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# Santander UK plc

# CMA Retail Banking Market Investigation

## Response to the CMA Issues Statement

## 3rd December 2014

RESPONSE OF SANTANDER UK PLC TO THE CMA ISSUES STATEMENT

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## 1 Introduction

1.1 In this response we describe the issues that, from our experience as a challenger bank, we consider impede the development of more competitive markets in retail banking. We do not comment on all of the matters discussed in the CMA's issues statement dated 12 November 2014 (**Issues Statement**) but focus on those where our experience of seeking to build a scale competitor to the incumbent "big four" banks will be of value to the CMA in this inquiry. Our emphasis is more on our business experience and the challenges we have faced rather than on the underpinning economic theory. Unless otherwise indicated, we adopt the terms defined in the CMA's terms of reference.

1.2 The response is structured as follows:

(a) in section 2 we describe our market position and our strategic objectives (including the milestones of our journey to date in Annex A);

(b) in section 3 we describe how our products and services are highly rated by customers and independent observers;

(c) in section 4 we set out why, despite the strength of our products and services, we face significant challenges in addressing the dominance of the big four banks;

(d) in section 5 we describe why customer inertia and reluctance to switch is a major issue and consider some of the reasons for this;

(e) in section 6 we set out why it is important for the CMA to consider the SME sector on a segmented basis because of material differences between larger and smaller SMEs;

(f) in section 7 we describe some of the barriers to more competitive retail banking markets; and

(g) in Annex B we identify how the contents of this response relate to the theories of harm (**ToH**) set out in the Issues Statement.

## 2 Our market position and strategy

2.1 Santander UK plc (San UK) occupies a unique position in the UK retail banking sector. While being considerably smaller than any of the four largest incumbent banks we are a scale challenger to the big four incumbents with a sizeable customer base and branch network larger than any other challenger.

2.2 Our growth to date has come about in part as a result of mergers, which started with the acquisition by Banco Santander, SA of Abbey National in November 2004, included the amalgamation of two other building societies in 2008 (Bradford & Bingley (B&B) and Alliance & Leicester (A&L)), and led to the rebranding exercise that launched San UK in 2010. Our growth has also arisen organically because we have offered attractive products to ensure that we retain and win customers from our competitors. Details of our journey are set out below and in Annex A to this response.

**PCA market share growth**

2.3 The charts below show San UK's growth in market share in adult current accounts over the past five years, and the relative impact of the A&L and B&B mergers on San UK's position in adult current accounts since 2004.

[✂]

**SME market share growth**

2.4 The chart below shows the growth in San UK's market share of SME business (based on assets, rather than current accounts, given the strategic lending growth objective of our business) since 2008.[1]

[✂]

2.5 Today San UK is a credible "scale challenger". We have made significant investment in the infrastructure needed alongside our product portfolio to continue to grow our market share in retail banking markets. In the more established SME market there have been substantial costs in building the SME franchise and infrastructure to supply the breadth of products and services required to enable us to pursue our aim of being the bank of choice for UK businesses and our wider corporate strategy of being a better balanced retail and commercial bank. Following the significant investment in the bank, we are continually improving our customer proposition and the range of services we are able to offer.

2.6 However, our strategic transformation is not complete; [✂]. Our ultimate goal is to create a fully-fledged, diversified, and customer-focused bank: an institution of choice for both personal and SME customers with the overall objective of helping people and businesses prosper. We

[1] [✂]

want to be a leader in efficiency, customer satisfaction, and quality of service. We are further developing our corporate banking capabilities, enhancing our products and systems and expanding our network. We are seeking to innovate, disrupt the status quo and further grow our market share, and our 123 Current Account (described below) is a good illustration of how innovative new products need to be in the PCA market in order to make an impact.

2.7 We seek to differentiate ourselves as a bank that is simple, personal and fair. Transparency and the simplification of pricing structure are at the heart of our retail banking strategy. We believe that the key to increasing transparency is to simplify charges to make them more easily understood by our customers, not through increasing the number of communications sent to customers. Banks already provide considerable amounts of account information in the form of notifications of changes, annual account statements, monthly statements and the like, and customers are more likely to find increasing the volume of communications to be inconvenient and confusing. We are committed to helping our customers retain control of their finances, through services such as text and email alerts highlighting payment details and balance levels.

2.8 [✂]

2.9 Our approach to transparent and simplified banking is manifested in a number of ways:

**PCA products:**

(a) To ensure our customers receive the information they need to understand the costs and benefits of their banking service, we provide annual statements with the charges and benefits clearly explained. In addition, for several years we have provided online current accounts with 12 months transaction data in a user friendly and exportable format. This allows customers to review and understand their expenditure and is available to all customers who are registered to use internet banking. This is in addition to online statements which are available for up to seven years for those customers who have elected to receive electronic statements.

(b) Our flagship 123 Current Account was launched in 2012 and offers cashback and relatively high interest rates on credit balances, with a simple, transparent charging structure and a greater and sharpened focus on excellent customer service. The 123 Current Account benefits include an interest rate up to 3% for balances up to £20,000 and up to 3% cashback on household bills paid by Direct Debit in return for a £2.00 monthly fee. Funding the account with at least £500 each month and setting up at least two Direct Debits is all that is required for customers to begin benefitting. Customers holding either a 123 Current Account and/or a 123 Credit Card are eligible for a range of ‘123 World’ product offers. 123 World products are preferentially priced alternatives to our already competitive products.

(c) Existing PCA customers are able to internally transfer to any of our PCA product offerings, including the 123 Current Account. This is an important aspect of our goal to build an actively engaged and loyal customer base on a long term basis.

(d) We have removed Added Value Accounts (AVAs), also known as packaged accounts, from our PCA product offering. AVA accounts receive a range of insurance related benefits such as travel insurance, breakdown assistance and mobile phone cover. We consider AVAs to be complex and that AVA customers may potentially be paying for additional benefits that they do not need.

(e) We recently improved and re-launched our online banking service and launched newly designed and improved mobile banking applications and the mobile San UK website. Online banking credentials are now sent within five days of customer request instead of the previous 14 days.

(f) We provide all our PCA customers with a range of text and email alerts to highlight events such as payments made and balance levels. These alerts, in conjunction with other account features below, are designed to help customers manage their finances by providing greater account control.

**SME products:**

(a) To ensure SMEs receive the information they need to understand the costs and benefits of their banking service, we provide 15 months transaction data and statements in a user friendly and exportable format.

(b) In February 2013, we re-launched our Commercial Banking BCA proposition. The principles of design for the new banking proposition focused on:

- competitive value-for-money services;
- simple and straightforward propositions;
- transparency in approach - i.e. no small print or hidden charges;
- incorporation of the latest available technology;
- consistency and continuity to propositions across all Commercial segments; and
- choice and flexibility to ensure suitability of products to meet customer needs and also to support relationship teams and relationship development.

2.10 We explain in section 3 below that this approach has paid off, in that customers and independent analysts recognise the improvement in our product proposition and overall service levels. However, this recognition has not been reflected in a material increase in our market share. While we have succeeded in growing our retail banking business in recent years, as illustrated by the graphs above, we still only have a [✂] per cent share of the SME market (an increase of [✂] per cent of the market share since 2012) and we have a [✂] per cent share of the PCA market (an increase of [✂] per cent of the market share since 2009).

2.11 As we explain in section 4, we face substantial challenges to overcome the incumbency advantages of the big four banks, where switching is a significant issue (see section 5) and there remain barriers to expansion (see section 7).

## 3 Customers and independent analysts regard our product proposition as very strong

3.1 We know that we offer products that customers find attractive and that are ranked very highly in industry surveys:

**PCA products:**

(a) Our 123 Current Account has proved to be very attractive to potential switchers. According to TNS data[2], more accounts have been switched to San UK than to any other bank making us the most favoured destination for PCA customers switching banks.

(b) Customer satisfaction for our PCA customers has improved steadily, month on month over the last year as noted by FRS and Moneysavingexpert. Over the same period some of our competitors' scores have deteriorated.

(c) A Which? survey released in January 2013 compared the cost of running a current account and calculating unauthorised overdraft charges. Customers found San UK costs and charges to be the easiest to calculate correctly amongst the banks surveyed. We were significantly ahead of the next competitor. Out of a total possible score of 24, our score of 17 was by far the highest, six points ahead of the next competitor, NatWest, which scored 11. Since this ranking, we have further improved the ease of finding our overdraft charges online.

(d) In the Moneyfacts 2013 awards, San UK's 123 Current Account won the award for innovation in personal finance.

(e) San UK's 123 Current Account was voted as having the Best Rewards in the Uswitch 2014 current account awards.

(f) San UK was crowned best current account provider at the 2014 MoneySuperMarket Supers Awards.

2 TNS Current Account Switching Index October 2014

**SME products:**

(g) We are rated higher for customer satisfaction in SME banking than any of our large competitors. [✂]

(h) Our phone and online services are rated top among our UK competitors[3].

(i) Our Business and Commercial BCA range has been recognised by Moneyfacts 12 years in row for being the Best Current Account Provider. Our on-sale range also has a Moneyfacts Five Star rating.

## 4 The challenges that we face in competing with the big four banks

4.1 The evidence therefore demonstrates that we have a strong customer proposition and good levels of service. While this has helped us to grow market share we have not succeeded in making significant inroads into the market position of the big four. As the Issues Statement sets out, the big four account for 85 per cent of BCAs and 77 per cent of PCAs in England and Wales and their market shares have remained stable over a prolonged period. There is no correlation between satisfaction levels and the gain or loss of market share.

4.2 Although a good product range and high levels of service are essential elements of the competitive process for challenger banks, this alone is not sufficient. The strength and resilience of the big four incumbents is built not just on their products (which, as explained above, are generally not superior to – and in many cases are inferior to – our offering and those of other competitors) but on their possession of strong infrastructure built up over time. In particular, this includes: an extensive physical branch presence; large IT and payment infrastructures; a large number of relationship personnel on the ground; access to large marketing budgets; and, for SMEs, ingrained professional networks that have existed for many years with brokers, accountants and lawyers. All of these factors contribute to a very strong brand profile. The big four also benefit from very large, passive (in terms of unwillingness to switch) incumbent customer bases, which is in contrast to the customer base for challenger banks which is typically more volatile.

4.3 This means that in order to win customers from the incumbent banks, material investment is required to build the infrastructure needed alongside our product portfolio to continue to grow market share in retail banking markets. In this respect it is important to emphasise that customer inertia and barriers to switching reduce the return on such investments and thereby risk acting as a major disincentive to challengers to make large scale investments.

4.4 These investments are expensive [✂]. As for any other business, our return on equity needs to be at or above a certain level to ensure our long term sustainability and from an investor perspective and this requires patience as there is a time lag following investment before returns

[3] Charterhouse UK Business Banking Survey 2014

can be made to make the investment worthwhile. The Association of British Insurers commented in their December 2012 report, 'Investibility of Banks', based on investor research, that "*failure to achieve at least cost of capital across the cycle is likely to lead to banks' businesses being unsustainable in the longer term and will inevitably constrain asset growth and lending to the wider economy*."

4.5 Nonetheless, to date we have made significant investments across our retail banking business:

**PCA market**:

(a) We have invested in developing the innovative 123 Current Account which differentiates us in the market. [✄] particularly given the central issue of lack of switching, which we describe in Section 5 below.

(b) In order to ensure that we are able to meet our customers' current needs for a local branch network and create brand awareness in the PCA market, [✄].

**SME market**:

(c) We have expanded our corporate business centre network (we now have [✄] corporate business centres). During 2013, we opened [✄] new centres and employed an additional [✄] relationship managers.

(d) We have further expansion plans to achieve an additional network of approximately [✄] corporate business centres.

4.6 While one expansion strategy may be to focus on niche markets (perhaps specific products in the SME banking sector or specific consumer groups in the PCA sector) this is not a strategy likely to make material inroads into the incumbent banks' market strength, which is built on a bundle of qualities focused around relationships and branding and the perceived ability to provide for, and connect, across a wide range of customers' banking needs. [✄]

4.7 For both SME and PCA businesses, there is a material difference between customer acquisition strategies of the incumbents and challengers. An incumbent's focus is on retaining its existing customer base. A challenger's focus is on winning new customers. In a market where customers are, for various reasons, very reluctant to switch, the principal focus of the incumbents can be on avoiding customer dissatisfaction and, where they identify customers displaying a greater propensity to switch than the norm, targeting measures at such customers.

4.8 More specifically in the SME market, challengers will find it hard to target potential dissatisfied customers of incumbents (because the challenger will not know who they are) whereas the incumbent is much better placed to identify, and take steps to placate, potential switchers. Thus, while the incumbents can focus on 'protective' measures, ensuring that their customer base does not become materially dissatisfied (and perhaps identifying particular customers in this category and taking measures to protect such customers at the expense of their wider customer base), we have to disproportionately focus on more costly "pull" mechanisms designed to attract new customers.

4.9 A challenger therefore has to create reasons for a customer to want to switch. This requires significant effort in marketing, promotion and building infrastructure with the costs spread over a smaller, and more volatile, customer base than that of the incumbents. However the investment challenges in achieving this are significant. To attract switchers, a challenger IT platform must offer the same level of capability as the established players have built up over decades. For example, we do not believe an SME would switch to a challenger where they perceive dilution of their products or services. [✂] For this reason, lower barriers to switching could improve dynamic incentives to invest.

4.10 SMEs will typically employ one of two strategies when considering switching their banking provider. They will either take one or two services and remain with multiple banks whilst they ‘test’ the proposition, or they will want to switch the whole relationship in one seamless move. If a full switch of banking relationship is undertaken, the SME will require access to a similar suite of products and services after moving. To compete effectively, a challenger bank must therefore offer a broad range of products and services at least comparable with their existing provider. As mentioned above, this requires a significant and sustained level of investment by the challenger to develop their capability as a viable full banking alternative.

4.11 In addition to the direct investment costs, in the SME market [✂]. When an SME is in a long term relationship with a bank this allows the bank to build up a detailed track-record of their account and credit activity. This makes it easier for the SME to apply for additional products and services as their bank will have detailed financial knowledge of the SME and can access their history for decision-making. [✂] The track record built up by the existing provider, including credit and banking transactional data, gives the existing provider a timing edge over an alternative where a borrowing request requires a quick turnaround. Furthermore, even when the alternative provider can match the timing of the existing provider, they will reach this decision on the basis of having far less granular information available. As a result, with lending led switching[4], challengers take on significantly more credit risk and levels of uncertainty which are not borne by the incumbents.

4.12 [✂]

## 5 Switching – a key issue

5.1 In our view, if there is to be a material change in competitive conditions in retail banking there are a number of issues that need to be addressed in the course of this inquiry. While some of these issues will emerge as the inquiry develops, some are apparent even at this early stage and we outline these in the following sections of this response.

[4] See further below paragraph 7.2 where an adverse credit event (which is likely given the nature of early inflow business) can have a material impact on Internal Rating Based outcomes as the portfolios lack economic depth.

5.2 A major issue is customers' relative reluctance to consider switching from the incumbents even when attractive products appear to be available elsewhere. In part this can be remedied by further simplifying the account switching process but this is not the whole answer. In our experience, many PCA and SME customers are simply not motivated to look to compare banking services, and then to switch.

5.3 As the Issues Statement recognises there are complex issues of behavioural economics that need to be considered in the context of switching. Improving the availability of and access to information about the true costs of services is undoubtedly beneficial and will influence switching to some degree. However, we believe that the major obstacle to switching, particularly for PCA and smaller SME customers, is the fact that customers do not have to pay for their current account. They therefore lack any feeling of being a true “purchaser” of the service. Material change in customer behaviour could be brought about if this issue is addressed.

**PCA market:**

5.4 For PCA customers, the reluctance to contemplate switching stems from three connected factors:

(a) While customer satisfaction levels are low, so too are customer dissatisfaction levels. According to data from the Financial Research Survey (FRS), run by GfK Nop, only a very small proportion of customers, just [✂] per cent, are dissatisfied with [✂] per cent classed as being ‘very’ or ‘extremely dissatisfied’. In other words customers are largely neutral as regards their PCA. It does not materially register in the consciousness of customers as a service to get greatly excited about – whether positively or negatively. We believe that the reason for this is the prevalence of the “free if in credit” banking model. While of course this does involve a cost to customers in the form of foregone interest on current account deposits they do not perceive it as an expense (or as an expense to be concerned about) because it does not involve a payment out of funds in their possession. If the cost of a service does not register with an individual that individual is unlikely to be focussed on the quality of the service so long as it is delivered with at least a basic level of competence.

(b) The impact of this is exacerbated by incumbents offering packages of products as part of a current account, for example bundling insurance with the account or offset mortgages[5]. Where the current account is bundled with other products the customer’s focus (given the largely ambivalent feeling about the current account which is perceived as a “free” service) is on the other product – attention is thus focussed away from the value for money of the current account. Bundling may also act as a deterrent to switching the current account where a switch might involve losing the bundled product. For banks such

[5] We note that offset mortgages are outside the scope of the CMA’s terms of reference. However, given their prevalence in the market and the effects outlined above, we believe the CMA should extend the scope of its investigation to include offset mortgages.

as San UK which do not bundle products (because to do so would depart from our proposition of simple products and pricing) this creates an additional pressure to ensure that our accounts are competitive because it is easier for our customers to switch away than is the case for many of the incumbents' customers.

(c) These factors ("free" banking and bundling) make it very difficult for customers to determine how much they are paying for their current account and therefore how much they would lose or gain by switching accounts.

5.5 These factors mean that, absent a "trigger event" such as a serious service failure, the apparent benefits of switching may not be high enough to prompt consumers to even consider shopping around.

**SME market:**

5.6 For most SMEs, where existing bank arrangements are simple and straightforward and operating reasonably efficiently, banking is not a high priority. SMEs are likely to be particularly concerned about the risks that switching accounts might present to their business, for example supplier payments or customer receipts missed or employee wages unpaid. They may perceive the likelihood of such an event arising as greater than in fact it is but, given that they are likely to share with PCA customers the view that current accounts are not a major focus of attention – positive or negative – they are unlikely to regard any material risk as worth taking.

5.7 We explain in section 6 below that SMEs differ significantly in their usage of banking services depending on their size. Larger SMEs are likely to be less influenced by their perception of pricing of current accounts, as compared to PCA customers or smaller SMEs, but they are more likely to have a close relationship with their bank built around a relationship manager and the purchase of a number of products, and the size of their business will mean the consequences of something going wrong are likely to be material. Further, relationship managers will be on the lookout for signs of discontent and will take steps to address such concerns at an early stage thus "heading off" serious problems.

5.8 Again, in the absence of a "trigger event", such as a serious service failure or the departure of a trusted relationship adviser which acts as a "push" factor, there is unlikely to be a sufficiently strong "pull" factor to persuade a customer to move to a new bank. If banking arrangements were to become a higher priority, with a SME needing to borrow to expand or wanting to enter in to new markets, this might give rise to a specific opportunity for challengers to offer an alternative. However, BMG research for BIS in October 2013 indicated that SMEs leave such financing decisions to the week before they require a loan and spend less than an hour searching for a solution. This gives challengers little opportunity to talk to potential customers about moving their banking to a new provider. Importantly, it means that SMEs may miss the chance to switch to better products.

5.9 As mentioned above in section 4, the incumbent bank with a long term relationship with an SME has an important advantage over the challenger by virtue of it having built up a detailed track-record of the account and credit activity. The SME considering switching will be aware that a potential new provider will lack the in-depth knowledge and track record. Decisions will be based on using external data sources such as credit reference agencies and company searches. In effect, the SME will have to build up a track-record once again. The uncertainty that this gives rise to for the SME is in our view very likely to contribute to SME switching inertia.

5.10 [✂]

5.11 The more recent Business Banking Insight Survey conducted in November 2014 also found that:

(a) [✂] said they were 'not very likely' or 'not at all likely' to switch provider in the next six months.

(b) The research found that [✂] are 'quite likely' or 'very likely' to switch to a different business current account in the next six months.

5.12 Based on our experience, we have identified a number of "push" and "pull" factors impacting businesses' ability to shop around and consider switching bank. We describe these below but it is important to note that for a number of reasons, some of which are described in section 7 below, the level of customer inertia is high – even where these push and pull factors operate there needs to be significant level of dissatisfaction or a significantly attractive alternative to incentivise a customer to switch.

5.13 Push factors are related to the general satisfaction level with an existing current account provider and willingness to shop around. Typically, where the banking relationship operates without issue it takes a push factor to stimulate a move. Examples of these include:

- Charges and fees increase;
- Change of bank relationship contact;
- Severe service failure;
- Closure of local branch/business centre;
- Decline for a borrowing request;
- Product and services gap/need emerges; and
- End of free banking period.

5.14 Pull factors are the factors that can act as a pull towards a new provider without any of the above push factors having occurred. Examples of these include:

- New product or differentiated service launched;
- Proactive local relationship contact by a new bank;
- New physical location – opening of a branch or business centre;
- Recommendation/referral from a trusted advisor; and
- Recommendation from another business/peer.

5.15 We are looking forward to receiving the results of a customer survey into SME bank switching that we have commissioned. [✂] The survey results are expected by the end of Q4 2014 and we would be happy to share these with CMA in due course.

## 6 Segmentation of the SME "market"

6.1 We agree with the CMA's broad approach to define SMEs as those businesses with up to £25 million turnover. In our experience, SMEs are a diverse group with a wide spectrum of sizes, product needs, growth trajectories and financial sophistication. In particular, the complexity of banking needs evolve as SME businesses grow and there are material differences between smaller and larger SMEs.

6.2 We would strongly encourage the CMA to differentiate between larger and smaller SMEs when reviewing competitive conditions. In our experience smaller SMEs have characteristics which are in many respects similar to PCA customers while larger SMEs have different qualities. The larger SME businesses are particularly reluctant to switch from the big four incumbents. This is a serious barrier because this segment is important in terms of revenue and margins and the ability to offer a broad range of services. The inability to penetrate this segment with any scale therefore significantly increases investment costs and risks.

6.3 We internally segment our SME customers into two core groups:

- business banking (i.e. [✂] – this segment is referred to as "Business Banking"); and
- commercial banking ( [✂] – this segment is referred to as "Commercial Banking")[6].

6.4 [✂].

6.5 The needs of Business Banking customers are closer to those of personal banking customers than our larger business customers. Their product requirements are also similar to personal

[6] [✂]

banking – current accounts, loans, overdrafts and cards, i.e. simple banking solutions. Their needs are typically satisfied via self-service channels such as online, telephony and post office. A recent survey suggests that 18 per cent of SMEs use a personal rather than a business account for their business banking.

6.6 Larger SMEs, which fall within our Commercial Banking segment, are likely to have started off mainly using self-service channels. As such businesses experience growth, their needs change and move from being generic/straightforward to more specific. At this point, relationship banking is likely to become more relevant and important. We are able to introduce such businesses to our specialists, for example to help them trade overseas or manage their transactional banking on a day to day basis. Their needs will still include self-service channels and, in the absence of our ability to provide these to a high standard, this can act as a push factor. However, we can add value via relationship support by helping to spot growth opportunities and threats. Relationship banking is built on credibility, trust and a deep insight into the business. It goes well beyond a transactional relationship. The knowledge of the business is built up over many years. That is why a change of relationship contact can be a strong push factor to switch banks. Often these businesses will follow a particular relationship contact to another bank.

6.7 [✂]

6.8 As set out above, we shall continue to invest in developing our network and service proposition. However, investment incentives would be improved in a more competitive market; [✂] as the next section further explains.

## 7 The barriers to a more competitive market

7.1 In addition to customer inertia, as described in section 5 above, we would include the following among the immediately obvious barriers to expansion for the challenger banks:

**Factors common to PCA and SME markets:**

7.2 Under the capital adequacy rules, the established institutions have developed advanced Internal Rating Based (IRB) approaches to quantify required capital for credit risk. This means that the established institutions under these rules have to hold less capital in terms of SME lending compared to the new challengers. [✂]

7.3 The level of regulatory change is considerable and increasing with an associated requirement for increased investment and allocation of resource and management time. We support proportionate, forward looking regulation that underpins good customer service and a healthy economy. However, regulators should be mindful of the risk that, in aggregate, the regulatory demands on firms could become so extreme and far reaching that they act as barriers to entry and expansion and stifle economic growth and innovation. This may be particularly the case because regulatory requirements result in the need, for example, to increase staffing levels in risk/compliance, and this disproportionately affects smaller banks because the same fixed cost is applied to each bank but must be spread over fewer assets for smaller banks.

**PCA market:**

7.4 While CASS has been an effective industry-delivered initiative in the PCA market which has increased customer confidence in account switching, it requires continued promotion by the Payments Council to drive the required levels of awareness. We believe it would be helpful for greater independent promotion of CASS, for example, by industry commentators such as Which? and Moneysavingexpert. In any event CASS alone cannot deliver fundamental change in the degree of switching without a number of other measures to address some of the issues discussed in this response.

7.5 It is difficult for consumers to interpret the relative costs/benefits of different accounts to take account of the specifics of their individual financial circumstances. We have committed to working with other banks to develop a simple, standardised data download (MIdata) which the customer can give to a comparison website. The comparison website can then analyse this data to help the consumer make an informed choice about the best account provider for them. This will assist consumers in understanding the materiality of changing their PCA provider. We would encourage the CMA's support to seek to ensure that MIdata tools are user friendly and based on actual and projected usage.

7.6 There is scope for the annual account summary to be improved to highlight the MIdata facility. This should give consumers the ability to use their personal data to model the earnings and charges that they would have incurred with another provider. We consider this to be the most appropriate time to highlight the opportunity to shop around.

**SME market:**

7.7 There appears to be a sense of "lock in" in SME banking arising from a number of factors including the number of products and services held with the existing provider and the length of the existing relationship (this is a key indicator of likelihood to switch). The perceived risks of switching are much greater for business banking than PCA. Our discussions with customers lead us to believe that a key obstacle to greater switching of BCAs is customer concern that something may go wrong that will impact on their payments, suppliers or employees. While CASS has been a success in the PCA market, we believe that there is scope for important improvements to the application of CASS in the SME market, for example, in the area of bill payments which are not automatically transferred.

7.8 We welcome the recent reports which suggest that the application of CASS will be widened to SMEs with turnover up to £6.5 million (from €2 million) and the extension of the guarantee to be given by banks around redirection of bill payments to a customer's account from 24 to 36 months. However, we believe that CASS could be improved and would be more effective for SMEs if, for example, bill payments from a customer's account were automatically transferred.

7.9 An enhanced switching process which is fully and properly publicised, to include aspects such as payment mandates, could help overcome customer engagement issues and the perception of insuperable switching costs. Continuity and consistency are critical to SMEs given the impact of payments and related banking issues coming out of a change of banking arrangement might have on an SME's performance, services and reputation with its own customers and suppliers.

7.10 As noted in paragraph 6.6 above, for larger SMEs, relationship banking is a key factor in retaining or winning business. Relationship banking is built on credibility, trust and a deep insight into the business. It goes well beyond a transactional relationship. The knowledge of the business is built up over many years. That is why a change of relationship contact can be a strong push factor to switch banks. Often these businesses will follow a particular relationship contact to another bank. [✂]

7.11 Exit fees on loans for SME customers act as an obvious barrier to switching, and we would welcome measures to address these. Banks should, of course, be able to recoup the costs of setting up a loan. However, if these costs were reflected in the initial arrangement fee and, for example, break fees were made clear to the business when setting up the loan, SME customers might feel more able to switch bank more freely (and have more transparency of the actual costs at the point of taking out an SME loan).

7.12 The arrangements for transferring securities on SME loans can lead to time lags for customers wishing to switch. We suggest an industry standardised fee for the work involved in releasing the security. We also believe the incumbent bank should be required to relinquish the security to the new bank within an agreed and industry defined timescale, such as 30 days, after which it should indemnify the new bank to the value of that security. As a quid pro quo, the new bank should indemnify the incumbent bank for any items in clearing which are not resolved by the point of the transfer.

7.13 The financial decision maker for an SME will generally change as a business grows and will vary between sole traders, where the proprietor will be the decision-maker, and the larger SMEs which are likely to have a dedicated Financial Director. Decisions are also often made by internal specialists with a high degree of financial sophistication. This can be in conjunction with external professional advisors such as accountants and lawyers who act as intermediaries. In Commercial Banking, these intermediaries have a key role to play in the provision of banking information to their clients. Intermediaries can also influence both the choice of a bank and whether to remain or subsequently switch provider. We would encourage the CMA to examine the role of intermediaries and their potential ability to affect competition in the retail banking markets.

7.14 [✂] While some barriers to switching may be hard to avoid in the short term, where avoidable barriers can be removed (e.g. to increase SME engagement, confidence in the switching process and reduce exit fees on loans), this allows challengers to build customer relationships earlier and more generally enhances their incentive to invest.

7.15 [✂]

## 8 Conclusion

8.1 We welcome the decision of the CMA to commence this inquiry which we see as an opportunity to address some fundamental issues that have resulted in inefficiencies in the functioning of the retail banking market for many years with negative consequences for consumers and the economy as a whole. While San UK has innovated and won strong plaudits from customers and industry analysts there is a limit to what we (or any other challenger) can achieve given current market behaviours, in particular the unwillingness of a high proportion of consumers to consider alternative providers to their incumbent bank even though levels of satisfaction are not high.

8.2 There have been a number of inquiries into retail banking over the years and, though there have been some improvements, it is generally acknowledged that such inquiries have not succeeded in bringing about material change. This is in large part because, while the problems are reasonably clear - particularly as regards switching behaviour - the means of addressing them in a proportionate manner, other than at the margins, are not. We would therefore encourage the CMA to put the exercise of seeking to identify effective and proportionate remedies at the heart of this inquiry.

NON-CONFIDENTIAL VERSION

RESPONSE OF SANTANDER UK PLC TO THE CMA ISSUES STATEMENT

# Annex A

## 1 Our Journey

San UK is a subsidiary of Banco Santander, S.A. Banco Santander, S.A. and its subsidiaries (the Santander Group) focuses on retail banking activities, which provide services to 102 million clients through 14,400 offices around the world. However, whilst Santander Group's history began on 15 May 1857, our UK history is much more recent.

Since our entry into the retail banking market in November 2004, San UK has been and continues to be on a transformational journey. Our journey began with the acquisition of Abbey National. We progressed from a collection of three former building societies (Alliance and Leicester, Abbey National and Bradford and Bingley) to a full-service retail and commercial bank. Our objective now is to work to deliver a best-in-class customer experience by developing products and services that are simple, personal and fair for our customers.

**Key Milestones in our journey**

| | |
|---|---|
| **November 2004** | Banco Santander, S.A.'s acquisition of Abbey National plc approved by the courts. This was at the time the largest ever cross-border financial acquisition. |
| **2008** | Journey started on building a Corporate & Commercial Bank |
| **September 2008** | Bradford & Bingley savings business acquired by San UK |
| **October 2008** | Alliance & Leicester acquired by Banco Santander S.A. |
| **January 2009** | Alliance & Leicester plc transferred to San UK. |
| **2010** | Abbey, Bradford & Bingley and Alliance & Leicester rebranded as San UK |

| | |
|---|---|
| **December 2011** | Breakthrough – A programme of funding, business support, events and consultancy which helps high-performing SMEs leap to the next level of sustainable growth, launched. |
| **2012** | Simplification from 14 legacy PCA products to four on-sale products |
| **March 2012** | Launch of our successful 1\|2\|3 Current Account, offering market leading interest rates and cashback on household bills |
| **March 2014** | Launch of our 'Simple, Personal, Fair – what a bank should be', our new campaign |

# Annex B

As stated above, our response is based on our experience as a challenger bank, and does not attempt to deal with all matters discussed in the Issues Statement. Below, we highlight paragraphs in our response that relate to a particular ToH for the CMA's ease of reference. However, we share the CMA's view that the issues are interrelated, and so this table is indicative only.

| Theory of Harm | Our position and paragraph references |
|---|---|
| **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** | Our experience of switching is set out in section 5. General comments are found at:<br><br>5.3; 5.4; 5.9; 5.10; 5.11; 5.12; 5.13; 5.14; 5.15 |
| **1a. lack of accessible and transparent information means that customers do not have the information they need to compare offers or make informed decisions about how they use their existing banking services** | We use accessible and transparent pricing.<br><br>2.7; 2.9; 7.4; 7.6; 7.9 |
| **1b. Product and pricing structures exploit customers' cognitive limitations and behavioural biases and inhibit their ability to compare offers and understand true costs of banking products** | We think it can be difficult for consumers to choose the best account available for them.<br><br>4.12; 5.2; 5.4; 7.5 |
| **1c. Costs and risks of switching and the absence of prompts due to the evergreen nature of banking products, act as a disincentive for consumers to shop around and switch** | We think that consumers are disinclined to shop around, but not only because of these factors.<br><br>4.2; 4.3; 5.4; 5.5; 5.6; 5.8; 5.9; 7.7; 7.8 |
| **2. Concentration giving rise to market power of some banks leading to worse outcomes for customers** | The big four banks have significant incumbent benefits which hamper competition from challengers.<br><br>2.10; 4.9; 4.10; 5.4; 7.14<br><br>Section 6 relates to further market segmentations, which the Issues Statement, at paragraph 45, considered relevant to this Theory of Harm. |

## RESPONSE OF SANTANDER UK PLC TO THE CMA ISSUES STATEMENT

| Theory of Harm | Our position and paragraph references |
|---|---|
| **3. Barriers to entry and expansion leading to worse outcomes for customers** | Our experience is that there are barriers to expansion in the UK retail banking markets. These barriers include and reinforce the market power of the big four.<br><br>2.10; 4.1; 4.2; 4.3; 4.4; 4.6; 4.7; 4.8; 4.9; 4.10; 4.11; 5.4; 6.7; 7.2; 7.3; 7.10; 7.11; 7.12 |