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# Will neobank disruptors face the same fate as their predecessors in wealth management?

Article

**What we're thinking:** Looking back at the disruptors from a decade ago and where they are now might help us understand what to expect in the future, per CNBC.

**The original disruptors:** Ten years ago, the idea of handling financial and investment affairs completely online was nearly unheard of. But then a revolution happened within the wealth management space—the creation of all-digital robo-advisors and investment platforms.

- **Wealthfront**, an automated investment platform founded in 2008, attracted clients from NFL teams and Big Tech firm Facebook, boasting $1.3 billion in assets under management (AUM) in the early days.
- **Robinhood**, which offered the first commission-free trading platform for stocks and ETFs, was founded in 2013.
- **Personal Capital**, an online financial advisor and personal wealth management company, was founded in 2009.

Although these startups were innovative, they couldn't outcompete the larger incumbents, which were able to co-opt the technology, and also do it on a much bigger scale and more cost-effectively.

- Wealthfront grew to $27 billion AUM before it was **purchased by UBS earlier this year**. Its scale was impressive, but was no match for large investment firms such as **Vanguard** with $200 billion AUM and **Schwab** with $60 billion AUM.
- Robinhood's commission-free business model was quickly replicated by Vanguard, **Fidelity**, and Schwab. Robinhood is now trading at **89% below its highest valuation**.
- Personal Capital was ultimately **sold to Empower Financial in 2020.**

**Today's disruptors:** Those wealth management startups look similar to another group of major disruptors: neobanks, which similarly have been pushing digital banking to the next level. Still, incumbent banks aren't far behind. **Goldman Sachs** offers digital bank **Marcus** and **JPMorgan** offers digital bank **Chase.** But neobanks' efforts to scale and the cost of scaling differ from the effort and cost for incumbents.

- Neobanks are struggling to reach profitability, with less than 5% of them breaking even, per Simon-Kucher & Partners. And as they struggle with profitability, they continue to focus on customer acquisition through the purchase of social clubs and media companies. But their customer acquisition costs may make profitability impossible.
- Conversely, JPMorgan's CEO told shareholders earlier this year that the bank's You Invest platform had reached $55 billion in assets "without us doing virtually anything," per CNBC.

**Venture funding cools:** Neobanks now face an additional challenge. After last year's funding boom, venture capitalists are putting the heat on them.

- Funding has dropped off significantly in 2022, and CB Insights expects a **28% drop in fintech funding** in Q2 2022.
- Major investment capital fund managers, such as Ben Horowitz, founding partner of **Andreessen Horowitz,** are now meeting with startup companies before investing. The managers are reviewing how the startup companies spent their money over the past two years, and want the companies to offer truly differentiated products.

Startup valuations are also down. Neobanks that were looking to go public may end up putting that plan on the back burner until the markets rebound.

**The big takeaway:** Neobanks must spend their money prudently to make it through tougher times. They need new products that will help them to stand out in a saturated market. We expect them to challenge incumbent banks on more niche offerings and personalization. Neobanks that are running out of money and lack differentiation need to consider stronger partnerships. Or, with their valuations lower than ever, getting bought out by a midsize or large bank with plentiful resources might not be such a bad prospect.

**Types of Wealth Management Providers Used by Investors Worldwide, 2021 & 2024**

*% of respondents and % change*

| | 2021 | 2024 | % change |
|---|---|---|---|
| Fund manager | 38.5% | 36.9% | -4.2% |
| Full-service institution | 36.2% | 37.1% | 2.4% |
| Brokerage firm | 33.7% | 33.0% | 1.9% |
| Retail bank | 25.2% | 22.5% | -10.4% |
| Private bank | 20.1% | 21.1% | 5.2% |
| Fintech (e.g., robo-advisor, neobank) | 8.3% | 14.5% | 73.8% |
| Independent financial advisor | 7.8% | 8.9% | 14.3% |
| Family office | 5.6% | 6.2% | 10.4% |

*Source: EY, "Where Will Wealth Take Clients Next?: 2021 EY Global Wealth Research Report," April 22, 2021*

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