Free products and services win customers, paid ones help sellers monetise

Try to save cost on mode of investing, but it is usually not wise to scrimp on the cost of advice

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Today, a host of providers of financial products and services advertise their “free” offerings. Since they are commercial enterprises, the question that arises is: How do they make money? And further, as a user of their product or service, what are some of the things customers need to watch out for?

The reality is that most sellers follow a mixed model. Some of their products and services are free. They charge their customers for others. The free products and services are meant to attract customers and retain them. As people get accustomed to using their products and services, the hope is that they will use the same platform to buy other products and services on which they will pay a fee. “The business model usually is to transition customers from the segments where they don't pay to those where they pay,” says Vishal Dhawan, chief financial planner, Plan Ahead Wealth Advisors.

Even if only a small percentage of customers graduate to paid products and services, that may be sufficient for the business to be profitable.

Broking-cum-mutual fund platforms

India’s leading broker today is Zerodha. It charges zero brokerage for stocks purchased on delivery basis. Customers also don’t have to pay anything for the direct plans of mutual funds that they purchase from their platform. However, if a customer does intraday trade in equity, currency, or commodity, or in futures and options, Zerodha charges Rs 20 or 0.03 per cent (whichever is lower) per executed order. Many other discounts brokers follow a similar model.

For such platforms, the traders provide the bulk of revenue.

Many mutual fund platforms today (like Groww, Paytm Money, ETMoney) offer direct plans on which they make no money. “These platforms treat mutual funds as a loss leader. A loss leader is a product that you give away for free, or at a very low cost. It allows them to do customer acquisition. And they hope these customers will buy other products from their platform,” says Srikanth Meenakshi, founding partner & head, platform and technologies, PrimeInvestor.in.Some of these platforms offer robo advisory which they charge for. Some offer loans and insurance on which they earn a commission.

Real estate broking

In real estate, Nobroker.in is a player that has eliminated the broker from real estate transactions. Its basic services are free of cost. “You can post the details of your property for buying, selling, or renting. Property buyers can get in touch with sellers, tenants with landlords, directly without going through an intermediary,” says Amit Agarwal, chief executive officer and co-founder, NoBroker.in.

The way NoBroker.in monetises its venture is that if a customer needs value-added services, such as a phone relationship manager, or some other service, she pays for it. These charges vary from Rs. 1,000 to Rs. 4,000, with Rs. 2,500-3,000 being the average amount.The phone relationship manager arranges the tenant’s meetings with prospective landlords. As soon as a property matching a buyer’s specification gets listed, the latter is informed about it in real time. Owners who pay can their get property listed in a more prominent slot.Nobroker.in also offers services like documentation and registration for a fee.

Loans

If you are looking for a loan, one player that offers advice to retail borrowers is Andromeda. It offers advice on home loans, personal loans, vehicle finance, working capital loans, and overdraft facilities. It has tie-ups with over 70 pan-India lenders and over 25,000 agents (who guide customers). “We help customers borrow at the lowest possible cost without charging them any fee,” says V Swaminathan, executive chairman, Andromeda and Apnapaisa.It monetises its services by charging lenders a fee for the loans the platform facilitates.

Buy now pay later

Buy now pay later (BNPL) is another service that has caught shoppers' attention in a big way because of its promise to offer them something for free.Let us examine two of the most popular models of BNPL. The first is BNPL at the check-out point or point of sale.In this model, you need to go to a lender and obtain a credit limit from it. At the check-out stage of shopping, you will be offered various payment options.

BNPL will be one of them. If you choose BNPL, you get a zero-interest period that can vary from 15 to 30 days. You can make a one-shot payment at the end of this period. You can also convert your payments into equated monthly instalments (EMIs).Sometimes, if you are not able to pay at the end of the interest-free period, it is possible to convert the one-shot payment into EMIs at this later date.The second is a pure EMI-based model. Here the ticket size tends to be high, so the buyer usually prefers to pay in EMIs.

The cost is zero for the customer. "Usually, the original equipment manufacturer (OEM) or the merchant passes on the discount on the product to the lender. This discount substitutes for the interest that the lender would have earned," says Yashoraj Tyagi, chief business officer and chief technology officer, CASHe.

In other words, the discount the buyer would have enjoyed if she had paid the cost upfront goes to the lender as interest payment.Manufacturers are willing to pay BNPL providers because the latter help them access customers whom they would not have been able to, if BNPL was not available.In the first model, if the customer is not able to pay the cost of purchase on time, he pays interest, which could be as high as 0-26 per cent annualised. Similar penal interest rates will also apply to customers who fail to pay the EMIs on time.

"Your credit score will also be impacted if you don't repay on time," says Dhawan. If you have a low credit score or insufficient credit history due to which you are unable to get a credit card, BNPL may be the right option for you. "The model is similar to that of a credit card, but excessive documentation is not required," says Mahesh Shukla, founder and CEO, Payme India.

What should customers do?

As far as investing is concerned, investors must focus on cost savings. They should go with discount brokers or invest in direct plans of mutual funds, where they don't pay any distribution commission.

"The mechanism of investing is the smaller, more commoditised part. The second, more important, part is which products they invest in. Unless they are highly proficient, investors should not try to save cost on portfolio construction and selection of investment instruments," says Meenakshi.In case of brokers, avoid keeping excess money in your trading account over and above what you need. The interest that the money earns for you in a fixed deposit will instead go to your broker.

When availing any of these free products or services, give primacy to whether it is suited to you. "Don't avail of any product or service just because it is free or low-cost, unless it is right for you. The core proposition being offered must be relevant to you, before you start thinking about whether it's a good deal," says Dhawan. Intraday trading in stocks or trading in futures and options is risky and can cause large losses due to the element of leverage.

"There is also the risk of getting addicted to such high-risk trading as it offers a similar adrenaline or dopamine rush as gambling," says Avinash Luthria, a Sebi-registered investment advisor and founder, Fiduciaries.Luthria adds that in the financial world, a higher-cost product is often not better than a lower-cost product. The former just tend to be hard-sold more because they offer higher commissions to intermediaries. On the other hand, investors need to reach out themselves for lower-cost products based on their own knowledge, or based on good advice.

Save on mode of investing, pay for advice

- Some discount brokers charge zero fee on delivery-based purchases of equities
- Many mutual fund platforms offer direct plans on which they earn zero commission
- However, most of them also have offerings on which they earn commissions or other forms of revenue
- They hope that customers will graduate from their free products to the paid ones
- While the cost of product is important, what is even more important is that the product is right for you
- What you save by investing via discount brokers or direct plans of mutual funds should be channeled into paying for good advice, so that you only pick products that are suited to your needs and risk appetite