

Q4 2018 overview of investment firm sector

At the end of 2018, there were five investment firms operating in Estonia.

| Key indicators | Q3 2018 | Change | Q4 2018 |
|---|------------|--------|------------|
| Volume of customer assets | 911 mln € | ? | 674 mln € |
| Volume of assets of investment firms | 56 mln € | ? | 60 mln € |
| Profit | 2,1 mln € | ? | 2,9 mln € |
| Gross income | 10,2 mln € | ? | 11,4 mln € |
| Return on equity (cumulative, annualised) | 21,4% | ? | 21,5% |
| CET1, consolidated | 30,9% | ? | 33,3% |

Investment firms had client assets of 674 million euros under management at the end of the year. The value of client assets dropped sharply by 26% in the fourth quarter. The main reason for this was that one market participant reduced its client base. The volume of client assets shrank by 27% over the year. Estonian clients had only 3.1% of total client assets at the end of the year.

The sector earned 11.4 million euros in gross revenue in the fourth quarter, which increased the revenue base by 11% over the quarter. For the year as a whole the sector earned one fifth more gross income than a year earlier at 44 million euros. The revenue base mainly increased because of profit earned from trading and service fees for consultation.

The largest share of income was the 76% earned from trading, while 10% came from interest income, and 12% from service fee income for providing investment services. The largest part of service fee income for providing investment services was the service fees for securities transactions and consultation activities. The sector earned trading profit through its market exposure positions, usually using derivatives. Trading portfolio positions require active management and so are a relatively volatile component of the revenue base.

The investment firm sector earned 2.9 million euros in net profit in the fourth quarter, which is 35% more than the profit of the first quarter. The sector earned a total of 10.5 million euros in net profit in 2018, which was 72% more than in 2017. This large increase was mainly due to the growth in the revenue base. The return on equity was 22% for the sector in 2018, which was one of the highest figures for profitability in the Estonian financial sector.

The consolidated capital standards indicator for the sector increased to 33.29% in the fourth quarter.

Capitalisation was improved by a reduction in risk assets, which was caused by the partial closure of currency positions in the sector.

Finantsinspektsioon has set elevated additional capital requirements for most investment firms to make sure that they hold sufficient own funds to cover their exposures. The additional capital requirements mean that many investment firms have only a small buffer of own funds despite the high capital standards, and are not able to take on any additional exposure.

Main development trends and risks

- The income and profitability of the investment firm sector remained at high levels. Net profit in 2018 was the highest of the past decade.
- The investment firms in Estonia mostly operate internationally, and the greatest part of revenues, some 83%, were earned from transactions concluded abroad.
- A large part of the profit was earned from positions taken in the trading portfolio.
- Investment firms sell the majority of their services outside Estonia and mainly to non-residents, and this creates money-laundering risks.
- The large volume and complexity of the regulations that apply to investment firms are a challenge for Estonian market participants with slim organisations.

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