

ROBO AND TRADITIONAL MODELS WORKING TOGETHER

The Rise of the Digitally Augmented Advisor

By Rob Klapprodt

In 2015, a feature story in a prominent advisor trade magazine touted that one of every 10 advisors had never heard of robo-advisors.¹ Now it's hard to find any news about advisors without seeing the term "robo" attached. Most major broker-dealer platforms have launched robo solutions—Fidelity notably made a splash with robos in 2016.

Can advisors survive in an age of the robo solution? Or should they abandon the traditional press-the-flesh model and go all in on digital?

The answer depends on the advisor's or the financial institution's business model and target audience. Regardless, be certain that consumers of all types are expecting their financial firms to provide compelling digital experiences. According to the PwC Strategy & Global Wealth Management Survey 2016, 69 percent of high-net-worth individuals (HNWIs) now are using online/mobile banking but only one-quarter of wealth managers offer digital channels beyond e-mail.² The survey also found that 45 percent of HNWIs under age 45 who don't use robo services would consider using them in the future. Fortunately there is plenty of room for individual firms to create their own places within this trend by blending their successful value propositions with new tools and technology.

Even if fully automated advice isn't appropriate for your clients or your practice, the technology has a role in augmenting your client relationships and improving your operational efficiency. Exactly what to do inevitably varies by firm, and it's important

not to rush into something that may not be right for your clients or practice. Advisors should pause now and take this opportunity to think about how robo technology can best meet current and future investment needs of clients along with sustainably growing their businesses and minimizing operational risk.

Based on our work developing solutions for some of the largest financial firms in the industry, we see a definite trend toward "digitally augmented advice." Simply described, digitally augmented advice is traditional advice delivered by a financial advisor enhanced with a flexible suite of digital capabilities that aid in collaborating with and servicing a client. Digital solutions can run the gamut depending on the firm type, from intuitive easy-to-use client portals to complete automated advice and account access.

Digital advice solutions come in many forms, and each possesses a range of operational implications that deserve consideration. Financial firms need to carefully evaluate their business models to determine optimal implementation. It's also critical to understand the nuanced differences among various robo/digital solutions to determine how best to address current needs and provide a path to flexibly evolve for the future.

Meeting Investor Demand for Investment Information

Service standards in the digital age for both advised and self-directed customers increasingly center on convenience and always-on access to information. As such, static performance reporting and paper-

heavy processes resulting from a lack of back-office investment can dilute both client experience and loyalty. The 24/7-driven worldview also extends to the advisor. The ability to access information, in real time and on any device, supports service provision and product delivery (i.e., cross selling), and it helps differentiate the advisor. From a management perspective, strategic planning requirements and regulatory risks mean the home office must be plugged in to data as well. All vendors offer management dashboards and analytics, but executive-level reports offer a deeper view.

Digital innovation is most visible on the front end (think robo-advisory platforms and advisor iPads), but it depends heavily on the back office. This interdependence holds the key to meeting the heightened service requirements of customers post-financial crisis. Previously, back-office processes drew attention only in the event of an operational mishap or customer-related error. Today, processing firepower and flawless handling of data (not to mention wholly back-office-owned enhancements such as digital vaults) drive the client experience.

Most robo offerings available today are technology islands: bolt-on, digital-only advice-delivery mechanisms completely disconnected from existing middle- and back-office infrastructure. This disconnection leads to inconsistencies in the advice that firms provide and inefficiencies across the organization. The best solutions solve for these shortcomings by offering a comprehensive platform that leverages each organization's core competencies and

current suite of advisory offerings (e.g., mutual fund advisory, exchange-traded fund (ETF) advisory, separately managed accounts, unified managed accounts, and advisory-discretionary programs), and also offers a highly configurable blend of human and automated advice delivery.

Digital Advice in the DOL Era

Because of the pending Department of Labor (DOL) fiduciary rule, firms may face a dilemma if they have a robo program that's not fully integrated into their offering. Such a "siloe" system will have its own set of capital market assumptions, asset allocation targets, and ETF products, which inevitably will vary from what the firm is using for its traditional advice offerings, resulting in inconsistencies. For example, consider two clients with similar profiles, investment objectives, and risk tolerance, one served by a robo solution and the other directly managed by you. If the robo solution has a different outlook on emerging markets than you, this would lead to differences in the asset allocations recommended to each client. Ditto for the products and securities used, which, if not consistent, should at least not be contradictory. But you might choose to sell out of a mutual fund or ETF for an account you're directly managing just as the robo is choosing to buy into those same securities for the other account.

The differing underlying assumptions could drive completely different outcomes for the two clients—one portfolio could tank and the other might perform particularly well. How would you reconcile this for a regulator and explain it to your client? Firms using this type of solution may find themselves challenged to prove that they are operating in the best interest of their clients and fail to comply with the DOL fiduciary ruling. Comprehensive, integrated solutions provide a framework to enable comprehensive, consistent advice across all channels, which enables firms to streamline compliance with regulation and mitigate operational risk.

The ability to deliver consistent advice (at the asset-class, manager, and product level) across digital and face-to-face contexts has

become paramount in the current market and regulatory environment. Engaging a robo provider may mean embracing investment strategies and risk assumptions that diverge from the firm's in-house view. Real consistency requires a clear view of assets held in-house, which in turn implies product stacks and their underlying technology silos.

Developing a Plan to Integrate Robo and Traditional Advice Delivery

Firms considering a digital strategy need to explore the following questions:

What's your firm's value proposition?

Many firms that provide robo technology to advisors also provide investment services directly to consumers. Are your client relationships strong enough and is your value proposition differentiated enough to retain clients over time? Advisors should be thinking about this as a general matter, but it's even more important if you are going to steer clients to an external robo service.

Who owns the client? Many third-party robos structure contracts so they control the advisory agreement and therefore effectively own the client. At the onset, this might seem a trivial matter and advisors may welcome such outsourcing. After all, many advisors are seeking to use a robo to service their smallest accounts. But advisors need to consider their long-term business strategy when choosing a robo. Today's small accounts are tomorrow's core book of business. Robos are constantly evolving, making this an even more important issue to raise during due diligence.

How do you meet clients' needs? Robo solutions are generally algorithm-driven, providing a range of portfolios tailored to investor profile and risk tolerance. These solutions don't necessarily enhance an advisor's ability to deliver advice as much as they automate away administrative needs on small accounts. Key questions in this area to consider include:

- What information do clients desire and how will they access it?

- Is there room for the advisor to provide advice on the portfolio constructed for a specific client?
- Does the platform offer sufficient investment and manager options to effectively meet a client's needs?
- If a client's needs evolve beyond what the external robo solution can support, what is the path for that client to migrate to your advisory services?
- Is the underlying clearing and custody firm financially stable?

Are the assets custodied with the robo account the same place you custody your other accounts? If the robo doesn't custody at the same institution as your other accounts, you and your clients will receive different reports (e.g., Fidelity's statements are different from Betterment's statements) and it will be incumbent on you to reconcile the differences or explain to clients why they are receiving two separate reports for your service. Advisors may wish to consider accessing these augmented services by embracing platform consolidation. Platform consolidation enables one platform to manage all accounts, delivering your advice consistently across all channels. The big differentiator among providers is found in the scalability and flexibility of the platform. If a client wants to open an account for a child, for instance, will you maintain a single view of the client's household?

Can robo technology effectively integrate with other critical systems? Integration is the holy grail for every solution. Advisors need to clearly understand the robo's ability to integrate with other systems, custodial as well as best-of-breed third-party applications. Integration is especially critical for client reporting, and even more so if a client has an account managed by a robo and another account managed by you.

Robos need to be part of the existing business structure and should provide the advisor with tools to enhance the client experience. This starts with a unified, cohesive platform. Firms that have made the transition from point systems will be well-placed to evolve in line with the ever-evolving demands of their investors. This sort of

agility will be increasingly critical given the pace of digital change and the cost and regulatory pressures. Vendors must continue to focus on integration; ensuring that client, account, and other data is reconciled and that the right technology components are talking to each other. Firms seeking to integrate legacy technologies must balance their need for scalability against the risk of alienating their stable of advisors, who may resent the lack of pricing power implicit in a locked-down model, or who may be used to managing operational details (e.g., rebalancing) themselves.

The Winning Model

The future of investment advice is not a choice between a robo advisor or a traditional advisor; it's augmenting traditional advisors with a broad set of digital technology tools that enable them to capture and grow investor wealth.

Automated investment platforms can satisfy immediate investor demands, but they are not completely adept at addressing other areas of a sound financial plan or evolving with investors and their life circumstances. According to a recent report issued by *Investopedia* and the Financial Planning Association, no algorithm exists that can prudently assess the many areas of an individual's financial life and make the necessary strategic decisions related to retirement planning, estate planning, tax planning, healthcare planning, eldercare planning, and the many other personal financial areas most people face.³ High tech and high touch should work hand in hand, and the largest players in the industry are moving in this direction. This shift from investor-driven to advisor-robo—first noticed and grabbed by Vanguard's Personal Advisor and Personal Capital—has caused others to take note, including Schwab's Intelligent Advisory and Fidelity's AMP. Schwab aims to serve investors who require more guidance than is available on a retail robo with a balance of digital and human touch points. For example, Schwab investors will use a self-guided online tool to create a tailored financial plan followed by a conversation with a human consultant. The team of human advisors will be

available by phone or video-conference to answer questions or provide advice, and annual check-ins can be scheduled online.⁴ Fidelity's AMP allows investors to create goals and track progress, open and fund accounts, and monitor wealth in collaboration with their advisors.⁵ Robos that do little more than manage index portfolios at a low price could be threatened by the value that hybrid robos bring as they deliver high-touch, holistic plans and track assets to specific objectives.

The latest market movers support our position that firms should look to leverage the technology capabilities of robos versus completely outsourcing the management of certain clients to external robo solutions. Digital capabilities available to clients and investors enhance advisor-client engagement and collaboration, improve advisor growth and efficiency, and expand advisors' portfolio management capabilities. Today's robo tools will be commonplace five years from now. Advisors should embrace and integrate platforms now so they can attract new clients, focus on their key

areas of expertise, and sustainably grow the value they offer to their customers. ●

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Endnotes

1. See Danielle Andrus, "1 in 10 Advisors Have Never Heard of Robos: Survey," *ThinkAdvisor* (July 31, 2015), <http://www.thinkadvisor.com/2015/07/31/1-in-10-advisors-have-never-heard-of-robos-survey>.
2. See Michael Spellacy and Arjun Patel, "2016 Wealth Management Trends: A Revolution Both Loud and Quiet," PwC Strategy & Global Wealth Management (2016), <http://www.strategyand.pwc.com/media/file/2016-Wealth-Management-Trends.pdf>.
3. See Doug Cubberley, "Investors Want the Best Tech, a Human Touch with Financial Advice," *Investopedia* (December 7, 2016), <http://www.investopedia.com/articles/financial-advisor/120716/investors-want-best-tech-human-touch-financial-advice.asp>.
4. See Ryan Neal, "Schwab Announces New Robo-Hybrid Service," *WealthManagement.com* (December 13, 2016), http://www.wealthmanagement.com/technology/schwab-announces-new-Robo-hybrid-service?NL=WM-16&Issue=WM-16_20161216_WM-16_30&svfc4enews=42&cl=article_1&utm_rid=CPG09000007854609&utm_campaign=7958&utm_medium=email&elq2=6fe5feff20564c62aa0349b6f2f0baae.
5. See Joel Bruckenstein, "Fidelity to Launch Digital Advice Platform" (October 18, 2016), <http://t3technologyhub.com/fidelity-to-launch-digital-advice-platform-for-advisors/>.



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