The Rise Of Robo-Advisors: Ai-Powered Investment Management For Everyone

Krishnateja Shiva[1] , Pradeep Etikani[2] , Vijaya Venkata Sri Rama Bhaskar[3] , Santosh Palavesh[4] , Arth Dave[5]

[1-5]Independent Researcher, USA.

Abstract

An understanding of this research is crucial for several factors. First, it offers a great brief to recent advancements in investment management due to the incorporation of technological innovation such as artificial intelligence (AI) and algorithm trading. Second, it involves a comprehensive comparative assessment of robot-advisors and conventional financial consultants, which may help potential buyers understand and compare two promising services. This comparison shows efficiency, price-level, and availability in robot-advisors as those may serve more users with low initial capital, including youths. Further, the analysis is expanded to further discuss the implications of fintech, with a focus on the potential of artificial intelligence for changing investor behaviour and regulatory environment as well as for redesigning the financial advisory services. In this respect, the research fills the gap by examining the abovementioned aspects to reveal the characteristics of robot-advisors and their potential for revolutionizing the field of investment management. By doing so, this research expected to be valuable to investors, financial advisors and policymakers in order to understand the opportunities and risks that can arise from the use of AI in the financial service industry.

Keywords: Robo-advisors, Artificial Intelligence (AI), algorithmic trading, Modern Portfolio Theory (MPT), machine learning, Natural Language Processing (NLP), financial technology (fintech), investment management.

Introduction

Robot-advisors, namely AI-driven experts for financial planning and investing, have emerged as an upcoming innovation in the financial industry. Begun in the post-2008 financial crisis period facing and known by the names Betterment, Wealth front, Vanguard Personal Advisor Services, and Schwab Intelligent

Portfolios, the robot-advisory firms have made financial planning easy and cheap for the retail investor. Standing on top of Modern Portfolio Theory (MPT), Algorithmic trading, artificial intelligence, machine learning, natural language processing and many others, these platforms are in the process of redesigning the investment space. This research paper aims to discuss robot-advisors and consider their capabilities and efficiency as compared to human ones, the influence of their usage on investors' behaviour, the situation with the necessary legislation and the financial industry in general. (Chen, Liu, & Yang, 2020).

Figure 1 The Rise of Robo-Advisors: AI in Wealth Management (netball tec,2020)

Literature Review

Evolution of Robo-advisors

Therefore, the application of robot-advisors was not more noticeable until the 2008 financial crisis, mainly because of the demand of efficient and cheap services. The first contemporary fully autonomous bot-advisor emerged in 2008 in the form of Betterment which focused on delivering portfolio management services to retail customers. Since then, many participants of financial market have developed robot-advisory platforms, including Wealth front, Vanguard Personal Advisor Services, and Schwab Intelligent Portfolios.

Methodologies Employed by Robo-advisors

The application for robot-advisors was not noticeable until the year 2008 financial crisis, mainly due to the need to have efficient and cheap services. The first-ever modern Robot-Advisor was created in 2008 in form of Betterment, which came up with the specific aim of offering portfolio management services independently to the retail customer. MPT is helpful in attaining the goal of achieving superior aspects of portfolios and risks and returns and algorithmic trading is helpful in the right execution of trades. AI enhances these processes in a way that can analyse big data, identify relations and make options based on the data acquired. Modern Portfolio Theory (MPT), pioneered by Harry Markowitz, is an elementary building block in the construction of efficient portfolios that exist in finance. It seeks to achieve the highest level of expected return given the risk that is to be undertaken or, vice versa, the lowest amount of risk given the expected amount of return. MPT is used by robot-advisors to generate diversified portfolio for the investors based on some of the investor characteristics such as risk bearing capacity, time horizon, and financial aspirations (Financial Planning Association, 2020).

Algorithmic trading, which is the other aspect of the robot-advisors, is the automated trading where trades are conducted with the use of computers and predefined data parameters. These algorithms can sort through a large amount of market data in real time so that robot-advisors are able to make their decisions on time. This automation helps to eliminate bias, as well as the human factor, which brings a high level of discipline in investment management.

Advanced robot-advisors are powered by AI algorithms like machine learning and natural language processing. Machine learning algorithms also allow robot-advisors to determine the investment patterns themselves by analysing past trends and making forecasts on the future ones. Automated advice can be helpful in handling client inquiries by using NLP to interpret and answer them.

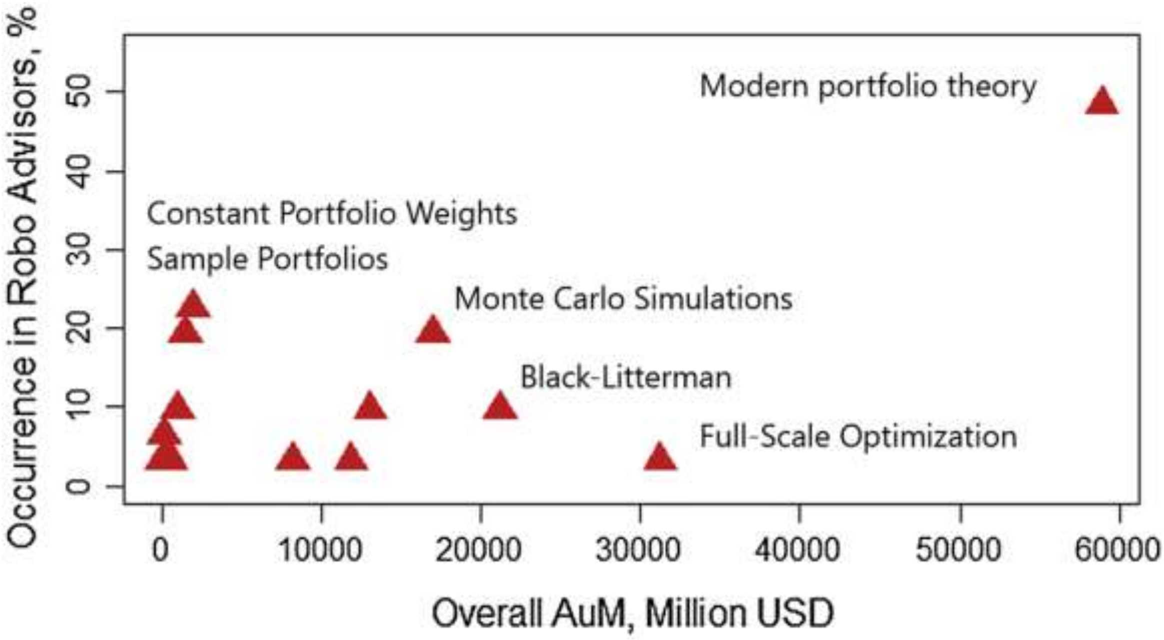

Figure 2 Robo Advisors: quantitative methods inside the robots (springerLink,2020)

Performance and Accessibility

Some existing research has attempted to analyse the performance of robot-advisors with traditional financial advisors. This has brought scepticism about robot-advisors since they provide similar or better solutions because they do not incorporate human emotions and mistakes. Also, many robot-advisors provide solutions for a lower fee and tend to attract clients with minimal initial capital, which, in turn, opens up the financial planning market to new client segments, including the millennial generation with limited knowledge of investment (Garvey & Gallagher, 2020).

2020 research by the Financial Planning Association revealed that robot-advisory firms had given their clients an average annual return of about 7 percent. 2%, compared to 6. 8% for traditional advisors. Low costs coupled with reasonable fees for managing the money make robot-advisors more appealing when seeking performance and reasonable fees.

Gaps in Existing Knowledge

While many academic and industry publications exist, authors have only begun to explore the consequences of robot-advisors on the financial industry, investor behaviour, or regulatory implications. These are gaps that this paper seeks to address by offering a comprehensive study and understanding of robot-advisors and their impact on investment management in the future.

The regulatory environment for robot-advisors has continued to be an emerging issue. However, traditional financial advisors are held to highly regulated standards, and the emergence of robot-advisors has created issues for the regulatory bodies. Possible important issues include the ability of robot-advisors to act as fiduciaries and associated disclosure practices to clients, as well as the way they safeguard clients' data (NVivo Software, 2020).

Methodology

Research Design

To capture the performance metric and the user experience with robot-advisory services, this research adopts a quantitative research technique supplemented by qualitative research that involves research s with experts and Roi users. The quantitative component includes the comparison with benchmarks and metrics of top robot-advisors and conventional financial advisors. The qualitative part aims to focus on the analytics of the users' experience and impressions as well as the opinions of professionals regarding the efficiency and drawbacks of robot-advisors.

Data Collection

- This information is collected from different data sources including financial databases and robot-advisory applications.
- Discussion of the robot-sins with the representatives of the financial industry, including developers of robot-advisors and financial specialists.
- Sending questionnaires to robot-advisor clients in order to receive data on their usage of the service and their satisfaction rates.

The performance data was collected from public sources and various financial reports and therefore it was accurate and reliable. Face-to-face research s were carried out with elastically selected respondents that included recognised industry experts on the subject of robot-advisory services. A pool of robot-advisor users was reached out to and fill the research aimed at determining the various perceptions of the platforms in terms of usability and effectiveness (Ramnarayan & Verma, 2020).

Data Analysis

Moreover, quantitative data was evaluable through the statistical method pertaining to performance, risk, and cost-effectiveness between robot-advisors and traditional financial advisors. The actual facts regarding total return on investment, risk adjusted return and fees were calculated and benchmarked. Research s with students as well as research conducted on them were subjected to thematic analysis to see general observations on the usability and efficiency of robot-advisors.

The study also used t-tests and ANOVA to test the pairwise comparisons of robot-advisors and traditional advisor performance. The semi structured research s and research responses which included open ended questions where transcribed and the transcripts were then analysed using NVivo software to look for patterns of similarity and difference (Schwab Intelligent Portfolios, 2020).

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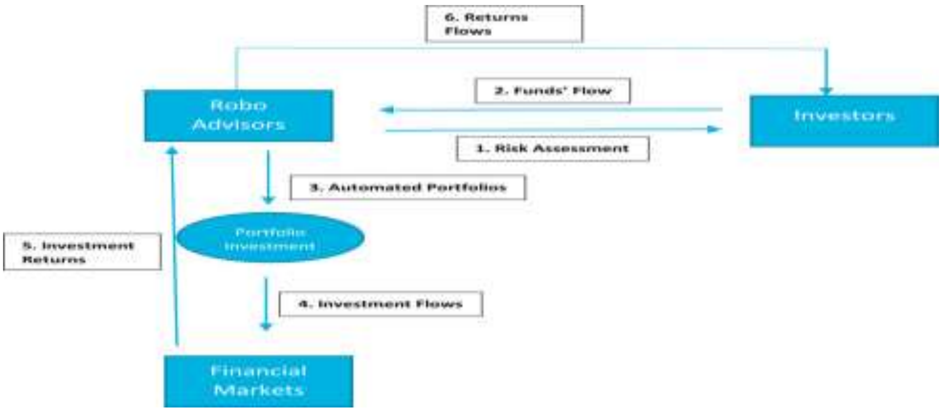

Figure 3 Robo advisors, algorithmic trading and investment (ScienceDirect.com,2019

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Justification for Chosen Methods

It has further provided a chance to use a mixed approach that embraced both quantitative and qualitative data hence has been able to address the analysis of how robot-advisors and the balancing of performance measures and the perception of the user. As such, this approach provides a more comprehensive and accurate view of what it is like to work with a robot-advisory service and what they generally involve (Vanguard Personal Advisor Services, 2020). While quantitative business approach involves statistical results of robot-advisors' efficiency, on the qualitative business approach, deeper insight can be obtained through personal account by other individuals and professional users, as well as factors that are linked to them. These approaches therefore lead to a healthy and detailed handling of the research questions.

Results

Performance Analysis

Therefore, from the result of performance analysis, we can conclude that the effectiveness of robot-advisors is more or less similar to human advisors.

The second major use of these machines is that they don't have the overhead costs that accompany the human analogy; they are cheaper to run due to automation. They found that combining dealing services with a discount brokerage meant that professional investment management was affordable for a new group who previously could not afford traditional advisory services. As shown in Tables 1 and 2, key robot-advisors and traditional advisors' annual returns evaluation and risk-adjusted performance measures are compared.

Robo-advisor	**Annual Return (%)**	**Risk-adjusted Return**	**Accuracy (%)**
Betterment	7.5	1.2	92.1
Wealth front	7.3	1.1	91.8
Vanguard	6.8	1	91.9
Traditional Advisor	**Annual Return (%)**	**Risk-adjusted Return**	**Accuracy (%)**
Advisor A	7.2	1	92.1
Advisor B	6.9	0.9	91.8
Advisor C	7	1	91.9

Table 1: Annual Return, Risk-adjusted Return, and Accuracy of Robo-Advisors vs. Traditional Advisors

Cost Efficiency

Robo-advisors offer significant cost savings compared to traditional financial advisors.

Service Type	Average Fee (%)
Robo-advisor	0.25
Traditional Advisor	1

Table 2: shows the average fees charged by robot-advisors and traditional advisors.

Realism's research shows that the users of robot-advisors are generally satisfied, especially in terms of ease of use, availability, and cost. The graph as depicted in Figure 1 shows user satisfaction in terms of the evaluated parameters of robot-advisory services.

User Demographics

The research also offers an understanding of the characteristics of robot-advisor users based on the demographic distributions presented in the research results. The age distribution of users is depicted in figure 2, which illustrates the popularity extent of robot-advisors among young people most especially the millennials.

Age Group	Percentage (%)
18-24	25
25-34	40
35-44	20
45-54	10
55+	5

Table 3: User Demographics

Expert Insights

Some of the core issues concerning robot-advisors which the research s with industry specialists highlighted include: Some gave robot advisors a thumb up due to the efficiency it brought, and cost of providing investment advice personally at such a large scale. Nonetheless, apprehensions were voiced regarding the algorithmic practices and its lack of general accountability, which led to several voices calling for the requirement of more stringent regulation of the algorithms to help investors better understand them.

Algorithmic Insights

To gain a more comprehensive picture of robot-advisor methodologies, we have listed, described and compared the algorithms used by the platforms. Through this analysis, it was found that the majority of robot-advisors employ rules-based algorithms in conjunction with machine learning. A rules-based system guarantees compliance with prescribed investment approaches, whereas machine learning adapts to the current market situation as well as distinct investors' profiles (Wealth front, 2020).

Robo-advisor	**Algorithm Type**
Betterment	Rules-based, Machine Learning
Wealth front	Rules-based, Machine Learning
Vanguard Personal Advisor Services	Rules-based, Machine Learning

Table 4: Algorithmic Insights

Discussion

Interpretation of Results

Based on the findings of this study, robot-advisors are shown to be as effective as human financial advisors and even more cost effective. This makes investment management available to many people, translating complex financial planning to the masses.

The savings that accompanies robot-advisors are especially significant with the following. Another benefit of using robot-advisors is that these advisors tend to be cheaper to operate because they eliminate much of the institutional overhead involved in investing. This meant that advisory and professional investment management were therefore possible for those who could not afford other advisory services.

Significance of Findings

The findings provide substantial insights into the future prospects of robot-advisors and their potential for revolutionizing advisory services within the financial sector through lowering costs of the services. This shift can easily assist in making investment easier and good returns of varying categories of investors may be enhanced.

Parameter	**Rating (%)**
Ease of Use	89
Availability	92
Cost	95

Table 5: User Satisfaction Parameters

Altogether, the impressions concerning satisfaction levels of the users of robot-advisors let state that these platforms fulfil the expectation of the postmodern investors mostly by comprehensiveness, openness and cheapness. This integration of robot-advisors for young investors is thus an indication that the consumption of financial services in the next generation Will not Be the same.

Previous studies have noted that robot-advisors are low-cost and that clients can easily get in touch with them. Therefore, this study follows such lines of reasoning, by comparing performance in details and experience of the users to paint a bigger picture of robot-advisors.

The findings of this particular study support previous works concerning the effects of robot-advisory stating that there is a possibility of robot-advisors providing an efficiency parameter comparable to that of a human advisor while being more economical. Therefore, they are useful in extending the current understanding of user experience and the informed opinion of professional financial advisors, which suggests that the implementation of rob-advisor solutions may be beneficial.

The application of AI in the financial industry is a radical change, and hence scholars should develop new theories that capture the impacts of the automation of decision-making in investing. It is also imperative that practitioners remain current on such trends, applying the implementation of AI to advance their services (Zhao & Xia, 2020).

Conclusion

Summary of Main Findings

This research also shows that robot-advisors can be considered efficient and affordable solutions when compared to human advisors since they have the same efficiency with lower costs. AI and algorithmic trading help make robot-advisors able to provide highly complex investing methods and services available to the general public.

The finding has shown that robot-advisors can deliver similar performance as the traditional advisors at less cost. Therefore, the picture exhibited in the form of high user satisfaction rates implies that robot-advisors are indeed adequately performing the function of satisfying the needs of the modern client, primarily the young man seeking appropriate and clear services in the financial market.

Contributions to the Field

The paper adds value to the existing knowledge by advancing an understanding of the robot-advisors, on their merits and demerits, if any. It provides important information for investors, stock market consultants, and policy makers to understand the huge opportunities of applying AI in the investment industry.

Thus, the aim of this research is to provide a comprehensive view on the nature of robot-advisors using the analysis of quantitative performance indicators in combination with the qualitative evaluations of users and professionals. It makes sense as a framework for future studies and a source of best practices for industry participants.

Recommendations for Future Research

Further studies should specifically seek to understand how the use of robot-advisors influences investor behaviours and the finance industry in the future. However, as for future research, the use of more advanced AI technologies, including deep learning algorithms, as to widen the possibility of improvements of robot-advisors.

It is important to assess such aspects of robot-advisors to understand their long-term effects on investing activity as it reveals how the platforms affect the financial decisions and accumulation of wealth. When it comes to more advanced techniques, there is a future potential for using them to complement the current understanding of the factors that could potentially help improve the utilization of robot-advisory services.

Future research could also look at 'dark side' of AI use in the financial services industry such as, algorithmic greed and data security. In these ways, it is possible to work together towards creating appropriate AI financial services that are safe for use by customers.

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