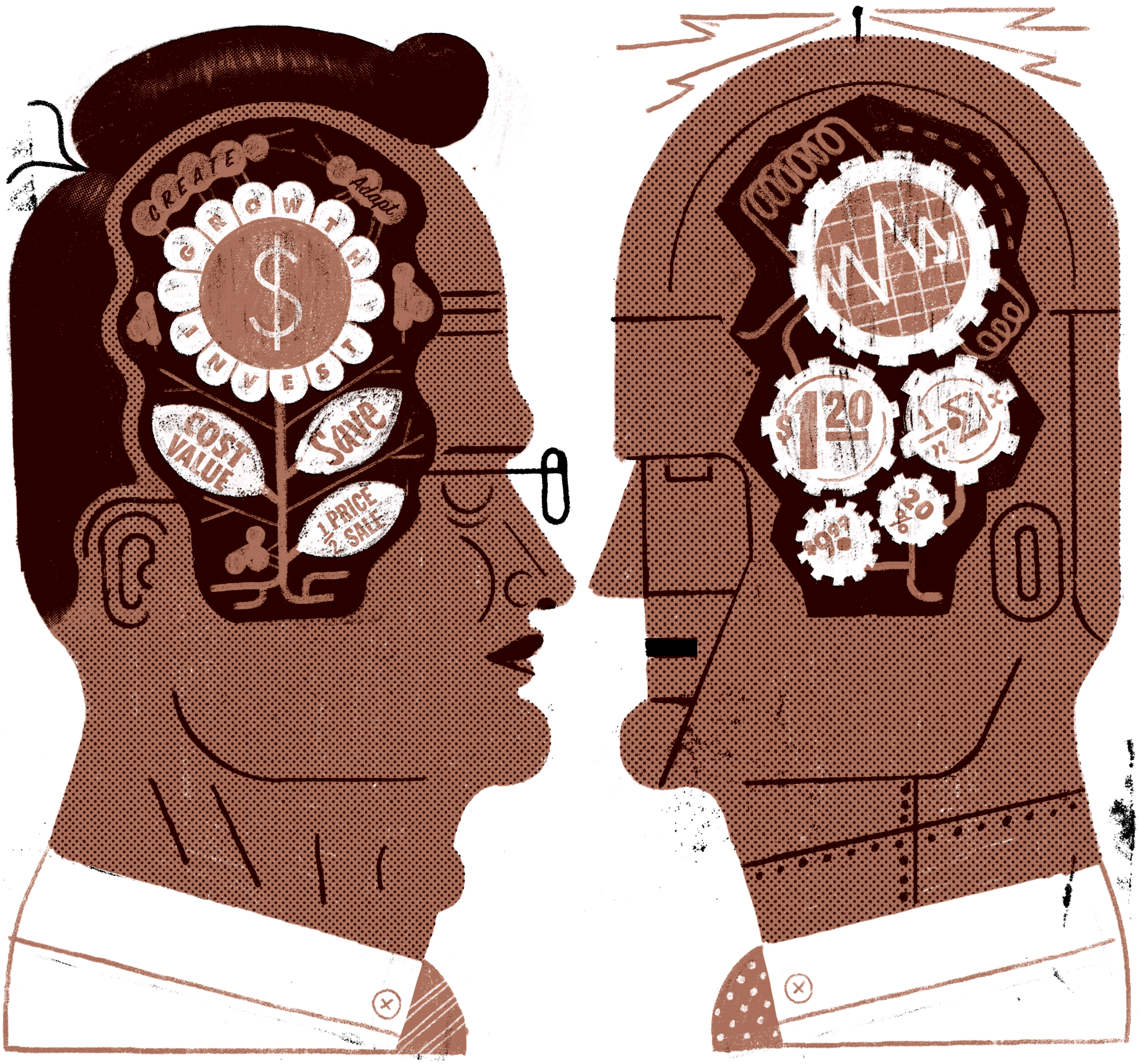
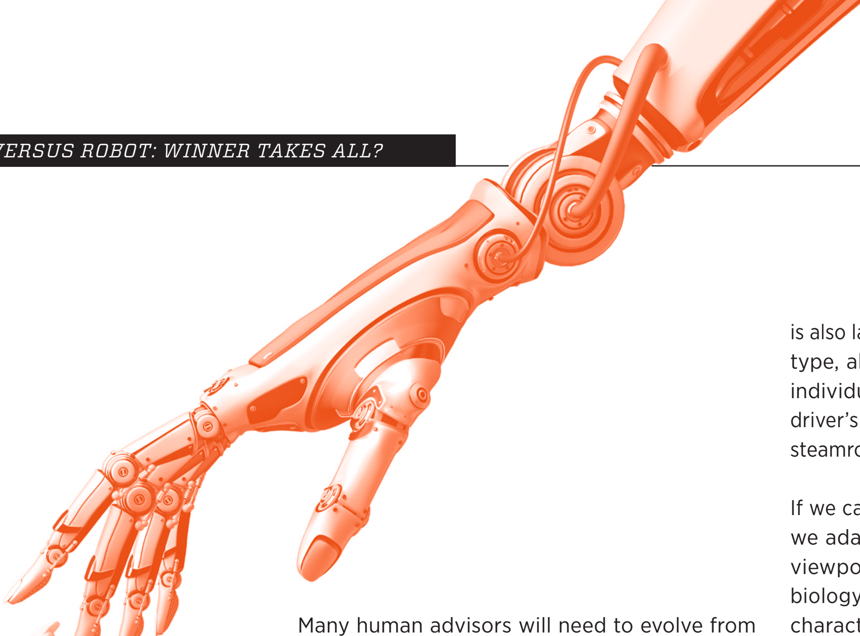


Human Versus Robot: Winner Takes All?

Text by Jesse Mackey

Illustration by Curt Merlo

THERE IS MUCH discussion in the investment management and financial planning world about the disruptive impact of technological advances on the industry and, in particular, the possibility of the "robo-advisor" supplanting human financial advisors as the primary source of financial services clients. Robo-advisor is the term the financial media use to describe an array of digitally-delivered services that leverage technology to potentially automate the bulk of investment advisory service processes for retail investors. In some instances, the fee-based financial planning process is also automated. These services purport to provide a low-cost, technology-dependent approach to personal financial life—early adopters were primarily from the Millennial demographic.



With various permutations of the robo-advisor concept coming first from venture capital-backed independent firms, and now from some of the larger, traditional custodians, the teeming hordes of human financial advisors are left to wonder what the impact will be to their roles and their livelihoods. The feedback from human advisors on this phenomenon range from denial to fear—and advisors have very good reasons to be fearful. Many of the Millennials and some Gen-X investors view the traditional advisor as a "middle man" that can be cut out of the transaction if they go directly to an automated online alternative. Very few human advisors are excited about what they view as a disruption in the accustomed way of doing business. This dynamic needs to change, for the sake of both investors and advisors.

Many human advisors will need to evolve from their traditional business models in order to remain relevant and profitable. An older Baby Boomer generation advisor who intends to retire in the next few years may have the luxury to espouse an attitude of denial about the impending impact robo-advisors could potentially have on their business. However, anyone who wants to remain vital in the industry moving forward will need to avoid falling victim to technological progress, not by fighting it, but in embracing it. The impending battle of human advisors versus robo-advisors in the financial services industry is unlikely to be a winner-take-all event. It is more likely that the future of finance will reflect a merger of the two. By placing emphasis on the uniquely positive aspects of human thought that automation and artificial intelligence cannot provide while simultaneously outsourcing the segments of their work that lend themselves to digital management, advisors effectively become bionic and meld a technological prosthesis to their brain.

Let's take a step back and look at the historical economic relationship between humans and machines; specifically, using the Luddites as an example. Between 1811 and 1816, self-employed English textile workers refused to accept the positive aspects of technology and resisted adapting to a new method of doing business. Ultimately, they became victims of technological progress, despite all government attempts to intervene. This is a lesson in economic history from which we can all learn. The technological juggernaut progresses whether we want it to or not. This is particularly true of capitalist societies, but is also largely true of virtually every other societal type, although perhaps to a lesser degree. An individual may choose to either jump into the driver's seat of the technology steamroller or get steamrolled by it. Sidestepping is not an option.

If we can accept that change is coming, how do we adapt to it? Thinking from an economist's viewpoint can provide answers; evolutionary biology helps, too. One of the most interesting characteristics of the human race is its ability to pre-empt the evolutionary process of natural selection through innovation and creativity. Most members of the animal kingdom need to die, and through a random mutation in their offspring's genetic code, produce a more suitable biology/behavior in order to adapt to changes in their environment. Humans don't have to die to change their behavior. We can innovate and pre-emptively create solutions to anticipated problems. These qualities make us far superior to artificial intelligence.

There are basically four roles that human beings can play as participants in our economy: creator, producer, trader and consumer. Most people embody a little bit of each of these roles during their lifetimes, but will focus on only one of them in their professional life. The angst associated with technological progress is largely due to the fact that computers, robots and artificial intelligence can potentially replace human beings in their performance of these roles. We know that robots can easily replace humans in many aspects of the producer role, as in the example of manufacturing.

The technological juggernaut progresses whether we want it to or not. This is particularly true of capitalist societies, but is also largely true of virtually every other societal type, although perhaps to a lesser degree. An individual may choose to either jump into the driver's seat of the technology steamroller or get steamrolled by it. Sidestepping is not an option.

Jesse Mackey | Syosset, N.Y. | 516.300.1617 | jmackey@4tfg.com

Algorithms and automation can easily replace humans in many aspects of the trader role, like with investment portfolio management or retail sales. Technology can even take on aspects of the consumer role through the material maintenance needs of machinery or the consumption of data by computer programs. The one area where human beings still maintain a major advantage over machine behavior is in the role of the creator. This role may be the most important of all, as it is the progenitor of economic growth and the basis of our success as a species. It can be loosely defined as the generation of ideas, innovation and the original creation of implementable solutions. Even the most advanced forms of artificial intelligence, including those currently under development, are still far behind human beings in this arena. Although it is possible that rapid progress can be made in this area on the part of artificial intelligence, it does not appear feasible that such progress will be enough to overtake the sheer versatility of human thought in the near term, if ever.

Human beings have a comparative advantage over robots in the form of creativity. The basic economic principles outlined by philosopher and political economist Adam Smith say that this task should be allocated to us, while many of the others tasks for the producer, trader and consumer roles may be better allocated to technological automation in order to make our economy more efficient.

A valuable lesson for any career-oriented person in any industry would be to focus on performing the high value-added tasks and developing those creative idea-oriented skills that computers cannot currently perform well. Doing so will likely secure a spot in the global economy, ensuring that you never become an unemployed victim of technological progress. The lesson is to use the technology to automate all menial tasks in order to free up time and resources to support your creative pursuits.

The optimization of human advisors lies in combining the best aspects of human thought with the cutting-edge aspects of technological might. Treat technological advancements as bionic enhancements for your brain, and the potential for longevity of human advisors is assured.

If we apply these sentiments to the financial services industry, it lends itself to a few potential revelations for traditional human advisors who are looking to use their unique abilities and adapt without becoming redundant. Here are a few ways traditional financial advisors can enact pre-emptive evolution:

Don't spend a lot of your time (or your employees' time) doing things that a computer can do faster, cheaper and better. For example, many tasks of Modern Portfolio Theory-based portfolio management can be automated.

Do not base your fees purely on assets under management (AUM), unless you can prove to your clients over time that you are providing enough value through your contribution to the portfolio management process to justify those fees; such fees are likely to be much higher than the fees charged by a robo-advisor. If your fees are AUM-based and higher than a robo-advisor's fees, you will need to do something unique enough that a robo-advisor cannot do—and you have to do it well—in order to charge a premium.

Focus on providing high-value services that a computer cannot do well, such as analyzing and providing highly tailored recommendations on issues related to complex financial planning and wealth management topics. Estate planning, succession planning, employer/employee benefits and creative investment planning are excellent examples.

Charge directly for the services you provide. If you are providing advice on complex issues related to comprehensive financial planning on an ongoing basis, charge a monthly or quarterly retainer financial planning fee instead of trying to get paid by elevating your fee on AUM. This will clarify what you can do for your clients that a robo-advisor cannot.