

YORKSHIRE BUILDING SOCIETY: RESPONSE TO THE CMA'S STATEMENT OF ISSUES

1. Introduction

1.1 Yorkshire Building Society ('YBS') Group welcomes the opportunity to respond to the CMA's 'Statement of issues' (the 'Statement') regarding its forthcoming investigation into the retail banking market. YBS responded to the CMA's consultation (the 'Consultation'), issued in July 2014, on personal current accounts ('PCAs') and banking services to small and medium sized enterprises. YBS is pleased that it now has the opportunity to offer a further submission in relation to issues it believes the CMA should consider as being within the scope of its investigation.

1.2 YBS is owned and governed by our members and is Britain's second biggest building society with over 3.4 million customers. Our primary business areas are deposit-taking activities, mortgage sales and administration and mortgage related insurances. We operate via a number of distribution channels including telesales, postal and the internet. Our primary distribution channel is, however, via our network of 231 branches across the YBS network and the other brands we trade under - Barnsley Building Society, Chelsea Building Society and Norwich & Peterborough Building Society. YBS also has a wholly owned subsidiary, Accord Mortgages Limited, which handles intermediary mortgage business.

1.3 In terms of the personal current accounts market, YBS offers current account services through its Norwich and Peterborough Building Society ('N & P') brand. YBS has a stated intention to introduce a new current account service across its network and brands for the benefit of its own members as a 'mutual alternative' to challenge the dominant providers in the market. For the purposes of this submission, YBS intends to focus on the PCA market, given its importance to YBS's current and future operations.

2. Market characterisation

2.1 Paragraphs 18 to 20 of the Statement outline a number of sector characterisations which are relevant to competition in the market. YBS considers that all of these characteristics are relevant and important and believes many of the characteristics directly or indirectly cause detriment to customers.

2.2 In summary, YBS believes that the main structural issues facing the PCA market are related to an inter-connected relationship of: (1) high levels of market concentration; (2) low levels of switching and high inertia; (3) low levels of innovation and differentiation; and (4) the dominant free-in-credit banking model that relies on cross-subsidisation. YBS supports the characterisation of the market set out in the Statement.

3. Theories of harm

3.1 YBS welcomes and agrees with the three groups of hypotheses, or 'theories of harm', which the CMA has identified in paragraphs 24 to 50 of the Statement as potentially adversely affecting competition in the banking sector.

3.2 ***Theory of harm 1: Impediments to customers' ability to effectively shop around, choose and switch products or suppliers, resulting in weak incentives for banks to compete for customers on the basis of price, quality and/or innovation***

In terms of the first theory of harm, we agree inertia in the market is significant. In terms of hypothesis 1(b), many of the dominant providers use overdraft fees and charges - which are not readily transparent or understandable, and are not a key factor in the decision making process for customers selecting a current account provider - as a key source of revenue and use this revenue to effectively cross-subsidise other products and services in the market.

3.3 On hypothesis 1(c) as the CMA has identified, customer satisfaction towards the 'Big 5' banks (including Santander) is low. However, account switching has only grown modestly since the launch of the Current Account Switching Service (CASS) in 2013, and a proportion of the uplift that was evident in the early days is likely to be due to customers switching between Lloyds and TSB as a result of the sort-code based approach of the TSB separation which led to a number of customers being separated from their local branch. CASS was proposed and implemented after the plc banks which dominate the current account market made the case it would give a more efficient and predictable switching process. However, there are outstanding problems, such as that the forwarding of payments only lasts for a limited period and even if this were extended, after this time they would still be bounced.

3.4 *Theory of harm 2: Concentration giving rise to market power of some banks leading to worse outcomes for customers*

In connection with this theory, YBS would agree market power is exerted unilaterally. It is right to examine market structure in detail. The fact TSB by providing better value and a decent service proposition, is attracting market share demonstrates there may have been an opportunity or opportunities for some time which some other market participants without the necessary scale had not been able to take up.

3.5 *Theory of harm 3: Barriers to entry and expansion leading to worse outcomes for customers*

In line with paragraph 49(b) of this hypothesis, those choosing their first PCA as young adults "sleep walk" into opening an account with big banks. This is enabled by the fact the nearest branch or one of the nearest will directly drive acquisition despite a multi-channel service model. Distribution presence also acts indirectly by shaping the new customer's friends and families historic choices, which then shape where they chose to bank.

In relation to paragraph 49(c) of this hypothesis, Norwich & Peterborough's experience having since launch relied on an agency bank, demonstrates functionality and proposition issues can be restricted by what the third party provider has the capability to offer, which is why direct access to the payments system for new entrants and smaller providers on fair commercial terms is important.

In relation to paragraphs 49(d) and 49(e) of the hypothesis, YBS would highlight some examples, such as the use of large current account books to drive cross selling into the savings market, and using in credit balances, for which little or no interest is paid under free in credit model, to cross subsidise loss leading savings products to attract retail deposits. These practices have been highlighted in the course of the FCA Cash Savings Market Review. YBS would argue pricing distortions in savings and in mortgage markets, where cross selling to customers by their PCA provider is also a dominant market feature, should be in scope for the investigation. It is the competition failures in PCA market which distort and are one of the root causes of the problems in other parts of the retail banking market.

4. Conclusion

YBS welcomes the Statement and looks forward to engaging constructively with the CMA during the investigation.