

Q2 2019 overview of investment firm sector

There were five insurance firms under supervision by Finantsinspektsioon at the end of the second quarter. There are no branches of insurance firms from foreign countries operating in Estonia. The largest Estonian investment firms operate in foreign countries though, through branches and by providing cross-border services. On average, 96% of the client base of the sector and 83% of the revenue base is associated with clients based in foreign countries.

Investment firms had 610 million euros of assets belonging to clients in the second quarter. The value of client assets continued to fall in the second quarter, losing 4% over the quarter. Estonian clients had only 3.5% of total client assets.

Key indicators	Q1 2019	Change	Q2
Value of client assets	636 million euros	?	610 million euros
Value of assets of investment firms	65 million euros	?	62 million euros
Profit/loss	0.05 million euros	?	2.3 million euros
Gross income	8.8 million euros	?	11.8 million euros
Return on equity (cumulative and annualised)	0.4%	?	8.7%
CET1 ratio, consolidated	30.97%	?	27.79%

The investment firm sector earned gross income of 11.8 million euros in the second quarter, which was 34% more than in the first quarter. The revenue base of the investment firm sector is affected by fluctuations from quarter to quarter in the income that is earned from trading with assets assessed at fair value. Trading income was down 29% in the first quarter but up 46% in the second. Revenue earned from trading is volatile because it depends on the activity of clients, on changes in market exchange rates, and on how effectively market participants manage their market exposures.

The sector earned net profit of 2.3 million euros in the second quarter, which is substantially more than the 0.05 million euros earned in the first quarter. The return on equity of the sector was 8.7% in the first half of the year. The improvement in profitability came from an expansion of the revenue base. The management costs of the sector were about the same as in the first quarter.

The consolidated CET1 indicator for the sector fell during the quarter from 30.79% to 27.79%. The small decline in profitability was due to the increase in risk assets, which was caused by an increase of 15% in market exposures over the quarter. Currency risk has seen an increase among market exposures, and accounted for 70% of all market risks. The total market exposure of investment firms

was 103 million euros, which is a very high level given that the equity of the sector is 55 million euros.

Finantsinspeksioon has set additional capital requirements for investment firms. This means that many investment firms have only a small buffer of own funds despite their high CET1 figures, and are not able to take on any additional exposure.

Main development trends and risks

- Investment firms have large market exposures, from which a large part of the income of the sector is earned.
- Business models based on market risk leave the financial positions of investment firms exposed to risks that could materialise in a short time if the market were to develop unfavourably.

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