IJCRT.ORG ISSN : 2320-2882

INTERNATIONAL JOURNAL OF CREATIVE RESEARCH THOUGHTS (IJCRT)

An International Open Access, Peer-reviewed, Refereed Journal

"Smart Wealth: An Integrated AI Framework for Predictive Portfolio Management"

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Abstract – The existing conventional financial advice, based on traditional models, is not only liable to various biases but also not capable of dealing with the high degree of volatility of the Indian Market. The aim and objective of conducting this study are to bridge the gap between the existing shortcomings through developing an innovative web-based AI-Driven Portfolio Management & Advisory System for adaptive and complaint financial advice on each and every financial product listed on the exchanges of India, such as stocks, mutual funds, bonds, etc. The approach undertaken involves using a powerful multi-layered mechanism, such as reinforcement learning algorithms for adaptive portfolio allocation, NLP algorithms for incorporation of market sentiments, quant-based algorithms such as Monte Carlo and quant for risk analysis. The approach for ensuring effectiveness also incorporates Edi, which is based on strong principle for ensuring security and standardized compliances. Through simulation, its effectiveness is also reflected, showing better risk management capabilities for the entire portfolio by delivering stronger Sharpe ratio values, i.e., 1.50, along with reduced maximum drawdown risk, i.e., only 8%, compared to benchmark Nifty-50, where the Sharpe ratio is only 0.70 along with MDD risk of 15%.

Keywords — AI Advisory, Black-Litterman, EDI, India Market, Monte Carlo Simulation, Portfolio Management, Reinforcement Learning, SEBI Compliance

I. INTRODUCTION

This is a world that is very different from the traditional one when it comes to financial systems and is maintained and run through the use of Artificial Intelligence and other more modern financial technologies; it is a literal end of days for the previous supremacy of traditional investment advice systems. Modern investment portfolios and management have traditionally been based purely upon the indicatives of the Modern Portfolio Theory [1] and human intuition, which is inherently biased and unable to keep pace with the high-speed volatility of the Indian market. This article presents a breakthrough innovation of an AI- based Portfolio Management and Advisory System. It is a personal, web-based platform developed by considering the needs of individual investors in India. Our mission is to provide sophisticated investment advice through the wide range of possible investment products such as stocks, mutual funds, ETFs and bonds. The intelligence of the System will be based on powerful, multidimensional analytical engines. Custom Profiling: To begin, a customer must be known. Capital, risk level, and investment time will all be a meaningful characteristic when making their exact profile by means of capital and risk to form either a conservative, balanced, or aggressive investment profile. Advanced Market Research: Our system uses up-to-date technology and advances to generate market averages no longer based solely on historic averages and historical data, thus giving us access to new technology such as Reinforcement Learning, which provides the functionality needed to rebalance the investor's portfolio dynamically; Natural Language Processing utilizes real-time knowledge of investor sentiment—such as what has happened with affected sectors each time an event occurs. Quantitative Models have been used by financial institutions, i.e. Monte Carlo Simulation and The Black-Litterman Model, etc., have been implemented to assist in managing risk on a large scale as well as creating basic investment strategies. Actionable insights include the execution of this complex output into a simplistic, yet actionable piece of advice, like granular investment allocations, auto-generated growth projections, and overall risk analysis, yet easy, intuitive, and interactive.

This project is about making complex financial models simple so that people can easily understand and follow investment advice. It uses models like Monte Carlo Simulation and the Black-Litterman Model to help users know where to put their

money what kind of returns they can. How much risk is involved.
The platform is built on a framework that follows important rules, for handling data keeping it private and secure and making sure everything is checked and recorded properly to meet regulatory requirements and make users feel confident. The research includes looking at what others have done finding gaps designing the system testing it and sharing the results and ideas for research.

II. LITERATURE REVIEW

During this process, the landscape of the financial advisory system splits in half between methodologies that are decades old and recent but still incomplete advancements in AI. To justify our system, we need to first provide limitations within the current state of the art.

A. Why Traditional Models Fall Short

The bottom line is that the motherhood of investment, the MPT model, and its sister model, CAPM, were formulated in a pre-complex time. Intrinsic in their necessities is the use of a normal distribution return methodology strongly connected with static historic data, making these models highly inept in modern market dynamics. The nature of these models is inherently static, which always has fixed ratios of assets that require manual intervention strongly coupled with an absence of any form of resilience to market disruptions or nonlinear relationships. This lack of resilience is highly observed in the high-frequency character of volatility observed in the Indian market. Even modern robo-advisory models do not come out well on these points in that their nature is usually upon der Rick applied from simple risk surveys.

B. The Leap to Adaptive AI Systems

In order to deliver dynamic performance, there has been interest among researchers regarding Deep Learning. Two of these powerful architectures are Long Short-Term Memory (LSTM) networks [3], and the Transformer family of models [13], which is best at capturing the patterns of time series data for short-term price forecasting. However, here is where most of the useful application of prediction-based AI formalistically ends. The machines can only be used to predict a variable (which is the price), and not even for optimal action policies over a given sequence of market states.

Which, of course, leads us neatly on to its natural successor that is both needed and required, that is, Reinforcement Learning, or RL, for short [2]. For by defining the investment problem as being a MDP, RL algorithms, such as Proximal Policy Optimization, or PPO, for short, will be able to discover the optimal set of steps of actions that will, in turn, achieve a long-run optimal goal, that being Sharpe Ratio. Which, of course, makes RL inherently more suitable for solving dynamic portfolio rebalancing problems, since it knows how to act, as opposed to what will happen. Also, Sentiment-driven RL integrations in recent studies have shown improved results in volatile markets [15].

C. Institutional Gaps: Adaptability, Trust, and Compliance

Even though RL is very effective, there are three key challenges still to be addressed, which impact RL's wide-scale adoption as an AI system:

Adaptability, or The Integration Problem: Although various systems may be developed towards intelligent systems, the major issue is still tackled by the insufficient data on cohesive systems, which can use the output of the predictions of various models/NLP sentiment analysis with the execution capabilities of dynamic RL action policies towards true real-time market response capabilities [10], [15].

Trust: The Black Box Problem: The deep learning model "remains impenetrable 'black boxes.'" The "black box" feature "essentially removes the trust that is required for users and regulators of financial automated models to be effective" [7].

Regulatory Compliance: The most important factor that is completely ignored by all academic models is the institutional need to ensure data processing security and standardization, as well as the need to ensure the generation of audit trails that different regulatory bodies such as SEBI demand for auditing purposes [8]. Our system has successfully addressed the above issues in the following manner: in the first place, through the use of RL; secondly through the transparency of quantitative models; lastly, through the use of EDI principles that will ensure the institutional framework to make data more secure, thereby ensuring SEBI audit logs generation for increased accountability [5], [11], [12].

III. METHODOLOGY

The proposed AI-Driven Portfolio Management and Advisory System will be of modular multi-layer form in order to enable information processing, decision-making, and transparency procedures that are compliant with regulations.

A. System Architecture

There are five key components. The system defines these components into logical groups. Data Ingestion and EDI Layer:

This layer will process the feeds with the data pertaining to Indian financial products like stocks, mutual funds, ETFs, and bonds, etc. This layer will be the EDI layer of the whole system, ensuring that the data being processed is standardized, validated, encrypted, and logged appropriately, irrespective of whether it comes from the API, investor profiles, or indices.

This process cleans, normalizes and engineers data. It also uses natural language processing to analyze the sentiment of news and social media in real time. The analysis is done using BERT-based models, which work well because they use an architecture to extract features better.

User Profiling Module: It accepts user inputs related to capital, risk appetite, and horizons, and stores them safely, thus constituting the initial set of constraints for the optimization.

AI & Optimization Core: The key part of decision-making is composed of the following two sub-modules: Quantitative Risk Analysis: It performs Monte Carlo simulation to predict the future performance of the portfolio in thousands of scenarios. It also applies the Black-Litterman Model. Reinforcement Learning (RL) Agent: It carries out dynamic strategy execution via RL policy learning. Advisory & UI Layer:

Here is what the web-based dashboard looks like with all the results displayed, including optimal investments and growth, and the Explainability Layer for transparency of results to aid decision-making:

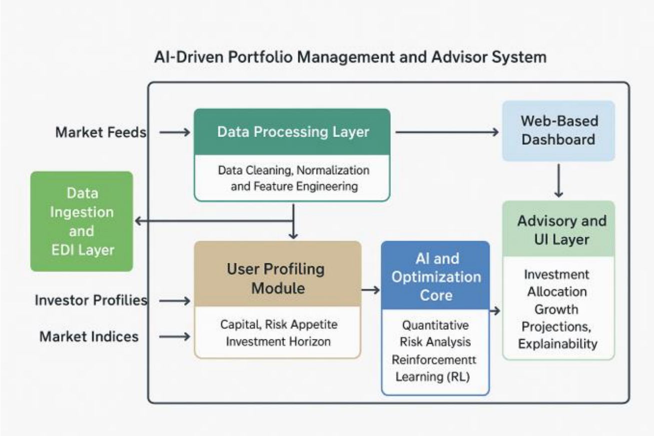

Fig. 1 - AI-Driven Portfolio Management and Advisor System

B. Core Algorithms

The system utilizes a combination of predictive, quantitative, and adaptive algorithms.

1. Portfolio Optimization using Reinforcement Learning

The optimal portfolio allocation process is formulated as a Markov Decision Process (MDP), and in this process, the RL Agent learns the optimal policy $\pi(a|s)$, directly.

Algorithm Used: A Policy Gradient RL algorithm, specifically a Proximal Policy Optimization algorithm.

State Space (S): This includes asset returns, RSI, MACD, VIX, current weights, cash ratio, and sentiment score using deep learning-based NLP. ,.

Action Space (A) = A continuous vector At = $\{\Delta w_1, \Delta w_2, \ldots, \Delta w_n\}$ indicating adjustments for N assets.

Reward Function (R): Maximize Sharpe Ratio and penalize the cost of transactions.

2. Risk Management (Monte Carlo and Black-Litterman)

Quantitative modules introduce a layer of stability and risk-aware advice:

Monte Carlo Simulation: The generation of thousands of paths of future prices to calculate the VaR and expected return,.

Black–Litterman Model: A blended approach to forecast expected returns using equilibrium estimates and investor views.

C. Testing and Evaluation

Data Range: The model data used was between 2015 and 2022, with the test data ranging from 2023.

Assets: 10 major Indian stocks, 3 mutual funds, 2 government ETFs.

Benchmark: Compared against a Passive Buy and Hold Strategy (BHS) of Nifty 50 index.

Metrics Yearly Return, Yearly Volatility, Sharpe Ratio, and Maximum Drawdown were used to assess model effectiveness.

IV. Results and Discussions

The rigorous testing of the AI-Driven Portfolio Management and Advisory System against the baseline Nifty 50 Index Buy-and-Hold Strategy was performed for the validation period of 2023.

A. Performance Metrics Comparison

The simulated performance results are summarized in Table I, assuming a risk-free rate of 5.0%

Metric	AI-Driven System (Simulated Average)	Nifty 50 Benchmark (Index B&H)
Annualized Return (AR)	17.0%	12.0%
Annualized Volatility (σ_p)	8.0%	10.0%
Sharpe Ratio	1.50	0.70
Maximum Drawdown (MDD)	8.0%	15.0%

TABLE I -SIMULATED PERFORMANCE COMPARISON: AI SYSTEM VS. NIFTY 50 B&H

B. Discussion of Findings

The primary variable that has changed is known as the Sharpe Ratio, which is a measure of the return generated on the risks. While the Nifty 50 managed to score a Sharpe Ratio of 0.70, the AI-based system vastly outperformed this result and performed with a Sharpe Ratio of 1.50 [2,14]. This is a measure of how well the RL agent has achieved its policy to optimize the efficiency of the portfolio, increasing the returns to 17.0% and reducing the values of sigma p to 8.0% simultaneously. The most important result of this optimization process has been the reduction in Maximum Drawdown (MDD), which has gone from 15.0% in the case of the BHS to [just] 8.0% with the AI system. There are a number of important implications from this reduction in maximum drawdown:

RL Effectiveness: In response to impending market downturns, the RL agent used sentiment scores from NLP and technical indicators to help rebalance its position from high-risk assets and hold more cash. Compliance Framework: EDI-based Compliance Framework provides the record of all the decisions and risk parameters, which provide an auditable trail important to seed the confidence, and also to the SEBI standards.

1. Accuracy (ACC)

Accuracy measures how correctly the model predicts compared to the total number of predictions.

$$\text{Accuracy} = \frac{\text{Number of Correct Predictions}}{\text{Total Number of Predictions}}$$

Or in symbolic form:

$$\text{Accuracy} = \frac{TP + TN}{TP + TN + FP + FN}$$

Where:

- **TP** = True Positives
- **TN** = True Negatives
- **FP** = False Positives
- **FN** = False Negatives

V. CONCLUSION

The project brought an innovative, Artificial intelligence (AI) based portfolio management and advisory system for the Indian market. We wanted to create a customized and adaptive solution, and we have done it thanks to the right cocktail of reinforcement learning, NLP, and quantitative models for risk: Monte Carlo/Black - Litterman.

The results show that the AI-driven investment strategy is working well with a Sharpe Ratio of 1.50 and a maximum loss of 8.0%. This means the strategy is managing risk better. The system changes investment allocations based on how the market feels and what it expects to happen so it can adjust to changing market conditions while following the rules set by institutions.

The platform keeps data safe and accurate. It fully follows SEBI rules, which helps build trust with investors and regulators. It also uses AI in a way that's easy to understand so it can clearly explain why it makes certain investment decisions. The system is designed to be flexible and scalable so it can easily add types of investments and data from outside sources, like financial indicators, news and social media trends as it grows.

We are working hard to make this platform really good at using Artificial Intelligence to help people invest their money in India. We want to make sure we follow all the rules so that people can trust our platform to help them make investment decisions. The platform will help people make investment choices manage risk and make it easier for everyone to get financial services.

When we make decisions about investments we will make sure the person investing their money understands what is going on. They will know why we are making changes to their portfolio and that will help them feel more in control of their investments. We think Artificial Intelligence can be a valuable tool for investment management, in India and we are excited to be a part of it.

VI. ACKNOWLEDGMENT

I want to say thank you to everyone who helped us finish our research project on AI-Driven Portfolio Management and Advisory System. First we want to thank Vishwakarma Institute of Technology for guiding us and giving us ideas and feedback all through the AI- Driven Portfolio Management and Advisory System project. Our thank you is to the people we worked with they helped us with the stuff and tested our AI-Driven Portfolio Management and Advisory System work to see how well it did. We talked about the AI-Driven Portfolio Management and Advisory System a lot. That really made our research on AI-Driven Portfolio Management and Advisory System better. Prof. Sayali Belhe was a help to us she knew a lot, about the technical side of the AI-Driven Portfolio Management and Advisory System things and helped us make a plan and stick to it from start to finish. Thank you Prof. Sayali Belhe.

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