WHAT HAPPENS WHEN ADVISORS USE ROBOS

Michelle Schriver / October 13, 2017

If the choice between human advisors and robo-advisors wasn't clear before, it is now: both, please.

By 2025, hybrid robo-services are expected to increase to US$16.3 trillion in AUM worldwide, a 2016 report by MyPrivateBanking has revealed. That means platforms comprising both advisors and computers will handle more than 10% of total investable wealth.

Research also shows investors prefer advisors for nuanced or complex situations, like wealth transfer after a death, tax optimization, decumulation and philanthropy. In fact, Accenture research finds 58% of Canadian investors say advisors provide the best customized advice, while only 6% think a robot could offer customized advice.

Far from losing clients to robo-advisors, human advisors are introducing clients to them. That's because those advisors report better client engagement, less compliance work and more time to focus on planning. Here's why.

LIVING LA VIDA ROBO

Adam Bornn, a financial advisor at Parallel Wealth in Surrey, B.C., outsources his clients' portfolios to Wealthsimple for Advisors.

Clients say, "This is way better," says Bornn. "'Did I make or lose money?' That's what clients want to know," he adds. Before using Wealthsimple, Bornn's firm offered nominee F-class mutual funds, so clients were already familiar with fee-for-service. Clients typically pay 1% of AUM to Wealthsimple as Bornn's referral fee, which covers his services.

Karen Richardson, a fee-only financial planner at Money Coaches Canada in Kenora, Ont., says online platforms are "a great tool" for client education. For the last three years, she's referred clients to Nest Wealth Pro Lite, typically when they want greater fee transparency or online convenience. (She receives no referral fee because she's not securities-licensed; clients pay for her services up front.) Both she and her clients appreciate the online statements and their visual presentation. "The gain/loss is clear," she says. And at meetings, "it's very helpful to have [statements] in front of you to go over and explain." In contrast, "Clients with paper statements bring them to meetings, but struggle to read them," she says.

Easy-to-read statements combined with online access have increased engagement. "Clients seem more informed about their investments because they have [been] checking their accounts," says Richardson. Further, clients "book more meetings, because they want to learn more," she says.

When interviewed, Bornn had been transitioning clients to Wealthsimple for less than a month. Ideally, all clients will choose to use the platform, he says. With investment management looked after, "we're going to focus on the planning." That means more time to consider the client's taxes and retirement.

It also means more time for his practice. He can take more continuing education courses; his unlicensed assistant now focuses on client experience.

Tony Mahabir, CEO of Canfin Financial Group in Toronto, has had a similar experience. He refers clients to Invisor CoPilot for investing. In particular, he says the robo-advisor is a good solution for smaller clients. He says clients still need help creating a budget, reviewing an employment offer or structuring estates — issues that aren't product-related.

That doesn't mean he's off the hook when it comes to clients' products. For example, his firm has a six-part value proposition that includes accountability. That means analyzing and monitoring product suppliers. While he's aware of a client's whole situation, he lets the supplier handle the investment analysis.

That said, "Whomever clients are going to go to for products, we're going to hold them accountable," he says. "Product[s] should perform as promised."

He sees himself as a client mentor who understands the subtleties of emotions and family dynamics. "We are […] managing the client, not managing the money," he says. "Computers will do a good job managing the money."

CLIENTS CALL THE SHOTS

Younger clients can benefit from mentoring, says Mahabir. "What they need is someone to guide them and show them things they don't have strengths in."

Young or not, clients decide for themselves if they want the platform. "We're responsive to letting the client have it their way," he says, adding that online platforms appeal to clients in remote locations or to those who work odd hours or require childcare to attend a meeting. (Such clients can also get advice online through VirtualSage, Canfin's online communication platform.)

Online platforms also appeal to those wary of financial services. "A lot of my clients are frustrated with the turnover at the banks," says Richardson, and that presents opportunities for other advisors to build new client relationships. Further, negative media coverage about fees has encouraged clients to look for change.

"People will come to a fee-only planner because they want a customized plan," says Richardson. Because she establishes relationships with clients and provides customized asset allocations, they more readily embrace an online platform, she says, which might have been perceived as only for do-it-yourselfers.

Bornn's firm prefers active management, so he uses Wealthsimple's active strategy, available only within the advisor channel. There's no minimum account size. Despite the increase in low-cost, passive ETF investing, "there's always going to be a big shift toward active managers that have a track record of outperforming the benchmark after fees," he says. Big clients, especially, want managed accounts, he adds. However: "If a client wants ETFs, that's an option, too."

IN POSITION TO TRANSITION

Despite a positive experience so far, Bornn warns of pitfalls.

"People don't like change," he says. "If your clients see you as a mutual fund picker or the investment guy, and you're giving that piece of your business up now, […] you have to be careful how you position this." To clients, he explains his role this way: "I'm the financial planner and quarterback, and we've found a better solution on the investment side."

Says Mahabir, "Advisors have to evolve and understand that they provide value beyond just picking out mutual funds or managing assets."

Mahabir's typical client conversation is: "There are things you can do on your own and things you'll need me to help you with. [Let's] identify those things." Though he had been using Invisor CoPilot for only two months when interviewed, Mahabir says he hasn't lost clients to the platform. In contrast, "We have lost clients to IIROC, to segregated funds or to portfolio managers — that's the norm of the business." (Mahabir is MFDA and exempt market licensed.)

With more requests for annual reviews, business is good for Richardson. Is the increased client engagement unmanageable? No, she says, adding that she appreciates how the growth of robo-advisors has helped educate clients. Before, “people didn’t know what an exchange-traded fund was, so they weren’t asking.” She considers the Nest Wealth platform a tool that initiates client conversation.

“We do a lot more for clients than just investments,” says Mahabir. When a client understands the advisor’s value, as well as observes the advisor’s confidence in outsourcing, “that looks good,” he says. “When you put the best interest of the client first, you get their goals met whether or not it can be done through you. That’s the new paradigm.”

FEES: HYBRIDS VERSUS TRADITIONAL ADVISORS

Will clients pay lower fees when they use an advisor-robo hybrid? It depends.

Consider a balanced, passive ETF portfolio. Depending on the platform or firm with which the client invests, such a portfolio could have an MER ranging from 13 to 30 basis points; transaction fees run from $0 at some robos and investment firms to $100 or more at others.

The potentially biggest difference-maker, however, is management fees.

For a portfolio worth $100,000, robo management fees range from about $350 to $480 at some platforms, while advisor referral fees range from a few hundred dollars to $1,150. Advisors might charge additional fees for services like tax and estate planning.

Clients working with traditional advisors wouldn’t incur the robo management fees, but advisory services could potentially run from $2,500 to $3,500 in the first year.

“On a small portfolio, can one justify paying that kind of fee?” asks Jordan Wilson, president of Wilson Wealth Management in Saskatoon. “I normally turn down [a $100,000] client as it is not fair to them or me.” He adds, however, that a fee becomes reasonable for a smaller client when compared to paying high total expense ratios for mutual funds over several years.

For a $1-million portfolio, it’s easy to find both hybrids and traditional advisors on both ends of the fee continuum. And you get what you pay for. For a new client, Wilson spends five to 10 hours on such things as risk assessment, determining objectives and constraints, and developing asset allocation. “In the initial year, getting to the appropriate target asset allocation (and suitable benchmarks) is the bulk of effort,” he says.

For some clients, complexity also impacts fees, he adds, citing options strategies or private equity analysis.

He also highlights the hand-holding and macroeconomic commentary advisors provide to clients during uncertain times, like during the U.S. election or when interest rates rise.

Advisors also identify circumstances that require changes to asset allocation. “Skilled advisor[s] can elicit the right information for planning purposes,” says Wilson. “But they need to know the questions to ask.”

Ryan Lewenza, senior vice-president and portfolio manager, private client group at Turner Investments, Raymond James in Toronto, says his 1% management fee includes portfolio management, financial planning, retirement planning, tax planning and advice on anything from wills to real estate. He considers his firm a hybrid because it offers low-cost ETF portfolios plus full service.

All firms we looked at cite relatively low MERs for ETF portfolios, but could a client require costlier ETFs to have a truly balanced portfolio?

Potentially, says Dave Nugent, head of investments for Wealthsimple. “While cost is an important consideration, [it’s] only one of many variables that goes into making our investment decision,” he says. “If there is additional value provided by an ETF with a higher fee, but that fee is justified, then we will consider it for our portfolio.” He adds that Wealthsimple’s subadvisors decide on portfolio construction and products for sub-advisory accounts.

Nest Wealth offers only seven ETFs and says its MER is 0.13% for a balanced portfolio. However, one ETF has a 0.39% MER — a Canadian government real return bond fund. As an inflation hedge, not a core holding, the fund wouldn’t be more than 10% of a client’s holdings, says Randy Cass, Nest Wealth’s founder and CEO.

For U.S. ETFs, both Nugent and Josh Miszk, vice-president of investments at Invisor, say currency exchange is 20 basis points or less, while Cass cites 15 to 20. Though clients don’t pay directly for currency exchange, Miszk notes that negotiating good rates is part of a portfolio manager’s fiduciary duty to clients.

Estimated fees for a $1-million passive ETF portfolio

- **Robo management fee — $960 to $4,000, plus HST (paid by clients using hybrids)**
- **MER — 0.13% to 0.30%**
- **Transaction fees — $0 to $200**
- **Advisor referral fees — $3,000 to $10,000, plus HST (paid by clients using hybrids)**
- **Advisor management fees — $3,500 to $10,000, plus HST (paid by clients using traditional advisors)**

Clients using online platforms could incur additional advisory fees if the referral fee doesn’t cover the advisor’s services.

Sources: Invisor, Nest Wealth, Wealthsimple, advisor Jordan Wilson, advisor Ryan Lewenza