OFFICE OF FAIR TRADING

Anticipated acquisition by Barclays Bank plc of certain assets of ING Direct N.V., including its UK retail savings and residential mortgage businesses

**ME/5746/12**

The OFT's decision on reference under section 33(1) given on 17 January 2013. Full text of decision published 5 February 2013

**Please note that the square brackets indicate figures or text which have been deleted or replaced in ranges at the request of the parties or third parties for reasons of commercial confidentiality.**

## PARTIES

1. **Barclays Bank PLC (Barclays)** is the operating company of the Barclays Group, a UK provider of retail and business banking services, including current account, savings, loans and mortgage services through a network of branches, as well as phone and online banking services.

2. **ING Direct N.V.** (**The Vendor**), headquartered in the Netherlands, is a provider of retail and business banking services in a number of countries in Europe and Australia. It is a wholly-owned subsidiary of ING Group N.V.

3. **ING Direct UK** (**Direct UK**) is a branch of the Vendor, and is a direct banking platform, providing savings and mortgage services to personal customers and savings services to business customers in the UK through online and mobile internet and telephone channels. As at 31 March 2012, Direct UK had mortgages assets of £[ ] billion, savings liabilities of £[ ] billion and [ ] million customers. In the 2011 financial year Direct UK generated UK turnover of approximately £[ ] million.

## TRANSACTION

4. On 9 October 2012, the parties signed an agreement pursuant to which Barclays will acquire certain assets of the Direct UK business (the Target). The Target was offered for sale as an asset and liability transfer under Part

VII of the Financial Services and Markets Act 2000. Direct UK's staff will transfer to Barclays under the TUPE regulations.[1] The ING Direct brand name is not part of the transaction.

5. The transaction was notified to the Office of Fair Trading (OFT) on 1 November 2012. Following receipt of a satisfactory submission on 14 November, the administrative deadline for a decision is 17 January 2013.

## JURISDICTION

6. As a result of this transaction Barclays and Direct UK will cease to be distinct. The UK turnover of Direct UK exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied. The OFT therefore believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

## MARKET DEFINITION

7. The parties overlap in the provision of retail savings/deposit products to personal customers and small and medium-sized business (SME) customers, and in the provision of residential mortgages in the UK.

### Product scope

#### Customer type

8. Barclays submitted that the OFT should not depart from the market definition used in previous cases,[2] which typically segmented the market first by customer type and then by product type. In particular Barclays pointed to the Competition Commission's (CC's) Report on the *Lloyds*

[1] Transfer of Undertakings (Protection of Employment) Regulations 2006.

[2] See Lloyds TSB Group plc and Abbey National plc: A report on the proposed merger, Competition Commission, July 2001;
Anticipated acquisition by Lloyds TSB plc of HBOS plc - Report to the Secretary of State for Business Enterprise and Regulatory Reform , OFT, 24 October 2008; and
Decision by Lord Mandelson, the Secretary of State for Business, not to refer to the Competition Commission the merger between Lloyds TSB Group plc and HBOS plc under Section 45 of the Enterprise Act 2002 dated 31 October 2008. www.bis.gov.uk/files/file48745.pdf .

*TSB/Abbey National* merger in which the CC segmented the banking market into four discrete customer groups:

- financial products sold to personal customers
- financial products sold to SMEs
- financial products sold to larger firms (corporate banking) and
- wholesale banking (such as money market or foreign exchange dealing).

9. No third parties considered the OFT should assess financial products sold to personal customers and SMEs within the same product frame. In the light of the relevant precedent and third parties comments the OFT considers it appropriate to segment the financial services market by customer type, specifically between financial products sold to personal customers and financial products sold to SMEs.

**Product Type**

10. Barclays also submitted that the product frame should be segmented further by product type, specifically into:

- personal savings
- residential mortgages and
- SME savings.

However, it did not consider that any other segmentation was necessary, for example by type of savings or mortgage product, or by distribution channel.

**Financial products sold to personal customers**

11. The CC, in *Lloyds TSB /Abbey National*, segmented the supply of financial services by product type, assessing the impact of the transaction on the supply of savings/deposit products and on mortgages separately. The OFT subsequently followed this approach in *Lloyds/HBOS*. In neither case did the CC or OFT segment further.

**Segmentation by product type**

12. Most third parties believed that personal customers tended to consider their savings and mortgage requirements separately such that they were likely to constitute separate product segments.

13. Some third parties considered that the product segments could be further segmented by specific product type – for example that savings could be segmented into instant access and notice accounts and mortgages could be segmented into fixed rate, variable rate, buy-to-let and 'sub-prime'. However, there was no agreement amongst third parties about how such segmentation should be made – other suggested splits were savings accounts segmented by ISA and non-ISA, and mortgages into purchase and remortgage and owner-occupied and buy-to-let segments. One competitor commented that while such segments may exist, they are unlikely to constitute separate relevant antitrust markets.

14. The OFT does not consider it is necessary to segment the type of financial products and, in line with previous decision practice, has assessed this merger in relation to financial products sold to personal customers into each of savings/deposit products and mortgage products.

**Segmentation by distribution channel**

15. The OFT also considered whether it was appropriate to segment the market by distribution channel, particularly in relation to mortgage products which can be sold either directly to customers or via mortgage brokers. Mortgage brokers typically offer a mortgage from a range of providers and may offer customers independent advice on suitable mortgages. Brokers receive a commission from mortgage providers for each product sold, but are required by law to give impartial advice to customers.

16. In *Lloyds/HBOS*, following the approach taken by the CC in the earlier *Lloyds TSB/Abbey National* case, the OFT did not segment the supply of mortgage products by distribution channel. Barclays submitted that, regardless of whether a mortgage was obtained directly from Barclays or via a broker, there was no difference in the products available to customers. Although it suggested that some providers may vary the products and/or terms available to customers acquiring mortgages via the

broker channel (reflecting the increased customer acquisition costs via the commission paid to brokers).

17. While it is plausible that some customers may see extra value in the range of products and providers offered by mortgage brokers, in addition to ancillary services such as independent mortgage advice, which are not offered directly by providers, it is not immediately clear that this would prevent customers from substituting between brokers and direct providers. The OFT is not aware of any evidence, in this case, of demand-side preferences that support the assessment of the supply of mortgage products via the broker channel as a distinct customer segment. Similarly, while some differences may exist in the range and cost of products available via brokers compared to the direct channel, the OFT is not aware of sufficient evidence in this case that these channels should be treated as separate product segments.

18. In any event, market share estimates provided by mortgage brokers appear consistent with estimates provided by competitors. Therefore, the OFT's substantive assessment is not materially affected whether the market is segmented by distribution channel or not. Consistent with case precedent, neither the parties nor third parties considered it appropriate for the OFT to segment the product market into branch-based banking, telephone banking and online-banking. Accordingly, for the purposes of the assessment in this case, the OFT has not segmented the product frame by distribution channel.

**Financial products sold to SMEs**

19. Barclays submitted that it is appropriate to assess the transaction on the area of overlap between the parties, namely savings/deposit products sold to SMEs.

20. The CC's SME Market Investigation Report[3] considered the SME banking sector to constitute four separate product segments:

- liquidity management services
- general purpose business loans

[3] The supply of banking services by clearing banks to small and medium-sized enterprises: A report on the supply of banking services by clearing banks to small and medium-sized enterprises within the UK, Competition Commission, March 2002

- other types of business loans
- other business deposit accounts held by SMEs.

21. While the OFT recognised this segmentation in its report on *Lloyds/HBOS*, due to the availability of information, it considered the supply of financial products sold to SMEs as a whole.[4] In general, third party competitors agreed that it was most appropriate for the OFT to focus its assessment on the area of overlap – that is, on the supply of savings/deposit facilities to SMEs. However, one commented that, according to British Banking Association data, approximately 50 per cent of overall SME deposits were held in current accounts and 50 per cent in savings accounts, while another told the OFT that it broadly splits its products into liability and asset products, implying that savings/deposit accounts may be part of a broader SME banking product segment.

22. The OFT considers that, in this case, it is appropriate to segment the product scope by broad product type, but not further by specific product characteristics or by distribution channel. It will, therefore, assess the impact of this transaction on the supply of savings/deposit products to SMEs as a distinct product segment.

**Conclusion on product scope**

23. The OFT has not needed to conclude on market definition, as no realistic prospect for a substantial lessening of competition was identified. However, for the reasons outlined above, the OFT has assessed this merger on the basis of:

- savings/deposit products sold to personal customers
- mortgage products sold to personal customers and
- savings/deposit products sold to SMEs.

**Geographic Frame**

24. Barclays submitted that the appropriate geographic frame for all relevant product segments was national in scope, given that both parties advertise nationally, provide national coverage and service, and serve customers in

[4] Paragraph 143, Anticipated acquisition by Lloyds TSB plc of HBOS plc - Report to the Secretary of State for Business Enterprise and Regulatory Reform , OFT, 24 October 2008

all parts of the UK. Barclays also submitted that, as the Target does not have a branch-based network, it is not meaningful to assess the transaction on a regional or local geographic frame.

25. In previous merger assessments and market studies, Northern Ireland has sometimes been excluded from the assessment or has been considered to constitute a separate geographic market, in part due to differences in the supplier base. The Independent Commission on Banking in 2011 assumed that markets were UK-wide given 'the great majority of retail banking products are available to customers across the UK without any difference in characteristics or prices.'[5]

26. In general, all third parties agreed that a UK-wide geographic frame was the most appropriate for assessing this transaction. Although some third parties stated that competitive conditions may vary in specific localities depending on the range of branch-based providers of retail banking services available (for example, in certain regions there may be a greater number of local building societies than in other regions). However, as the Target does not have a branch-based network, the transaction is unlikely to have a variable competitive impact in any specific region or localities within the UK.

27. Other third parties stated it is possible for personal customers and SMEs to obtain savings products from providers based outside the UK, although there wasn't particularly strong evidence in this case to support a geographic frame broader than the UK for any product or customer segment.

**Conclusion**

28. The OFT has not needed to conclude on the geographic frame of reference, as no realistic prospect for a substantial lessening of competition has been identified. However, for the reasons outlined above, the OFT has assessed this merger on the basis of the UK as a whole.

[5] Footnote 4, Chapter 7, www.hm-treasury.gov.uk/d/ICB-Final-Report.pdf

**Conclusion on market definition**

29. The OFT has not needed to conclude on market definition, as no realistic prospect for a substantial lessening of competition was identified. However, for the reasons outlined above, the OFT has assessed this merger with regard to the supply of retail financial products in the UK, segmented as follows:

- savings/deposit products sold to personal customers
- mortgage products sold to personal customers and
- savings/deposit products sold to SMEs.

**COUNTERFACTUAL**

30. The OFT can depart from using the prevailing market conditions as the counterfactual where, based on the evidence available to it, it appears that the prospect of such conditions continuing is unrealistic (that is where there is a realistic prospect of a counterfactual that is more competitive than prevailing conditions).[6]

31. In this case, the OFT understands that the Target had developed plans prior to the transaction to [ ]. The OFT considered therefore whether there was a realistic prospect of a more competitive counterfactual than the pre-existing prevailing conditions of competition. The OFT rarely departs from the pre-existing conditions of competition, and can take into account potential or future competition into its overall competitive assessment in any event. In this case, it does not consider that there is sufficient evidence to depart from the pre-existing conditions of competition as the appropriate counterfactual given that the plans to [ ]. In addition, the Vendor has supplied the OFT with sufficient evidence that it had effectively suspended [ ], importantly, its decision to do so was not determined by the sale of the business to Barclays. Accordingly, the OFT does not consider there is sufficient evidence to conclude that an alternative counterfactual based on [ ] is realistic.

32. Therefore, based on the evidence available, the OFT does not in this case consider it reasonable to adopt a counterfactual other than prevailing market conditions.

[6] Paragraph 4.3.5, Merger Assessment Guidelines, OFT and CC, September 2010

## UNILATERAL EFFECTS

33. Horizontal mergers give rise to unilateral effects where they increase the ability and incentive of merging parties to increase prices or reduce quality or service post-merger. Where products/services are differentiated, as is the case in relation to the supply of financial products and services, unilateral effects are more likely where the products/services compete closely with one another.[7]

34. Barclays submitted that horizontal unilateral effects are unlikely to occur as a consequence of this transaction in any product segment on the basis that the parties are not close competitors, that the market share increment is small or negligible in each segment, that customers will have sufficient choice in the market post-merger, and that barriers to entry and expansion are low.

### Savings/deposit products sold to personal customers

### Market shares

35. Barclays submitted that the parties' combined market share of savings by the value of total deposits in the UK as at 31 August 2012 would be less than 10 per cent, with an increment of [zero-10] per cent.

36. There are a range of competitors in the savings market, and Barclays submitted that its main competitors are Lloyds Banking Group, Santander and Nationwide. The Target stated that it is the twelfth largest savings provider and that a number of other suppliers are larger, including Nationwide, RBS, Co-operative Banking Group, Yorkshire Building Society, Bank of Ireland and Coventry Building Society. Further, Barclays submitted that there are a number of other providers, such as Tesco, the Post Office, insurance companies such as the AA, and the National Savings & Investments (NS&I) which will continue to be a significant constraint on it post-merger. Accordingly, Barclays argued that customers will continue to have significant choice post merger.

37. Barclays provided competitor market share estimates which the OFT has been able to broadly corroborate through its market testing. On the basis of

[7] Section 5,4, Merger Assessment Guidelines, OFT and CC, September 2010

these market share estimates alone, the transaction appears unlikely to give rise to a realistic prospect of an SLC, even taking into account the increases in market shares of both parties in recent years.

38. However, market shares may give a misleading view of the impact of a transaction on competition to the extent that a small market participant is innovative or disruptive such that its impact on competition is greater than its market share implies. In this case, some third parties identified Direct UK as being a 'challenger' brand. The OFT therefore considered the closeness of competition between the parties.

**Closeness of competition**

39. Barclays submitted that, while its product offering is similar, the parties are not close competitors in the supply of savings/deposits products to individuals because:

- Its approach to pricing differs. Barclays submitted that while its approach is to offer consistent rates to its customers, the Target's strategy is to offer very attractive initial rates for an introductory period, after which the rate drops to a lower core level. Barclays submitted that Direct UK's strategy is therefore closer to the Post Office, Virgin Money, Sainsbury's Bank, Nationwide and NS&I.

- Switching data collected by the Target does not show Barclays to be any closer competitor than [major high street retail bank] [major high street retail bank] [major high street retail bank] [ ].

- Direct UK does not appear in Barclays' internal market intelligence to any great extent.

40. Most competitors told the OFT they considered the parties to be close competitors in the supply of savings/deposit products. One commented that they were close only periodically and that there was a disparity in the size of the two suppliers. While two other competitors did not consider the parties to be close competitors. Even where third party competitors stated that they believed the parties were close competitors, they were also able to name a number of other competitors to the parties – for example, one competitor named 10 competitors to the parties in addition to itself.

41. Moreover, some third parties viewed Direct UK as part of a 'second tier' of savings product providers compared to the 'top tier' banks such as Lloyds Banking Group, Santander, HSBC, Nationwide, and NatWest/RBS. For example, one competitor told the OFT that Direct UK faced additional competition from 'challenger brands' whereas Barclays did not. A two tier market is common to many retail banking markets, where the large established providers tend to compete on service given their branch network costs and other challenger banks will compete on price and service, if challengers (collectively) start attracting too many customers, the established providers then respond on price/rate, even if only for a short time.[8]

42. The OFT understands that Direct UK consistently featured in lists of the top savings providers since its launch in the UK. However, Direct UK provided the OFT with evidence that, [ ]. The OFT understands further that [ ], discussed below, [ ]. By contrast, the OFT was told by a number of customers that Barclays rarely featured in lists of the top savings providers.

43. Of the 96 respondents to the OFT's web survey for savings customers, 58 stated that they believed the transaction would result in a 'very significant reduction in competition' or a 'material reduction in competition'. However, only seven of these respondents claimed that switching providers was either 'somewhat difficult' or 'very difficult'. Many of the concerns expressed by these respondents related to whether Barclays would maintain its existing interest rate date, the reduction in available Financial Services Compensation Scheme Compensation available to customers, or to the recent negative publicity surrounding the conduct of Barclays in the marketplace. Accordingly, the OFT does not consider responses from end customers indicate strong support for the potential for an SLC in relation to the supply of savings/deposit service to individuals.

**Customer switching**

44. Barclays submitted that customers can and do open a number of savings accounts and that the costs to them of switching savings between accounts and providers is low.

[8] The role of Challenger Banks is discussed at paragraphs 126 to 135, Anticipated acquisition by Lloyds TSB plc of HBOS plc - Report to the Secretary of State for Business Enterprise and Regulatory Reform , OFT, 24 October 2008

45. Barclays supplied internal documents to the OFT which showed its strategy for the Target's savings book post-merger. Based on its experience of integrating Standard Life's business[9], Barclays estimates that this strategy will result in approximately [ ] per cent of the savings business by value switching to alternate providers. The majority of the remaining [ ] per cent are already on Direct UK's lowest interest rate. [ ].

46. Of the 96 respondents to the OFT's web survey, only 12 stated that switching savings provider was either 'somewhat difficult' or 'very difficult', although 10 of these respondents stated they already had 'three or more' savings products and four of these respondents stated that their main savings account was held with a provider other than the parties. Indeed, a number of respondents told the OFT that they had already switched their savings to an alternate provider as a consequence of the announcement of the transaction, or were intending to do so.

47. This was supported in third party market testing to a degree. One third party, for example, said that the Target had a reputation for attracting price savvy customers and that it would expect these customers to switch to an alternate provider post-merger should the terms become less favourable to them. However the Independent Commission on Banking concluded that levels of switching were, in general, low despite switching by savings customers occurring with higher frequency than for PCA customers (around five per cent of customers surveyed had switched savings accounts in the last 12 months compared to around three per cent of PCA customers[10]).

**Conclusion**

48. The OFT considers that the transaction will not result in a realistic prospect of an SLC in respect to the supply of savings/deposit products to individuals because:

- The parties' combined market share is less than 10 per cent, with an increment of around [zero to 10] per cent. Accordingly, the transaction will have a limited structural impact on the market.

[9] In 2009, Barclays acquired the banking arm of Standard Life, comprising a portfolio of savings and mortgage products.
[10] Figure 7.3, Final Report, Independent Commission on Banking, September 2011

- While the parties offer similar products, there are a number of alternate providers remaining in the market post-merger, including several large banks, building societies and newer 'challenger' brands.

- Despite historically being viewed as a 'challenger' brand, the Target has [ ].

- In general, customers appear aware of available interest rates and levels of switching appear higher than for PCAs. Some customers of the Target have already switched their savings to alternate providers, and Barclays anticipates the majority will do so should they move customers onto its base rate.

**Mortgage products sold to personal customers**

**Market shares**

49. Barclays submitted that the parties' combined market share of total outstanding mortgage lending for 2011 would be [zero-10] per cent, with an increment of less than [ ] per cent.

50. Barclays further submitted that the mortgage market is characterised by a number of competitors, most or all of which offer a range of products including fixed and tracker mortgages, and that a broad range of competitors will remain post-merger. Barclays claims it is [one of the top four] providers of mortgages in the UK and that Direct UK is the fourteenth largest. The parties provided estimates of competitor's market shares, which were broadly corroborated by the OFT's market testing.

51. The OFT also considered the movement of the parties' market shares over several years. [ ]. [ ]. [ ]. [ ].[11]

52. On the basis of market share estimates alone, the transaction appears unlikely to give rise to a realistic prospect of an SLC, even taking into account the increases in market shares of both parties in recent years. In this case, as in the supply of savings/deposits products to individuals, some third parties have identified Direct UK as being a 'challenger' brand.

[11] In addition, [ ].

The OFT has therefore considered the closeness of competition between the parties.

**Closeness of competition**

53. Barclays submitted that the parties are not particularly close competitors in the supply of residential mortgage products for a number of reasons:

- Their strategies are different: Direct UK focuses on products with preferential rates at commencement, which then revert to standard variable rates, whereas Barclays offers 'lifetime' rates which track the bank's base rate.

- Barclays offers an extensive range of mortgage products, whereas Direct UK offers a more basic mortgage product range.

- The profile of new business differs between the parties: Direct UK's mortgage book is approximately [ ] per cent refinancing and [ ] per cent new purchases, whereas Barclays has historically maintained a portfolio of approximately [ ] per cent refinancing and [ ] per cent new purchases.

- The parties do not appear particularly strongly in internal switching and competitor monitoring documents.

54. Third parties generally agreed that the parties were not each other's closest competitor in the supply of residential mortgages, but that they were amongst a number of similar providers. However, two competitors told the OFT that the 'big six' could be viewed separately to the fringe of competition from smaller banks and building societies, with Barclays in the former and Direct UK in the latter. Another third party stated that the Target was only 'periodically' competitive with Barclays.

55. Barclays supplied internal documents to the OFT which showed its strategy for the Target's mortgage book post-merger. Barclays estimates that [ ] per cent of Direct UK's two-year tracker mortgage customers will switch to an alternate provider on maturity and that around [ ] per cent of customers on Direct UK's lifetime tracker will switch providers each year following completion of the transaction. Accordingly, Barclays anticipates that a high proportion of Direct UK's existing customer base will switch to alternate

providers at the end of their existing deals. This will obviously reduce the market share increment Barclay's will acquire as a consequence of the transaction over time, other things equal.

56. Mortgage brokers had mixed views on the parties closeness of competition, with one commenting that while the loss of a lender in a market short of capacity would be a blow, in reality, ING Direct were only evident in the market for a short period of time and only accounted for around three per cent of the overall market – and did this in mainstream parts of the market. As such, whilst very disappointing, the impact on both consumers and distributors of the merger would be relatively limited.

57. However, other brokers felt that the parties competed closely; in particular on certain types of products, for example in the term tracker market. Commenting that there have been times where the two lenders have been in direct competition and seeking to differentiate their propositions to attract different types of clients.

58. In previous merger assessments and market studies, customers have been found to be more likely to switch mortgage provider compared to switching other types of financial service. The OFT has not seen evidence in this case which would contradict that finding.

59. The OFT received responses from 10 end-customers via its web survey, all of which appeared to be Direct UK customers. Most respondents stated mortgage interest rates were the most important factor to them in choosing a provider. Most of the respondents had concerns with the transaction, but many of these concerns related to whether the terms of their existing mortgage would be continued post-transaction. Of the 10 respondents, only three stated that switching provider was 'somewhat difficult' or 'very difficult'.

**Conclusion**

60. The OFT considers that it is unlikely the transaction will result in a realistic prospect of an SLC in respect to the supply of mortgage products to personal customers because:

- The parties' combined market share is less than 10 per cent, increment less than [ ] per cent. Accordingly, the transaction will have a limited structural impact on the market.

- While the parties offer similar products, there are a number of alternate providers that will remain in the market post-merger, including several large banks in addition to building societies. Barclays has a broader product range than Direct UK.[12]

- Customers and competitors were generally not concerned by the transaction. Switching does not appear particularly difficult compared to other types of financial services product, and Barclays anticipates high outflows of customers upon maturity of existing Direct UK customers' deals.

- While the Target has grown relatively rapidly in recent years, [ ]. Absent the merger, the OFT understands [ ]. Therefore the Target is competing less strongly in the marketplace compared to recent years.

**Savings/deposits sold to SMEs**

61. Barclays submitted that the parties would have a combined market share of SME deposits in the UK of a level that would not usually give rise to competition concerns, and that the increment is small (even taking into account the fact the Target's product offering was only launched in 2012).

62. Barclays stated that its share of the SME savings/deposits market is approximately [10-15] per cent, based on balances of £[ ]billion and a total market size of £69billion (Bank of England). Barclays offers SME banking services to companies with turnover of up to £25million. The Target launched its SME savings/deposit product offering SME banking services to companies with turnover of up to £5million in May 2012. To 5 October 2012, it had opened [ ] accounts with deposits totalling £[ ] million. Accordingly, its share of the market is estimated at being [zero-five] per cent. Barclays submitted that Experian estimates the total size of SME

[12] The OFT notes that certain of the internal documents provided to it by Direct UK reference the potential launch of a [ ]. The OFT has not seen evidence that such plans were sufficiently developed to consider this as part of its substantive assessment.

banking deposits to be £[ ]billion, which would result in smaller market shares for both parties.

63. Given the Target's SME banking offer is nascent, the OFT has also considered its internal projections at likely market share. Internal documents provided to the OFT show that the Target planned on obtaining deposits with a value of £[ ] billion within five years. This would account for around [zero-five] per cent of the market using Bank of England data and assuming no growth in the size of the market in the meantime.

64. On the basis of market share estimates alone, the transaction appears unlikely to give rise to a realistic prospect of an SLC, even taking into account the increases in market shares of both parties in recent years.

65. The OFT understands from internal documents provided by Direct UK that its strategic rationale for launching an SME savings product was [ ].[13] [ ]. [ ]. Further, the OFT understands that Direct UK targeted its proposition [ ]. Direct UK's customer acquisition strategy meant that Direct UK was not actively competing for deposits worth around [40-50] per cent of the total SME savings/deposits market.[14]

66. Third party competitors were not concerned by the impact of the transaction on the supply of savings/deposit products to SMEs. Three third party competitors did not think the parties competed closely with each other, citing Handelsbanken, Aldermore and Metrobank as close competitors to the Target, whereas Santander, HSBC, RBS, the Co-Operative and Clydesdale were considered closer competitors to Barclays. Other third parties considered ING a minor player in the market, such that there was unlikely to be much of a competitive impact as a consequence of the transaction.

67. The OFT received responses from two SME banking customers. One told the OFT that Barclays offers good current account facilities, but that its interest rate on positive balances was too low. This customer felt that Direct UK had made a positive impact in the marketplace for deposits (but

[13] [ ].

[14] However, there were no restrictions on the customers representing these [40-50] per cent of deposits from opening an account. Rather, they did not form part of the Direct UK's marketing effort.

noted that even Direct UK's savings rate was below the rate of inflation). The second customer appeared less concerned with the transaction, but hoped that the savings rate offered by Direct UK would be maintained by Barclays.

68. While the OFT notes the concerns of the first customer, it considers that the SME customers most likely to have opened an SME deposit account with the Target since May 2012 are those customers most likely to switch provider in the marketplace (and, indeed, have done so recently). Accordingly, it is plausible that these customers would consider alternate providers in the event of a deterioration of their terms post-merger. In any event, such customers represent only a very small proportion of the total SME deposit market.

**Conclusion**

69. The OFT considers that the transaction will not result in a realistic prospect of an SLC in respect to the supply of savings/deposit products to SMEs because:

- The Target's product is very new and it is expected to achieve limited market share within five years of launch. The combined market share of the parties will be no more than [10-15] per cent, with a [zero-five] per cent increment. Accordingly, the transaction will have a limited structural impact on the market. This is notwithstanding the conclusions of the CC's SME banking review and the Independent Commission on Banking Report, which found that the market did not work well for SME customers.

- While their savings/deposit products are similar, the parties are not close competitors in the full range of services offered to SMEs. The Target's savings/deposit offering is likely to have had a small competitive impact on the broader SME banking marketplace given customer preference for a single provider of the full range of SME banking services.

- Customers and competitors were generally not concerned by the transaction, although some noted that the market generally exhibits low levels of competition.

**Barriers to entry and expansion**

70. When assessing possible supply-side responses, including entry, expansion and repositioning, the OFT will consider whether the response would be timely, likely, and sufficient.[15] In terms of timeliness, the guidance suggests that the OFT will look for entry to occur within two years.

71. In *Lloyds/HBOS*, the OFT considered that barriers to entry in the mortgage market had increased as a consequence of the financial crisis, in contrast to the CC's finding in *Lloyds/Abbey National*. The CC found in its review of SME banking that barriers to entry were high, and included factors such as establishing a branch network and reputation. The OFT found in its Review of barriers to entry, expansion and exit in retail banking that new entrants face significant challenges in attracting customers and expanding their market shares.[16]

72. The Independent Commission on Banking found that:

- There had been 19 new entrants to the savings market since 2000, achieving around five per cent market share by 2010.

- There had been 16 new entrants to the mortgage market since 2000, achieving around two per cent market share by 2010 (although the share of new entrants had been as high as four per cent prior to the financial crisis).

- Lack of branch network was a significant barrier to expansion given consumers' preferences.

73. Barclays submits that, in this case, the barriers to entry are surmountable:

- In the supply of residential mortgage products, Barclays submits the conditions which were present in 2008 have eased with the consequence that switching has increased. Barclays quotes FSA figures that the number of mortgage 'provider firms' increase by 10.4 per cent

[15] Paragraph 5.8.3, Merger Assessment Guidelines, OFT and CC, September 2010.
[16] Review of barriers to entry, expansion and exit in retail banking, OFT1282, November 2010.

in 2011/12 to 137[17] and that the recent entry of Tesco and Metro Bank are evidence that barriers to entry and expansion are surmountable.

- In the supply of savings/deposit products to individual, Barclays submits that there are numerous examples of new entry from a range of players indicating that barriers are not significant.

- Barclays did not provide comments on the ease of entry or expansion in the supply of savings/deposits products to SMEs.

74. The OFT was sceptical of the examples of entry provided by the parties. In general, most new entrants have partnered with an existing financial services provider (for example, M&S Bank partnering with HSBC). Tesco Bank is an example of a financial institution that launched as a joint venture with an existing financial services provider, but has since become fully independent. Evidence of Greenfield entry is rare – the only example of de novo entry in recent years is Metrobank in the South East of England.

75. Most third party competitors highlighted the requirement to have an FSA licence as the primary barrier to supplying savings/deposits and mortgage products, although one third party stated that the acquisition of an existing licence holder made entry easier to a degree. Another highlighted what it perceived to be a tension between the desire for more competition amongst providers and the desire to ensure the regulatory suitability of licence holders.

76. Most third parties told the OFT that barriers to supply savings/deposits products were lower than for the supply residential mortgages. With one commenting that the barriers were 'primarily regulatory and capital', and suggested that new entrants could partner with an existing provider with the appropriate regulatory approvals. Another said that organic expansion was not easy except when partnering with an existing provider, due to the need for a strong customer base and a deposit-taking licence. While a third

[17] The OFT notes that the FSA report which Barclays quotes these figures from states "In the period 2011/12, in line with the observed increase in the number of mortgage sales, there has been a rise in both the number of selling firms (which rose by 0.8 per cent to 7,706) and of provider firms (which rose by 10.4 per cent to 137), although both remain well below their long-term average." Mortgages, Product Sales Data (PSD) Trend Report 2005-2012, FSA, August 2012

said that membership of the Financial Services Compensation Scheme was a 'leveller' in terms of trust amongst consumers for deposit-taking.

77. However, third party competitors in general told the OFT that barriers to entry in the supply of residential mortgages were high. With comments such as: that entry could be slow, expensive and time consuming and that 'the Bank of England's 'Funding for Lending Scheme' allows established institutions access to cheap funding, which can make it harder to compete.' Or that entry since 2007 has 'become substantially more difficult', and that the lack of wholesale funding resulted in a substantial drop in the number of independent providers. With 'any new entrant seeking to build a mortgage balance sheet through traditional means requiring sophisticated credit risk systems, infrastructure and sufficient capital resources to support its business.'

78. However, one third party competitor disagreed. Commenting that the mortgage segment was highly competitive with low barriers to entry or expansion, highlighting the intermediary market as being a channel through which new entrants could achieve scale, accounting for around 50 per cent of all product sales.

79. In relation to entry and expansion in the supply of savings/deposits products to SMEs, the same competitor considered both entry and expansion relatively easy providing the supplier has FSA Part 4 permissions, citing the entry of ING, Metrobank and Aldermore and the expansion of Santander in this product segment. Another third party agreed that entry and expansion were 'relatively easy'. While a third said that while there has been some new entry, 'it was difficult for new entrants to achieve critical mass as the large banks have stronger, more established brands and better distribution networks.' However, these comments contrast with the OFT's findings in relation to SME banking in its review of barriers to exit, entry and expansion in retail banking in 2010.

80. The OFT is not aware of any planned entry in any of the relevant product markets within the next two years.

81. However, as no competition concerns arise in any of the relevant product markets, it has not been necessary to conclude on the likelihood of entry or expansion.

## THIRD PARTY VIEWS

82. Third party views have been referred to above where relevant. In general, third party competitors did not raise competition concerns in relation to the transaction. The OFT received comments on the transaction from nine competitors of the parties, and three mortgage brokers.

83. To obtain views from end customers, the OFT requested the parties place links prominently on their savings and mortgage product websites to web surveys hosted by the OFT. The survey and links were active for a period of ten days during the market testing phase. The OFT received 98 responses to its savings survey and 10 responses to its mortgages survey.

84. In addition, the OFT received three responses to its Invitation to Comment (ITC). Of these, two were from customers of the parties and one was from a competitor.

## ASSESSMENT

85. The parties overlap in the provision of retail savings/deposit products to personal customers and small and medium-sized business (SME) customers, and in the provision of residential mortgages in the UK.

86. For the reasons discussed above at paragraphs 9 to 29, the OFT has assessed this merger with regard to the supply of retail financial products in the UK, segmented as follows:

- savings/deposit products sold to personal customers
- mortgage products sold to personal customers and
- savings/deposit products sold to SMEs.

87. Based on the evidence available, rehearsed at paragraphs 30 to 32, the OFT has not adopted a counterfactual other than prevailing market conditions.

### Savings/deposit products sold to personal customers

88. The parties' combined market share is less than 10 per cent, with an increment of around [zero to 10] per cent. Accordingly, the transaction will

have a limited structural impact on the market. The parties offer similar products, however, there are a number of alternate providers remaining in the market post-merger, including several large banks, building societies and newer ‘challenger’ brands. Despite historically being viewed as a ‘challenger’ brand, the Target has modified its business strategy in recent years to focus on less rate-sensitive customers and is therefore competing less strongly in the marketplace compared to when it launched in the UK.

89. In general, customers appear aware of available interest rates and levels of switching appear higher than for PCAs. Some customers of the Target have already switched their savings to alternate providers, and Barclays anticipates the majority will do so should they move customers onto its base rate.

**Mortgage products sold to personal customers**

90. The parties’ combined market share is less than 10 per cent, increment less than [ ] per cent. Accordingly, the transaction will have a limited structural impact on the market. While the parties offer similar products, there are a number of alternate providers that will remain in the market post-merger, including several large banks in addition to building societies.

91. Customers and competitors were generally not concerned by the transaction. Switching does not appear particularly difficult compared to other types of financial services product, and Barclays anticipates high outflows of customers upon maturity of existing Direct UK customers’ deals.

**Savings/deposits sold to SMEs**

92. The parties’ combined market share will be no more than [10-15] per cent, with a [zero - five] per cent increment. Accordingly, the transaction will have a limited structural impact on the market. This is notwithstanding the conclusions of the CC’s SME banking review and the Independent Commission on Banking Report, which found that the market did not work well for SME customers.

93. While their savings/deposit products are similar, the parties are not close competitors in the full range of services offered to SMEs. The Target’s savings/deposit offering is likely to have had a small competitive impact on

the broader SME banking marketplace given customer preference for a single provider of the full range of SME banking services.

94. Customers and competitors were generally not concerned by the transaction, although some noted that the market generally exhibits low levels of competition.

95. Most third parties told the OFT that barriers to supply savings/deposits products were lower than for the supply residential mortgages. With one commenting that the barriers were ‘primarily regulatory and capital.’ However, as no competition concerns arise in any of the relevant product markets, it has not been necessary to conclude on the likelihood of entry or expansion.

96. The parties do not appear particularly close competitors in any of the product segments in which they overlap and the market share increments are low or negligible. While the Target has a reputation in the UK for being a ‘maverick’ brand, it is not clear, based on the evidence available, that the competitive dynamic in any product segment will be materially affected by the transaction.

97. Consequently, the OFT does not believe that it is or may be the case that the merger may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

## DECISION

98. This merger will therefore **not be referred** to the Competition Commission under section 33(1) of the Act.