Q3 2019 overview of investment firm sector

Five investment firms operate in the market meaning that market is very concentrated. The two largest investment firms, Admiral Markets and KIT Finance Europe, have 97% of the market by assets.

The profitability of investment firms improved notably in the third quarter. The gross income of the sector increased by 25% over the quarter as income earned from trading grew. The majority of the income of the sector comes from trading with instruments assessed at fair value. Trading provided 81% of total revenues for the sector in the third quarter. The profit of the quarter was more than 2.4 times that of the previous quarter.

The return on equity of the sector was 13.6% in the third quarter, which represents strong profitability.

Key indicators	Q2 2019	Change	Q3 2019
Value of client assets	610 million euros	?	600 million euros
Value of assets of investment firms	62 million euros	?	67 million euros
Profit/loss	2.3 million euros	?	5.5 million euros
Gross income	11.8 million euros	?	13.6 million euros
Return on equity (cumulative and annualised)	8.7%	?	13.6%
CET1 ratio, consolidated	27.79%	?	23.63%

The average CET1 indicator for the sector fell during the quarter from 27.79% to 23.63%. The fall in capitalisation came from growth in risk assets, which in turn occurred because market exposure positions were increased.

Market risk is at the centre of the business of investment firms

Investment firms hold their market risk exposures on their balance sheet as bond investments and off-balance sheet derivatives. At the end of the third quarter the sector had 11 million euros in bond investments, which made up 17% of assets. The bonds are bought for liquidity management purposes and are of high quality. All of the ten largest investments were AA with high credit ratings.

Investment firms acquire derivatives while serving clients. They mitigate the risks from client transactions by making hedging transactions with other investment firms and credit institutions. Risks are usually hedged in part, leaving part of the position for the investment firm to earn profit. This means that a reduction in client transactions leads to a large amount of market risk exposure, which is an important source of income, but also of risk.

Market risk exposures increased by 29% over the quarter to 132 million euros. The exposures were 2.4 times the equity of the sector. Currency risk accounted for 68% of the market risk exposures, equity risk for 22%, and trading risk for 10%.

Main development trends and risks

- The revenues and profitability of investment firms are very changeable from quarter to quarter, but they still earn large profits over the year on average.
- Investment firms earn a large part of their profit from trading in derivatives. This allows them to earn large profits, but also creates risks that could be realised very rapidly.

Quarterly reviews of the investment firm sector

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