ROBO-ADVICE FOR PENSIONS

Robo-advisors: Added Value and Risks
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OECD
BETTER POLICIES FOR BETTER LIVES

OECD Working Party on Private Pensions
Roundtable on Robo-advice

EASYVEST

FCA FINANCIAL CONDUCT AUTHORITY

quirion

WealthKernel

FinTech innovation
ACPR BANQUE DE FRANCE

YOMONI

scalable .CAPITAL

BaFin

Smart Pension
fast secure free

esma European Securities and Markets Authority

Recent OECD publications on FinTech and Pensions

ROBO-ADVICE FOR PENSIONS

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TECHNOLOGY AND PENSIONS

The potential for FinTech to transform the way pensions operate and how governments are supporting its development

OECD

http://www.oecd.org/finance/private-pensions/latestdocuments/

Why now?

- Robo-advice is not new…
  - *Automated investing*: algorithms used for investing have already become common among traders (e.g. high frequency trading)
  - *Automated advice*: advisors have been using algorithms to help provide financial advice for decades
- …but the two functions are now being combined and used more at a retail level
- A combination of market, regulatory and technological changes is driving the emergence of this new form of robo-advice

The changing pension landscape

- Shift toward defined contribution pension schemes
  - Individuals are bearing more responsibility for saving on their own for retirement
  - Low levels of financial literacy and experience investing are prevalent
  - Pension savers need help to decide how to save for retirement

The changing regulatory landscape

- Increased disclosure requirements for advisors
  - Suitability reports
  - Conflicts of interest
  - Costs and fees
- Limits on conflicted remuneration structures
  - Move from commissions to fee-based services
    - Fee-based services perceived as too expensive by consumers
    - AUM fees decrease incentive to serve lower wealth clients
- Increased scrutiny on the costs of investing
  - Increased transparency of total cost of investing
  - Active managers criticized for not adding value for clients
  - Movement towards more passive investment strategies

The FinTech solution

- Cost reduction
  - Squeezing margins through improved efficiency
  - Cutting out the middleman
  - Low cost investment
- Accessibility
  - User-friendly interfaces
  - Investing made simple
  - Online

The appeal of robo-advice

- Mass market
  - Low initial investment requirements
  - Quick and easy to access
  - Simple to understand
- Niche affluent market
  - Hybrid models with human advice
  - Tax optimisation

Features of robo-advice

- Type of accounts offered
  - Brokerage
  - Tax-sheltered, e.g. pensions
- Investments available
  - Passive vs. active
  - Independent vs. proprietary
- Recommended portfolio
  - Variety of personal circumstances considered
  - Objective, time horizon, risk tolerance, income, wealth, other investments, tax
  - Large range in number of questions asked
- Other services
  - Automatic rebalancing, tax-efficient investment, self-directed financial planning tools, regulatory compliance (e.g. suitability reports)
- Pricing
  - Management fees
  - Fund/trading fees
  - Usually <1% AUM + fund/trading fees

Potential demand-side benefits of robo-advice

- Affordability
  - Reduced financial costs
  - Reduced search costs
- Accessibility
  - Online 24/7
  - User-friendly
  - No pressure/judgement
- Asset accumulation
  - Increased participation in stock markets

Potential supply-side benefits of robo-advice

- Increased objectivity of advice
  - Avoid biased advice from financial incentives
- Increased consistency of recommendations
  - Avoid human/emotional bias of advice
- Increased transparency of advice
  - Follows the logic of the algorithm
  - Artificial Intelligence, however, would be a challenge…

How does current regulation apply?

- Definition of advice
  - Who can give advice?
  - General recommendation vs. personalised advice
  - The disclaimer problem
- Suitability requirements
  - Which standards apply?
  - Are risk profiling questions sufficient?
- Qualification/licensing requirements
  - Tech knowledge vs. financial knowledge
  - Independent advisors vs. broker
- Remuneration requirements
  - Proprietary services
  - Conflicts of interest
  - Retrocession payments
- Disclosure requirements
  - Fees and charges
  - Fund selection process
- Dispute resolution
  - Consumer access to redress

Potential new challenges

- Consumer disengagement
  - Suitability for target market
  - Communication
- Robustness of Algorithms
  - Auditing, stress testing requirements
  - Risk of mass mis-selling
  - Responsibility of tech platform vs. investment platform
- Herd behaviour
  - Similar algorithms -> similar investment strategy
  - Criteria for investment selection, granularity of asset classes, investment methodology and assumptions
- Sustainability of business model
  - Customer acquisition, low account balance, high turnover

Final considerations

- New legislation may not be required, rather need to establish how existing requirements apply
  - Being regulated is generally welcomed in order to lend credibility and gain consumer trust
- Need to improve consistency in regulation
  - Create a level playing field within a given jurisdiction
  - Facilitate international expansion and portability
- Cultural shift needs to happen to adapt to a digital world
  - Shift from supervising humans to auditing algorithms
  - Shift from paper-based to digital compliance
- Future challenges
  - Pension decumulation
  - Machine learning

THANK YOU!

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