BETTER FINANCE
The European Federation of Investors and Financial Services Users
Fédération Européenne des Épargnants et Usagers des Services Financiers

PRESS RELEASE

Robo-advice: Automated? Yes. Intelligent? Not so much.

Extreme divergencies between platforms and investor profiles in terms of asset allocation and expected returns reveal significant deficiencies in the suitability of the algorithms' investment recommendations.

21 December 2021 – From virtual meetings and parties to shopping and dating online, people have *en masse* moved countless aspects of their lives into the virtual sphere due to restrictions imposed by the ongoing global Covid-19 pandemic. Financial matters and investments are no different in this regard, as illustrated by a marked increase in retail participation in financial markets and a shift over the last 20 months towards FinTech investment solutions such as Robo Advisors and online brokerage platforms.

This new reality underscores the growing importance of investor advice to ensure individual investors make informed and appropriate choices. Enter robo-advisors… online platforms that offer a simplified and often cheaper way of investing in capital markets and provide informative tools that allow investors to better understand the investment process and related costs and risks.

Low costs, almost no commissions

The success of robo-advisors hinges on their ability to keep costs low, and in this respect they do not disappoint. Their services continue to be far less expensive than those of their traditional counterparts such as banks, financial advisors and asset managers, mainly thanks to their use of inexpensive exchange-traded funds (ETFs).

What's more is that most robo-advisors covered by the research clearly claim that they do not come with the same conflicts of interests as traditional advisors, most of whom are paid commissions for selling certain products. In addition to the cheap service cost of robo-advisors, the near-absence of commissions or "inducements" also generally translates into less expensive products.

Despite their affordability and ease of access for non-professional investors, it is important to keep in mind that robo-advisors still deal with products and services that require clients to be financially literate and familiar with certain financial concepts in order to fully understand the products on offer.

Divergent asset allocation and expected returns

For the sixth year in a row, despite some improvement, the most concerning finding of the research into the 18 robo-advisors from 11 different countries across Europe, Australia, the USA and Singapore, remains the extreme divergences between platforms and investor profiles in terms of asset allocation and expected returns. Platforms "advise" significantly different equity exposures and "project" very divergent annual returns for exactly the same investor profile.

This very high discrepancy between the different platforms and investor profiles in terms of asset allocations and expected returns, raises concerns about the methodologies and algorithms used to determine suitability for the user.

The raison d'être of financial advisors, be they automated or "human", is to match the needs and preferences of the client with the investment product that best corresponds to their interests. Yet,

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research reveals consistent important biases affecting the advisory process of traditional financial advisors, often leading to a "one-size-fits-all" approach instead of personalised financial advice.

A far cry from artificial intelligence

Ostensibly, robo-advice should do away with these biases, since the idea is that the advice provided is based on an automated algorithm that will steer individual investors to the best-suited products based on the information they provided themselves. Yet the important divergences in advice point toward algorithms that do not sufficiently take into account the specificities of each individual investor.

"The Robo-advice sector continues to grow - albeit at a slower rate than could be expected - and is well-placed to provide a wide range of benefits for individual investors, such as considerably lower fees, better accessibility and availability, and less biased advice, compared to traditional advisors", says Guillaume Prache, Managing Director of BETTER FINANCE. *"Yet, their claim of personalised investment advice is all too often proven wrong by the lack of suitable and adequate recommendations adapted to the specific needs of each individual investor, clearly showing a tendency to perpetuate the "one-size-fits-all" tradition. The added value of the much-touted algorithms in too many cases fails to materialise. One does not need to have access to the algorithms' functioning to come to the conclusion that they are little more than basic questionnaires, and a far cry from intelligent systems akin to artificial intelligence."*

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