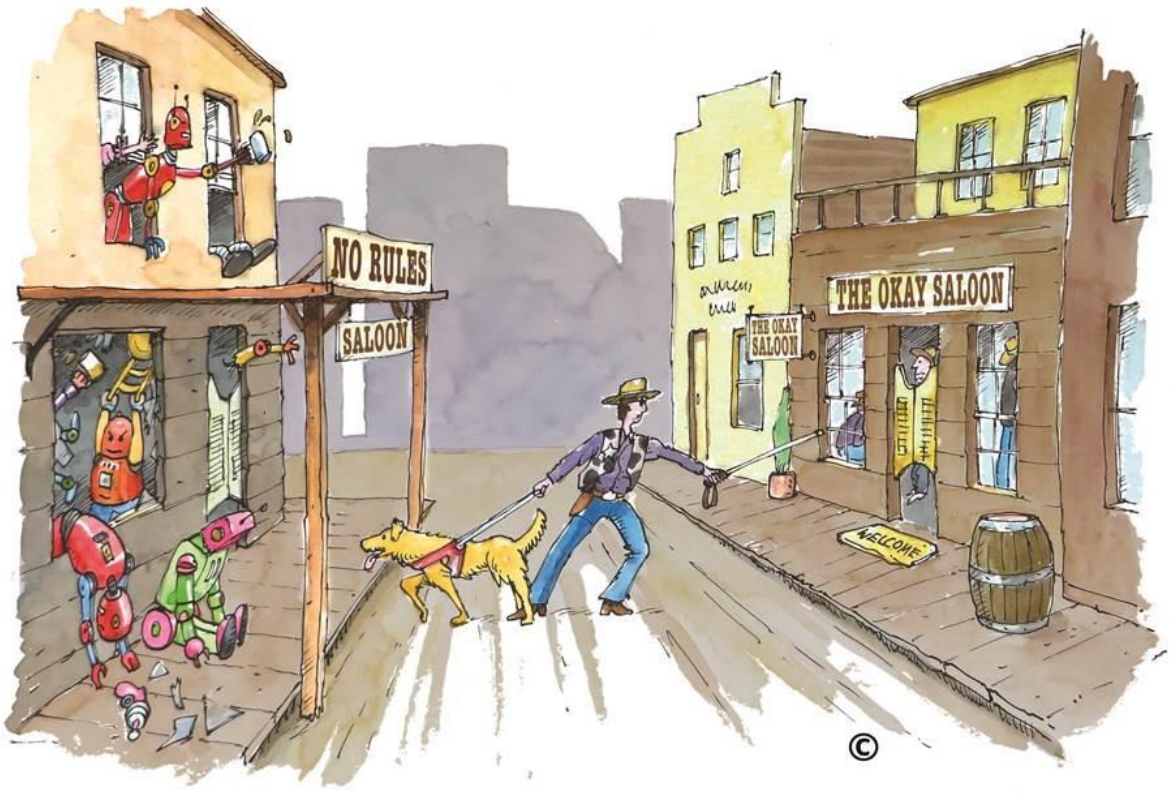
scm DIRECT
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TRUE&FAIR

Fintech Folly

The Sense and Sensibilities of UK Robo Advice



Report – 6 July 2016

Summary

Financial Issues:

- UK Robo Advisers are 'wired' to lose money, and most will go bust before acquiring the sizeable assets under management to ensure their sustainability.

- The research findings within this report estimate that the average UK robo-adviser receives revenue of just £147.50 pa per account, but the cost of acquisition is at least £180 pa per account; plus, considerable additional annual business costs. These additional recurring costs, were a robo adviser to reach the same economies of scale as much largest competitors, amount to £130 pa per account.

- One well known UK robo-adviser firms reported costs in its latest available accounts of £9.42 for every £1 of revenue.

- SCM Direct estimates that an average UK robo account would have to be invested for nearly 11 years to reach break-even. However, research findings show the average holding period for a robo-adviser client may be just 3 years.

- Most UK robo firms appear to be targeting 'millennials', a group that accounts for just 5% of the total investable market.

- Financing fatigue likely as demands for capital injections increase even though the reported growth rate from large US robo-advisers has decreased to a 1/3rd of the 2015 growth rate.

Regulatory Issues:

- Many firms appear to be straying into giving advice without possessing the requisite regulatory permissions or following the appropriate regulatory procedures.

- Evidence from a sample of 10 UK robo-adviser firms reveals misleading performance calculations, questionable statements regarding fees, a reliance on risk questionnaires, missing pages of key legal documents, and questionable claims.

- 80% (8 out of 10) of websites use risk questionnaires but 25% of these firms (2 out of 8 firms), did not possess the regulatory permission to give advice to retail clients. This would be a material regulatory breach were the services of these two firms to be deemed by the FCA or the FOS (Financial Ombudsman Service) to be advice.

Background

Against a backdrop of a supposedly widening advice gap, defined as those who cannot or will not pay for full regulated advice, and a failure to increase the number of people saving or investing, the UK Treasury and the Financial Conduct Authority are energised and focussed on automated 'robo-advice' as providing the silver bullet to resolve this issue.

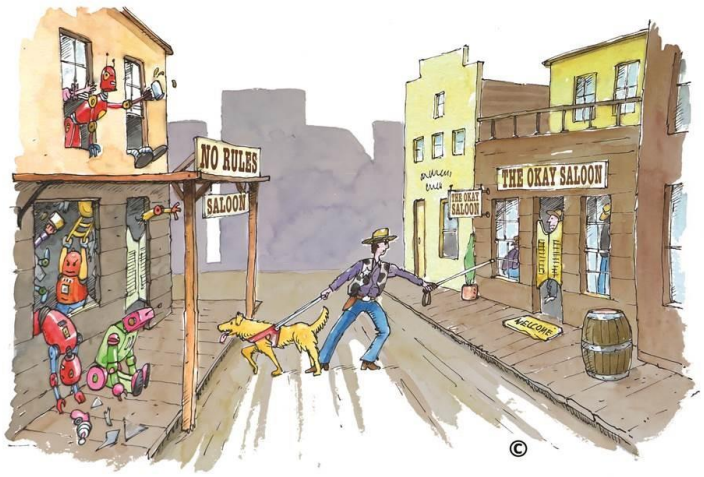
The high cost of advice is blamed by many for the 'advice gap', with the FCA finding '*that more than 85 per cent of investors were not willing to pay more than £200 for online advice'*. At the same time, advisers are unwilling to advise those with limited assets, with 69 per cent reporting they had turned away potential clients in 2015.

IFAs typically charge £150 an hour on average, according to unbiased.co.uk, which many consumers regarded as too expensive for their needs. On the adviser side, if a client has less than £100,000 to invest, many IFAs do not want to compete for their business.[1]

In the Treasury and FCA's eagerness they are even consulting on changing the definition of 'financial advice' to make it easier for cheaper and simpler services, including automated, robo-advice, that uses algorithms to offer general guidance and pick suitable investments for clients. Mark Garnier, an MP who sits on the Treasury committee, has said: '*As we move into an increasingly digital age, it is inevitable that the traditional financial adviser will be available in a robotic form. This is not a bad thing as it will make standardised advice available to everyone cheaply.'*

In SCM Direct's view there is a fundamental flaw with the tag 'robo-advice' as it implies these new firms are offering the same range of advice as a face-to-face adviser. This is not the case in most robo-advice models that are simply offering direct to consumer investment solutions.

In this report SCM Direct details why we believe 'robo-advice' could be a poisoned chalice not a silver bullet, and rather than creating a level playing field for the advice and investment industry it is creating a Wild West, where the admirable over-arching principles of the FCA of 'clear, fair and not misleading' are being completely disregarded.



[1] https://next.ft.com/content/4324f4dc-e9c8-11e5-888e-2eadd5fbc4a40

State of Play

Open any investment or advisory publication, and the pages are littered with new Fintech or Robo Adviser launches explaining why the march of the machines will end financial advice and investing as we know it; as well as close the advice gap by offering affordable advice to the mass market. Whilst there is no doubt that technology will evolve the investment and advice industry, it is the authors' view that caution needs to be exercised.

On the 30th June 2016 the FCA stated that since the launch of Project Innovate, they have received more than 500 requests for support and offered direct support to more than 250 firms who presented innovative ideas; many with a robo-advice model. These companies are not just securing countless column inches, but attracting huge amounts of investment capital on incredibly high valuations.

It has recently been reported[2] that the FCA has given its new robo-advice department a £500,000 budget for its first year. The Advice Unit will provide individual feedback for innovative firms looking for authorisation, and is likely to publish more general guidance and toolkits for firms looking to develop automated advice models.

This robo-advice space was pioneered in the US by companies such as Wealthfront and Betterment, with Betterment hailed as the robo-advice poster-child globally. At present Betterment manages over $4.8bn[3], and recently raised $100m. This fundraising valued the firm at $700m, a valuation of circa 14.6% of the value of its $4.8 bn assets under management.

To put this into context, this is 12x the valuation of the much larger asset manager e.g. Blackrock, that is valued at 1.2% of its assets under management[4]. Blackrock is currently forecast by analysts to make profits of c. $4.6 bn this year, as compared to Betterment that does not appear to be making a profit.

Based on Betterment's current estimated assets under management of $4.8bn and their average account size of $28,571[5] and 0.25% pa fees, this implies $12m pa of revenues. However, one 'fintech grandee' is reported[6] to estimate their total costs at $40m-50m a year.

In the UK, one established UK robo-adviser firms reported costs in its latest available report and accounts, that were 9.4x its revenues. Another new UK robo-adviser firm said following its recent launch: *'I wouldn't expect to be reaching breakeven before we have £2 billion AUM,'… 'We're talking about several years, maybe five or six.'*[7]

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[2] http://citywire.co.uk/new-model-adviser/news/fca-puts-500k-behind-new-robo-advice-unit/a926885?ref=new-model-adviser-todays-news-list

[3] http://uk.reuters.com/article/us-wealth-summit-betterment-idUKKCN0Z02NY

[4] Based on Bloomberg data as at 30th June 2016 of Blackrock Assets Under Management of $4.65 trillion and current market cap of $55.5 billion.

[5] http://uk.reuters.com/article/us-wealth-summit-betterment-idUKKCN0Z02NY

[6] http://www.economist.com/news/finance-and-economics/21677245-growth-firms-selling-computer-generated-financial-advice-slowing-does-not

[7] http://citywire.co.uk/wealth-manager/news/city-grandees-back-ex-goldman-partners-online-wealth-firm/a912815

Robo Business Models – Emperor's New Clothes?

Revenue per account

SCM Direct researched 10 UK 'robo-advisers', and found their average fee excluding VAT for a £25,000 portfolio, where disclosed, was 0.59% pa (the fees ranged from 0.3% pa - 0.94% pa). **The revenues ex. VAT for a £25,000 account based on an average 0.59% ex. VAT is just £147.50 per annum.**

Initial Advertising / Acquisition Costs

As start-ups, most 'robos' do not have brands presence or awareness so require well-funded strategic marketing campaign to attract customers. Many appear to be spending large sums on Google AdWords, which SCM Direct's own experience informs us that even a successful online campaign costs circa £3.15 per click. It has been estimated[8] that the Finance & Insurance sector, has an average conversion rate via Google Display Network of just 1.75%. Thus **the customer acquisition cost is £3.15/0.0175 = £180 per account for this one advertising channel alone.**

This estimate of £180 acquisition cost is probably lower than that faced by many firms since online advertising media rates have risen considerably over the last 12 months. One firm of consultants[9] has shown how much the key Price Per Click (PPC) Costs have risen over recent years for advertisers generally:

Average PPC Costs

Metric	2015	2014	2013
Cost per click (CPC)	$1.58	$1.02	$0.92
Click through rate (CTR)	0.8%	0.9%	0.5%
Conversion rate	3.6%	4.7%	8.8%
Cost per conversion	*$44.50*	*$30.25*	*$10.44*

Source: Hochman Consultants

[8] http://www.wordstream.com/blog/ws/2016/02/29/google-adwords-industry-benchmarks
[9] https://www.hochmanconsultants.com/cost-of-ppc-advertising/

On 31st March 2015, a paper by Morningstar[10] looked at the major publicly traded US retail brokerages, and found that it took approximately $300 (£225) of advertising to attract a new account and $1,000 (£751) to add a net new account after factoring in attrition.

Custody and Administration Costs

SCM Direct has calculated, from the latest report and accounts of four leading UK custody and administration platforms, all of which concentrate on UK financial advisers, that their average operational cost as a proportion of assets is c. 0.29% pa. We have included the net interest income payable/receivable within the overall costs below but have excluded any other operating income within this analysis.

If we use this to model **just the underlying custody and administration related costs of these robo-advisers, even as they become much larger businesses, the estimate is 0.0029*£25,000 = £72.50 per account.**

	Assets Under Management Latest Accounts	**Costs (calculated as Cost of Sales + Admin Expenses + Net Finance Costs) as % Assets Under Management Latest Accounts**
Transact (Integrated Financial Arrangements Ltd)	£19,100m	0.22%
Ascentric (Investment Funds Direct Ltd)	£8,900m	0.27%
Novia Financial	£3,808m	0.35%
Parmenion (Parmenion Capital Partners)	£1,705m	0.30%
Average	**£8,378m**	**0.29%**

Source: Companies House as at 4th July 2016

Other Operational Costs

It is reasonable to expect robo-adviser business models to encompass efficiencies, outside operational custody and administration costs, but this does not appear to be the case.

The robo-adviser business model appears to be employing, pro-rata, more investment management staff for managing investments, more IT staff for managing the algorithms, processes, risk controls, on boarding and money laundering checks, more sales and marketing staff for online marketing or social media, more customer service staff, and more compliance staff than expected - all of whom appear to be highly paid.

[10] http://fsc.org.nz/site/fsc/files/FAAR%202015/Morningstar%20%20Hungry%20Robo-Advisors%20Are%20Eyeing%20Wealth%20Management%20Assets%20We....pdf

For comparison purposes, SCM Direct analysed some of the largest UK quoted fund management groups and platforms. We segmented these into two groups: Group A - the traditional mutual fund groups and, Group B - platform or private client groups.

Group A tends to be far more profitable as the fees are typically higher, and they benefit from the efficiencies of running large unitised funds. Therefore, Group B is a fairer comparison with a typical robo-adviser.

The results are as follows:

Group A	Total Financial Compensation Per Employee	Net Revenue Per Employee	Total Financial Compensation as % Net Revenue	Total Operating Expenses as % Assets Under Management
Schroders PLC	£203,013	£449,884	45%	0.31%
Aberdeen Asset Management PLC	£145,127	£357,362	41%	0.28%
Henderson Group PLC	£273,634	£655,311	42%	0.46%
Jupiter Fund Management PLC	£244,610	£767,752	32%	0.64%
Average of 4 above	£216,622	£557,577	40%	0.43%
Group B				
Rathbone Brothers PLC	£96,714	£240,877	40%	0.55%
Hargreaves Lansdown PLC	£64,038	£333,299	19%	0.33%
Brewin Dolphin Holdings PLC	£60,505	£160,355	38%	0.69%
Average of 3 above	£73,752	£244,844	32%	0.52%
UK Robo Firm Example	**£68,478**	**£17,172**	**399%**	**N/A**

Source: Bloomberg, Companies House as at 4th July 2016

On the average cost base (0.52% of AUM) of Group B, we estimate the average cost of managing a £25,000 investor account is £130 per annum.

(NOTE: this assumption is incredibly generous as most robo-advisers are managing sums overall that are a fraction of the named firms here, and whose cost base is therefore likely to be much more than the 0.52% of AUM assumed).

SCM Direct's Fee Assumptions May Be Far Too Optimistic

Many UK clients have been attracted to new robo-adviser firms via special offers e.g. free management for a certain time period or up to a certain sized account. Such offers have attracted younger or less sophisticated investors, but are they at a significant cost to the businesses?

For example, one firm offers free management up to £10,000 and then charges on a sliding scale from 0.6% pa. A £25,000 account would therefore be charged 0.36% including VAT i.e. just 0.3% net.

The UK Robo-Adviser Financial Model Does Not Compute

In view of the financials above, SCM Direct has made the following assumption of the number of years it would take to receive a return on investment on just the £180 acquisition cost of each client. From our calculations, it would take more than 10 years for these robo-advice companies to break-even, and nearly 11 years to make a profit.

In a best case scenario, even if a robo-adviser managed to achieve a 10% pa investment return whilst keeping growth costs to just 5% pa, it would still take five years to break-even.

The Defunct £25,000 Robo Model

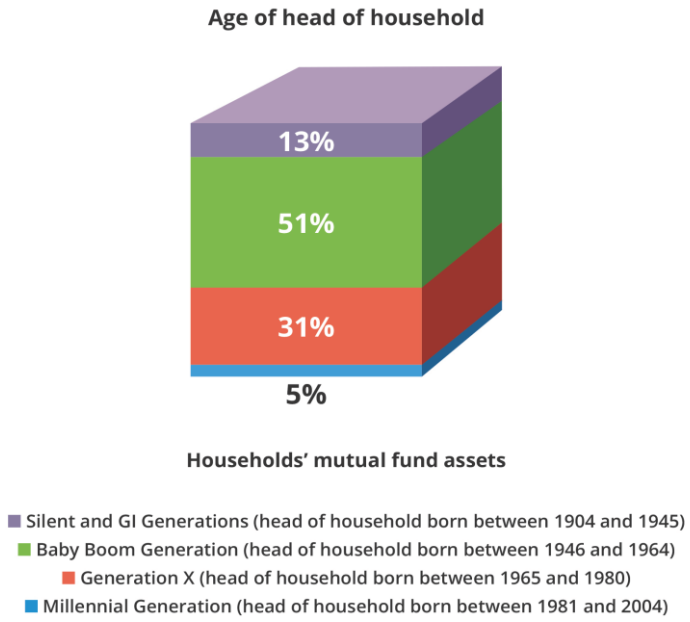
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11
C/F		-£163	-£145	-£128	-£110	-£93	-£75	-£58	-£40	-£23	-£5
Acquisition Cost	-£180										
Annual Revenue	£147.5	£147.5	£147.5	£147.5	£147.5	£147.5	£147.5	£147.5	£147.5	£147.5	£147.5
Ongoing Costs	-£130	-£130	-£130	-£130	-£130	-£130	-£130	-£130	-£130	-£130	-£130
Total B/F	-£163	-£145	-£128	-£110	-£93	-£75	-£58	-£40	-£23	-£5	£13
IRR		-89%	-61%	-41%	-27%	-18%	-11%	-7%	-3%	-1%	1%

Client Retention

Vanguard Group, have reported that their redemption rate is currently close to 40 percent, bringing the average holding period down to about 2.5 years[11]. This is similar to estimates elsewhere in the US of 3.3 years.[12] **Although we were unable to find similar data for UK client retention rates, we believe that the 3-year estimate is a good guide to UK robo advisers, given their younger investor targeting.**

[11] http://wealthmanagement.com/archive/fund-industry-frets-about-shorter-holding-periods
[12] https://blog.folioinvesting.com/2012/05/11/the-most-common-mistake-investors-make/

ICI Research Perspective, "Characteristics of Mutual Fund Investors, 2014"



According to research from the US fund manager, Legg Mason[13], less than 1/5th of age 18 – 35-year-old clients would hold an underperforming fund for more than a year, as compared to almost three times this for investors over the age of 40. Many UK robo advisers are targeting these 'millennials' so the average holding period may well be even less than 3 years.

UK Robo-advisers Not Financially Wired to Target the Mass Market

By targeting investors with very small investment pots, and who are likely to invest for three years or less, UK robo-advisers will be hampered by managing uneconomic accounts. In addition, this client segment tends to be novice investors requiring a higher level of hand holding due to their lower investment experience and younger age profile. This would also impact negatively on the overheads for robo-advisers.

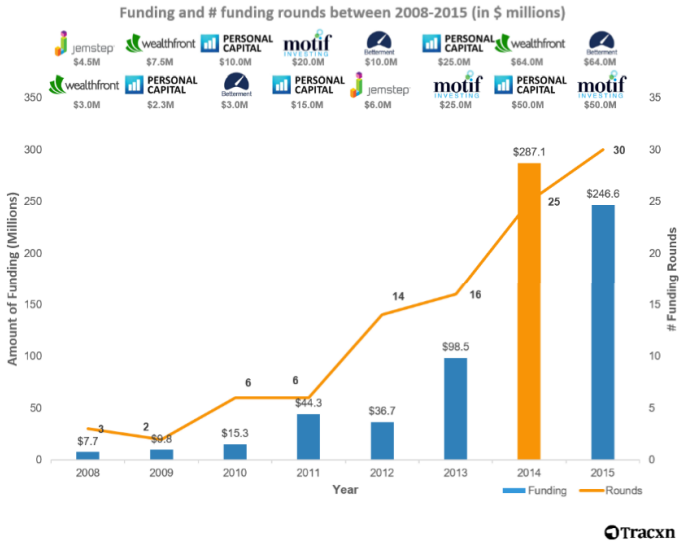
These younger client's investment portfolios often represent a significant amount of their overall wealth (as younger people tend to have less surplus assets). This is substantiated by Betterment's findings in the US where *'About 30 percent of Betterment's clients are in the 35-and-under set known as millennials…On average, those clients have 70 percent of their assets with the firm.'*[14] As naïve investors, they are more prone to sell when faced with losses or scary media headlines, resulting in a behavioural profile that can be more short-termist. It is perfectly understandable that if your investment represents 70% of assets as seems to be the case here, you would be more susceptible to a panic attack when markets fall.

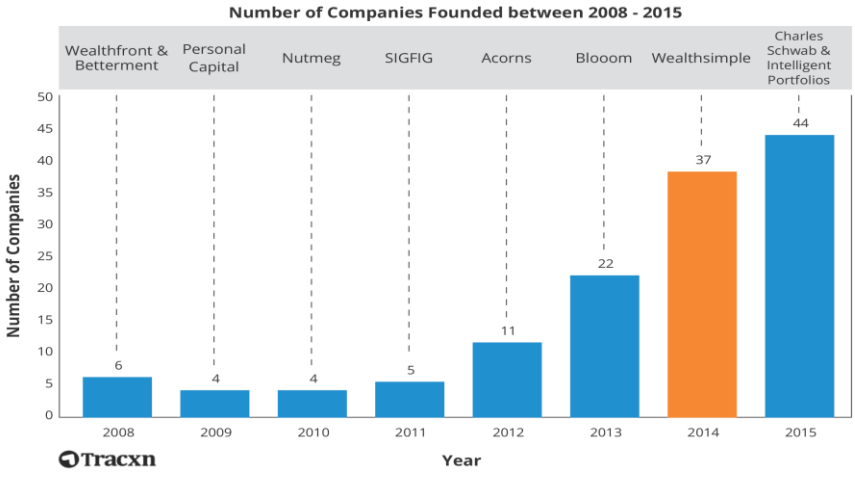
The escalation in robo-advisers all targeting millennials is surprising as this target audience represents just 5% of the overall investment market. Of course they may well have more to invest later in life, but by that life stage many of the current robo-advisers may be bust.

[13] https://next.ft.com/content/ef9e391e-1766-11e6-9d98-00386a18e39d
[14] http://uk.reuters.com/article/us-wealth-summit-betterment-idUKKCN0Z02NY

Fintech Backers Folly - More Money Than Sense

The raft of new robo-advice firms being launched appear to be raising huge sums of money from venture capitalists, private equity and professional private investors. Meanwhile, the existing companies continue to require capital injections to fund their continuing losses.



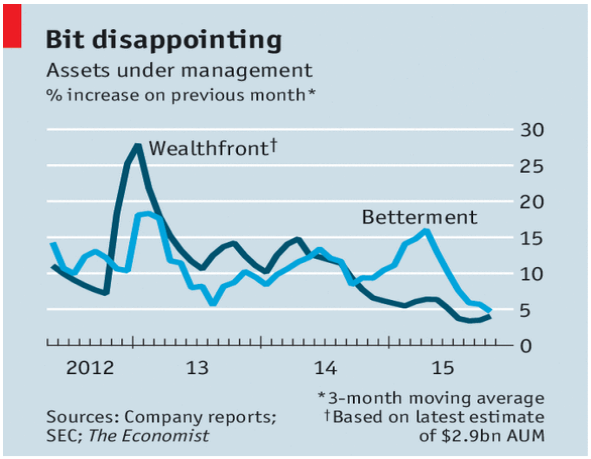


Source: http://blog.tracxn.com/2016/02/11/tracxn-report-robo-advisors/

The only way out of this financial mess for many new robo-advisers is to substantially grow their assets and achieve the necessary economies of scale to attract the next round of investment backers, enticed by the promise that a profitable business is just around the corner.

However, the evidence of growth rates from some of the US largest robo-advisers shows they have fallen to about a third in 2016 compared to the previous year[15], making this prospect even more elusive than usual.

[15] https://www.kitces.com/blog/robo-advisor-growth-rates-and-valuations-crashing-from-high-client-acquisition-costs/



This trend is likely to be replicated in the UK which has seen the 2016 ISA season reported as the worst for decades[16].

It is reasonable to assume that at some point private equity or individual funders of these robo-advisers will run out of patience and stop putting their hands in their pockets if there is no prospect of a return on the horizon.



Investment Expertise - Where are the Fund Managers or Chief Investment Officers?

The selection of the funds within any clients' portfolio is normally controlled by one or two individuals; regardless of quantitative rather than qualitative selection criteria. Even if the investments are based purely on an algorithm, presumably there must be one or two human individuals responsible for ensuring that these algorithms are fit for purpose.

Bearing in mind that many of these companies are in reality, online investment managers rather than robo advisers, we were surprised at how difficult it was to find details of the

[16] http://www.telegraph.co.uk/personal-banking/savings/the-worst-isa-season-ever-savers-told-dont-hold-your-breath-as-r/

person or persons or investment committees responsible for investment decisions. In 40% of the firms analysed (4 out of 10), we could not ascertain from the website, the names or backgrounds of the key investment staff. These companies seem to rely on clients to take a lot on trust in the circumstances.

Regulatory Issues – Significant Potential Liabilities

The UK regulator has seemingly turned a complete blind eye to misleading statements, misleading performance, misleading fees, and a lack of appropriate regulatory permissions of many UK robo-adviser firms. Even if all the 10 firms analysed, were somehow operating from the recently created FCA Regulatory sandbox[17] or Project Innovate, firms are still not allowed to mislead clients or breach existing various FCA rules, designed to protect retail clients.

As a result of the FCA desire to fill the advice gap they appear to be plugging one hole whilst creating an even larger regulatory one. Many of these companies appear to be storing up huge liabilities if down the road either their algorithm fails or markets collapse, leading to customers complaining to the Financial Ombudsmen of bad advice (whether or not these robo advisers believe or not that they have given advice).

Many clients will rightly believe that if a firm recommends investing in Portfolio A rather than Portfolio B, based on questionnaires they completed, they have been given advice.

Should markets fall and a client complains, it may well transpire that an independent adjudicator will judge that the firm did not undertake the appropriate steps for advice in terms of risk profiling, attitude to risk, capacity for loss etc. In some cases, these firms do not even possess the requisite regulatory permissions to give advice in the first place.

In the US, the Massachusetts regulator has recently warned[18] that robo-advisors may not be able to deliver "*appropriate*" investment advice as there is no checking whether the information given by clients via electronic questionnaires is accurate.

The Secretary of State for Massachusetts, said; *"Entities that create computer-generated portfolios but fail to do the necessary due diligence to know their customers and who specifically decline most if not all the fiduciary duty is not performing the duties of investment advisers*"

SCM Direct's research into 10 UK Robo Advisers should prompt the FCA into conducting a thorough review, **before** rather than after the stable horse has departed.

[17] https://www.fca.org.uk/static/documents/regulatory-sandbox.pdf
[18] http://www.reuters.com/article/us-massachussets-regulator-adviser-idUSKCN0WY51P

Performance

Whilst 70% (7 out of 10) legitimately did not show any historic performance record within their sites (as were mostly new companies) one robo-adviser showed performance in a highly questionable format:

One robo-adviser showed performance by converting the returns of its Euro portfolios prior to 2015 into Sterling, even though an employee told us that these Euro portfolios "*are different to the UK ones*" i.e. would not be the same portfolios in which UK investors would be investing.

During the four-year period in which their overall returns were represented by their Euro portfolio returns, Sterling strengthened significantly against the Euro accounting for a significant element of the overall reported return for some of the portfolios. Furthermore, these returns were shown before "*taking account of their fees*" but the impact of such fees on returns, was not shown.

Advice

Can a robo-adviser give advice without regulatory advice permission?

SCM Direct's research found that 80% (8 out of 10) relied on client risk questionnaires to select investments yet 25% (2 out of these 8) of companies using risk questionnaires did not possess regulatory permission to give advice to retail clients.

The issue is not simply whether or not advice was given. There are also significant questions regarding the use of risk tools in this context.

80% (8 out of 10) relied on a risk questionnaire filled out either online or subsequently in order to determine which fund or strategy should be selected.

However, of these 8 companies, 25% (2 out of 8) according to the FCA register, did not have permission to give advice to retail clients. It is our view, that if a site provides a suggested fund or portfolio to a client on the basis of that client's answers to a risk questionnaire, they are giving advice since they must be giving a personal recommendation as it is clearly based on that person's individual circumstances.

Under European rules, personal recommendations are deemed advice[19] – '*MiFID investment advice involves the provision of* ***personal recommendations*** *to a customer'.* A **personal recommendation** is defined by the FCA as '*A recommendation relating to taking certain steps in respect of a particular investment, made to a person in their capacity as an investor or potential investor (or their agent), which is presented as suitable* ***based on a consideration of the person's circumstances***.'

[19] https://www.fca.org.uk/static/documents/guidance-consultations/gc14-03.pdf

In our view, if a 'robo adviser' chooses a strategy based directly on answers to specific personal questions, then surely this must be advice, as it is based '*on your information*' and is being presented as suitable based on your particular circumstances.

Anyway, it is highly debatable as to whether robo-advisers are giving advice in the widest sense that the name 'robo adviser' might suggest. Many do not look in detail at the overall financial attributes and requirements of each client. Many will never ask whether or not a client might have a large commitment next year e.g. daughter's wedding or an illness that might require significant medical bills in the future or even what the other investments are held by the individual. Thus these firms could be considered the worst of all words – they purport to be 'robo advisers' that presumably advise, but then claim in their legal documents they don't give advice, often based on data from clients that is vastly inferior in terms of extent or quality, to that collected by human financial advisers.

Risk Questionnaire Tools

In addition, it is highly questionable whether many of these risk questionnaires are compliant anyway. In 2011, the FCA[20]reviewed 11 risk-profiling tools and found that nine of the eleven tools had weaknesses which could, in certain circumstances, lead to flawed outputs.

Considering some robo sites are employing a shorter version of standard risk questionnaires used by advisers, the chances of these tools being compliant must be even lower. Also, how does the 'robot' check whether the answers are actually correct rather than a client simply ticking the middle option everywhere to get to the end as quickly as possible? There is also the strong possibility of emotional bias or mood when completing online risk questionnaires which should increase, not decrease, the need for human oversight. The adage is: Garbage in, Garbage out.

The US regulators appear to be taking this issue very seriously – the top securities regulator in Massachusetts recently stated that "*fully-automated robo-advisers, as they are typically structured, may be inherently unable to act as fiduciaries and perform the functions of a state-registered investment adviser*" [21] **Massachusetts worries that these questionnaires are filled out electronically but often do not check if the information given is accurate.**

Wider Issue - how do robo-advisors assess their clients' best interests?

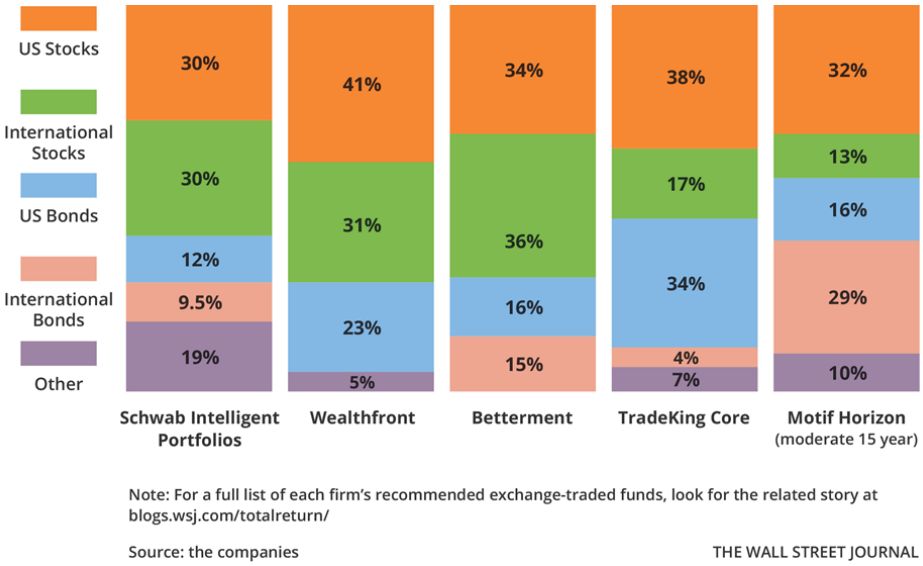
When someone sees a human advisor, they tend to give them other significant unconscious information as a result of body language, facial expressions and tone of voice. A standard online risk questionnaire does not ask whether the user has children or large present or future financial liabilities e.g. medical care etc., that might affect the best choice for the individual.

[20] https://www.fca.org.uk/static/documents/final-guidance/fsa-fg11-05.pdf
[21] http://www.reuters.com/article/us-massachussets-regulator-adviser-idUSKCN0WY51P

The UK Financial Services Panel has rightly pointed out these risks to the FCA[22]:

'*Regulatory scrutiny and assessment of the risk and suitability tools used by automated or 'robo-advice' services will be essential as those services become more widely used by consumers. Tools that are poorly developed and/or monitored have the potential to give rise to widespread systemic mis-selling and therefore further undermine confidence in the sector*.'

A cynic might suggest that risk questionnaires tend to put most investors into the middle option. It is interesting to note how much the asset allocation within five leading US robo-advisers can vary for the same moderate risk profile client:



Fees and Charges – Highly Confusing

One of the most appealing competitor advantages of robo-advisers compared to traditional incumbents is their lower fees. Many claim that their fees are not just low but completely transparent and simple to understand. SCM Direct's review has found that this is not necessarily the case.

Only 30% of the companies reviewed (3 out of 10) added up all their own fees, all the underlying investments costs, and other charges to produce one overall total fee number.

In fact, none of the companies provided any indication of the full underlying transaction costs including the spreads.

Given that most companies utilise ETFs, there is normally a transaction cost even when the firm pays no commission, as there will normally be a spread between the buying and selling price of an ETF. Therefore, a strategy that sells one ETF to buy another will inevitably be incurring 'spread related' dealing costs.

[22] https://www.fs-cp.org.uk/sites/default/files/fscp_response_project_innovate_call_for_input.pdf

One firm stated that transaction or trading or rebalancing fees were '£0' yet unless every single trade is crossed between clients at exactly the middle price rather than a lower bid price or higher offer price, this would seem unlikely.

Other Examples:

- One firm states that it gives '*expert financial advice for just £69'* but this figure related to just the first advice appointment of up to one hour.

  It did not include the cost of further advice that might be agreed with the client or the advice charges or investment related charges in connection with the recommended investments, should the client go ahead. Nowhere on their site could we find what these charges might be. Their site was a trading name of another company which stated on its site that it charged up to 3% initial charges, 0.25%+vat pa ongoing discretionary charges, and 0.7% pa ongoing advisory charges.

- Another firm stated that it had '*no minimum level of investment to open an account…You can start from £1 and top up as much as you want…. Having an amount under £1,000 would mean that the asset allocation of the portfolio will not be balanced and the risk level may not match your investor profile.'* However, its terms and conditions revealed that any initial investment below £1,000 would be held in cash.

- Another firm stated on one page of its site that it charged '*an initial charge of 0.25% to arrange investments*' and 0.75% pa for '*continuing administration and management*'. However, its key facts page stated that the '*on-going charge for yearly reviews*' was 0.5% pa. Its fees page then stated that the ongoing charge, once underlying fund charges of 0.18% pa are included, was 0.93% pa.

- Another firm stated on its fee page that '*We charge a simple annual fee that covers everything. It's never more than 0.7% and can be as low as 0.5%, depending on the value of your Plan(s). So the cost of investing is clear and affordable, with no surprises*.' In a much smaller font, lower down on the same page is then disclosed '*Your money is invested in a number of carefully selected funds, each of which has a small charge, averaging 0.28% a year*.'

Missing Legal Documents and Other Statements

One firm had four downloadable legal documents on its site – Terms of Use, Client agreement, About our Services, and Service levels. As at the 21st June 2016 we found that the Terms of Use agreement contained missing pages, the Client Agreement contained just one out of four pages, and the About our Services document contained just one out of three pages.

One website offering its services for investments of $10,000 or above, was found to only act for those clients that are were either a 'professional client or an Eligible Counterparty'. This was only made clear to investors once they had gone through the on boarding process or read the full Terms and Conditions.

The levels of protection for professional clients differs markedly from retail clients – they are not eligible to seek the services of the FOS and may not be eligible for compensation under the FSCS and will be required to follow different, generally less demanding, rules by the FCA.

Are Robo Advisers 'Robo' at all?

There is little evidence that any of the offerings are purely algorithm driven or offering true financial advice as opposed to investment management, which makes the name 'robo-adviser' not just inappropriate, but misleading.

A review by a well-known consultancy firm[23] stated that the word 'robo' can be defined as "*the software (commonly known as a 'robot') used to capture and interpret existing applications for the purpose of transaction processing, data manipulation and communication across multiple IT systems".*

It then says that robots are typically scalable and 1/9th the cost of a typical UK employee. Yet we could not find any evidence of a robot adviser with lower costs than traditional alternatives, nor even evidence of any "offshoring" to lower costs.

Melanie L. Fein, the former senior counsel to the board of governors of the Federal Reserve, says[24] robos cannot provide fiduciary advice and that advice is best left in the hands of human advisors. "*If a robo advisor cannot perform overall portfolio analysis, it cannot perform a critical function of an investment fiduciary*." The US self-regulatory organisation, FINRA (Financial Industry Regulatory Authority) says that firms employing digital advice need to "*govern and supervise the algorithms they use in digital advice tools*" and "*should also establish governance and supervision structures and processes for the portfolios digital investment tools may present to users*."

[23] http://www2.deloitte.com/uk/en/pages/finance/articles/robots-coming-global-business-services.html
[24] http://www.financial-planning.com/news/no-robos-still-cant-act-as-fiduciaries-attorney-contends

Conclusion

The findings of this review and research report leads SCM Direct to believe that the FCA needs to urgently apply the brakes and systematically review this nascent sector. But instead they announced on 5 July 2016 they are allocating £500,000 to a new robo-advice unit.

Innovation and evolution is vital for any sector to remain competitive and ensure they are offering the best customer outcomes, but it should never be at a medium to longer term cost of the client.

Our conclusion is that there is little evidence of robust innovation, as new robo-advisers appear to be fundamentally financially unviable and/or seem to be regularly flouting key FCA rules.

Is it time for the FCA to step in and protect consumers, and uncharacteristically act before the horse has bolted?

TRUE&FAIR

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Past performance should not be seen as a guide to future returns. The value of investments and the income from them can go down as well as up and investors may not recover the amount of their original investment.