How to build a successful robo (yes, a robo)

Once seen as an imminent existential threat for human advisers, the growth of the robo-advice market has yet to realise its enormous potential. A recent Cerulli report shows profitability as the number one headwind for digital or robo-advisers, with a significant number of offerings failing to gather significant assets under management.

UK investors have seen a proliferation of robo-adviser and digital investment platforms enter the UK market, offering easy-to-understand, low-cost digital investment services. This is a great outcome for consumers, who now have more options than ever before when it comes to financial advice, with many at a lower cost with less jargon.

And this is set to continue. Nutmeg passed a significant milestone after its assets under management in the UK rose above the £2B threshold. The digital wealth business' client numbers are now at 78,000 and it expects strong demand in 2020. In December, Scalable Capital recently claimed the pole position in the European robo race, as assets hit €2B.

The emergence of low-cost robo-advisers has been seen as a possible solution to those with smaller investment pots, despite the digital propositions' relative infancy. Research by YouGov and Open Money has shown that 5.8M people in the UK are willing to pay for advice, but think it is too expensive, with a further 14M people neither knowing how to obtain financial advice nor considering it as an option.

Startup slow down

Since Nutmeg's 2012 launch in the UK, we have witnessed a wave of innovative disrupters entering the digital wealth space, aiming to take market share from the traditional wealth management sector – guardian to more than one trillion in assets under management.

According to a 2015 study by Accenture, an inter-generational transfer of $30T is expected between 2011 and 2050 in North America alone, whilst in the UK, research from CEBR in 2017 has projected that £1T is set to pass to the next generation in the decade from 2017 to 2027, representing a significant opportunity for financial adviser and the wealth management industry.

Despite the seismic impact of *robos*, which has forced traditional wealth managers to embrace tech, a number of digital propositions have struggled. HSBC issued a sobering report last year on the wealth management industry, revealing the stark difficulties facing robo-advisers and digital advice platforms. The report found that a robo-advisor (assuming a 0.45% fee) operating in Europe would require between $3.5B and $5.3B of assets under management to break-even, highlighting the importance of scale and efficiency in the robo business model.

But as we have seen some propositions struggle, we are also seeing emerging winners increase customers and take market share amidst growing consumer demand. The question is: what is the secret of success in the robo world?

How robos can win

A differentiated edge is crucial, but the ability to achieve foundational efficiencies is perhaps more vital to a sustainable digital platform. In supporting a diverse range of these platforms, we have observed one critical success factor – the ability to create and maintain strategic partnerships that drive efficiencies and support collaborative ecosystems.

Having outsourced providers enables you to embed important cost savings that are crucial to long-term success. By tapping into the leading-edge institutional infrastructure, such as custody and dealing, digital advice services not only reduce costs and achieve best-in-class operational efficiencies, they also free up resources to focus on core capabilities and, crucially, attract and increase clients and assets.

Outsourcing also enhances propositions by delivering in-built innovation. For example, fractional dealing allows platforms and advisers to invest any amount of money easily and cost-effectively, so clients can better pursue their financial goals.

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Often and early

Fractionals are leading the way in the 'democratisation' of investing, helping to lower the barrier to entry for retail investors and supporting a key trend in savings – the concept of 'round-ups'. This is investing or saving spare change automatically from everyday purchases.

We are already seeing this fractional technology being used by popular digital advice propositions, such as Moneybox, to help millennials save early and often. Fractionals also create efficiencies in portfolio rebalancing – optimising allocations and investment returns.

Innovation is enabling financial services to catch up with other industries quicker to adopt technology that enhances customers journeys. Through integration via APIs, open banking offers a game-changing level of accessibility to financial services, creating seamless experiences, as customers have come to expect from Amazon, Paypal, etc.

At the forefront in breaking down barriers and improving choice are pioneering digital platforms like Wealthify, whose intuitive, the jargon-free approach is a breath of fresh air. Wealthify is also raising the bar for investor engagement by creating engaging and easy-to-understand communications. This can help the financial services sector win back the trust it has lost in recent decades due to an unwillingness to embrace change.

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Aligning investor principles

Nutmeg believes it will see a surge in demand in the coming years from investors seeking to access ethical or ESG investments, as issues like climate change come to the fore, with Morningstar data confirming that global net inflows into ESG products grew by c.2500% between 2014 and 2019. This ability to align principles to portfolios has been supported by an increasingly diverse range of ETFs.

We have already started to see a proliferation of ETFs as more investors require greater choice and granularity. Existing robo solutions will pivot from the model portfolio of limited ETFs to a more expansive universe of passive choice that collaborates with individuals to create unique customer journeys. Meanwhile, biodata is going to help drill down into specific biases, such as thematic, religious and ethical, where investment options will be tailored to bespoke client needs.

Some digital firms are bringing institutional-level concepts to every-day investing. Scalable's pioneering technology adjusts the weights of the individual asset classes in a portfolio, to keep risk stable over time and deliver better risk-adjusted returns. In addition, Wealthify uses a mix of smart algorithms and human expertise to make sure plans stays on track.

The new breed of robos is also evolving their business models to provide hybrid services, comprising over-the-phone and face-to-face advisory services, recognising how the human touch can create an optimum hybrid solution. For example, Scalable's telephone advisers discuss investment profiles to tailor investment services.

As the industry has faced stiff headwinds, the winners of the robo race have begun to emerge. The direction of travel is clear: new and existing entrants must embrace collaborative partnerships that can deliver efficient, transparent and differentiated strategies.

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He has extensive experience in the design and solution side of financial services, particularly in digital wealth management, and has worked with some of the largest investment companies in the UK.

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