

Overview of Prime Brokerage

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In a nutshell, a **Prime Broker** is a firm, or division of a larger financial entity, that provides a suite of services to institutional clients, e.g., hedge funds, managed funds, and other money managers.

Not only is the activity of prime broking highly profitable, but it also represents a route to sell other services to clients. Ideally, a prime broker strives to become a “one-stop shop” to its clients, thereby offering a whole range of financial services.

Prime broking started in the late 1970s, with prime brokerage business picking up in the 80s and 90s with the participation of major investment banks like Goldman Sachs and Bear Sterns. Nowadays most major investment banks have their hands in the prime broking business. Moreover, most potential and actual clients of prime brokers will often engage with multiple prime brokers to obtain the best deal.

Above there is allusion to the **Services** offered by Prime Brokers. Here they are:

- **Trade Execution and Settlement**
 - Prime Brokers impel institutions to enter orders through them as payment for their services (“soft dollars”), thus earning revenue either as trade commission or price-markup for assets traded
 - They can also offer their clients exotic or exclusive assets and derivatives
- **Securities Lending**
 - Prime brokers will most often hold shares, which they may lend to their clients in exchange for collateral¹
 - This is incredibly beneficial to firms that engage in short-selling.
- **Reporting and Reconciliation**
 - Institutions can address their accounts with executing brokers to their Prime Broker, thus making the prime broker the recipient of the paperwork, confirmations, statements, and any other documents that postdate the execution.²
 - The Prime Broker consolidates all of the above “noise” and reports back to its client
- **Trade Financing**
 - Prime brokers may act as funding intermediaries, and thus obtain better borrowing costs and terms for their clients.
 - Prime brokers will very often have greater access to funds and assets than their small / specialized clients.
- **Start-up Services**
 - Prime brokers are known to provide start-up services for hedge funds, e.g., legal, tax, IT, reporting services. They can even become “hotels” and provide an exhaustive suite of services for the right business prospects³
- **Capital Introductions**
 - Prime brokers often provide their clients with targeted introductions to pension plans, endowments, wealth funds, consultants, and private banks, in an effort to assist their clients’ day-to-day and expansion needs.⁴

Why engage in Prime Broking? The Prime Brokerage industry is now dominated by major investment banks, but, in principle, any firm that engages in Prime Broking can enjoy the following benefits:

- Earn revenue from clients’ trading activity and paid services
- Enhance and reduce the costs of a number of the broker’s activities: Trade processing, lending, etc.
- Prime broking is a conduit to strengthen and forge relationships with other financial firms, as well as means to enter new businesses

¹ <https://www.investopedia.com/terms/s/securitieslending.asp>

² <http://www.goldmansachs.com/what-we-do/securities/prime-brokerage/reporting-and-technology.html>

³ <https://www.investopedia.com/terms/p/primebrokerage.asp>

⁴ <http://www.goldmansachs.com/what-we-do/securities/prime-brokerage/capital-introduction.html>