



Neo-brokers in the EU: Developments, benefits and risks

ESMA webinar, 17 July 2024

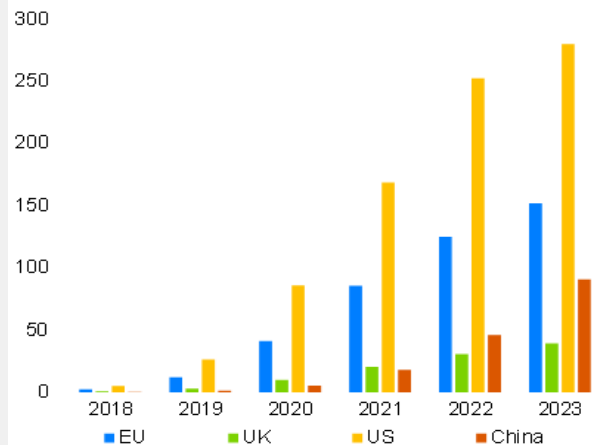
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Background

Rise in use of neo-brokers

Chart 1

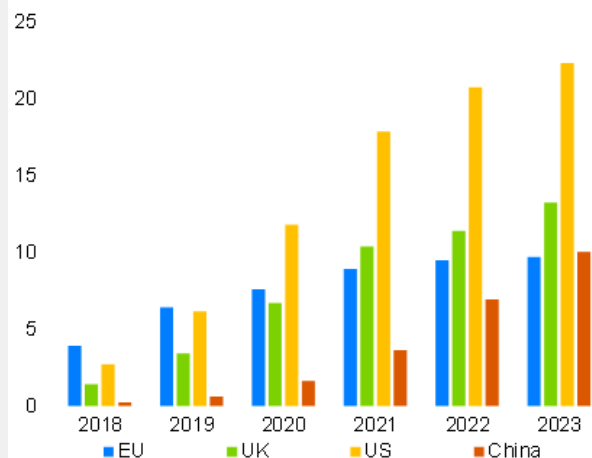
Neo-broker client assets by region
Rapid growth in assets



Note: Net assets held via neo-brokers by selected region, EUR bn. Neo-brokers exclude robo-advisors; assets exclude crypto-assets.
Sources: Statista, ESMA.

Chart 2

Neo-broker accounts as % of adult population
Widespread use especially in the US



Note: Number of neobroker users (or accounts) divided by the adult population, by selected region, %. Neo-brokers exclude robo-advisors; assets exclude crypto-assets.
Sources: Statista, ESMA.

Neo-brokers are a new generation of digital financial entities that enable consumers, mostly retail, to trade real-time in financial products

Rapid growth in client assets but from a low base; ~ EUR 1tn in 2023

Widespread use suggests many small investors

Globally, highest-valued firms include:

- eToro (EUR 8 bn)
- Robinhood (EUR 8 bn)
- TradeRepublic (EUR 5 bn)

New entrants may change market structure, affecting trading conditions

Some firms known to receive Payment for Order Flow (PFOF)

- In 2021, [ESMA warned investors](#) of risks around PFOF, including around potential conflicts of interest and limited transparency, e.g. where firms claim to offer 'zero-commission' trading

Neo-brokers are innovative users of technology, with gamified features in some cases

- In 2023, ESMA published a [discussion paper](#) on investor protection aspects of digitalisation, including on 'dark patterns'
- Potential to harness new technology to promote retail investor participation

Working with NCAs, ESMA carried out a market survey in 2023

Sampled firms

27 EU-based neo-brokers, authorised by 11 NCAs

Firms in sample identified as neo-brokers based on supervisory judgement

Client coverage

~ 10 million client accounts, mostly EEA retail clients

3 firms provide 72% of these accounts



Range of services and products offered

Neo-brokers invest in process automation and user-friendly features

- Aim to curb costs and attract clients

Some offer additional services beyond trading, e.g. portfolio and wealth management, investment advice, custody and safekeeping

Most common types of financial instruments traded:

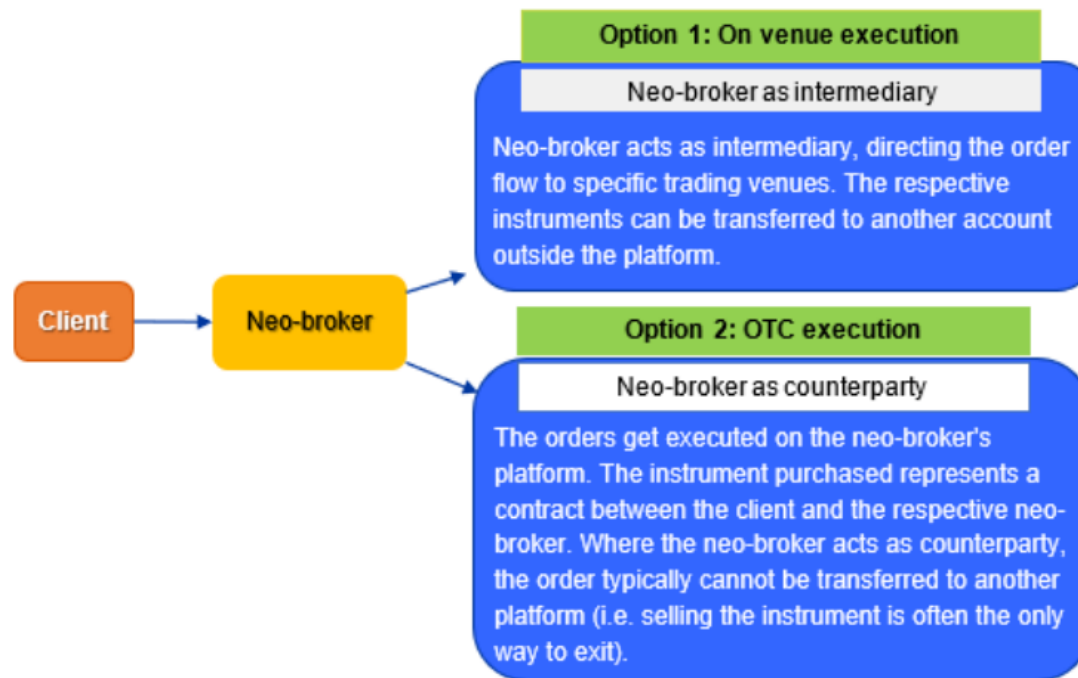
- Shares
 - ETFs
 - Fractional shares/ETFs or other contracts replicating shares and ETFs
 - CFDs
 - Derivatives
 - Crypto assets
- 
- A decorative graphic consisting of a thick, curved band that starts light blue and transitions into a greenish-yellow color, curving upwards from the bottom right towards the center of the slide.

Execution model depends on instrument type

Chart 4

Neo-broker execution models

Neo-brokers may execute orders on venue or over-the-counter (OTC)



Note: Schematic account of different execution models available to investment firms, including firms considered as 'neo-brokers' for the purpose of this article.

Source: ESMA

Different types of costs and charges

Main sources of revenue:

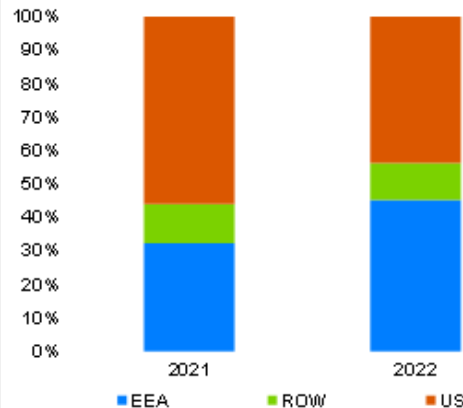
- order based commission fees
- bid-ask spread
- currency conversion fees
- Payment for Order Flow (PFOF)
- fees for other services

Since the period studied, an EU-wide ban on PFOF has been put in place

- However, transitional provisions apply till June 2026

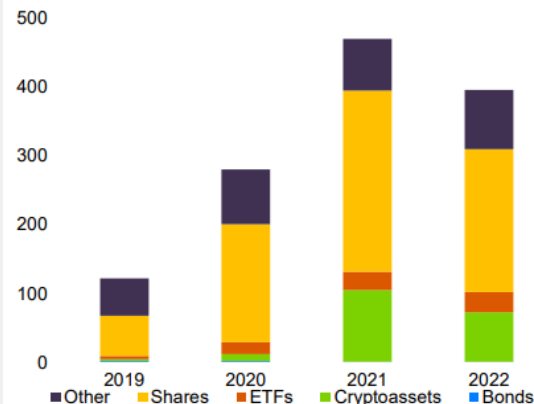
High market concentration within sample

Chart 3
Shares traded by location of the issuer
EEA-issued shares become more popular



Focus on US-based share issuers, but EEA issuers gaining ground

Chart 5
Selected instruments by annual trade volumes
Shares more traded than crypto, ETFs or bonds



- Shares/ETFs: 5 firms with 90% of total trade volume in sample (2022 figure)
- Crypto: 2 firms with 97% of volumes
- CFDs: 86% among 3 firms

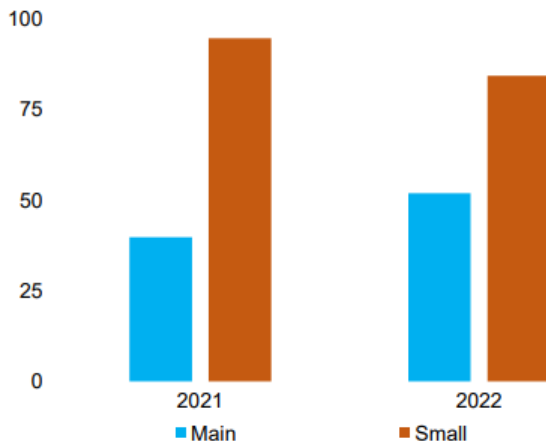
Total traded share volumes among neo-brokers were only 1.5% of EU total volumes

Smaller venues often used

Chart 6

Main versus small venues

Some order flow routed to main venues



Note: Total volume directed by surveyed neo-brokers to selected venues, in EUR bn. 'Main' = two larger venues from the same corporate group. 'Small' = aggregated volumes for five smaller venues. The venues represented are not exhaustive of those used by entities in the survey sample.

Sources: Neo-brokers survey 2023, ESMA

Neo-brokers tend to route many trades in shares and ETFs to small venues

Research suggests that such fragmentation could affect the spreads applied by market makers

Glosten and Milgrom (1985) find the spread applied by market makers *decreases* in the proportion of 'noise traders', as the market maker has less need to protect itself against informed trading

Potential consequences for consumers

Risks

- Complex/risky products (e.g. crypto) may be offered
- Gamification of investment could exploit investor biases
- Social media may be integrated into platform; risk of misleading information
- Some products may not bestow the holder with the same rights as others (see [ESMA Statement](#) on fractional shares)

Potential benefits

- Encouraging retail participation in EU financial markets
- Far more convenient for many consumers
- Potential to promote financial literacy
- Greater competition; potential for lower trading fees





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