Are robo-advisers doing what they say? And should we even call them that?

BY **SAMUEL RHEE**

"What's in a name? That which
we call a rose
By any other name would
smell as sweet."
— *Shakespeare*

In Shakespeare's classic story of star-crossed lovers, Juliet declares that a name itself does not hold any worth or meaning, and it simply acts as a label to distinguish one thing from another. What is important is the worth of the underlying individual or thing. Unfortunately, a name is often the first impression you get, and this can be deceiving. Robo-advisers, as the name suggests, are supposed to be companies that provide financial advisory services digitally, with minimal human intervention. The "robo" in the name implies that there is use of algorithms and artificial intelligence (AI) in the process. However, closer examination suggests that the name is fast becoming a misnomer, with little "robo" or advice.

Who are you, Robo?

The robo-advisory business model originated in the US and is barely a decade old. The landscape is still evolving and many players started out by targeting the new generation of investors — the millennials. While the US market has seen the fastest growth and penetration rates, there has been a proliferation of robo-advisers across the globe: Most are copycats of the US business model and have provided little innovation of their own. With the growth of new players in the market and some success in gathering assets, the largest traditional financial institutions have taken note and launched their own robo-advisory services, either through internal or external product development (including acquisitions). This includes traditional brokerage firms, fund management companies and financial advisers such as Vanguard, Schwab, **Morgan Stanley** and **BlackRock**.

Independent direct-to-consumer business-to-consumer (B2C) robo-advisers with the largest assets under management (AUM) globally are companies such as Betterment in the US, Nutmeg in the UK and Wealthsimple in Canada. We are seeing some differentiated business models emerge in this space, such as Acorn, Blooom and Stash, which are carving out their own niche in terms of target market, size of investor or style of investing (that is, environmental, social and governance-conscious, thematic). Due to the supportive regulatory environment, Singapore has seen several robo-advisers launch services in the past couple of years. There are now both B2C players providing direct-to-consumer services as well as (business-to-business) B2B players who target the growing wealth management industry here. Some have launched "bionic" services that marry robo with human interaction, which also have their roots in the US. Some are startup fintech companies and some are services launched by incumbent financial institutions.

Current solutions popular in the market have shown little to no real application of AI, especially in the investment decision-making process, choosing instead to mostly deploy proven and traditional models of asset allocation based on modern portfolio theory. Some have even gone off the beaten track by choosing to go with unproven active investment processes (such as macroeconomic regime-based active management, which has no systematic investing methodologies and effectively tries to time the market — something that has been proven to be a futile effort). Most use simple rules-based algorithms in areas such as optimisation and rebalancing, which is what traditional investors also use. Using a computer to calculate mean-variance optimisation through critical line algorithms does not mean you are using AI or machine learning, just like selling something on Amazon does not make the company a robo-retailer. The offline-to-online (O2O) conversion of the user experience is in itself meaningful, especially in reducing cost and broadening access, but that is why it probably makes more sense to call these companies digital financial advisers or online wealth managers.

Robo-adviser or robo-fund manager?

Also, almost without exception, robo-advisers today are licensed fund management companies, not independent financial advisers. They are technically robo-fund managers if you insist on putting robo in there somewhere. They have built active funds, with the only difference being that they use exchange-traded funds rather than single securities (such as stocks or bonds) and oftentimes trade them actively, just like any other active fund, instead of focusing their efforts on providing high-quality, value-added advisory services. By becoming fund management companies, robo-advisers are narrowing the investment opportunities for their investors by using only their own funds, made up of cheap, readily available ETFs. Often they are not tax-efficient and can easily be replicated by an individual directly purchasing the ETFs rather than paying for the additional layer of fees robo-advisers charge for managing the ETFs.

Good financial advisers should be independent and open to finding the best investment solutions for their clients. It is important to be agnostic to any particular solution or product provider. The most suitable product for an investor could be a passive equity index fund (ETFs are funds too — they are just exchange-traded). However, it could also be a factor-based smart-beta fund or an actively managed fixed-income fund. A financial adviser should provide personalised financial planning throughout a client's life cycle, especially in areas such as long-term retirement planning or tax-efficient investment solutions (which US-listed ETFs are not for non-US investors). Robo-advisers should capitalise on personalising advice at scale, using the best investment solutions available as building blocks, which is also unfortunately not the case currently.

One area in which the robo-advisers have focused on, and have somewhat delivered, is lowering the cost of accessing investment portfolios. Cost is the single-biggest barrier to better long-term returns for investors. Although robo-advisers in Asia and Singapore charge lower fees than existing expensive channels, these fees are still far higher than those of other international players. Betterment in the US, for example, charges a flat fee of 0.25% for its digital-only solution, with no minimum balance. Vanguard Advisors charges an advisory fee ranging from 0.05% to 0.30%, depending on AUM. Of course, finding the most suitable investment that delivers is more important than costs, but a truly independent digital financial adviser should be able to deliver both.

The key therefore is not the name, but the core mission of robo-advisers, which is to provide access to low-cost solutions for those who cannot meet the high investment thresholds of traditional financial adviser channels (such as the private banks). The cost of accessing intelligent investment solutions is prohibitive for most investors, owing to the stranglehold by incumbent financial institutions on distribution channels, especially in markets such as Singapore. B2B players, some of which have taken money from fund management companies and have possibly had their advisory independence jeopardised, enable incumbent financial institutions to maintain their dominant position. This is where independent digital (robo) advisers must step up and disrupt the market in order to provide lower-cost solutions and access to those who would not otherwise be able to receive financial advisory services. This may also be the solution to improve the quality of retirement income planning, which is essential for Singaporeans. This could include managing their CPF together with their private retirement plans in a holistic manner to improve their chances of success.

Fast does not mean better in financial services

We have observed the focus of many of these robo players on quickly building out their technology platform rather than providing best-in-class financial advice. They have taken an almost e-commerce approach to selling financial products, but apart from the fact that they both target retail customers, there are very little similarities. It is unfortunate that the depth of financial domain knowledge is also weak. Most of the management team of robo-advisers globally have started with weak or little financial experience, especially in actually managing large sums of money for investors. Though this may still "work" in the type of trending bull market we have experienced over the last decade, we suspect an inevitable downturn will cause an exodus of "lazy" money from these platforms. The concern is the lack of deep domain knowledge that is required for running a financial services business and communicating effective and long-term financial advice that will help clients behave intelligently across market cycles.

Furthermore, risk management, an essential requirement for a financial services provider, seems to be a weak aspect of most existing Asian robo-advisers. This applies even more to robo-advisers licensed as fund management companies rather than as financial advisers. Financial advisers do not directly touch or manage clients' money, as opposed to fund management companies, which have discretion over clients' money and often custodise the asset internally, and therefore a deeper level of compliance and legal and custodian expertise is expected of them.

In terms of the fund performance, a "robo" fund management company is competing against existing fund management companies, often with their global scale, wealth of knowledge and experience built up over decades running billions in client assets. For a new entrant to deliver a benchmark-beating solution consistently is slim, just as the chance of consistently delivering alpha through active management in equities is slim. Given the ease of direct access to underlying ETFs, we see little benefit in the higher cost structure of in-

The cost of an additional 1% in fees

*Assuming an equal 8.5% annualised return before fees vesting through a robo-adviser. We have begun seeing early adopters replicate robo-adviser portfolios through their own low-cost broker options.

The high and hidden costs of investing in Singapore

Another key concern that has been raised in Asia (including Singapore) is that robo-advisers have for the most part decided to invest via listed ETFs. There are several issues with using listed ETFs:

- Investing via US-listed ETFs will incur withholding taxes and estate taxes for Singaporeans that are often much greater than the total fees actually paid to the robo;
- Non US-listed ETFs may lack liquidity and have wide bid-ask spreads, eroding the benefit of the low-cost nature of ETFs; and
- Many robo-advisers trade ETFs actively in their portfolios, which could negate the benefit of passive investing entirely and raise costs as well as being inefficient from a tax perspective.

The financial advisory industry in Singapore is ripe for disruption. Costs are too high, outcomes are poor and conflict of interest is proliferating, all at the expense of end-investors. The existing compensation model places the adviser and client in conflict, and needs to change from a transaction and distribution commission-based market to an AUM-based model. Fees for quality financial advice and investment products are too high. For example, a retail investor would need to pay the following fees to invest in a fund:

- Upfront sales charge of 2% to 5%;
- Fund management fee of 1% to 2% a year (of which fund management companies rebate a large portion back to distributors such as banks/brokers/advisers in the form of trailer fees or distribution commissions); and
- Wrap fee/platform fee of 0.2% to 1.5% a year

These fees eat away at investor returns and are still a major challenge for investors to achieve general wealth accumulation or prepare well for retirement — a headwind that Singapore is roughly 15 years behind the US in fighting. When fees are charged at such exorbitant and unjustifiable levels on someone's retirement income today, this high-margin business is stealing from the life savings they have put aside to sustain them post-retirement. While there has been some progress in this regard, there is still further room for improvement and active self-regulation by fiduciaries in the private sector may be required.

A new digital manifesto for financial advice in Singapore

We see opportunities for the digital wealth management and financial advisory industry to create great value through the following efforts:

- Greater financial expertise and domain knowledge, combined with a deeper understanding of a client's needs, to create a better consumer product. A seamless online platform that integrates onboarding, know your client (KYC), account opening, needs and goals analysis, digital customer service and account management, and also offers innovative solutions to meet a client's needs in wealth management, and specialised areas such as retirement. This will require a greater shift in financial talent from traditional financial institutions into this new burgeoning field and a significant improvement in the financial domain knowledge of all players to gain the trust of customers;
- Provide retail customers with access to a better and broader set of investment products with low institutional-level fees, beyond just ETFs or stocks and bonds. The biggest and best institutional investors, such as university endowments at Yale or Harvard, or the largest sovereign wealth funds do not just buy ETFs but a diversified portfolio of both passive and active managers to generate great returns. We must create optimised globally diversified, multi-asset class portfolios at different levels of risk, and leverage the collective scale of the robo-adviser to further drive down the cost of best-in-class investment products for its clients. This may eventually include investment products that may have been previously inaccessible for individual investors. The effective use of technology to democratise opportunities for investors will continue and gather pace;
- Appropriate application of technology to meet the key financial needs of investors beyond portfolio optimisation and O2O services. One such area of need would be trying to solve the conundrum of how to increase the probability of achieving a retirement income target. This means trying to solve a defined-benefit problem (a fixed-target retirement monthly income) within a defined contribution framework (principal and monthly savings plans), which we are hopeful technology can help the industry achieve through personalised glide-path solutions, for example; and
- Continue to find ways to use technology for distribution and delivery of better-than-human advice at scale. This is the challenge and raison d'être of the robo-adviser, or more broadly, the digital wealth management industry — to meet and anticipate the financial needs of clients through technological solutions. ■

Samuel Rhee is chief investment officer at Endowus, a Singapore-based financial technology company that empowers people to take control of their financial future. The firm's proprietary systems provide data-driven digital wealth advice on constructing personalised investment solutions. Rhee was previously CEO and CIO at Morgan Stanley Investment Management in Asia. He is an advisory council member at the NUS Business School's Centre for Asset Management Research & Investments (CAMRI).

MARKET diary

Tuesday, March 12

Singapore

Retail Sales (y-o-y, Jan)

Advanced Holdings Ltd — EGM

Wednesday, March 13

Singapore

Unemployment Rate (Q4)

Ramba Energy Ltd — EGM

US Producers Price Index (Feb)

US Core Producers Price Index (Feb)

US MBA Mortgage Applications

Thursday, March 14

Singapore

Datapulse Technology Ltd — EGM

US Export Price Index (y-o-y, Feb)

US Import Price Index (y-o-y, Feb)

Friday, March 15

US Industrial Production (y-o-y, Feb)

LISTINGS

Wednesday, March 13
Topic: A Guide to Property Stocks
Highlights: Understand the Real Estate Industry. Learn about the main factors that will influence the industry and, hence, the profitability of property companies. Gain insight into how property companies make money. Participants will learn how to differentiate the different property companies based on their risk/return profile.
Time: 7pm to 10pm
Venue: Academy 1 and 2, 2 Shenton Way, SGX Centre 1
Organiser: Singapore Exchange
Tel: 6327 5438
Registration: https://www.sgxacademy.com/event/a-guide-to-property-stocks/

Thursday, March 14
Topic: How to Spot Intraday Gold Trend Within a Minute Using Technical Analysis
Highlights: Introduction to technical analysis and types of trading strategies; identify the intraday trend of spot gold with indicators; techniques to enter and exit a trade; live chart analysis with MT5
Time: 7pm to 8pm
Venue: 250 North Bridge Road, #07-01, Raffles City Tower
Organiser: Phillip Futures
Tel: 6538 0500
Registration: https://www.phillipfutures.com.sg/investors/education/seminars-events/register/357

Tuesday to Thursday, March 26 to 28
Topic: 5th Annual Mining Investment Asia – Conference and Exhibition
Highlights: Women in mining; mining investment; mining tech
Time: 9am to 6pm
Venue: Marina Bay Sands
Organiser: Spire Events
Tel: 6717 6019
Registration: vishal.sengupta@spire-events.com
Website: mininginvestmentasia.com

CORPORATE MOVES

Hafary Holdings Ltd
Jackson Tay Eng Kiat has been appointed COO wef March 1
Work experience: CFO, Singhaiyi Group; director, Hafary Pte Ltd

Hong Fok Corp Ltd
Adrian Chan Pengee has been appointed non-executive independent chairman wef March 1
Work experience: Director, Yoma Strategic Holdings Ltd; director, Global Investments Ltd

Megachem Ltd
Tatsuyuki Sakoda has been appointed non-ED wef March 1
Work experience: Executive officer, corporate planning division, Chori Co Ltd

Quest Ventures
Goh Yiping has been appointed partner wef March
Work experience: Co-founder/CEO, All Deals Asia; co-founder/chief product officer, MatahariMall.com
Jeffrey Seah has been appointed partner wef March
Work experience: CEO, Southeast Asia/chair, Asia Digital Leadership Team, Starcom MediaVest Group

Stamford Land Corp Ltd
Huong Wei Beng has been appointed independent non-ED wef March 1
Work experience: Director, Novus Corporate Finance Pte Ltd; director, 3 Peaks Capital Pte Ltd

Star Pharmaceutical Ltd
Tan Wen Wen has been appointed non-ED wef March 1
Work experience: GM, Beijing Shenghuajie Industry and Trade Co Ltd

Tat Seng Packaging Group Ltd
Kong WeiLi has been appointed non-executive and independent director wef March 1
Work experience: Plant financial controller, Sanmina-SCI Systems Singapore Pte Ltd
Siu Wai Kam has been appointed non-executive and independent director wef March 1
Work experience: Assistant director, Communications and Information Technology, Singapore Institute of Technology
Jasper Goh Yang Jun has been appointed non-executive and independent director wef March 1
Work experience: Managing partner, Back Office Partners Pte Ltd

Uni-Asia Group Ltd
Juliana Lee Kim Lian has been appointed independent non-ED wef March 1
Work experience: Practising lawyer/director, Aptus Law Corp
Zac K Hoshino has been appointed senior MD wef March 1
Work experience: MD, Uni-Asia Group Ltd; director, Uni Asia Shipping Ltd

Y Ventures Group Ltd
Lew Chern Yong has been appointed executive chairman/director wef March 1
Work experience: ED, Wong Fong Industries Ltd; program executive, TOUCH Community Services Ltd — *Compiled by Rahayu Mohamad* ■

Companies are invited to submit notices of senior corporate appointments and changes. Announcements will be edited for brevity. Email rahayu.mohamad@bizedge.com; attention: editorial coordinator, Rahayu Mohamad.