# IMPACT OF ROBO-ADVISORS IN WEALTH MANAGMENT

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The wealth management industry is undergoing a serious transformation with traditional methods of providing financial advice being disrupted by new and innovative forms of technology. With the unprecedented widespread adoption of the internet and digital devices, customer expectations have changed. Clients expect a flawless customer experience that requires businesses, products, and services to be available whenever and wherever they want. It's that simple. Companies that provide wealth management services must address this trend quickly or risk being left behind.

## A BRIEF REVIEW OF WEALTH MANAGEMENT

According to Investopedia, wealth management is a "service that combines financial/investment advice, accounting/tax services, retirement planning, and legal/estate planning for one fee." While that definition is an oversimplification of the term, it's safe to say that wealth management has historically been a service for high-net-worth individuals.

For purposes of our conversation, note that Investopedia indicates that high-net-worth individuals typically have at least $1 million in liquid assets. Those with more than $5 million are considered very-high-net-worth individuals. Have $50 million in wealth? Then you're an ultra-high-net-worth individual. If you're not fortunate enough to fall into any of those categories, chances are you've never been a good prospect for a company focused on providing wealth management services. The fees would simply be too high for the individual investor and, frankly, the bank wouldn't make enough money from you as a customer.

While this is how wealth management has operated for decades, that doesn't mean that it should stay that way. It doesn't mean that an individual investor, without an accumulation of massive wealth, shouldn't be able to receive the same solid financial advice the wealthy do.

## WHAT ARE ROBO-ADVISORS?

While your clients may have never obtained advice from traditional wealth management companies, the times are changing through the introduction of robo-advisors.

Unlike traditional human-to-human financial advice, robo-advisors provide personalized, automated financial advice based on algorithms. They work without the need for human intervention, making such advice cost-friendly and ultimately eliminating common high-net-worth membership figures.

Robo-advisors can tell investors:

- How to allocate their money across stocks and bonds, keeping your risk tolerance in mind
- How much to deposit each month based on the total amount they want to invest and their goals
- Their total net worth
- How to take advantage of advanced tax strategies

According to some reports, tens of billions of dollars are currently being managed by robo-advisors, and some estimates indicate that robo-advisors could be managing hundreds of billions, and possibly even trillions, of dollars in just a few years.

## THE ROBO-ADVISOR CLIMATE

The benefits of robo-advisors are clear: trustworthy and affordable financial advice for everyone, regardless of net worth. Although some may debate what role robo-advising will play in wealth management, we've reached a point where it's hard to imagine a world without it.

Ever since the evolution of the internet and the widespread adoption of digital devices, customer expectations have changed and continue to do so at a rapid pace. Today, convenience is a top customer priority. Many people either don't want or are unable to spend the time it takes to visit a physical location or talk on the phone to manage their daily lives – including their wealth. Instead, they prefer to manage everything from the convenience of their homes or offices.

For financial institutions to remain relevant in wealth management, they must adapt to the new digital times by transforming the way they operate. We're seeing this digital transformation taking place now. Wealth management firms are partnering with, acquiring, and even building their own technology solutions to meet the increasing demand for a better customer experience that robo-advisors offer.

Human-to-human interaction is strong, and traditional wealth management services offer a sense of trust. If an investor goes to a financial advisor and asks where to invest, he or she will provide recommendations. Chances are, the client won't question them. They'll just choose what they like best.

However, digital technology such as robo-advisors also has the benefit of being transparent. These solutions will review all your clients' assets, give them a complete view of where they stand and where they should be, and then provide a set of recommendations with reasons for each one.

While the vast majority of assets are still with traditional financial institutions, this is changing. More and more, individuals are leveraging robo-advisors due to their convenience, ease of use, affordability, and transparency. As people learn about their options with robo-advising, we will likely see that portion of the market grow.

## HOW TRADITIONAL WEALTH MANAGEMENT COMPANIES VIEW ROBO-ADVISORS

As much as they are disruptors of sorts, traditional banks view robo-advisors as healthy. They represent a challenge for incumbents, one that will ultimately result in better customer experiences. Financial institutions believe that the foundation of what they do is not going to go away; however, it puts pressure on them to focus on the customer experience and, ultimately, the customer journey.

The conversation between incumbents and entrants has evolved over time. It went from hostility to a much healthier debate on how all parties are going to collaborate. Incumbents have been around for a very long time and customers have made a conscious decision to trust them with their assets. Trust is the foundation.

Robo-advisors may not necessarily eliminate traditional human-to-human relationships, but they put the onus on traditional banks to put forth a better customer experience with digital technology. If banks don't respond to the challenge and stick their heads in the sand, customers will gravitate towards convenience and simplicity. The pressure is no doubt real.

Traditional wealth management services and robo-advising are actually quite complementary. Part of the market currently wants, and will continue to want, a hands-off approach to investing and wealth management, one in which everything is done for them. On the other hand, a growing portion of the market prefers to manage their wealth on their own. To meet this new demand from current and potential clients, banks must satisfy their thirst for this digital experience. Robo-advisor tools can help address this need.

## THE RELATIONSHIP BETWEEN WEALTH MANAGEMENT COMPANIES AND ROBO-ADVISORS

Many robo-advisors are thriving with growing customer bases. Not only are they flourishing, they're partnering with – and in some cases being acquired by – traditional institutions that offer wealth management services. Take UBS, for example. The company's wealth management division recently formed a strategic alliance with SigFig, a robo-advisor that will help develop solutions for the bank's wealth management advisors that ultimately enhance their clients' digital experience. Two other notable examples include Ally Financial's acquisition of TradeKing and Blackrock's purchase of FutureAdvisor.

The automation that robo-advisors provide drives down costs and enables better control and compliance. It gives firms scale by allowing them to better serve existing customers and address new segments of clients who were traditionally unserved by wealth management institutions due to a lack of assets. Remember, robo-advisors eliminate the need to hand-hold, therefore allowing financial advisors to support those who prefer more attention. The robo-advising model simply gives banks the opportunity to scale while meeting customer expectations for a better digital experience.

Some companies, like HSBC, have historically taken a slightly different approach. Similar to the way they built a traditional IT business that keeps the lights running and software applications up-to-date, they invested heavily in technology and innovation rather than acquiring FinTech companies. Other financial institutions, such as Vanguard, Bank of America, and E*TRADE, continue to pour money into developing their own robo-advising solutions. Today, they're collaborating with all the big names in IT to improve what they do for customers from beginning to end.

## REPLACING TRADITIONAL WEALTH MANAGEMENT OFFERINGS WITH ROBO-ADVISORS

Robo-advising will likely never take over wealth management, but there are certain elements it could replace. For example, tax-loss harvesting and digital account opening can be streamlined through technology and automation. Any tasks that serve as barriers to receiving services should be accomplished by machine. Financial advisors should instead do more of what they do best.

Customer engagement is key in banking, especially with the seemingly ongoing market turmoil. Old methods of communicating, such as calling and emailing on a one-off basis, are unsustainable. Automation and smart machines enable you to communicate with all customers quickly and personably, whether it's through an email or a text message. It's something all customers expect. Robo-advising can help provide better, more efficient communication methods, resulting in better customer service.

One particular area in which robo-advisors can make a positive impact is advisory services. With the high costs of advisory services and thresholds that enable one to obtain financial help, a massive portion of the investing population is being excluded.

Robo-advising isn't just for people with lower assets than high-net-worth individuals. High-net-worth individuals are also showing interest in this technology because the fees aren't as high, it's easy to use, and it gives investors the feeling of more control than what they would probably feel with traditional wealth management firms.

While many believe that millennials are the best – if not the only – target for robo-advisors because of their lack of wealth, the data shows otherwise. FutureAdvisor reported that more than half its clients are over the age of 40. For Betterment, 25% of its business comes from customers over the age of 50. All age groups are interested in and choosing this service because of the convenience the technology brings to the table. In fact, many are going straight to digital investing tools, bypassing traditional wealth management institutions altogether.

## WORLD VIEW OF ROBO-ADVISORS

Depending on where investors are located in the world, investor behavior is vastly different; therefore, robo-advising may play a different role depending on the region. Some counties are more conservative and prefer traditional forms of wealth management services, while others are much more comfortable with investing on their own. The World Economic Forum conducted research into online behavior and concluded that people who use the internet in emerging markets are much more open and willing to experiment with innovative solutions than those in developed markets.

While geographies dictate how robo-advising is perceived, the same can be said for psychographics. Each segment of a robo-advisor's customer base has differences in terms of engagement and conversation rates. Aside from demographics and psychographics, it's also important to remember that industry regulations naturally play a role in the adoption of new banking technologies. The bottom line is this: companies and governments should meet the expectations of their constituents with the right products and services.

## FUTURE OF ROBO-ADVISORS

There's no question that the core function of managing money in a heavily regulated industry is difficult and expensive. New companies with robo-advising technology will need to learn how to navigate the regulatory landscape, making it critical to collaborate with traditional wealth management firms.

From a bank's perspective, robo-advising remains critical in terms of servicing customers. Banking's familiarity with rules and regulations is unmatched and the personal touch one feels coming into an office creates trust that is irreplaceable. For companies with customers who are not comfortable with investing or navigating the financial markets, banks are a saving grace.

On the other hand, services delivery can still be through a mechanism other than humans. In the financial services industry, consider large broker-dealers like Vanguard and Fidelity, which carry people's entire savings. These customers have never met an employee. Outside the industry, take Uber. Chances are you have never met the Uber driver who recently started working for the company, yet you are able to trust the operating model. Boundaries will be broken. The average retail investor today has the confidence to go straight to robo-advising. In due time, we're likely to see that segment of the market increase.

The future of robo-advising is very bright. In business, we tend to overestimate progress in the near term and underestimate the impact and direction things will take in the long term. As with most technology, slow adoption for a short period of time is not out of the ordinary. At some point there will be an S-curve and a point of no return.

It's in the best interest of financial institutions to invest in these digital solutions and be there when it takes off. The key is to not miss the boat. Those who recognize the benefits and future of robo-advising first will lead the way.

The perfect scenario for the wealth management industry is this: in several years, we won't necessarily be discussing the effect robo-advising is having on financial institutions. Instead, robo-advising will be a tool used by nearly everyone, from financial advisors in wealth management firms to the average at-home retail investor. The cost savings and better customer experience offered by robo-advising are a win-win for everyone.

## WHY PERFICIENT

Whether it's keeping pace with today's digital transformation and cross-channel customer experience demands, improving operational efficiency, or dealing with the complexities of regulatory reform, we're helping you redefine the future of financial services for your customers.

Companies in banking, asset and wealth management, capital markets, and insurance turn to us to help solve their most complex business and technology challenges.