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The Growth of Robo-Advice in Banking Services

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Abstract

Robo banking is a revolutionary and technological advancement has disrupted the traditional banking landscape in India. This article reconnoiters the concept of robo banking, its impact on the financial services industry, and its potential implications for customers and the banking sector. The study reviews existing literature on robo banking, its benefits, challenges, and regulatory framework. The discussion delves into how robo banking has improved customer experience, enhanced financial inclusion, and increased operational efficiency. The article concludes with an analysis of the future prospects of robo banking in India and its role in shaping the banking sector.

Introduction

A Robo-Advisor, also called digital advisors, can be defined as a self-guided online wealth management service that provides automated investment advice at low costs and low account minimums, employing portfolio management algorithms. They provide financial advice or investment management online with moderate to minimal human intervention. To get to know the client's risk tolerance, he or she has to fill out a questionnaire first. Based on this information the Robo-Advisors creates individual investor profiles so that it is able to invest automatically in different assets. In many cases, Robo-Advisors invest in low-cost ETFs. The first robo-advisors were launched in 2008 during the financial crisis. The first robo-advisers were used as an online interface to manage and balance client's assets by financial managers.

Robo-advisors are digital investment platforms offered by brokerages. This catch-all term includes investment managers and software that use complicated computer algorithms to administer your investment portfolios. The best robo-advisors may be entirely automated, while others offer access to human assistance.

Robots can be beneficial for trading as they execute trades based on predefined rules without emotional biases. They operate quickly, handle complex data, and can run continuously. However, success depends on the effectiveness of the strategy, proper risk management, and adaptability to changing market conditions.

The world's first robo-adviser, Betterment, launched in 2008 as a low-cost automated digital investment platform, providing algorithm-driven financial advice. Viewed by the industry as a potential competitor, it also opened the doors for wealth management firms to acquire or create their own virtual advisory platforms. Robo-advice currently holds a relatively small market share in the UK. According to GlobalData's 2020 Global Wealth Managers Survey, just 3.4% of retail investors currently prefer to use this channel to arrange investments, though 66% of UK wealth managers agree that traditional players will continue losing market share to robo-advisers.

A 'hiccup' in the market, alongside the difficulty in making them a profitable business arm, has seen UBS, Investec and other larger institutions close down their robo-adviser platforms in the past decade. But the global pandemic's acceleration of digital transformation and continued support from millennials, has seen a turnaround for robo-advisers, with a 30% increase of managed assets from 2019, with $460bn managed globally in 2020. This substantial growth and an increasingly digital-centric world, is likely to see this trend continue with analysts predicting robo-advising will become a $1.2 trillion industry by 2024.

Objectives

1. To understand the Robo Banking functions and Robo advisors
2. To analyze the Robo banking advantages and disadvantages and
3. To estimate the future prospects of robo banking in India.

The benefits of digital partnerships

JP Morgan's partnership with Nutmeg is intended to provide a ready-made investment solution to complement the company's new digital bank, JP Morgan Chase, which it plans to launch in the UK later this year. Nutmeg has a solid foundation with around 140,000 customers and managed assets of around £3.5bn, but the bank is looking to leverage the technology and counter the threat from fintech's.In his annual letter to shareholders in April, Jamie Dimon, CEO of JP Morgan Chase, stated that fintech's have "done a great job in developing easy-to-use, intuitive, fast and smart products" while acknowledging that banks are held back by "inflexible legacy systems" and "extensive regulation".

Meanwhile, Lloyds' deal with Embark - which has more than £400bn under administration, 500,000 customers across the country and was recently named one of Britain's most important fintech - will help the bank increase the reach of its investment offerings and support its robo-advice business ambitions.

Antonio Lorenzo, Chief Executive, Scottish Widows and Group Director, Insurance & Wealth, Lloyds Banking Group said: “Through Embarks technology, we will be able to increase the reach of our investment offerings for customers who are happy to manage their own portfolios, through modern, easy to use technology.”For both banks, speed to market, the combining of tech and banking experts to provide a positive customer experience and meeting customer expectations through digital investment services, are key partnership wins.

Expanding their customer reach through a hybrid approach to investment management, particularly to the millennials who are big supporters of digital investment platforms and whose wealthis likely to accrue in future years, will also be a consideration.

Advantages of Robo-Advisors

Robo-advisors come with many benefits. This is especially true for retail investors who don't have a lot of capital to work with and are novices or have a rudimentary knowledge of the investment world. They allow you to craft smaller portfolios without a lot of the hassle and investors don't have to deal with pushy advisors trying to lock in a commission. Having said that, the following are the most common advantages of investing with a robo-advisor.

1. **Lower Fees**

Before robo-advisor platforms, you were lucky if you received professionally managed investment assistance for less than 1% of assets under management (AUM). Automation has significantly changed that paradigm, and there are many low-cost robo-advisors to choose from.

For instance, there are no advisory fees or commissions for those who use Charles Schwab’s Intelligent Portfolios while the wealth front and betterment and models also favor cost-conscious consumers.

2. **Robust Investment Models**

Many of the algorithms used by robo-advisors, such as betterment rely on Nobel Prize-winning investment theory to drive their models.4 Generally, best practices investment theory strives to create an investment portfolio with the greatest return for the smallest risk.Some of the best robo advisors use cutting-edge investment portfolio research informed by modern theories to drive their products.

3. **Easy Account Opening**

It's becoming more common for traditional financial planners white lables robo-advisor platforms for their clients. This takes the cumbersome task of choosing assets out of their hands so financial advisors can spend more time with their clients addressing individual tax, estate, and financial planning issues.

Some consumers, such as younger investors or those with a lower net worth may not have considered professional financial advice. However, robo-advisors are growing the existing market of financial advisory clients. Because robo-advisors provide easy access and lower fee models, more consumers may choose this type of professional management over the do ityourself investing model.

4. **Lower Account Minimums**

Investors with a small net worth can get professional financial management through a robo-advisory service. With zero and near-zero minimum balance, technology-enhanced robo-advisors include Betterment and Folio Investing.56 Other robo-advisors are accessible with $1,000 to $5,000 to get started.

Disadvantages of Robo-Advisors

It may seem like an easy decision to invest using a robo-advisor, but it's always a good idea to review the drawbacks. Remember, you don't get the human service you would with a

Financial advisors guiding you through your investments. And despite the low cost, you may end up paying more in fees in the end. Here's a look at some of the most common disadvantages of using a robo-advisor to invest your money.

1. **Limited Personalization**

Robo-advisors can be configured or programmed to meet the needs of many investors by allowing you to set and edit your goals using their financial planning software. However, they don't consider that you also may have money-related issues and concerns.As such, you may benefit from talking to a human being who can help tailor your investment plan to your specific situation—something you won't get using a robo-advisor.

2. **Limited Flexibility**

Most robo-advisors won't be able to help you if you want to sell call options on an existing portfolio or buy individual stocks. There are sound investment strategies. that go beyond an investing algorithm.Sophisticated and even some newer investors may want a broader investment portfolio with a wider range of asset classes than the typical robo-advisor offers.

3. **No Human Contact**

If you want a relationship with your financial advisor, then most robo-advisors aren't for you. Robo-advisors don't have an office where a client walks in and talks directly to an advisor. This type of personal contact is relegated to the traditional financial advisory models.Most robo-advisors won't hold your hand and comfort you after a significant market drop. By contrast, a human financial advisor can be available to assuage your fears and explain how the investment markets work. Whereas a financial planners can integrate your finances, taxes, and estate planers, robo-advisors lack this human touch and cannot take a holistic view of your financial life.

4. **May Be More Costly**

Robo-advisors often charge fees, which vary based on your account balanceFor example, Betterment charges a monthly fee of $4 for accounts with low balances. This fee automatically switches to 0.25% annually once the account grows to above $20,000 or if there are monthly recurring deposits of $250 or more.It's also important to note that your money will often be invested in ETFs. Even though these ETFs often have a low expense ratio. this is an additional cost that should be factored into your total cost.

What's the future of the industry?

The neobanks are also broadening their offerings, with recent announcements of growth into the investment space. Recently valued $33bn digital bank, Revolt, is planning on adding robo-investing to its product suite, while Marcus, Goldman Sachs' digital bank, is set to bring its US offering 'Marcus Invest' to the UK later this year.With digital investment platforms and digital wealth management here to stay, the banking industry needs to remain flexible in its processes and its partnerships.Joining forces with digital experts such as Nutmeg and Embark, enables banks to grow their breadth of offerings and to pivot much more quickly than they would alone.

No tech giants have yet made a deliberate move into the wealth management sector, but entry in the not-too-distant future appears likely. Apple has already created a financial and advisory services provider (Braeburn Capital) to manage a large amount of its cash reserves and Asian tech companies such as Alibaba and Tencent have made major investments in a leading Chinese investment bank.To keep up with tech innovations, remain relevant in the market and meet the emerging needs of its customers, the banking industry needs to consider partnering with those who already have a foothold in the digital space, leveraging specialist strengths and becoming more agile and digital.While few expect robo-advisers to replace human consultants in the near future, hybrid services that combine human and digital advice can be a major win for investments in partnerships, enhancing the digital customer service and allowing advisers to spend more time on what really matters: building relationships with clients. If your bank would like to explore whether a digital investment platform could help you deliver services that add value to customers and keep them in your ecosystem.
In India, currently, there is no specific regulation governing the Robo Advisory platforms in India and SEBI has just extended its oversight over Robo Advisor Platforms with respect to risk profiling, record-keeping, and compliances under the ambit of existing IA Regulations. Robo-advisors, like human advisors, cannot guarantee profits or protect entirely against losses, especially during market downturnseven with well-diversified portfolios. Because most robo-advisors only take long positions, when those assets fall in value, so will the portfolio it has constructed.

Robo banking in India

It is the country's first banking robot launched by the City Union Bank (CUB). Lakshmi is a two-foot robot used in the Kumbakonam-based City Union Bank. It is fondly called CUB Lakshmi in the bank. The robot speaks English and can gesture and engage in conversations.Robo advisory system in India is not very old & a list of Robo Advisors in India will be a short. But this is something that is catching the eyes of a lot of young people nowadays.In last few years, quite a few companies have started operations in robo advisory space. At present, there are 39 robo advisory companies in India according to Tracxn, a data analytics company.Out of

39 fintech companies, ~10 have announced receiving funding in robo advisory domain. The very early entrant was FundsIndia.com. They have received $15.41 million so far from the Foundation Capital, Inventus Capital Partners & Faering Capital.The other robo advisory companies who have received substantial funding includes MyUniverse and Scrip box .

Few years ago, use of robots may have seemed to be many years away from reality, but it now appears that we are reachinga tipping point in human-robot collaboration.

Meet Lakshmi, the two-foot robot that is pushing the Kumbakonam-based City Union Bank (CUB) towards a new self-service era. CUB Lakshmi, as it is fondly called in the bank, speaks English, can gesture and engage in conversations. It can interact on more than 125 subjects with customers, and can answer queries around interest rates on loans, checking the account balance and more.

Robo-Advisors - India

“This artificial intelligence (AI) powered robot will be our first on-site bank helper and answer generic banking-related questions of customers. We felt that in a branch this robot will be in a position to answer basic questions to our customers. Over time, it can support other banking roles with insightful data and analytics, making humans smarter and more efficient in value delivery,” says N Kamakodi, MD and CEO, CUB.

- The Robo-Advisors market in India is projected to witness significant growth in the coming years.
- According to forecasts, the assets under management in this market are expected to reach a staggering amount of INR US$19.76bn by 2024.
- This growth is likely to continue, with an estimated annual growth rate (CAGR 2024-2027) of 9.21%, resulting in a projected total amount of INR US$25.74bn by 2027.
- Moreover, the number of users in the Robo-Advisors market is expected to rise to approximately 3.250m users by 2027.
- This indicates a growing interest and adoption of Robo-Advisors market among investors in India.
- In terms of average assets under management per user, it is anticipated that each user will have around INR US$6.45k invested in Robo-Advisors market by 2024.
- This showcases the potential for significant wealth accumulation through these platforms.
- When comparing the assets under management globally, it is noteworthy that United States leads the pack with an estimated amount of US$1,459,000.00m by 2024.
- This highlights the dominance of the US market in terms of Robo-Advisors market and their assets under management.
- Overall, the Robo-Advisors market in India is poised for substantial growth, with increasing assets under management, a growing user base, and the potential for significant returns on investment.
- India's Robo-Advisor market is experiencing rapid growth, driven by increasing digital adoption and a young tech-savvy population.

Conclusion

Hybrid models combining the best of both worlds (digital and traditional) are seen as the future of investing with digital solutions for investment experience, digital-led advisor connects, and robo-models for goal-based investments with added options of human advisor interactions. Some of the advantages of the hybrid. With the advancement of technology in areas such as advanced analytics, artificial intelligence (machine learning) and natural language processing, the effectiveness of robo-advisory is set to increase. This will enable robo-advisors to have higher impact across the value chain further strengthening the value proposition.

More than a decade since their inception, robo-advisors are at an inflection point. Despite the buzz and early success, mainstream adoption has been elusive. They are now facing the first major test for their goal-based, algorithm-driven investment model; the COVID-19 crisis has brought in an unprecedented level of uncertainty for investors across all categories. The ultimate impact on investor wealth and how well robo-advisors can wade through this crisis remains to be seen.

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