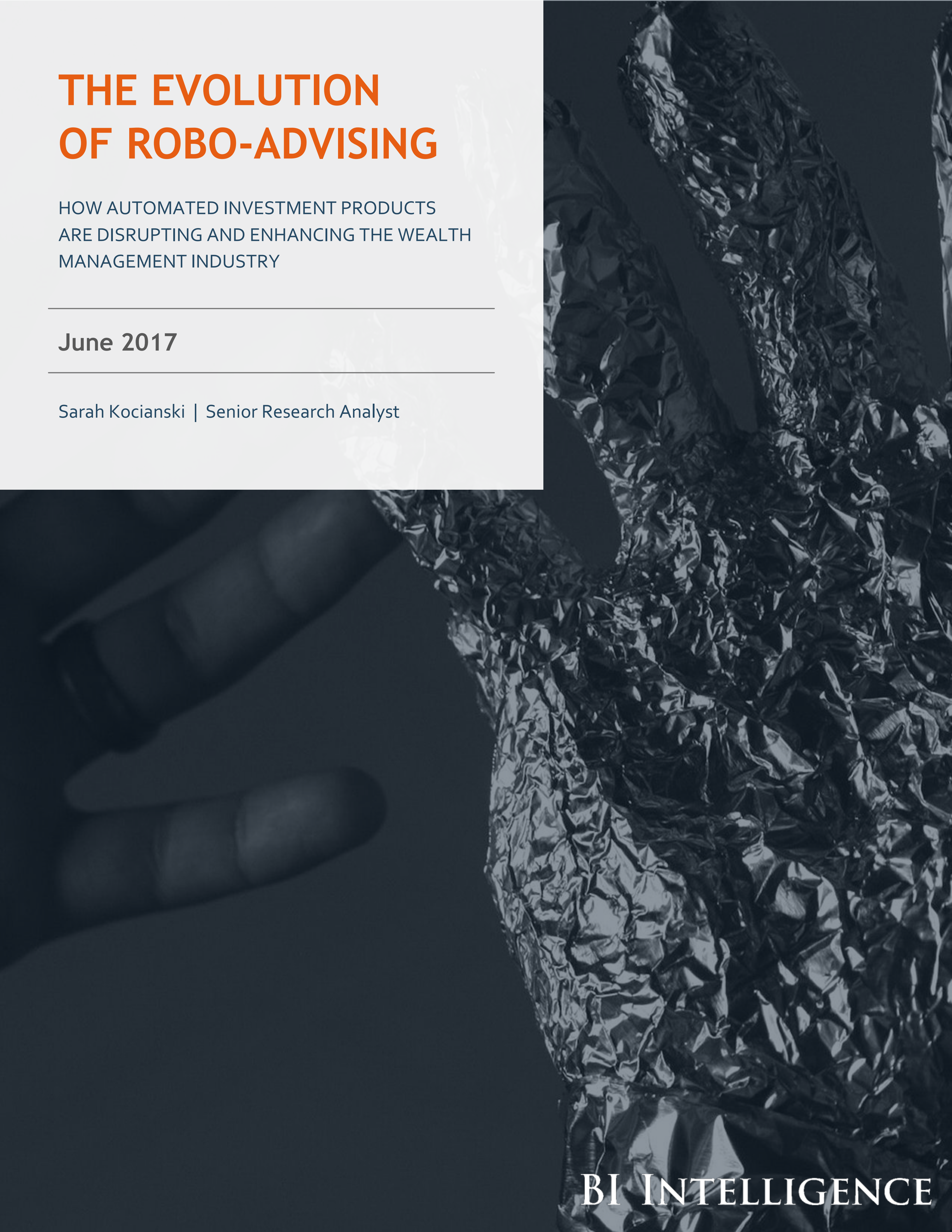
THE EVOLUTION OF ROBO-ADVISING

HOW AUTOMATED INVESTMENT PRODUCTS ARE DISRUPTING AND ENHANCING THE WEALTH MANAGEMENT INDUSTRY

June 2017

Sarah Kocianski | Senior Research Analyst



BI INTELLIGENCE

KEY POINTS

- **Robo-advisors — investment products that include any element of automation — continue to disrupt and enhance the wealth management industry.** They are increasingly offered by both startups and incumbents, and come in business-to-consumer (B2C) and business-to-business (B2B) form. Most of these solutions promise to streamline the investment process, leading to lower costs and greater transparency for investors.

- **However, the market is now very crowded, and consumer uptake isn't matching expectations.** That's made it difficult for startups with robo-advisor products to attract the assets under management (AUM) they need to build sustainable businesses. As a result, many are being forced to reexamine their strategies, or even pursue additional revenue streams.

- **BI Intelligence forecasts that robo-advisors will manage around $4.6 trillion by 2022.** We've moderated our forecast to account for ongoing weakness in AUM levels in the near term. That said, we expect growth to pick up by the end of the five-year forecast period as robo-advisors come to the fore in Asian markets and incumbent products increasingly go live.

- **Startups are employing a number of strategies to increase competitiveness and boost AUM.** Many now offer a variety of products, some of which are not investment related, while others are white-labeling their technology in order to act as third-party suppliers to incumbents. In addition, a number of startups are partnering with large firms, not necessarily in the wealth management industry, to scale more easily.

- **Few winners will emerge in the startup space, while incumbents are set to ramp up robo-advisor launches.** Despite attempts to differentiate and bolster business models, there will be a winnowing in the startup space. Incumbents will use this to their advantage, acquiring the technology startups that have fallen by the wayside, to launch their own products at low cost.

Download the charts and associated data in Excel »

INTRODUCTION

Consumers looking to invest their assets, whether for retirement, to prepare for college tuition costs, or even just to plan for a trip, have a bevy of options these days. Beyond traditional wealth managers, robo-advisors offered by startups are proliferating at a rapid pace, and incumbents are beginning to launch their own automated solutions. We use the term "robo-advisor" to refer to investment products that include any element of automation. Most of these solutions promise to streamline the investment process, leading to lower costs and greater transparency for investors.

However, while robo-advisor products were brought to the fore by startups looking to upend the wealth management industry, many of these players have failed to make good on their initial promise to achieve lofty heights by winning over previously underserved markets. At the same time, the market is becoming increasingly crowded as new startups launch and incumbents get their own products live. The majority of startups are struggling to acquire enough customer assets to maintain viable businesses with just automated investment products, pushing them to work harder to differentiate themselves from the competition. Many are also looking to add alternative sources of revenue to bolster their businesses.

Meanwhile, incumbents' robo-advisors are accumulating large volumes of assets under management (AUM), thanks to a number of inherent advantages they possess. Legacy players in the wealth management industry have come to realize that robo-advisors enhance their propositions, attracting new customers and boosting the loyalty of existing clients. This has also been understood by a number of startups with robo-advisor products that are adapting their technology to act as third-party suppliers to incumbents.

In this report, BI Intelligence scopes the current market for robo-advisors, providing an updated forecast through 2022. In addition, we explain the different types of robo-advisors emerging, detail how startups and incumbents are working to ensure the success of their products, and outline what will happen to the market over the next 12 months.

THE GLOBAL ROBO-ADVISOR MARKET

As part of our ongoing robo-advisor coverage, we have identified changes, both in the broader wealth market, as well as in the robo-advisory market specifically, over the last 12 months.

- **Global AUM/wealth is growing at a sluggish pace.** Global total AUM grew just 1% between 2014 and 2015, the latest period for which data is available, reaching $71.4 trillion, according to Boston Consulting Group. That means the total addressable market for robo-advisors will also grow more slowly than previously expected.

- **Customer acquisition has been lackluster.** Only 11% of global consumers have used a robo-advisor as part of their retirement planning, according to exclusive data from BI Intelligence. While this shows the usage of just one type of robo-advisor, it suggests the initial success of these products may have stemmed more from the onboarding of early adopters than wider appeal.

As a result of these developments, we have updated our forecast of the AUM robo-advisors will manage globally, revising down the volume of assets these players will manage through 2020. In addition, we've extended our forecast out to 2022, when growth will likely pick up as robo-advisors come to the fore in Asian markets and incumbent products increasingly go live.

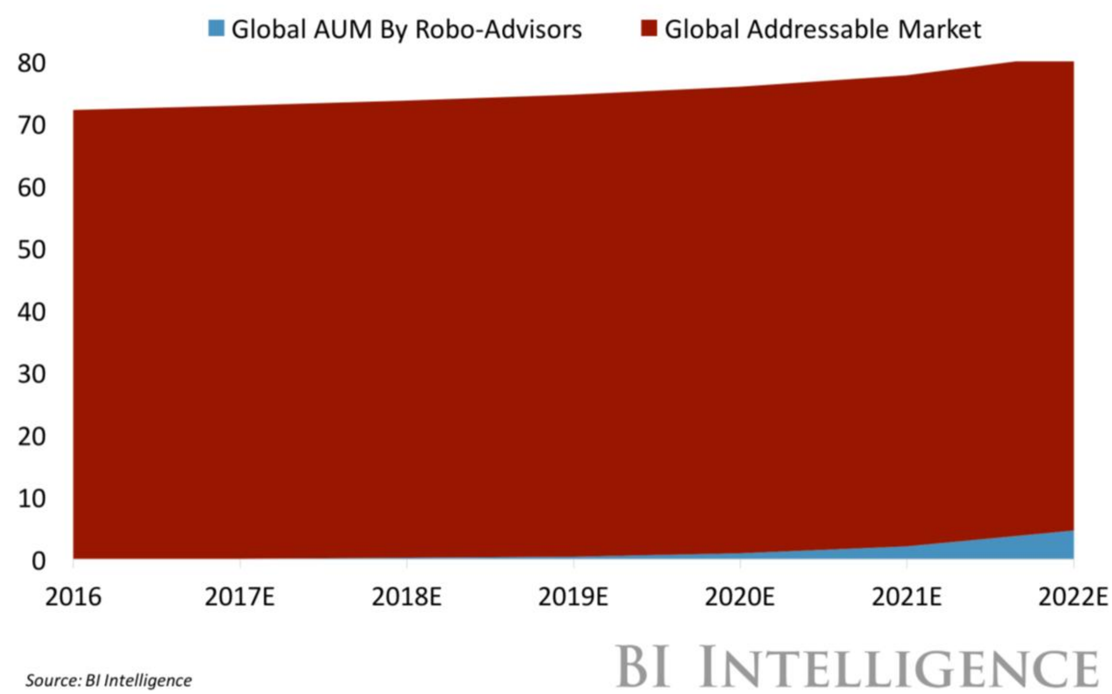
- **Robo-advisors will manage about $1 trillion globally by 2020,** according to our updated forecast. That's around 13% of our original estimate of $8 trillion.

- **This equates to 1% of an estimated $75 trillion addressable market in 2020.** We expect the global addressable market for robo-advisors will reach $77 trillion by 2022.

- **In 2022, robo-advisors will be managing $4.6 trillion.** That's up from an estimated $75 billion by the end of 2017, and represents a five-year compound annual growth rate (CAGR) of 199%.

FORECAST: Total Addressable Market For Robo-Advisors And Global AUM By Robo-Advisors

Trillions ($)



Source: BI Intelligence

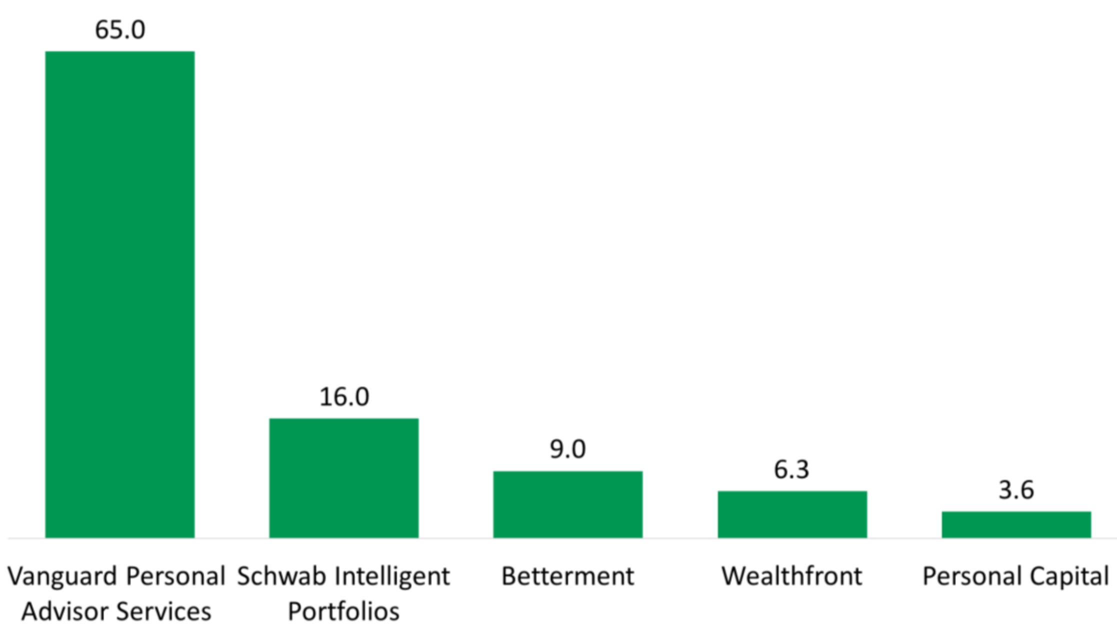
Geographic Segments

Outside of the US, growth among startups' robo-advisors has been slower than expected, with none in Europe or Asia breaking the $1 billion AUM barrier. That's a problem because these firms rely on increasing AUM to grow revenue — fees are typically charged to customers as a percentage of AUM. Incumbents in these markets have also been slower than their US peers to launch their own offerings.

North America. North America continues to lead the way as the region with the largest number of robo-advisors — as well as those with the largest volumes of AUM. This largely comes down to the size and maturity of the wealth management industry in the US — AUM in North America hit $36 trillion in 2015, accounting for around half of global AUM. In addition, the region boasts a cultural propensity to self-manage investments. Together, these factors inspired large numbers of startups to create robo-advisor products earlier than elsewhere, and incumbents to launch their own products in response. However, this is starting to create overcrowding in the market, which is forcing many firms to rethink their strategies and business models.

AUM Of Major US Robo-Advisors

Billions ($), May 2017



Source: Company websites, ADV filings

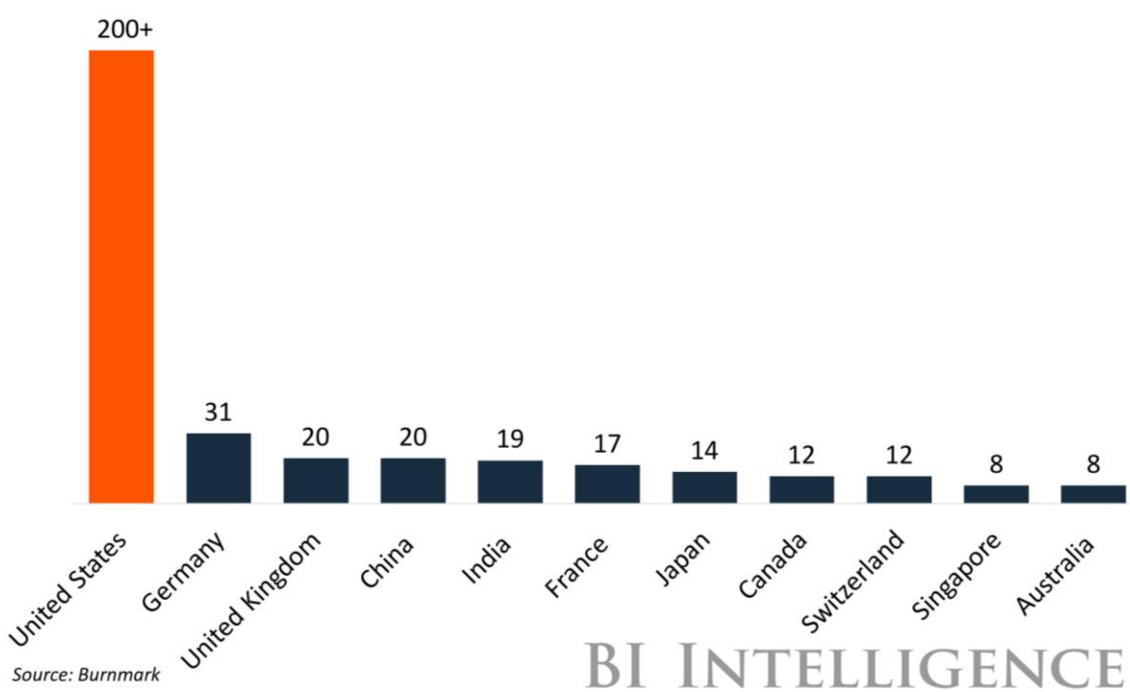
BI INTELLIGENCE

Asia. The robo-advising industry in Asia is still nascent, but as might be expected of the region leading the way in global wealth creation, robo-advisors are increasingly making their mark. Of particular note are the markets of China (including Hong Kong), India, and Japan where firms have already launched robo-advisors, some with white-label solutions for incumbents. This region also boasts wealthy individuals (those with investable assets of over $1 million) with the greatest propensity to use automated advice, meaning it will likely see faster adoption of such solutions than the US or Europe. We therefore maintain our expectation that use of robo-advisors by Asian investors will overtake the US in the near future.

Europe. The European robo-advisor market is newer than that of the US, and therefore comparatively smaller in both numbers of solutions and volume of AUM. That said, we are now starting to see market leaders emerge, particularly in the UK and Germany. It's worth noting that European robo-advisors face several challenges that hinder their ability to attain scale at the speed of some of their US and Asian peers. These include smaller addressable markets in individual countries, and for those that choose to address this by expanding multinationally, hurdles in the form of different tax laws, know-your-customer (KYC) requirements, culture, and payment systems.

Number Of Robo-Advisors, By Country

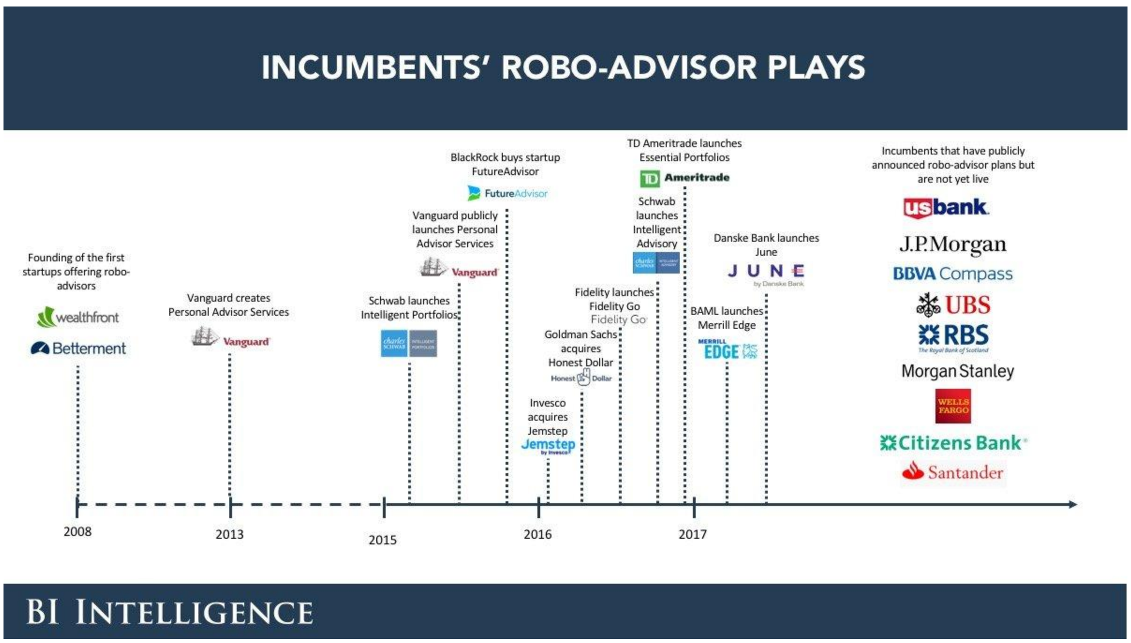
April 2017



Source: Burnmark

Incumbents Vs. Startups

Despite a later entry to the market, incumbents' robo-advisors have accumulated larger volumes of AUM, faster than competitors operated by startups. Vanguard's Personal Advisor Services now manages $65 billion, around two years after launch, while Charles Schwab's Intelligent Portfolio offerings have accumulated $16 billion in AUM in two-and-a-half years. In comparison, the leading startup robo-advisor Betterment has $9 billion after nine years in operation, while second-place firm Wealthfront attracted $6.3 billion over the same period. All these firms are based in the US, and as of yet, no European or Asian firms have come close to accumulating similar levels of AUM. That provides further evidence of the greater maturity of the US robo-advisory market.



The success seen by incumbents stems from number of advantages, including their well-known and trusted brands, existing customers they can move onto robo-advisory products, and greater resources that can be used for product development and customer acquisition. Many also have different motivations than startups — some are simply trying to make serving existing customers more efficient, while providing their clients with lower-cost products to boost customer loyalty.

MAJOR INCUMBENT ROBO-ADVISORS

	Robo-Advisor	B2B or B2C	Products	Fee: Additional third-party fees often apply. Ex. ETF fund fees average to 0.2%.	Min. Investment	AUM	Location
charles SCHWAB INTELLIGENT PORTFOLIOS / charles SCHWAB INTELLIGENT ADVISORY	Charles Schwab Intelligent Portfolios/Intelligent Advisory	B2C, B2B	Goal-based, fully automated, retirement, hybrid (advisors)/hybrid (portfolio management, advisors)	Free/0.28%	$5k/$25k	$16B	US
NatWest	NatWest Invest	B2C	Goal-based, hybrid (portfolio management)	0.35%	£500	N/A	UK
Fidelity Go	Fidelity Go	B2C	Hybrid (portfolio management), retirement	0.35%	$5k	N/A	US
FutureAdvisor	FutureAdvisor (BlackRock)	B2C, B2B	Hybrid (portfolio management), retirement	0.5%	$10k	$969M	US
Vanguard	Vanguard Personal Advisor Services	B2C	Hybrid (portfolio management, advisors)	0.3%	$50k	$65B	US
MERRILL EDGE	Merrill Edge Guided Investing (BAML)	B2C	Hybrid (portfolio management)	0.45%	$5k	N/A	US
JUNE by Danske Bank	June.dk	B2C	Hybrid (portfolio management)	0.55%	$15	N/A	Denmark
TD Ameritrade	TD Ameritrade Essential Portfolios	B2C	Goal-based, fully automated, retirement	0.3%	$5K	N/A	US

BI INTELLIGENCE

Source: Company websites, SEC Filings, BI Intelligence

A major consequence of incumbents' success is that more mature startups with robo-advisors are being forced to adapt their models to remain competitive, while new entrants must come up with increasingly innovative solutions to differentiate. We previously highlighted the need for startups launching robo-advisors to diversify their products in order to succeed, and we're now seeing this come to fruition.

DIFFERENT TYPES OF ROBO-ADVISORS AND APPROACHES

As the industry matures, many different types of robo-advisors are emerging. And firms are increasingly offering a combination of these products, rather than a single flagship solution, with some operating in both the business-to-consumer (B2C) and business-to-business (B2B) spaces. Below, we outline some of the different product types currently on the market:

- **Fully automated investment products.** These are solutions that automate the entire investment process, including assessing potential clients, creating and managing portfolios, and providing forecasts and potential outcomes. They're typically positioned as alternatives to traditional wealth managers.

- **Goal-based products.** Some products build a client's portfolio around a specific goal — like funding a child's education. These can also incorporate other elements of the client's finances including savings, current, and retirement accounts to provide a holistic view of their financial life.

- **Hybrid products.** These are products that include a human element, either via access to a human advisor, or by having teams of investment professionals monitor and manage portfolios. In the latter case, portfolios are typically designed by an algorithm and then maintained by humans. In order for this to be sustainable, clients aren't typically offered bespoke portfolios. Instead, they are matched with one of a smaller number of pre-existing options created by the firm.

- **Problem-solving products.** These aim to solve a particular ongoing issue for a client — for example, tax planning. In some cases, such products are positioned as employment benefits. They differ from goal-based products in that they're designed to tackle recurring needs, rather than achieve a specific goal.

- **Advice products.** Despite what their designation suggests, very few robo-advisors actually offer financial advice. Those that do fall into this category provide automatically generated guidance on how much clients should invest and where. These robo-advisors are typically geared toward those looking for an alternative to a human financial advisor.

MAJOR STARTUP ROBO-ADVISORS IN NORTH AMERICA AND EUROPE

	Robo-Advisor	Model	Products	Fee: Additional third-party fees often apply. Fees typically decrease as client AUM increases.	Min. Investment	AUM	Location
Betterment	Betterment/ Betterment Institutional	B2B, B2C	Goal-based, retirement, problem-solving, hybrid (advisors)	B2C: Under $10k and no auto-deposit $3/mo; 0.15%-0.35% for $10k+; B2B 0.25%.	None	$9B	US
blooom	Blooom	B2C	Retirement	$10/m.	None	$500M	US
Hedgeable	Hedgeable	B2B, B2C	Goal-based, problem-solving, hybrid (portfolio management)	0.3%-0.75%.	$1	$63M	US
moneyfarm	Moneyfarm	B2B, B2C	Hybrid (portfolio management, advisors), retirement, advice	B2C: 0%-0.6%	None	N/A	UK, Italy
nutmeg	Nutmeg	B2C	Hybrid (portfolio management), retirement	0.35%-0.75%.	£500/£5k	£700M	UK
PERSONAL CAPITAL	Personal Capital	B2C	Goal-based, hybrid (advisors)	0.49%-0.89%	$100K	$4.2B	US
scalable CAPITAL	Scalable Capital	B2C, B2B	Fully automated, problem-solving	B2C: 0.75%.	£10k	£200M	UK, Germany, Austria
SIGFIG	SigFig	B2C, B2B	Goal-based, hybrid (advisors)	B2C: 0%-0.25%.	$2k	$120M	US
wealthfront	Wealthfront	B2C	Goal-based, retirement, advice, fully automated	0%-0.25%.	$500	$6.3B	US
wealthify	Wealthify	B2C	Goal-based, hybrid (portfolio management)	0.5%-0.7%.	None	N/A	UK
Wealthsimple	Wealthsimple	B2C	Goal-based, retirement	0%-0.5%.	None	$750M	Canada
Wealth Wizards	Wealth Wizards	B2B	Retirement, advice	Fees set by clients or £65-£100 for pension reviews, £50-£150 for one off advice.	None	N/A	UK
WiseBanyan	WiseBanyan	B2C	Goal-based digital wealth management; retirement planning	Free.	None	$94M	US

BI INTELLIGENCE

Source: Company websites, SEC Filings, BI Intelligence

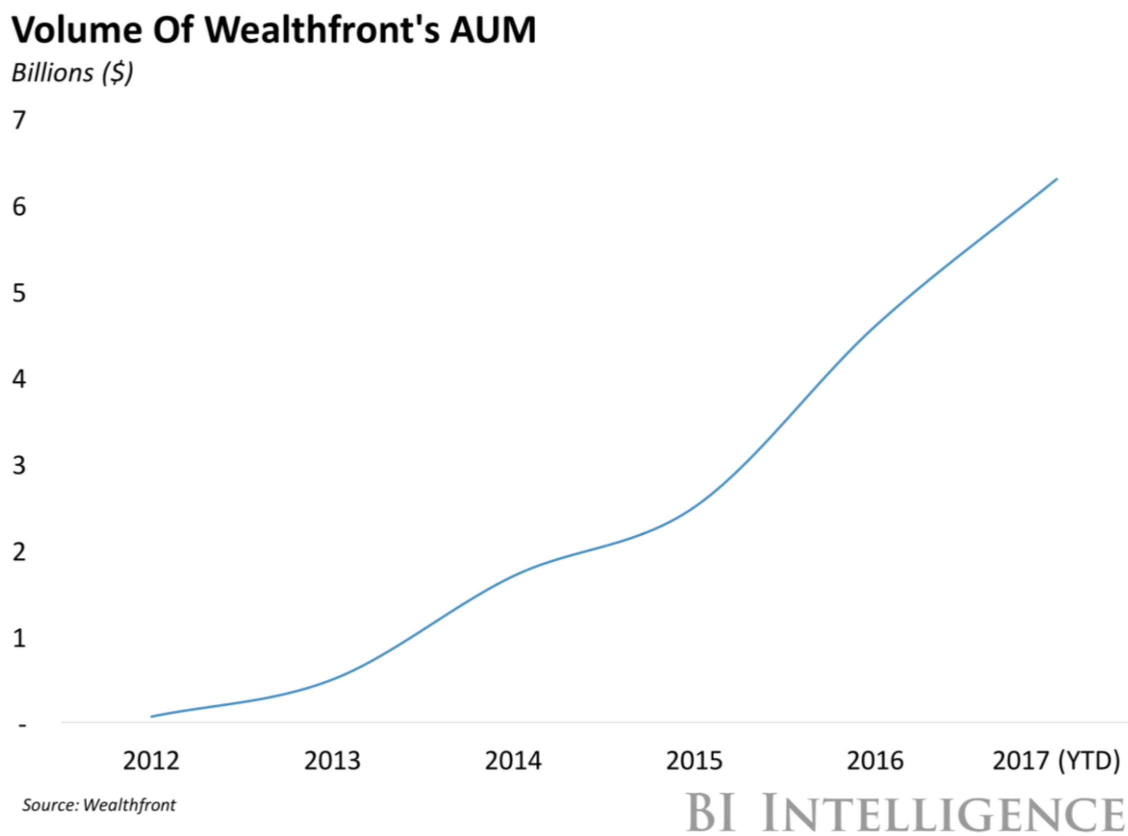
Business Strategies Used By Robo-Advisor Providers

Robo-advisor providers are increasingly experimenting with different strategies to stand out in an increasingly crowded market. These tactics are geared toward attracting customers and AUM, as well as identifying new revenue streams. Here are some of the most common examples:

Targeting Specific Demographics

A common narrative accompanying the emergence of early robo-advisors was that they would capture an underserved market of digitally native millennials. However, as more of these products are launched, two truths are emerging: First, automated investment alone is not yet enough to attract enough of this demographic to build sustainable business models, and second, robo-advisors may have more appeal to other groups. As a result, some firms are adapting their offerings to factor in one, or both.

US firm **Wealthfront's** clients are mostly in their 30s and 40s, a demographic likely craving more than just simple investment. To better cater to this group, the company has revamped its offerings and marketing over the last 12 months to position itself as a solution to all a customer's financial needs. In addition to its investment products, it now provides automated financial planning to help clients achieve life goals, like buying a home. In line with this strategy, Wealthfront is also launching nonadvisory products, including a line of credit offering, which will not only help it meet a wider range of client needs, but also bring in additional revenue.



Meanwhile, legacy players **Charles Schwab** and **Vanguard** continue to target baby boomers, consumers aged 57+, with their offerings, a tactic bringing them considerable success. That's unsurprising seeing as this demographic makes up the majority of their existing customers. Vanguard, in particular, has been working to move customers to its Personal Advisor Services, likely because the elements of automation it includes results in significant cost savings for the firm. Interestingly, while Charles Schwab's first offering, Intelligent Portfolios, didn't include access to human advisors, it has since launched a second robo-advisor product, Intelligent Advisory, which does just that. The new service boasts a higher minimum initial investment, and charges fees — which Intelligent Portfolios does not. This is further evidence that Schwab is targeting older consumers, as these clients often have more wealth, both in the form of assets to invest, and with which to pay fees.

Other firms targeting specific demographics with their robo-advisor products include Canadian firm **Wealthsimple** and investing platform **Motif**, which offer socially responsible investment options. In addition, there are a number of robo-advisors designed specifically for women, including products from **Ellevest** and **WorthFM** in the US, and **Miss Kaya** in Singapore. However, this segment has already seen one relatively high-profile casualty in the form of **SheCapital**, which closed a year after launch after failing to attract enough AUM.

A strategy of targeting a specific demographic will work best for firms that have had time to build, or leverage, brand awareness. Later market entrants will likely struggle to differentiate themselves, meaning that this approach could be considered risky for new startups. Instead, firms looking to launch robo-advisory products in the near future would do better to consider a holistic approach.

Launching Additional Products

The majority of firms taking this route are startups that have seen some success in acquiring customers, and are now looking for additional lines of revenue. There is also a growing acceptance that retirement-specific products are a requirement for firms in Europe and the US, so for the purposes of this report, they will not be considered additional products.

Several firms are deploying premium products with higher fees alongside their original low-cost, advisor-free offerings. For example, one of the oldest firms in the space, **Betterment** now offers three products that include various levels of access to human advisors, in addition its original digital-only plan. They are Plus, which has a fee of 0.4% and a minimum investment of $100,000; Premium, which has a fee of 0.5% and a minimum of $250,000; and the Betterment Advisor Network for clients who want access to Betterment's automated investment technology, while maintaining a deep relationship with a human advisor. Offering a broader product suite is not a bad idea for firms looking to boost customer acquisition and AUM, so long as the costs associated with bringing on human advisors don't outweigh the revenue generated from new clients.

Another US firm, **WiseBanyan**, which offered its first robo-advisor for free, has since introduced paid-for packages that include additional services like tax-harvesting. As mentioned above, **Wealthfront** has taken a different route and added noninvestment products to its line. It remains to be seen which model will reap the most benefits for firms when it comes to customer acquisition and revenue added.

Incentives

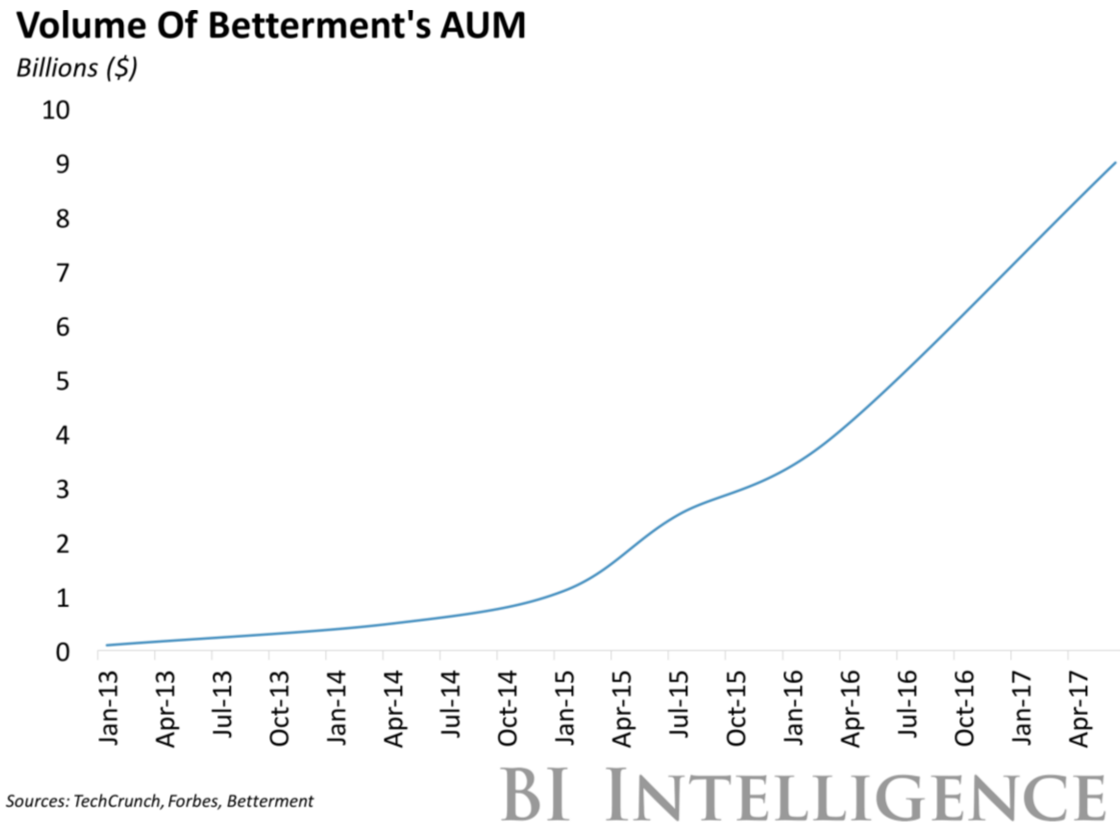
Another approach firms can employ to boost customer acquisition is one tried-and-tested by the legacy financial services industry — incentives.

UK firm **Wealthify** offers £50 ($64) cash back to investors who meet certain conditions, including keeping a minimum of £500 ($639) with the platform over a period of 11 months. It also provides fee discounts to users who get their friends and family investing on the platform. Toronto-based **Wealthsimple**, on the other hand, uses nonfinancial benefits to draw customers in — users of its Wealthsimple Black product get VIP access to airport lounges, for example. This tactic may work to get customers on board, but it adds to the already hefty cost of acquisition these firms face. As a result, such an approach is unlikely be enough to generate the AUM they need to build sustainable, and profitable, businesses. However, it could work well in tandem with other models outlined in this report.

Acting As Third-Party Suppliers

Firms operating as third-party suppliers of robo-advisors generally fall into one of two camps — those that were initially B2C firms and have added B2B offerings, and those that have always operated a B2B model.

Betterment falls into the first camp with Betterment for Business, a 401(k) plan management product targeted at employers, which has brought the firm considerable success. It garnered 300 clients in its first year, and is likely responsible for Betterment's high AUM growth rate, as employee assets at each client are counted in its overall AUM. Betterment also offers a white-labeled version of its service, Betterment For Advisors.



Another US firm that started out as B2C but later pivoted to B2B is **FutureAdvisor**. The company shifted focus after being acquired by incumbent asset manager BlackRock. Like Betterment, it has seen some success with this strategy, inking agreements with BBVA Compass and US Bank, among others, to provide the technology behind their own planned robo-advisors. Meanwhile, US-based **SigFig**, while remaining independent, now has a model that resembles FutureAdvisor's — it maintains its B2C arm but has also signed deals with Wells Fargo and UBS to help them build robo-advisors. SigFig will also build tools for the firms' human advisors to use.

Jemstep, acquired by Invesco in 2016, is one firm that's always operated a B2B model. For those breaking into B2B early and carving out a share of the market, this is likely to be a successful approach. However, soon the market for white-labeled robo-advisors will become as crowded as the B2C space, particularly as more firms look to cater to both. This means operating a purely B2B model will become risky as time goes on.

There are also several firms providing robo-advisory products to businesses that actually provide advice, rather than automated investment, to end consumers. A good example of this is the UK's **Wealth Wizards —** the firm's products are used by end consumers, but they are distributed either in branded form via employers, of which it currently has 14 signed up, or as a white-labeled platform used by incumbents in the financial advice industry. The advice it provides includes recommendations on how much an end user should invest, what sort of pension they should get, and when they will be able to retire based on their current status. All the advice is formulated by algorithms and delivered to end users via an app. This model remains relatively unusual in Europe, meaning firms using it have an advantage over their less well-differentiated peers, particularly in the UK where the regulator is pushing hard for incumbents to make access to financial advice more accessible.

Partnerships

This approach is widely seen throughout the fintech industry, with many firms striking partnerships with larger players in order to leverage their customer bases, experience, and greater resources. Firms taking this approach differ from third-party suppliers as they pick each partner individually, and typically maintain control and branding of the end product, rather than building to another company's specifications.

European firm **Scalable Capital** is partnering with larger firms in order to scale, a particular challenge for startups in this region, as highlighted earlier. It is already working with German electronics giant Siemens, whose employees are offered a Scalable Capital portfolio as an employment benefit, and is currently in discussions with other large companies. BlackRock also recently took a stake in the firm, a relationship Scalable Capital will leverage to help it get access to and partner with the incumbent's financial services and corporate clients. Scalable Capital is unusual in that its product is entirely automated — portfolio creation and management are both done by algorithms. Moreover, customers aren't assigned one of a limited number of risk bands — instead, they set a percentage of their total investment they'd be prepared to lose in a bad year. The firm's software then creates their portfolio using this measure, rather than metrics associated with a pre-defined risk appetite. That the firm's robo-advisor is more automated than most likely means its costs are lower than competitors, making it much easier to scale and integrate with partners, and affording it a greater chance of success.

Italian firm **Moneyfarm** is also working with incumbents and has built a cobranded solution for insurance and wealth management giant Allianz's UK employees. In addition, it's embarked on a similar partnership with Uber in the UK, providing discounted pension products and financial advice to the ride-hailing firm's drivers, while Betterment has a similar arrangement with Uber in the US. Uber is part of the sharing, or gig, economy, which is growing exponentially in Europe and the US. A defining feature of this sector is that workers are typically not employees, meaning they don't have access to standard employee benefits. This makes them a highly underserved market, and partnering with the firms they work for is an excellent opportunity for firms offering robo-advisors.

THE 12 MONTHS AHEAD FOR ROBO-ADVISORS

Even as firms experiment with different approaches to make their offerings more competitive, it's likely the robo-advisor space will only continue to crowd in the next year, making it even more difficult for those without firmly entrenched positions to survive. There are two key trends we expect to see in the next 12 months:

- **More incumbents will launch robo-advisors.** The robo-advice market is now so advanced in the US that incumbents without an offering are behind. That means we will see legacy players in the wealth management industry rapidly step up their plans to launch robo-advisory products in the year ahead. We also expect to see incumbents in Asia jumping on the robo-advice bandwagon, spurred on by client demand. In Europe, it will likely take longer before incumbents view robo-advisors as essential, largely due to a less-well developed culture of self-directed investing, and a heavier regulatory burden sucking up resources.

- **A significant number of startups will fail.** Many startups fail, but we expect their shuttering to be more pronounced in the robo-advisor space over the next 12 months. This will be driven by several factors, including the huge numbers of market entrants, slower-than-expected uptake by consumers, and the ongoing proliferation of incumbent solutions.

As a result, startups need to retain a focus on scale, while building customer loyalty, and where possible, look for alternative sources of revenue. For many, this will mean readjusting their business models. Those that manage to form significant partnerships, or become third-party suppliers, will have greatest chance of achieving success, as they will find it easier to accumulate the £1 billion ($1.3 billion) in AUM that providers generally agree is required to achieve profitability. For those that fail to meet this goal, a potential way out is acquisition by an incumbent. That's because buying a failing startup, on the cheap, is likely to be a popular way for legacy firms to acquire the technology required for a robo-advisor product.

THE BOTTOM LINE

- Robo-advisors continue to disrupt and enhance the wealth management industry. They are increasingly offered by both startups and incumbents, and come in B2C and B2B form.
- However, startups with robo-advisor products are struggling to attract the AUM they need to build sustainable businesses.
- BI Intelligence forecasts that robo-advisors will manage around $4.6 trillion by 2022.
- Startups are employing a number of strategies to increase competitiveness and boost AUM.
- Few winners will emerge in the startup space, while incumbents are set to ramp up robo-advisor launches.

BI INTELLIGENCE

BI Intelligence, Business Insider's premium research service, provides in-depth insight, data, and analysis of everything digital. Our research is fast and nimble, reflecting the speed of change in today's business. We give you actionable insights that enable smarter and better-informed decision-making. We publish in-depth reports, news, and an exhaustive library of charts and data focusing on key areas of tech: mobile, e-commerce, digital media, payments, the Internet of Things, and more.

If your organization would like to learn more about our research, including a license to republish our charts, please contact: intelligence@businessinsider.com