How Fools Can Play the Robo-Advisor Revolution Indirectly

Description

Like Bitcoin, robo-advisors are one of those topics that just don't seem to be going away any time soon. However, here at the Motley Fool, our focus is on neither of these hot topics. As for the former, can you say, "The train has left the station"? And as for the latter, we note that robo-advisors are really two steps removed from our preferred approach of identifying quality individual stocks and profiting from them.

But that doesn't mean we can't profit from robo-advisors, even if we don't plan to invest directly in one of their services.

Let me explain by elaborating on those two steps. The first is that robo-advisors are almost all packages of exchange-traded funds (ETFs), which generally invest in both the good and the bad in the chosen subsector of the stock market. And the second is that robo-advisors in turn package up multiple ETFs, both equity and fixed-income ETFs, in various combinations appropriate for a particular investor's investment objectives and risk tolerance.

Of course, you'll be paying a fee for the privilege—generally about 50 basis points (0.5%), PLUS the underlying fees of the component ETFs. (NestWeath.com is an exception, since it uses a monthly subscription model, as we've said in a previous blog here).

That said, even Fools need to pay some attention to what is going on in the robo space, because in Canada alone, the big guys are starting to enter this space in a large way, including at least two Canadian banks (**BMO** and recently **Royal Bank**), and giants of the mutual fund industry, notably **Invesco**.

Note that, as in the case of the above-named two banks, many of these new entrants are themselves publicly traded. So, just as shrewd investors sometimes eschew retail mutual funds but instead buy the stocks of the publicly traded fund companies (e.g., Mackenzie Financial or CI Funds), so too might investors want to buy the companies that plan to prosper by joining the robo bandwagon.

If you believe the combination of ETFs and robo-advisors are themselves a threat to the entrenched mutual fund industry, consider that the big fund companies themselves seem to be hedging their bets by jumping into the robo space themselves. Exhibit A is Invesco Canada Ltd., which, in November, became roughly the 15th robo operation to launch in Canada from a standing start for the industry just five years ago.

Invesco has dubbed its new platform advisorDUO. That name reflects its novel status as a service that's being rolled out exclusively to mutual fund dealers: individual do-it-yourself investors need not apply. At least seven fund companies have signed up so far.

advisorDUO provides exposure to ETFs but does so via a "fund of fund" approach, with five Invesco Target Risk Portfolios that hold both Invesco's own PowerShares ETFs as well as the ETF companies that show up in almost all robo platforms: Vanguard Canada and BlackRock Canada. Annual charges for fee-based accounts are between 0.41% and 0.51%, while the Advisor series tack on another 1% for a total range of 1.41-1.51%, which includes the underlying ETF fees. It's a bit cheaper than retail mutual funds, but not a lot!

Moving on to the big banks. Until recently, BMO ETFs was the dominant ETF player among Canadian banks. After testing the waters with its robust suite of BMO ETFs (including several innovative equal-weighted ETFs), in 2016 BMO launched its own robo service that invests in those same inhouse ETFs; it's called SmartFolio.

In mid-November, rival **Royal Bank of Canada** announced plans to launch its own robo service using its inhouse ETFs managed by RBC Global Asset Management. While it's still being pilot-tested, it may end up being called RBC InvestEase.

It's safe to say most other Canadian banks are looking at joining them, and Fools should keep in mind that most of them are publicly traded. You can expect some of the domestic robo start-ups to be acquisition targets from these bigger financial fish. For example, in the first half of the year, **National Bank of Canada** invested $6 million in one of the first robo-advisors to set up shop here: the aforementioned NestWealth.com. Another, WealthSimple, has declined to comment on a possible courtship with **CIBC**. Earlier this year, **Power Financial Corp.** raised its ownership in WealthSimple to $100 million, following its initial stake made in 2015. As with Invesco, this seems to be Power's hedge on its ownership of such mutual fund companies as Mackenzie and Investors Group Inc., both also publicly traded on the TSX.

Power Corporation of Canada (TSX:POW) is, of course, itself publicly traded. So, as with the banks, this is one way Foolish do-it-yourself investors can jump on the robo bandwagon without having to pay fees.

But if you don't mind reasonable fees and want a diversified way to play the Canadian financial sector (and hence robo-advisors indirectly), consider an ETF I've long owned: the **iShares S&P/TSX Capped Financials Index ETF** (TSX:XFN). Launched way back in 2001 and now with more than $1 billion in assets, XFN owns 27 securities, including all the banks, some fund companies, and the major insurance companies. The MER is 0.61%.

Not all the underlying stocks will be robo plays, but you surely will be participating indirectly and won't have to feel the robo revolution is passing you by completely, which is more than I can say for Bitcoin!

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TICKERS GLOBAL

1. TSX:POW (Power Corporation of Canada)
2. TSX:XFN (iShares S&P/TSX Capped Financials Index ETF)

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Date
2025/07/21
Date Created
2017/12/01
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