

Concentrated stock strategies



Wealth
Management

The stock of a single company may represent a considerable portion of your wealth because the proportional value of the stock contributes to your overall investment portfolio. When that happens much of your wealth is concentrated in that one position.

Generally speaking, any individual stock position that makes up more than 20% of the value of your total investment portfolio is considered a “concentrated position.”

How it happens

Concentrated stock positions are built every day. You may develop yours through employer retirement plans, inheritances, employee stock options or selling businesses. You may also accumulate such a position over time when stocks achieve superior returns and/or through splits and dividend reinvestment opportunities. Plus, they can result from avoiding rebalancing a low cost basis stock that has grown in value because of capital gain tax consequences. Or they may be the product of owning restricted or controlled shares that may be difficult to trade because of securities regulations. So there are many ways you may acquire a concentrated stock position.

Potential drawbacks

It is not uncommon for people to develop an emotional attachment with a concentrated stock position. While this is understandable given the role it may have played in your financial success, it can be a concern, because it may make diversification decisions

difficult to both think about and follow through. Another possible problem is that a concentrated stock position makes a large portion of your wealth dependent on the movement of one particular stock. Which means you may be exposed to greater volatility, lower liquidity and higher risk compared to a more diversified portfolio.

What can you do?

A highly concentrated equity position can serve as a cornerstone of your financial security. So it may be prudent to develop an exit strategy to help maximize the value and minimize the risk intrinsic to your concentrated stock position.

Our consultative process

Your RBC Wealth Management[®] financial advisor can collaborate with experienced concentrated stock diversification specialists to help you choose a strategy appropriate for your unique goals and circumstances. Our goal is to help you address three important issues:

1. **Liquidity:** How can a concentrated position be monetized most efficiently?
2. **Taxes:** Are there prudent alternatives available to minimize or defer the tax consequences of enjoying your hard-earned rewards?
3. **Risk:** How should you gauge and manage the risk inherent in a concentrated position?

Key considerations

No two transactions are the same. Before we begin, we will answer questions related to the opportunities, requirements and hazards that define the parameters of a successful exit strategy:

- Are you classified as an insider after the event and subject to restrictions?
- Are there any political issues within the firm or among shareholders as you diversify?
- Do you have a need for short-term liquidity?
- How much risk are you comfortable assuming during the diversification process?
- What are your wealth management objectives following diversification?
- What is your opinion on the near-term prospects for the stock, as well as those of our own analysts?
- What is the relative size of your holding to your total assets?

Determining an approach

Analyzing and quantifying the cost and risk of your position compared with a diversified portfolio is the first step. The next step involves your current tax situation and considers the implications of diversification. These steps enable us to visually explain and compare strategies. Having a clear, objective presentation of all possible diversification techniques provides the information you need to make a well informed decision. This may also help you feel more confident about taking action, and more likely to do so.

Choices

We can review a variety of techniques to diversify the position in the most efficient way, including the following:

- Selling now
- Selling over time
- Employee stock option exercise strategy
- **Gain liquidity** — find ways to increase accessibility of wealth with or without an actual sale, using loans and pre-paid forward contracts
- **Hedge and speculate** — Utilize simple or complex instruments or opportunities, such as: equity collars, pre-paid forward contracts, protective puts, covered calls, exchange funds or transfer wealth to family and or charity
- **Transfer wealth** — Consider wealth transfer strategies that benefit you, your family or charity, including family gifting strategies, charitable gifting strategies (direct gifts, charitable foundation or charitable remainder trust)

Gain peace of mind

Choosing and implementing a concentrated stock exit strategy appropriate for your situation and objectives depends on having access to planning, quantitative, trading and derivatives expertise. Your RBC Wealth Management financial advisor can deliver strategies and solutions to help you effectively manage and diversify concentrated stock positions — while also helping you accomplish your overall wealth management goals. Contact them today to discuss concentrated stock strategies right for you.

Options are not suitable for all investors. Prior to buying or selling an exchange traded option, a person must be provided with, and review, a copy of CHARACTERISTICS AND RISKS OF STANDARDIZED OPTIONS. A copy of this document may be obtained from the RBC Wealth Management® Compliance Department, 60 South Sixth Street, Minneapolis, MN 55402, phone (612) 371-2964.

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