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Investing Doesn't Have to Be Intimidating: Every Pro (and Con) of Robo-Advisors

You don't need a lot of time, money or a degree in finance to start investing. Robo-advisors can help you invest and chill.

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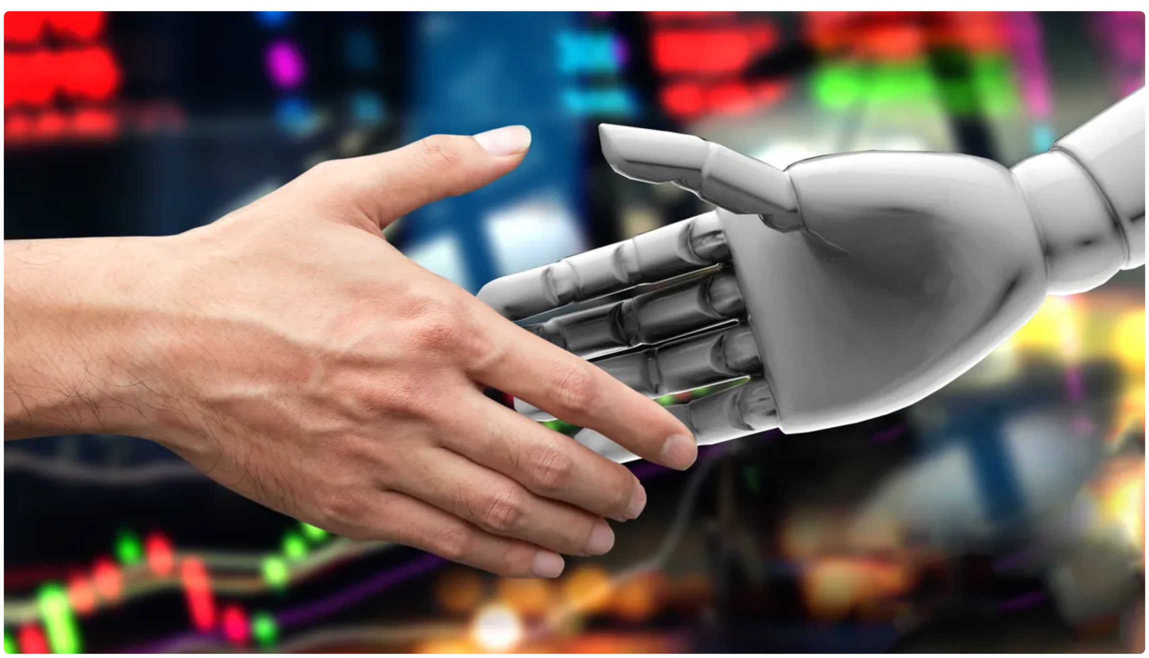

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Beginning your investing journey can be daunting. How do you invest

Beginning your investing journey can be daunting. How do you invest in stocks? What about cryptocurrency? Do you need a lot of money to start? There are mountains of financial literature answering these questions and more, but it can still be difficult to know where to start and which stock and securities are worth investing in. There's one beginner-friendly option that'll do the heavy lifting for you: a robo-advisor.

These automated financial advisors are driven by AI and programmed to put your money to work. The best part is that you don't need large sums of money, investing know-how or large amounts of time. All you need to sign up is to answer some questions about your investing goals and meet the account minimum (if at all), and boom, you'll be well on your way to investing.

Here's everything you need to know about these automated investing services and what you should consider when picking one.

What is a robo-advisor?

A robo-advisor is an automated financial advisor and investment platform. The system uses a software algorithm to build and manage your portfolio so you don't have to. When you sign up for a robo-advisor, you'll answer a few questions, such as:

- How old are you?
- When do you plan to retire?
- What type of investor are you (conservative versus aggressive)?
- What are your investing goals?
- Do you want to invest to retire, generate income, create wealth or save up for a major purchase?

Robo-advisors use automation and software to craft and manage your portfolio, instead of a financial expert.

While some robo-advisors have minimum account requirements to start, it's usually a low barrier to meet. For instance, you might only need $500 to get started. Others don't have an account minimum, which means you can start investing with just a few extra dollars in your bank account.

Read more: Investing for Beginners: Everything Experts Want You to Know for 2022

What's the difference between a robo-advisor and a traditional brokerage?

A brokerage account is a place for you to manage your investments yourself. Robo-advisors let a computer manage it for you based on your style and preferences. Most robo-advisors usually charge a low, flat fee, around 0.25% a year on your total investments. Online brokerages tend to charge more or higher fees.

Robo-advisors are great for hands-off investing. They use your personal choices and investing approach -- including your risk tolerance -- to select how to invest your money and then manage it for you.

These services also offer automatic rebalancing, which means the robo-advisor buys or sells assets in your portfolio to maintain the desired level of asset allocation or risk. Some robo-advisors also perform tax-loss harvesting. That means they'll drop securities that aren't working their hardest for you by decreasing tax liability, and the money kept from paying less taxes will go toward your investments instead.

Read more: 5 Investment Accounts Everyone Should Have

What do robo-advisors invest in?

Robo-advisors tend to invest in index funds and exchange-traded funds (ETFs) to keep costs low.

Index funds are investment funds that track the performance of a set market benchmark (e.g., index), such as the Standard & Poor's 500 Index. Essentially, it's a form of passive investing since your funds follow a preset formula for investing. Index funds come in the form of mutual funds and ETFs, the latter being a basket of securities -- including stocks, commodities, bonds or a mixture of these -- that follow an index, sector, commodity or other asset. ETFs are vastly the most common investment vehicle for robo-advisors.

Brokerages let you actively pick between different types of securities, but you'll have to pay a little more for the privilege. Plus, you'd need to be more hands-on with your assets, including determining and managing the securities you'd like to invest in.

Read more: What Does It Even Mean to Build Wealth in 2022?

Pros and cons of robo-advisors

If you know managing your money is important but aren't sure where to start, a robo-advisor is a good introduction to investing. But they're not always the best choice for everyone.

Pros:

- **Save time.** Robo-advisors put your money to work without your hands on the wheel. These services save you from needing to sift through online investing advice, and ultimately save you time by managing your investments for you.
- **Instant diversification.** While brokerage accounts let you select your own stocks and other securities, there's a chance you could get too much of a good thing -- which means you could also face a huge loss. Robo-advisors diversify your portfolio through index funds and ETFs so that in case you do have a loss, it's not significant. Thanks to rebalancing and tax-loss harvesting, you'll also drop investments that aren't doing well.
- **Minimum investing requirements.** Depending on the robo-advisor you choose, you might not have an account minimum to get started. If you do need something to get started, it's usually around $500 (though it varies).
- **Low fees.** Since robo-advisors use fewer humans than brokerage firms, they can charge lower fees.
- **Easy to use.** Most robo-advisors have simple interfaces and apps to look at your investments and add funds.
- **Socially responsible investing.** Some robo-advisors allow you to choose investments that align with your values without charging a premium.

Cons:

- **Limited human interaction.** While robo-advisors have solid customer service, you're limited in the help you receive. You don't always get a chance for expert advice. If a robo-advisor does offer the chance to talk to a financial professional, it tends to come with an extra cost. Most robo-advisors are online-only, which means you don't have the option to visit a branch if you need to talk to someone about your account.
- **Few securities.** If you're looking to broaden your investment choices, you might not have it with a robo-advisor. Most of them invest your money in ETFs, which is great for diversification. But if you're looking to get into different kinds of securities, you might want to look elsewhere. Moreover, some robo-advisors have a limited number of ETFs they invest in. For example, Vanguard Digital Advisor only invests in four Vanguard ETFs.
- **Not great for everyone.** Robo-advisors are a good choice for most people, but not always the right choice for everyone. Depending on your investment strategy, your risk tolerance, retirement plan, assets and where you want your money to go, it might not work for you.

Where to get started

As you're browsing through robo-advisors to start investing, ask yourself a few questions before deciding.

- **What are the minimum requirements?** Do you need to make a large contribution to get started or maintain a minimum account balance? The lower the threshold to qualify, the easier it'll be to get started.
- **What are the fees like?** Some firms have a flat annual fee, but do the math: A 0.25% fee looks a lot different for a $10,000 investment compared with $100,000. Make sure you're OK with what you're forking over.
- **What features are included?** While many robo-advisors include automatic rebalancing, not all do, and this is certainly a feature worth having. Moreover, not all robo-advisors include tax-loss harvesting, a great perk from any robo-advisor. Not only would tax-loss harvesting save you money, but it alone could cover the fees associated with some robo-advisors. For example, Wealthfront states that 96% of their customers more than wipe out the 0.25% fee with the money earned from tax-loss harvesting.
- **Are other perks included?** Some robo-advisors include extra perks as part of their service. For example, SoFi offers career coaching to all its members at no additional cost. Ellevest also offers career coaching and online workshops at an additional cost, but members on the most basic plan will get 20% off one-on-one coaching
- **Do you have a chance to talk to a human?** Many advisors select portfolios based on answers from a set questionnaire, but other circumstances could influence how you invest your money. If you need to talk to someone about your unique situation, does your potential robo-advisor offer personal financial advice?

There are some leading robo-advisors in the game, but not all of them have the same requirements and offers. Here are a few.

- Ellevest: No account minimum. Monthly membership fees ranges from $1 to $9. Specifically designed for women.
- Wealthfront: $500 account minimum. 0.25% annual fee. Great for most investors.
- Betterment: No account minimum. 0.25% annual fee. Opportunity for professional financial advice for an extra cost.
- Ally: $100 account minimum. No fees. Good for current Ally customers, pulling your banking and investing under one roof.
- Acorns: No account minimum. $1-$3 per month to use. Invests your spare change.

Regardless of which robo-advisor you choose, it should be easy to get started and maintain an investment portfolio. Just be sure to do your homework first to determine the fees you'll be paying and find the best robo-advisor to help you reach your investment goals.

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