This space is clearly growing – Robinhood and Coinbase (though not technically a brokerage) have seen incredible growth in 2021 with AUMs up a 311% and 608% respectively.

The largest stock brokerage firms by assets under management



Note: Coinbase isn't a stock brokerage firm, but we've included it here to show just how popular cryptocurrency is.

(Source: [The Motley Fool](https://www.motleyfool.com))

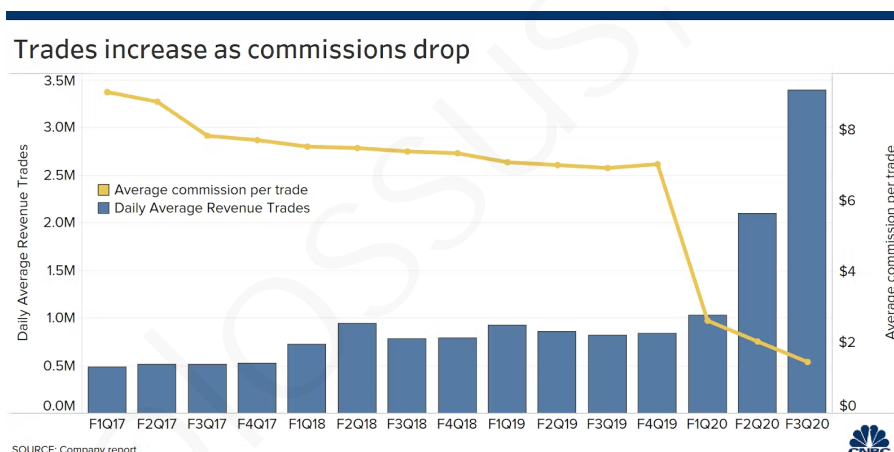
Competitive advantages:

- **Client-first:** From its very beginnings the firm has always had an obsessive focus on the customer. The firm has challenged long-held industry practices to create a better experience for the client and fostering deep personal relationships with customers.
 - "Always put the client first... No matter what." - Charles Schwab
 - "...forging personal relationships through digital channels and delivering superior customer service have helped brands such as Charles Schwab, Discover and American Express become direct banking powerhouses" - J.D. Power 2022 U.S. Direct Banking Satisfaction Study

- **Fast and first-mover advantage:** The firm is a fast mover in adopting and leveraging tech to deliver value. It automated its systems long before its competitors and has leveraged technology over the years and reaped huge rewards from this. At the onset of the internet boom in 1996, Schwab was the first to venture into online trading and within three years became the No. 1 online trader. They were also the first among the traditional brokers to slash trading commissions to zero, following in the footsteps of online broker Robinhood.
- **Strategic M&A:** The company has a strong history of making strategic acquisitions to bolster assets under management or to help it enter new markets. Schwab has made a total of [10 acquisitions](#) including its largest acquisition of TD Ameritrade for \$26 billion in November 2019. To add to that, Schwab has also made 12 investments, 2 lead investments, and 4 successful exits.
- **Strong brand name:** Charles Schwab is a well-known brand name in the US. Their marketing normally features Charles's photo in marketing ads which provides a personal touch that gives its customers a feeling of being able to relate to a human.
- **Economies of scale:** Being one of the largest investment firms in the US, the company is able to reduce costs and increase the capacity to serve clients through sharing of infrastructure and resources across its subsidiaries. This results in competitively priced products and services.

Risks and Challenges:

- **Fee compression and race to the bottom:** With increased competition in this space, there has been a steady decline in trading commissions over time. The aim of reducing fees is to drive up the volumes of trades which has proved true as the figure below shows. This has also forced brokerage houses to look for alternative ways to make money. For Schwab, that has meant investing more in offering investment advice and guidance and in building its assets under management, especially via acquisitions.







(Source: CNBC/Schwab)

- **Crypto and blockchain technologies and the era of Robinhood:** The rise of crypto and the fractionalization of shares has meant that firms like Schwab have had to adapt to the times. More younger investors are interested in crypto and in trading on Robinhood. In this regard, Schwab has [added](#) the ability to trade cryptocurrency products, including coin trusts and bitcoin futures. Schwab has planned to launch its own crypto ETF, in order to attract this sort of clientele.
- **Fraud:** The company has been [charged by SEC](#) for allocating clients' funds in a less profitable manner and failure to disclose hidden fees. For a firm that is supposedly built on putting the client first, isn't this inconsistent with its purpose of "championing every client's goal with passion and integrity"?

Useful Resources

Title	Type	What You Will Learn (sub-140 characters)	URL (Must be https://)
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Thursday Deep Dive: Charles Schwab	Podcast	An exploration of Charles Schwab's history, industry, management and performance.	
EP 78: Raul Rodriguez, Charles Schwab	Podcast	A conversation with Raul, Managing Director, Innovation Accelerator at Charles Schwab, on what it takes to build and foster a culture of innovation at a large-scale financial institution.	
Charles Schwab Liz Ann Sonders: Masters in Business (Audio)	Podcast	A conversation with Liz, Managing Director and Chief Investment Strategist at Charles Schwab on her career journey, and	
Can the Fed Win the Inflation Battle?	Podcast	Liz, Managing Director and Chief Investment Strategist at Charles Schwab, discusses the Fed's aggressive approach on inflation, and the chances of a recession.	
Charles Schwab: How One Company Beat Wall Street and Reinvented the Brokerage	Book	Kador explores how Schwab reinvented the brokerage industry, and provides valuable lessons on how businesses can survive and thrive in any	