

# Anticipated acquisition by OneSavings Bank plc of Charter Court Financial Services Group plc

## Decision on relevant merger situation and substantial lessening of competition

ME/6819/19

Please note that [X] indicates 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.

### SUMMARY

1. OneSavings Bank plc (**OSB**) announced a public offer (subject to the Takeover Code) to acquire Charter Court Financial Services Group plc (**Charter Court**) (the **Merger**). OSB and Charter Court are together referred to as the **Parties**.
2. The Competition and Markets Authority (**CMA**) believes that it is or may be the case that each of OSB and Charter Court is an enterprise; that these enterprises will cease to be distinct as a result of the Merger; and that the turnover test is met. Accordingly, arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.
3. The Parties primarily overlap in the supply of buy-to-let (**BTL**) mortgages<sup>1</sup> in Great Britain (**GB**).<sup>2</sup> The CMA has assessed the Merger with reference to BTL customer segments based on evidence that customers in different segments of BTL lending have particular needs. The CMA observed that, while the Parties and most of their competitors operate across different customer

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<sup>1</sup> A BTL mortgage is one specifically designed for when the borrower's intent is to rent the property out after purchase.

<sup>2</sup> The Parties also overlap in other financial services including the supply of owner-occupier mortgages, second charge mortgages, bridging loans and savings products to personal customers. The Parties' involvement in the supply of owner-occupier mortgages, second charge mortgages and savings products is discussed in paragraph 32; and the Parties' involvement in the supply of bridging loans is discussed from paragraph 26 onwards.

segments, there were differences in margins, variation in the identity and shares of competitors, and some evidence that there were barriers to quick and easy shifting of capacity between customer segments. The CMA has therefore assessed the impact of the Merger in the supply of BTL mortgage lending overall in GB, and in the following frames of reference:<sup>3</sup>

- (a) Supply of BTL mortgage lending in GB on Homes in Multiple Occupation (**HMOs**);
- (b) Supply of BTL mortgage lending in GB to limited company landlords;
- (c) Supply of BTL mortgage lending in GB to portfolio landlords; and
- (d) Supply of BTL mortgage lending in GB to expat landlords.<sup>4</sup>

4. The evidence (including internal documents and third party evidence) showed that the Parties are close competitors in the supply of BTL mortgage lending in general and within each of the frames of reference identified in (a) – (c) above. In particular, the Parties offer a similar service and are two of the largest competitors active in supplying BTL mortgages to limited company landlords and on HMOs.
5. However, the CMA found evidence that several other lenders of a similar size and with a similar product offering are also close competitors to the Parties and are therefore able to provide a strong competitive constraint in all of the frames of reference considered. The evidence also suggested that the development of the BTL customer segments considered by the CMA is relatively recent and competition within these segments is dynamic in nature, with smaller lenders able to compete for customers against larger lenders because of the distribution of products through intermediaries. There is also evidence that lenders that are already active in certain BTL customer segments have been able to enter or expand into new customer segments relatively quickly, subject to their risk appetite.
6. During its investigation, the CMA saw some evidence to suggest the possibility of a more competitive counterfactual in BTL mortgage lending to expat landlords than the current competitive conditions. The CMA considered whether, absent the Merger, Charter Court might have entered this customer segment, and whether that entry would lead to greater competition such that the Merger would result in a loss of actual potential competition.<sup>5</sup> The CMA

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<sup>3</sup> For definitions of the terms used in the frames of reference, see paragraph 39.

<sup>4</sup> The Parties do not currently overlap as Charter Court does not currently offer BTL mortgages to expat landlords, but the CMA observed internal documents suggesting it may enter this customer segment.

<sup>5</sup> This theory of harm is discussed at paragraph 118 onwards.

found that, even if Charter Court were to enter this segment, the Merger would not result in a loss of competition because there is already sufficient competition for these customers and the evidence showed that some other lenders have recently entered, or were planning to enter or expand to serve these customers in the foreseeable future.

7. The CMA believes that the constraints from other lenders in each of the frames of reference are sufficient to ensure that the Merger does not give rise to a realistic prospect of a substantial lessening of competition (**SLC**) as a result of horizontal effects.
8. The Merger will therefore **not be referred** under section 33(1) of the Enterprise Act 2002 (the **Act**).

## ASSESSMENT

### Parties

9. OSB is a UK-listed group active in the provision of specialist lending and retail savings services in the UK. It conducts its activities through a number of trading brands including: (i) Kent Reliance (OSB's main lending business and saving branch operator);<sup>6</sup> (ii) InterBay Commercial (a specialist commercial mortgage lender); and (iii) Prestige Finance (a second charge lender).<sup>7</sup> OSB's total turnover in 2018 was £287.3m, with £280.1m generated in the UK.<sup>8</sup>
10. Charter Court is a UK-listed group active in the provision of specialist lending and retail savings services in the UK. It conducts its activities through three main brands: (i) Precise Mortgages (which is active in BTL mortgages, specialist residential mortgages, second charge loans and bridging loans); (ii) Charter Savings Bank (which provides retail savings products); and (iii) Exact Mortgage Experts (which provides mortgage administration services). Charter Court's total turnover in 2018 was £283.5m, all of which was generated in the UK.

### Transaction

11. On 14 March 2019, the boards of OSB and Charter Court announced that they had reached agreement on the terms of the Merger, by which OSB will acquire the entire share capital of Charter Court. Completion of the Merger is

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<sup>6</sup> OSB operates retail branches in the South East of England.

<sup>7</sup> Second charge lending is where a customer secures a second loan against their property for additional capital, typically at a higher rate to account for the additional risk to the lender.

<sup>8</sup> It also operates Heritable Development Finance (specialist development finance provider), InterBay Asset Finance (hard asset finance provider), and osblIndia (office support in India).

conditional on approval by OSB's shareholders and regulatory approval from the CMA.

12. The Parties submitted that their rationale for the Merger is to create a leading specialist mortgage lender in the UK with greater scale and resources to explore further organic and inorganic growth opportunities. They stated the Merger would bring together complementary product and underwriting capabilities for a better customer proposition and a more diversified platform, and would lead to cost synergies.

## Procedure

13. The Merger was considered at a Case Review Meeting.<sup>9</sup>

## Jurisdiction

14. Each of OSB and Charter Court is an enterprise. As a result of the Merger, these enterprises will cease to be distinct.
15. The UK turnover of Charter Court exceeds £70 million, so the turnover test in section 23(1)(b) of the Act is satisfied.
16. The initial period for consideration of the Merger under section 34ZA(3) of the Act started on 5 June 2019 and the statutory 40 working day deadline for a decision is therefore 30 July 2019.

## Counterfactual

17. The CMA assesses a merger's impact relative to the situation that would prevail absent the merger (ie the counterfactual). For anticipated mergers the CMA generally adopts the prevailing conditions of competition as the counterfactual against which to assess the impact of the merger. However, the CMA will assess the merger against an alternative counterfactual where, based on the evidence available to it, it believes that, in the absence of the merger, the prospect of these conditions continuing is not realistic, or there is a realistic prospect of a counterfactual that is more competitive than these conditions.<sup>10</sup>
18. The Parties submitted that the appropriate counterfactual against which to assess the Merger is the current competitive conditions. In this case, the CMA

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<sup>9</sup> See *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), January 2014, from paragraph 7.34.

<sup>10</sup> *Merger Assessment Guidelines* (OFT1254/CC2), September 2010, from paragraph 4.3.5. The *Merger Assessment Guidelines* have been adopted by the CMA (see *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), January 2014, Annex D).

has considered the prevailing conditions of competition to be the relevant counterfactual for its competitive assessment within the frames of reference where there is an actual overlap between the Parties (ie BTL mortgage lending in general and BTL mortgage lending to limited company landlords, portfolio landlords, and on HMOs).

19. During its investigation, the CMA saw some evidence to indicate that, absent the Merger, Charter Court might have entered the expat landlord customers segment. This scenario is more competitive than the prevailing conditions of competition. Consistent with its standard practice,<sup>11</sup> the CMA has assessed the impact of the Merger in the supply of BTL mortgages to expat landlords against a counterfactual in which Charter Court is active in this frame of reference (see paragraph 118 onwards). However, for the purposes of the present case, the conclusion on whether or not this is the appropriate counterfactual can be left open as no competition concerns arise under any plausible basis.

## **Background**

20. The Parties are both retail banks with lending activities. They offer saving and deposit products to individuals and these are the primary source of funding for their lending activities. The rest of their lending is funded by wholesale capital markets. Their main lending activity is mortgages, and more specifically, BTL mortgages. BTL lending represents the largest part of each of the Parties' business (72% of OSB's and 68% of Charter Court's loan book at 31 December 2018). Residential owner-occupied mortgage lending represents the second largest business area for the Parties (17% and 33% of OSB and Charter Court's loan book at 31 December 2017).
21. There is a wide variety of lenders active in mortgage lending. This includes mainstream lenders, such as high-street banks and building societies, and specialist lenders. Specialist lenders are active in areas where customers may be relatively underserved (eg customers where mainstream lenders are less active) and may include customers that are more complex to serve (eg those with complex income streams) or customers where lending is riskier (eg those with adverse credit history). Specialist lenders can either be banks (funded mainly through deposits such as the Parties and a number of their competitors such as Aldermore, Paragon, and Axis Bank) or non-banks (funded mainly through capital markets such as Foundation Home Loans, Kensington, and Vida Homeloans; these companies also compete against the Parties).

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<sup>11</sup> See [Mergers: Guidance on the CMA's jurisdiction and procedure](#) (CMA2), January 2014, paragraph 4.3.5.

22. The Parties' BTL products are distributed through intermediaries such as brokers who also offer mortgage advice. The role of intermediaries in this sector is to act as a link between end-users (ie borrowers) and lenders and typically advise borrowers on the choice of available products based on their requirements and qualifying criteria. Intermediaries typically pursue a 'whole market approach'; that is, the ability to offer a full suite of mortgage products covering both mainstream and specialist lenders. In recommending potential lenders to a customer seeking a mortgage, the CMA understands that intermediaries typically prioritise customers' needs and requirements (ie which lenders have lending criteria that the customer will meet and offer the appropriate level of flexibility), then price, followed by service (ie which lender will accept and process the application quickly). Intermediaries are remunerated through fees paid by the borrower and/or commission fees paid by the lender. Intermediaries for both OSB and Charter Court are generally remunerated by way of a procuration fee paid by the Parties calculated as a percentage proportion of the relevant loan value.

## Frame of reference

23. Market definition provides a framework for assessing the competitive effects of a merger and involves an element of judgement. The boundaries of the market do not determine the outcome of the analysis of the competitive effects of the merger, as it is recognised that there can be constraints on merging parties from outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others. The CMA will take these factors into account in its competitive assessment.<sup>12</sup>
24. The Parties overlap primarily in the supply of BTL mortgages in GB. The Parties also overlap in the supply of owner-occupier mortgages, bridging loans, second charge mortgages, and savings products to personal customers.<sup>13, 14</sup>

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<sup>12</sup> [Merger Assessment Guidelines](#), paragraph 5.2.2.

<sup>13</sup> Charter Court is also active in mortgage administration services, which is an upstream service whereby it conducts administrative functions such as payment processing, statement production, arrears management and general customer service, on behalf of other lenders. Given Charter Court's immaterial presence in these services, the CMA has not needed to consider these services further as no competition concerns could arise.

<sup>14</sup> Both Parties offer savings and deposit products (such as fixed rate bonds, notice accounts, easy access accounts and ISAs), which are used to fund their lending activities. The Parties have an estimated share of supply of [0-5]% in savings and deposits and the CMA has not received third party concerns in relation to the supply of these services. Accordingly, the CMA does not believe the Merger raises prima facie competition concerns in relation to these products and has not examined the effects of the Merger in the supply of these products in this decision.

## **Product scope**

25. The Parties submitted that the relevant frames of reference should be mortgage products sold to personal customers and other loans sold to personal customers (such as bridging loans) but acknowledged that mortgage products may be differentiated by product type (owner-occupied, BTL, second charge mortgages), customer type (such as prime customers),<sup>15</sup> or type of lender (specialist or mainstream eg a high-street bank).

## **Bridging loans**

26. Bridging loans offer short term access to funds at a typically higher rate of interest than mainstream lending and can be used, for example, when a customer is required to complete a purchase before selling their existing home, or where the customer is purchasing and renovating a property for a quick sale.
27. The Parties submitted that bridging loans could be considered separately from mortgage lending as they typically have a higher rate of interest and are used in different circumstances. The Parties also submitted that OSB supplies only unregulated bridging loans (secured against a property that will be used for development or commercial purposes) whereas the majority of Charter Court's activity relates to regulated bridging loans (secured against a property that will soon be occupied by the owner).
28. The CMA and its predecessors have not previously considered bridging loans, although in *Lloyds TSB/Abbey National*<sup>16</sup> a separate market was identified for loans other than mortgages to personal customers in the UK.
29. In this case, the CMA observed evidence suggesting different competitive conditions for bridging loans compared to other mortgage lending, including different competitor sets, different prices, and differences in the level of regulation. The CMA also observed similar evidence suggesting different competitive conditions for regulated and unregulated bridging loans. The CMA has not had to conclude on whether to segment bridging loans into regulated and unregulated loans as no competition concerns arise under any plausible basis, given the availability of a range of alternative lenders including

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Both Parties also offer second charge lending. The Parties have an estimated share of supply of [5-10]% in second charge lending in the UK in 2018, and there are a large number of alternative lenders. On this basis, the CMA does not believe the Merger raises significant competition concerns in relation to second charge lending and has not examined the effects of the Merger in the supply of these products in this decision.

<sup>15</sup> A 'prime' customer is a customer with no adverse credit history.

<sup>16</sup> [Lloyds TSB/Abbey National \(2001\)](#)

challenger banks and non-bank specialist lenders, and the Parties' moderate shares of supply.<sup>17</sup>

### *Mortgage lending*

30. In past cases,<sup>18</sup> the CMA's predecessor organisations have treated all mortgages as a single frame of reference. In all of those cases the focus was on residential owner-occupied mortgages.
31. In the context of this investigation, the CMA received evidence that it is appropriate to treat owner-occupied and BTL mortgages separately. Firstly, customers are unable to switch between the two as, typically, a customer with an owner-occupied mortgage is not able to rent out a property under the terms of that mortgage. Additionally, the CMA found evidence showing differences in the competitive conditions between BTL and owner-occupied mortgages and also differences in the levels of regulation (with BTL generally not being regulated by the Financial Conduct Authority (**FCA**)). The Parties' internal documents clearly consider these two types of mortgages separately,<sup>19</sup> and third parties also confirmed that there are many differences between owner-occupied mortgages and BTL that limit the extent to which mortgage providers would quickly and easily shift capacity between them. One such point was that some mainstream banks are reluctant to enter BTL lending because it may not fit with their risk appetite.
32. The Parties estimated that they have a combined share of supply in lending originated<sup>20</sup> in 2018 on owner-occupied residential mortgages of less than [0-5]%, with many alternative lenders active in serving these customers. No third parties expressed concerns in relation to the effects of the Merger in owner-occupied residential mortgages. Given that the evidence available indicates that the Merger does not give rise to prima facie concerns in the supply of owner-occupied residential mortgages, the CMA has not examined residential owner-occupied residential mortgage lending further in this decision.

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<sup>17</sup> The Parties estimate they have a share of supply in bridging loans of [10-20]% and a share of supply in unregulated bridging loans of no higher than [10-20]%.

<sup>18</sup> Competition Commission case of [Lloyds TSB/Abbey National \(2001\)](#), and the Office of Fair Trading (**OFT**) cases of [Nationwide/Cheshire Building Society \(2008\)](#), [Lloyds TSB/HBOS \(2008\)](#), chapter IX, and [Barclays/ING Direct N.V. \(2013\)](#), par. 13-14. In [Barclays/ING Direct](#), the OFT cited third party responses that suggested there could be some further differentiation by customer type within residential mortgages.

<sup>19</sup> See for instance, document 110 of the response to the s109 Notice and attachment 1.3 - Board strategy away day.

<sup>20</sup> Loan origination is the level of mortgage lending (new or refinanced) processed by the lender in that year.



### *BTL mortgage lending*

33. The Parties submitted that they do not consider it appropriate to segment the wider market for BTL mortgage lending by different customer groups given that suppliers tend to offer a range of different types of BTL products to different types of customers and that suppliers can easily and quickly move between different segments. The Parties also submitted that lenders do not price discriminate between segments and that the Parties return broadly the same margin across segments.
34. The Parties' internal documents and submissions from third parties present a range of different approaches to segmenting BTL mortgage customers. This could be:
- (a) by reference to the customer themselves (based on their credit history, based on their level of experience as a landlord, whether they operate as a limited company landlord, whether they have multiple properties, or other complexities such as living outside the UK – 'expat' borrowers – or being self-employed),
  - (b) by reference to the property (the level of the loan-to-value (**LTV**), whether the property is a new build, whether it is a House in Multiple Occupation (**HMO**)), or
  - (c) by reference to the loan itself (whether it is a first or second charge mortgage, whether it is a long term or bridging loan, whether the interest rate on the mortgage is fixed or variable, and if fixed, for how long).
35. As stated at paragraph 30, the CMA and its predecessor organisations have not specifically considered BTL mortgage lending, however the OFT did consider that customer segmentation could be appropriate in relation to owner-occupied mortgage lending.<sup>21</sup>
36. In this case, the CMA has considered whether it is appropriate to segment BTL mortgage lending by any of the customer, property or loan types listed in paragraph 34. In doing so, the CMA has considered both demand-side and supply-side substitution.

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<sup>21</sup> [Barclays/ING Direct N.V. \(2013\)](#), par. 13-14

- *Demand-side substitution*

37. The CMA considered that there is limited demand-side substitutability between many of the possible customer segments. It is very difficult for a customer to switch segments (eg to change their credit history or to change their level and type of income) or to change the characteristics of the property without switching to buy a different property. The Parties did not provide evidence to the contrary.<sup>22</sup>
38. On this basis, the CMA considered it was appropriate to segment BTL mortgage lending by reference to customer segments. Given the possibility of a large number of granular frames of reference (in particular because of intersections between the possible segments, whereby a customer could simultaneously be, for example, self-employed, buying a HMO and a portfolio landlord), the CMA has taken a pragmatic approach of considering these segments individually without defining a large number of frames of reference based on the intersections between these segments.<sup>23</sup> This means that some customers will fall within more than one frame of reference.
39. The CMA considered a wide range of customer segments, and based on evidence from the Parties' submissions, internal documents and information provided by third parties (see paragraphs 49 and 51), the CMA focused, for the purposes of this investigation, on the following customer segments, *inter alia*:
- (a) BTL mortgages on HMOs;<sup>24</sup>
  - (b) BTL mortgages to limited company landlords;<sup>25</sup>
  - (c) BTL mortgages to portfolio landlords;<sup>26</sup>

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<sup>22</sup> The Parties submitted that a landlord could readily switch between operating as an individual and operating as a limited company when securing a BTL mortgage. The CMA observes growing popularity of operating as a limited company landlord in recent years as a result of tax and regulatory changes. The CMA considers that these tax and regulatory advantages mean that landlords currently operating as limited companies would generally be reluctant to return to borrowing as individuals.

<sup>23</sup> To the extent competition concerns arise for each of the segments individually, those concerns would be compounded for customers falling into the intersection between those segments. The CMA has sought to account for this within its competitive assessment.

<sup>24</sup> The CMA has defined HMOs in accordance with the statutory definition given in the Housing Act 2004, which is that a property is a HMO if both of the following apply: (i) at least three tenants live there, who form more than one household; and (ii) the tenants share toilet, bathroom or kitchen facilities with other tenants. A household is either a single person or members of the same family who live together.

<sup>25</sup> A landlord may choose to incorporate as a limited company in order to own and manage their BTL property(ies).

<sup>26</sup> The CMA has defined this as a landlord with 4+ properties, as in line with Prudential Regulatory Authority (PRA) guidelines. The CMA also looked at 'professional landlords' although it found a wide variation in the application of this term and as such, was not able to examine this customer segment separately.

- (d) BTL mortgages to expat landlords;<sup>27</sup>
  - (e) BTL mortgages to customers with adverse credit history;
  - (f) BTL mortgages to first time landlords;
  - (g) BTL mortgages to self-employed individuals with limited trading history;  
and
  - (h) BTL mortgages on new build properties.
40. In determining which customer segments to focus on, the CMA took a pragmatic approach and focused on customer segments where it believed there are prima facie competition concerns. These segments were: BTL mortgages to limited company landlords, portfolio landlords, expat landlords and BTL mortgages on HMOs.
41. In relation to the other customer segments listed in paragraph 39 above, given evidence of a range of lenders active in serving these customers and the absence of third party concerns, the CMA did not identify prima facie competition concerns and has not considered these segments further in its decision.<sup>28</sup>
- *Supply-side substitution*
42. While the boundaries of the relevant product market are generally determined by reference to demand-side substitution alone, the CMA may widen the scope of the market where there is evidence of supply-side substitution. In particular, the CMA may aggregate several narrow relevant markets together where (i) firms outside the market can quickly (generally within a year) shift production to products within the market, and (ii) the same firms compete to supply these different products, and the conditions of competition are the same for each product, such that analysing the supply of the different products as one market does not affect the CMA's decision on the competitive effect of the merger.<sup>29</sup>
43. The Parties submitted that there is a significant amount of supply-side substitution between different types of BTL mortgage products. They submitted that to supply a new product, a lender would require appropriate underwriting capability, knowledge of the regulatory requirements and

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<sup>27</sup> The CMA has defined this as a BTL mortgage in which the landlord lives abroad but their BTL property is in the United Kingdom.

<sup>28</sup> The CMA has not needed to conclude on whether all of the customer segments listed in paragraph 39 constitute frames of reference.

<sup>29</sup> [Merger Assessment Guidelines](#), paragraph 5.2.17.

appropriate systems to assess applications. The Parties highlighted that many of the same lenders are active in supplying different types of mortgage products and customers and there has been significant entry in mortgage lending in the past 10 years.

44. The CMA found mixed evidence of supply-side substitution, but overall considered that the evidence is not sufficient to suggest widening the frames of reference from the customer segments identified in paragraph 39 above. In assessing supply-side substitution, the CMA considered evidence on competitor sets, pricing, margins, and evidence from the Parties' internal documents and from competitors.
45. **Competitor sets:** The Parties provided the CMA with a table<sup>30</sup> showing the various suppliers active in specialist BTL lending, when they entered, and which customer segments they are present in.

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<sup>30</sup> Parties' Issues Meeting Presentation.

**Table 1: Parties' assessment of active BTL lenders**

Lender	Entered BTL	Limited Co.	HMO	Ex Pats	Portfolio Landlords
Paragon Bank	Pre-2009	✓	✓	✓	✓
Together	Pre-2009	✓	✓	✓	✓
Kent Reliance (OSB)	Pre-2009	✓	✓	✓	✓
The Mortgage Works	Pre-2009	✓	✓	✗	✓
BM Solutions	Pre-2009	✗	✓	✗	✓
Leeds Building Society	Pre-2009	✗	✓	✗	✓
Woolwich	Pre-2009	✗	✓	✗	✓
Precise Mortgages (CC)	May 2010	✓	✓	✗	✓
Aldermore	May 2010	✓	✓	✓	✓
Kensington	Nov 2012	✓	✓	✗	✓
Pepper Money	Jan 2015	✗	✗	✗	✓
Fleet Mortgages	Jan 2015	✓	✓	✗	✓
Foundation Homeloans	Feb 2015	✓	✓	✓	✓
Axis Bank	Apr 2015	✓	✓	✓	✓
Bluestone Mortgages	Oct 2015	✗	✗	✗	✓
Vida Homeloans	Oct 2015	✓	✓	✓	✓
Landbay	Jan 2017	✓	✓	✓	✓
Lendinvest	Nov 2017	✓	✓	✗	✓
The Mortgage Lender	May 2018	✓	✓	✓	✓
Keystone	Sep 2018	✓	✓	✓	✓
Zephyr Homeloans	Dec 2018	✓	✓	✗	✓

46. As can be seen from the table above, the majority of the lenders listed operate across a number of customer segments, and 16/21 are active in BTL lending to portfolio landlords, limited company landlords, and on HMOs, indicating a similar competitor set across customer segments. But the CMA also found evidence of lenders being active to different degrees in customer segments. The CMA observed variation in the shares of supply across customer segments, with some lenders having a high share of supply for some customers and a low share of supply for others. Additionally, some lenders will only offer BTL mortgages to less complex customers within a segment (eg portfolio landlords with a smaller portfolio),<sup>31</sup> or under certain

<sup>31</sup> The various criteria and limits applied by the Parties and their competitors is carefully assessed in a number of internal documents, such as Charter Court documents 245 Buy to Let Sector Review and 123 Competitor Risk Matrix – Buy to Let, and shows lenders being active to different extents in different customer segments.

limited conditions, such as only lending to customers where they already have a pre-existing relationship.<sup>32</sup>

47. **Pricing:** A difference in prices between customer segments is consistent with the Parties and their competitors facing different competitive conditions in different segments. The Parties provided evidence that the Parties apply the same or very similar pricing across segments,<sup>33</sup> and told the CMA that they apply their published pricing to all or almost all of their lending and that individualised pricing is offered only as a very limited exception to this.<sup>34</sup> On the other hand, the CMA observed the Parties' competitors pricing differently between customer segments, and some intermediaries told the CMA that they have observed price differences between the Parties' products.<sup>35</sup>
48. **Margins:** The CMA gathered evidence from third parties showing differences in the margins earned between segments. For example, third parties indicated to the CMA that BTL segments such as HMOs, limited company landlords and portfolio landlords typically yielded higher margins, reflecting the increased complexity of customers within these segments. A difference in margins is prima facie evidence of different competitive conditions, since easy supply-side substitution would tend to make margins equal across segments.<sup>36</sup>
49. **Parties' internal documents:** The Parties' internal documents show that they make commercial decisions separately for different customer segments (including limited company landlords, portfolio landlords and on HMOs) and that they record and monitor these segments separately. For example, broker survey reports<sup>37</sup> monitor the performance of lenders and broker recommendations of individual segments separately, notably limited company landlords and HMOs, and [REDACTED].<sup>38</sup>
50. The Parties' internal documents show that they frequently assess the BTL market and the offering of their competitors to identify new markets or customer groups with different borrowing needs, and then look to develop and launch new products for these customers.<sup>39</sup> The internal documents also show how lenders develop and extend their product offering over time, such as increasing the portfolio size limit or extending other borrower criteria.<sup>40</sup> As can be seen in Table 1 above, there have been a large number of new

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<sup>32</sup> Third party responses to the CMA.

<sup>33</sup> For example, [REDACTED].

<sup>34</sup> OSB agreed to an individualised product for only [REDACTED]% of its customers in 2018.

<sup>35</sup> Indeed, slide 15 of the Parties Issues Meeting Presentation clearly shows that nearly all of the Parties' competitors have at least some difference prices between limited company landlords and on HMOs.

<sup>36</sup> [Merger Assessment Guidelines, paragraph 5.2.19.](#)

<sup>37</sup> H.15 BDRC Commentary – August 2018

<sup>38</sup> Annex 147: Precise Mortgages – Market Insights Presentation – 2018 Year End.

<sup>39</sup> For example, [REDACTED].

<sup>40</sup> [REDACTED].

entrants into BTL lending, who have followed the Parties into lending into the various customer segments.

51. **Evidence from competitors:** Responses received by the CMA to its merger investigation highlighted several factors that are relevant for whether a lender could shift to operating in new customer segments. Competitors highlighted the need for board or committee approval, thorough risk assessment and approval, technical and system changes and marketing and training. In addition, some competitors indicated to the CMA that they consider certain segments too risky to enter, particularly expat landlords, either because of the credit risk of the customer type or the potential reputational risk.<sup>41</sup> This is likely to be particularly true for the more mainstream BTL lenders, who may lack the necessary manual underwriting processes to supply complex products and may have an unwillingness to offer products to risky customers because of reputational risk.
52. Most competitors indicated that they may possess the technical ability to enter new segments within a reasonable timeframe, and that, for those already present in specialist BTL lending, barriers to entry or expansion in new customer segments were likely to be reasonably low. Although low in absolute terms, the CMA noted one example where the barriers to entry were sufficient to deter one lender from entering a new segment for several years, partly because the available market was small.
53. Overall, the CMA considered that evidence relating to supply-side substitution was mixed and not sufficient to justify aggregating customer segments and assessing overall BTL lending as one product frame of reference. The CMA recognises however that the dynamics of this industry do involve entry by rivals into new customer segments over time; the emergence of new customer segments (such as limited company lending in response to changes in the tax regime); and that the barriers to entering new segments are reasonably low. The CMA considers these factors further in the competitive assessment when it considers the constraint alternative lenders will exert on the Parties post-Merger; for example when considering how to interpret shares of supply and competitor counts in individual segments.

### ***Geographic scope***

54. The Parties submitted that the appropriate geographic frame of reference is the UK. They submitted that lenders offer substantially the same product

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<sup>41</sup> Some Charter Court internal documents also suggest that [redacted] supply side substitution between customer segments. [redacted].

offering in England and Wales and Scotland and therefore any geographic frame of reference is likely to be wider than the regions of the UK.

55. In past cases, the CMA has considered the frame of reference to be UK-wide, although as noted in paragraph 30 the focus of these investigations has not been on BTL lending or other types of loans.<sup>42</sup> However, in its retail banking market investigation, the CMA defined separate geographic markets for Great Britain and for Northern Ireland, due to the different competitor sets in both regions.
56. Neither of the Parties currently lend in Northern Ireland. Further, OSB's activities in Scotland are limited to second charge lending only.
57. The CMA considers that GB is the appropriate geographic frame of reference. This is because neither Party, nor a number of their competitors, is active in Northern Ireland, indicating different competitive conditions for Northern Ireland to the rest of the UK. The CMA notes that there are some differences in property law between England and Wales and Scotland, but that most of the Parties' competitors are active across all three nations. The CMA did not find evidence of regional pricing. Given the small presence of the Parties in Scotland and the small size of specialist BTL lending in Scotland in general (estimated at less than 10% of the total BTL GB market), the CMA does not consider that the inclusion or exclusion of Scotland in the geographic frame of reference will alter the outcome of the CMA's assessment.
58. For the reasons set out above, the CMA has considered the impact of the Merger using GB as the geographic frame of reference.

### ***Conclusion on frame of reference***

59. For the reasons set out above, the CMA has considered the impact of the Merger in the following frames of reference:
  - (a) Supply of BTL mortgage lending in GB on HMOs;
  - (b) Supply of BTL mortgage lending in GB to limited company landlords;
  - (c) Supply of BTL mortgage lending in GB to portfolio landlords; and
  - (d) Supply of BTL mortgage lending in GB to expat landlords.
60. The CMA has also considered the impact of the Merger in the supply of BTL mortgage lending (as a whole), on the basis that there is some indication that

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<sup>42</sup> Eg [Lloyds/ HBOS \(2008\)](#), [Lloyds TSB/Abbey National \(2001\)](#).



some elements of competition are wider than the individual segments, and that the Parties and their competitors may set and implement important aspects of their competitive offerings consistently across all their BTL lending. This includes aspects of competition such as service quality, product range and mix, and certain lending criteria (eg OSB does not lend to customers with an adverse credit history). Indeed, the Parties submitted that they use the same assumptions and inputs for pricing mortgages across the customer segments identified by the CMA, and that Charter Court uses the same financial appraisal model for these different customer types (limited company landlords, portfolio landlords and on HMOs).

## **Competitive assessment**

### ***Horizontal unilateral effects***

61. Horizontal unilateral effects may arise when one firm merges with a competitor that previously provided a competitive constraint, allowing the merged firm to profitably raise prices or to degrade quality on its own without needing to coordinate with its rivals.<sup>43</sup> The concern under this theory of harm is that the removal of one party as a competitor could allow the parties to increase prices, lower quality, reduce the range of their services and/or reduce innovation. After the merger, it is less costly for the merging company to raise prices (or lower quality) because it will recoup the profit on recaptured sales from those customers who would have switched to the offer of the other merging company. Horizontal unilateral effects are more likely when the merging parties are close competitors.
62. The CMA assessed whether it is or may be the case that the Merger may be expected to result, in an SLC in relation to horizontal unilateral effects in the frames of reference described above in paragraph 59.
63. In order to assess the likelihood of the Merger resulting in horizontal unilateral effects, the CMA considered:
  - (a) Shares of supply within each frame of reference;
  - (b) The closeness of competition between the Parties; and
  - (c) Competitive constraints from alternative lenders.

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<sup>43</sup> [Merger Assessment Guidelines](#), from paragraph 5.4.1.

## ***Overall supply of BTL mortgage lending in GB***

64. As stated in paragraph 60, the CMA observed some elements of competition as being wider than the BTL customer segments identified as frames of reference. The CMA has therefore assessed the overall supply of BTL mortgage lending, described below, before it considers the impact of the Merger in each frame of reference.

### *Shares of supply*

65. The Parties estimated that they have a combined share of supply in BTL mortgage lending of [10-20]%, or [20-30]% (including specialist lenders but excluding high-street banks).
66. Because of the lack of available external data on the size of BTL lending and the lenders present, the CMA calculated share of supply estimates using data related to the value of loans originated in 2018, obtained from the Parties and their competitors. Based on the CMA's estimate, the Parties have a combined share of supply of BTL mortgage lending in GB of no more than [20-30]%.<sup>44</sup>
67. The CMA makes the following general observations in relation to its shares of supply estimates which apply to all of the product frames of reference:
- (a) The shares calculated by the CMA are upper estimates of the Parties' true market share because some competitors' lending will not be captured in the share of supply estimates (eg if they did not respond to the CMA's market testing);
  - (b) The CMA observed evidence that competitors are differentiated and may not cater to all customers within a frame of reference, particularly, for example, if they are not a specialist lender. This means that some lenders will be closer competitors to the Parties than others and may act as more or less of a constraint on them than their share of supply alone might suggest;
  - (c) The CMA's estimates provide a historical and static 'snapshot' of competition in the market in 2018. As explained above, the CMA believes that BTL lending is a dynamic market (see recent entry in paragraph 45 and further discussion at paragraphs 92 and 93), with large growth seen in various customer segments in recent years, particularly limited company landlords. This means that the shares of supply calculated may

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<sup>44</sup> This estimate excludes high-street banks, but includes The Mortgage Works and BM Solutions, which are BTL lending arms of Nationwide Building Society and Lloyds Banking Group, respectively.

not effectively capture recent or new entrants in the different customer segments, and that it may be relatively easy for these lenders to grow their shares of supply in the future. While historical trends can provide some insight, the CMA believes that relatively little weight should be placed on static shares of supply in this sector.

### *Closeness of competition*

68. The Parties submitted that they are not particularly close competitors in BTL lending because OSB has a broad offering and targets larger professional and limited company landlords, as well as high net-worth individuals, with a bespoke underwriting process. In contrast, Charter Court has an automated decision-making platform, which lends itself to a less complex customer profile, and also offers its products to those with some form of minor credit impairment.
69. The CMA considers that the available evidence indicates that there is close competition between the Parties in overall BTL mortgage lending, but that there are a number of other lenders who are also as close competitors to the Parties as they are to each other. In looking at the closeness between the Parties, the CMA assessed the Parties' offering in terms of price, quality, and range, and also examined their internal documents.
70. **Price:** When comparing the Parties' rates, OSB and Charter Court often have broadly similar rates, although OSB tends to be slightly more expensive. The evidence also showed that there are a range of alternative lenders offering a similar price to the Parties across the various customer segments and products (eg two-year fixed rate, five-year fixed rate, different LTVs, etc). Intermediaries also told the CMA that they often see the Parties pricing similarly to each other, alongside other specialist lenders.
71. The evidence indicated that the Parties, as specialist BTL lenders, typically have a higher price point than more mainstream lenders, and this is consistent with the Parties competing to supply more specialist customers (with higher costs and margins) or a higher level of service (see paragraph 72 below). For example, in one Charter Court document<sup>45</sup> it states that '[X]'.
72. **Quality:** Service quality was noted by intermediaries as important, alongside price and the criteria of a lender (such that it actually lends to a specific customer with the requested term and flexibility). Service was explained as referring to the ease of dealing with the lender and the time taken to

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<sup>45</sup> 095 – CAC 03 – Competitor Commentary – April 2018 PMC

underwrite and complete an application. Internal documents and third-party responses indicated that the Parties are closely matched in terms of the service they offer.<sup>46</sup> One OSB document<sup>47</sup> compares the Parties [redacted] and shows that the Parties [redacted] scores from brokers in terms of how satisfied they are and how willing they would be to recommend the company.<sup>48</sup> Third parties commented on the importance of lenders being able to offer a high-quality service. One intermediary noted that service levels were very important and noted that OSB has excellent service. It also mentioned that the service level of one of the Parties' main competitors had dropped recently compared to other lenders. Another intermediary explained that Charter Court works closely with brokers to 'educate' them in an 'exceptional' way.

73. **Range:** The Parties' BTL mortgage product offering is broadly the same, and it is common for the Parties to be among the first to introduce new BTL products, such as top-slicing,<sup>49</sup> and for them to look to widen their range based on what the other Party and their main competitors offer.<sup>50</sup>
74. **Parties' internal documents:** Internal documents reviewed by the CMA indicate that, whilst the Parties routinely monitor the mortgage rates of a wide range of lenders, there is evidence that the Parties closely monitor each other and a smaller set of other specialist lenders. For example, one OSB document assessing its lending criteria benchmarks itself against a [redacted] group of specialist lenders, namely: [redacted].<sup>51</sup> One Charter Court document assessing competition within the specialist sector monitors [redacted] group of lenders, namely [redacted].<sup>52</sup> A different internal document [redacted].<sup>53</sup>
75. One Charter Court board paper<sup>54</sup> noted that '[redacted]'. Charter Court said<sup>55</sup> that [redacted]. The CMA considered that this document supports its view that the Parties are leading specialist BTL lenders and that the impact of the Merger should be examined carefully.

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<sup>46</sup> In particular, the majority of intermediaries who responded to the CMA's market testing considered that the Parties' product offer is similar, noting similarities in the HMO, limited company landlord and portfolio landlord segments.

<sup>47</sup> G25. Charterhouse research – Oxford brand tracker (09.04.18).

<sup>48</sup> [redacted].

<sup>49</sup> Top-slicing refers to the use of a customer's personal income to top up any shortfall in rent needed in order for the customer to obtain the loan amount they require.

<sup>50</sup> Products that Charter Court doesn't offer but OSB does are seen as 'opportunities' in document 143 – MI 07 – OSB Analysis v5.

<sup>51</sup> Slide 6, Annex G3.2, Final Merger Notice.

<sup>52</sup> [redacted].

<sup>53</sup> [redacted].

<sup>54</sup> F.09 Project Azure – Board Paper – June 2018.

<sup>55</sup> At the Issues Meeting. As a general matter, the CMA will attach more weight to contemporaneous internal documents (particularly an internal board-level document authored by Charter Court's CEO, as in this case) than an ex post facto oral explanation of the document.

76. Overall, the CMA considers that the Parties are close competitors based on the range, price and quality of products they offer across the BTL lending sector, and the evidence from their internal documents and third-party responses. The CMA also observes a number of competitors who also appear to be close competitors to the Parties. The CMA considers this evidence on the general closeness of competition between the Parties to be relevant across all of the individual product frames of reference.

#### *Competitive constraints*

77. The CMA observed evidence of a large number of alternative lenders active in BTL mortgages. This includes specialist lenders such as Aldermore, Paragon, Kensington, Foundation Home Loans and Shawbrook. These lenders tend to offer a similar range and type of product to the Parties and are closely monitored in the Parties' internal documents. These lenders were frequently named by intermediaries as being alternatives to the Parties and offering various BTL mortgage products.

78. In addition, mainstream lenders are also present in BTL to varying extents. The Mortgage Works<sup>56</sup>, BM Solutions<sup>57</sup> and Godiva<sup>58</sup> offer a range of BTL products and account for a high share of overall BTL lending. Intermediaries commented that these and other banks and building societies are taking an increased interest in BTL products, although tend to focus their activities towards the less complex and less risky customers. The Parties also told the CMA that the commercial lending arms of banks and building societies, such as NatWest, HSBC and Barclays are also active in BTL lending, as indicated by their presence on a broker sourcing software platform.

79. As shown in paragraph 45, there is also a range of new entrants into BTL mortgage lending, which appear to be growing and expanding their presence, such as Landbay, Lendinvest, Vida Homeloans, Masthaven and Fleet.

#### *CMA conclusion*

80. For the reasons set out above, the CMA believes that although the Parties are relatively close competitors, they have a low combined share of supply in overall BTL lending and there remains numerous alternative lenders active in BTL lending, some of whom are close competitors to the Parties. Accordingly, the CMA has not identified evidence suggesting competition concerns would

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<sup>56</sup> The Mortgage Works is the specialist mortgage lending arm of Nationwide Building Society and offers a range of BTL mortgage products.

<sup>57</sup> BM Solutions is the BTL brand of Lloyds Banking Group.

<sup>58</sup> All Coventry Building Society BTL mortgages are offered through Godiva.

arise as a result of the Merger in overall BTL lending that could manifest in any of the specific frames of reference considered by the CMA.

**Horizontal unilateral effects in the supply of BTL mortgage lending in GB on HMOs**

*Shares of supply*

81. The CMA estimated that the Parties are the first and fourth largest suppliers of BTL mortgages on HMOs in GB, with a combined estimated share of this frame of reference of up to [40-50]%.

**Table 2: CMA share estimates for the supply of BTL mortgage lending in GB on HMO properties, 2018**

	Origination (£m)	Share
<b>OSB</b>		[20-30]%
<b>Charter Court</b>		[10-20]%
<b>Parties</b>		[40-50]%
<b>Aldermore</b>		[0-5]%
<b>BM Solutions*</b>		[10-20]%
<b>Fleet</b>		[0-5]%
<b>Foundation</b>		[0-5]%
<b>Kensington</b>		[0-5]%
<b>Masthaven</b>		[0-5]%
<b>The Mortgage Works</b>		[0-5]%
<b>Paragon</b>		[10-20]%
<b>Shawbrook</b>		[5-10]%
<b>Together</b>		[0-5]%
<b>Vida</b>		[0-5]%
<b>Total</b>	2010	

Source: CMA estimate for 2018 using the Parties' and third parties' data which includes data from almost all of the key competitors listed by the Parties in their submissions and internal documents.

\* BM Solutions was unable to provide an estimate for the HMO segment. The CMA has used an estimate of BM Solutions' share of supply of the entire BTL sector as a proxy for its share of the HMO segment.

82. The Parties submitted that the CMA's share estimates overstate their position in this segment for the following reasons: (i) competitors may apply different classifications to HMO properties, so the CMA's shares may not capture all of the relevant lending activities; (ii) the CMA's share estimates exclude many

significant BTL lenders, including both mainstream banks and specialists who lend to HMO properties; and (iii) it is a dynamic segment with many active competitors entering/expanding and leading to frequent variance in shares.<sup>59</sup>

83. The Parties submitted evidence from other sources illustrating that the total market size as calculated by the CMA was too small, for example:
- (a) The Parties estimated a combined share of supply of [0-5]% based on a share of all estimated mortgaged HMO properties in the UK,<sup>60</sup> and
  - (b) Data related to property valuations indicates that approximately 1,700 HMO mortgage applications are placed each month and that the Parties comprise only a small fraction of these.<sup>i</sup>
84. Given the rough methodology and limited data used by the Parties to illustrate the market size, the CMA does not believe that it should adopt the Parties' estimates as an accurate measure of their shares of supply. The CMA considers the share of supply estimates in Table 2 are helpful in indicating the Parties' position and identifying who their main competitors are in the frame of reference. However, the CMA acknowledges that there are likely to be additional lenders active in BTL mortgages on HMOs in GB and therefore that the Parties' actual shares of supply would be lower than those shown in Table 2. For example, one high street bank confirmed that its commercial desk offers BTL lending on HMO properties but was not able to quantify this. In any event, the CMA also considers the shares offer only a static picture (as mentioned in paragraph 67) of competitive positioning in the sector.

#### *Closeness of competition*

85. The Parties stated that they are not close competitors in the supply of BTL mortgage lending on HMO properties in GB. They submitted that:
- (a) Price is the main driver of competition within the BTL mortgage sector (including all segments therein) and there is limited closeness between the Parties on this basis. In particular, the Parties argued that OSB's focus on manual underwriting for customers results in OSB being a more expensive lender than Charter Court, with a range of competitors pricing between the Parties.
  - (b) OSB lends a significant proportion of its loans above 80% LTV whereas Charter Court does not lend above this threshold.

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<sup>59</sup> The CMA addresses point (iii) in its consideration of competitive constraints.

<sup>60</sup> The stock of HMOs was taken from [local authority housing statistics data](#).

(c) Internal documents submitted to the CMA do not evidence close competition between the Parties.

86. The Parties provided data comparing competitors' product offerings on HMOs. These included comparisons on rates (for 2 and 5-year fixed interest rates) and maximum LTV thresholds. The data supported the Parties' submissions that OSB's products are typically priced higher than Charter Court and that there is a range of competitors between the Parties when comparing prices. This data also showed that Charter Court does not offer products above 80% LTV. This also is consistent with competitor monitoring included in Charter Court's internal documents, as submitted to the CMA.<sup>61</sup>
87. Some of the Parties' internal documents suggest that both OSB and Charter Court monitor a select group of competitors more closely than others in the supply of HMO products.<sup>62</sup> The Parties are always included in this smaller competitor set, which may indicate closer competition between the Parties than with some of their competitors. In particular, the Parties appear to monitor specialist lenders such as Aldermore, Paragon, Kensington and Vida Homeloans closely, as well as BM Solutions.<sup>63</sup> One intermediary also commented to the CMA that the Parties are very similar in HMO lending, particularly in terms of their underwriting standards. A few competitors raised concerns over the combined scale of the Parties in BTL lending on HMOs post-Merger.
88. The CMA believes that this evidence indicates that, although the Parties are close competitors to each other, there is evidence that they belong to a group of 5 or 6 close competitors in the supply of BTL mortgages on HMO properties.

### *Competitive constraints*

89. The Parties argued that there are many alternative providers available to customers looking to borrow for BTL HMO properties. These include both mainstream banks as well as a long tail of specialist suppliers. The Parties also argued that the nature of the distribution of these products through intermediaries also facilitates competition from a range of suppliers.

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<sup>61</sup> For example, Documents 076 – 106 Competitor Commentary/ Buy to Let Competitor Analysis documents.

<sup>62</sup> For example, Document 220 NPD HMO 1 (October 2017) or Document 190 Competitor cheat sheet (September 2018).

<sup>63</sup> For example, Document 49 Landlords Panel.



### *Alternative suppliers*

90. BM Solutions and Paragon appear to offer a significant competitive constraint in this segment, with estimated shares of supply of [10-20]% and [10-20]%, respectively. In particular, the evidence the CMA has reviewed suggests Paragon is of comparable scale to each of the Parties in this segment and supplies a comparable product.
91. Whilst the CMA was unable to clarify the exact scale of BM Solutions' lending in this segment, discussions with the company confirmed that it is active in and committed to this segment and [§<del>§</del>]. For some customers, BM Solutions will be a strong competitive constraint on the Parties in the supply of BTL mortgages on HMOs. For other customers, however, it may be less of a constraint as, based on the evidence available to the CMA, it appears that the majority of its lending appears to be to 'core' (ie less complex) BTL customers, as compared to the Parties, who tend to lend to more complex customers.
92. In addition to the larger suppliers, the CMA identified the presence of a 'long tail' of competitors active in this segment, including recent entrants. In particular, the CMA was able to confirm the presence of sixteen competitors active in the supply of BTL mortgages for HMO properties, supplying 2 and 5-year fixed products at a range of LTV thresholds. The Parties also identified nine instances of competitors entering this BTL segment in the previous five years (with five instances in the previous three years). The Parties pointed to a recent announcement by The Mortgage Works where it launched a range of new and cheaper products for landlords looking to buy HMOs, indicating that the constraint of this competitor was likely to grow. Given the role of intermediaries in BTL lending (see paragraph 95 below) and the importance of price in winning customers, it appears reasonable to suggest that The Mortgage Works (as well as small lenders who offer a competitive price) would impose a competitive constraint on the Parties.<sup>64</sup> In addition, intermediaries who responded to the CMA indicated that there was a range of lenders active in BTL mortgages on HMO. No intermediaries expressed concerns about the impact of the Merger in this segment, although one told the CMA that there was slightly less, but still a reasonable amount of, choice for these customers.<sup>65</sup>

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<sup>64</sup> The Parties provided some (limited) evidence suggesting that they win and lose customers from a wide variety of lenders, including mainstream banks and small, specialist lenders. (Appendix 1, Issues Letter response).

<sup>65</sup> The CMA also understands that the commercial arms of mainstream banks provide funding to BTL landlords (particularly those with larger HMO portfolios) and therefore will provide an additional competitive constraint not captured in the CMA's share of supply estimates.

93. Evidence gathered by the CMA appears to support the Parties' submission in paragraph 82 that HMO lending is dynamic, with entry and growth by various suppliers in the past few years. In particular, the Parties supplied evidence on Charter Court's growth within HMO lending, which showed it going from [redacted] of HMO BTL mortgages in 2016 to [redacted] per month within two years. Further, there have been several large funding lines announced in the past few months to smaller entrants Fleet and Landbay (and new entrant Habito), with associated commitments to lending within BTL and its various segments. One of these entrants, [redacted], was mentioned in one Charter Court internal document as being '[redacted]'.<sup>66</sup>
94. The CMA believes that, in light of the above, sufficient competitive constraints will remain post-Merger. There are a number of larger-scale competitors active in this sector, including large, established, more mainstream lenders (BM Solutions and The Mortgage Works) as well as a range of specialist lenders. In addition, the evidence received by the CMA indicates that the long tail of lenders can be expected to grow within this customer segment, such that it is likely to further constrain the Parties post-Merger.

#### *Distribution through intermediaries*

95. The CMA believes that the distribution of BTL mortgage products (including HMO) is likely to facilitate effective competition between lenders. Intermediaries tend to employ a whole-market approach, meaning that they survey a large range of competitive options on their panels on a customer's behalf. The CMA understands that obtaining access to intermediaries' supplier panels is relatively easy, with many intermediaries operating large rosters of alternative suppliers, and that intermediaries look to offer a wide range of solutions to customers. The CMA also understands that intermediaries generally make a supplier recommendation to customers based on price (ie typically they recommend the cheapest option). The CMA therefore believes that this distribution model facilitates competition between a large number of alternative suppliers.

#### *CMA conclusion*

96. For the reasons set out above, the CMA believes that although the Parties compete closely, they do not compete more closely with each other than with a number of other competitors, and a sufficient number of alternative lenders will remain to constrain the Parties post-Merger. Accordingly, the CMA found that the Merger does not give rise to a realistic prospect of an SLC as a result

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<sup>66</sup> 098 CAC 06 Competitor Commentary July 2018.

of horizontal unilateral effects in relation to the supply of BTL mortgage lending in GB on HMO properties.

***Horizontal unilateral effects in the supply of BTL mortgage lending in GB to limited company landlords***

*Shares of supply*

97. The CMA estimated that the Parties are the first and second largest suppliers of BTL mortgages to limited company landlords in GB, with a combined share of this frame of reference of up to [50-60]%.

**Table 3: CMA share estimates for the supply of BTL mortgage lending in GB to limited company landlords, 2018**

	<b>Origination (£m)</b>	<b>Share</b>
<b>OSB</b>		[30-40]%
<b>Charter Court</b>		[20-30]%
<b>Parties</b>		[50-60]%
<b>Aldermore</b>		[0-5]%
<b>Fleet</b>		[0-5]%
<b>Foundation</b>		[0-5]%
<b>Kensington</b>		[0-5]%
<b>Masthaven</b>		[0-5]%
<b>The Mortgage Works</b>		[0-5]%
<b>Paragon</b>		[10-20]%
<b>Shawbrook</b>		[10-20]%
<b>Together</b>		[0-5]%
<b>Vida</b>		[0-5]%
<b>Total</b>	3989	

Source: CMA estimate for 2018 using the Parties' and third parties' data which includes data from almost all of the key competitors listed by the Parties in their submissions and internal documents.

98. The Parties submitted that the CMA's share of supply estimate overstates their position in this segment. In particular, the Parties submitted that: (i) a landlord's status as a limited company is not a meaningful basis to identify a distinct customer segment, as this simply acts as a 'tax wrapper' for borrowers who would otherwise borrow as an individual, and that this would affect the reliability of how lenders record these customers, meaning estimates may not be accurate; (ii) The Mortgage Works recently entered the segment in 2018 and so its share is artificially low when compared to the scale of its current competitive presence in this segment; and (iii) there is a range of lenders,

including mainstream banks and building societies, who are not included in the CMA's estimate.

99. The CMA observed that the Parties and all of the competitors that responded to the CMA were able to easily identify their limited company landlord customers and provide data for these, indicating reliability of the data gathered. The CMA acknowledges that, due to the 'bottom-up' methodology used to calculate the Parties' shares, the CMA's estimate is likely to overstate their position, at least to some extent. However, the Parties were not able to identify any specific competitor that was currently of a large enough scale within this frame of reference to significantly alter the shares of supply (although the CMA notes the limitation of shares of supply showing only a 'snapshot' as discussed in paragraph 67).

### *Closeness of competition*

100. The Parties stated that they are not close competitors in the supply of BTL mortgage products to limited company landlords in GB for similar reasons cited for the HMO segment. These include price differences between Parties' products, the difference between the LTV thresholds at which they operate, as well as the lack of closeness of competition demonstrated in their respective internal documents.
101. The CMA notes that evidence relating to closeness of competition in the Parties' internal documents is mixed with respect to limited company landlords. Certain documents submitted to the CMA by the Parties indicated that they may be the largest suppliers in this segment and compete closely. For example, one Charter Court document tracking which lenders an intermediary was likely to recommend to limited company landlords showed [REDACTED].<sup>67</sup> However, additional documents appear to evidence alternative suppliers as close competitors in this segment ([REDACTED]).<sup>68</sup> Further, the Parties' routine competitor monitoring appears to track a relatively broad range of competitors, with no particular focus on the other Party.
102. The CMA believes that, similar to the HMO segment, the evidence indicates closeness of competition between the Parties but that, as shown in the Parties' internal documents,<sup>69</sup> they belong to a group of 5 or 6 close competitors in the supply of BTL mortgages to limited company landlords. A

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<sup>67</sup> H.15 BDRC Commentary August 2018.

<sup>68</sup> See for example documents 127, 137, 163, 235, and 245.

<sup>69</sup> For example, Document 104 Competitor Commentary, G3.2 Customer and Competition Board, and H.15 BDRC Commentary – August 2018.

few competitors raised concerns over the combined scale of the Parties in BTL lending to limited company landlords post-Merger.

### *Competitive constraints*

103. Paragon and Shawbrook appear to offer a significant competitive constraint in this segment, with estimated shares of supply of [10-20]% and [10-20]%, respectively. As specialist lenders they also offer a similar product to the Parties and are comparable in terms of pricing and product range. The CMA identified a tail of at least eight competitors accounting for a collective share of approximately 20%. The CMA accordingly expects existing competitors in this segment to exert a strong competitive constraint on the Parties post-Merger.
104. The Parties provided evidence of the impact of recent entry in 2018 of The Mortgage Works into supplying BTL mortgages to limited company landlords, which now has the largest share of broker recommendations, ahead of the Parties. Its entry was noted by Charter Court as being [redacted].<sup>70</sup> Given The Mortgage Works' strong position in other BTL customer segments and BTL lending overall, and its ability to access cheaper funding (as part of Nationwide Building Society) and therefore offer a low price for some customers, the CMA considers that The Mortgage Works is likely to provide a stronger constraint on the Parties post-Merger than its current estimated share of supply indicates, particularly because it started supplying limited landlord customers partway through 2018 and so the share of supply does not include twelve months of lending.
105. Given this customer segment has only developed over the past couple of years, and some lenders have entered only recently, the CMA expects lenders to continue to grow and will provide a constraint on the Parties post-Merger in the future. The Parties also explained that their process for lending to a limited company landlord was the same as to an individual (in terms of receiving a personal guarantee on the loan) and so this would not necessarily be a risky segment to lend in.
106. The CMA has been able to confirm entry by at least eight competitors in the last three years, as well as large publicly announced funding lines and plans to lend to customers in this segment from smaller competitors (see paragraph 93). As in HMO lending, the Parties supplied evidence on Charter Court's growth within limited company landlord lending, which showed it going from [redacted] of BTL mortgages to limited landlord companies in 2016 to [redacted] per month within two years. Again, the CMA considers that growth within BTL lending to

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<sup>70</sup> 098 CAC 06 Competitor Commentary July 2018.

limited company landlords by smaller suppliers would be aided by the distribution through intermediaries, described at paragraph 95, and considers that commercial arms of mainstream banks will provide an additional competitive constraint not captured in the CMA's share of supply estimates. Intermediaries who responded to the CMA indicated that there was a range of lenders active in BTL mortgages to limited company landlords, and none expressed concerns about the impact of the Merger in this segment.

107. The CMA therefore believes that, notwithstanding the Parties' large combined share of supply in this frame of reference, sufficient competitive constraints will remain post-Merger. This is demonstrated through the large number of alternative suppliers, the expected growth of lending to this customer group more generally, as well as the recent entry and expansion of both more mainstream and specialist/smaller lenders.

#### *CMA conclusion*

108. For the reasons set out above, although the Parties are currently 2 of the 4 main competitors in the supply of BTL mortgages to limited companies and have a high estimated share of supply, the CMA believes that the presence of alternative suppliers and particularly the growth of competitive options through recent entry and expansion in this segment will constrain the Parties post-Merger. Accordingly, the CMA found that the Merger does not give rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in relation to the supply of BTL mortgages in GB to limited company landlords.

#### ***Horizontal unilateral effects in the supply of BTL mortgage lending in GB to portfolio landlords***

##### *Shares of supply*

109. The CMA estimates that the Parties are the third and fourth largest suppliers of BTL mortgages in GB to portfolio landlords, with a combined share of this frame of reference of up to [20-30]%.

**Table 4: Shares of supply in BTL mortgage lending in GB to portfolio landlords in 2018**

	<b>Origination (£m)</b>	<b>Share</b>
<b>OSB</b>		[10-20]%
<b>Charter Court</b>		[10-20]%
<b>Parties</b>		[20-30]%
<b>Aldermore</b>		[5-10]%
<b>BM Solutions</b>		[5-10]%
<b>Fleet</b>		[0-5]%
<b>Foundation</b>		[0-5]%
<b>Kensington</b>		[0-5]%
<b>Masthaven</b>		[0-5]%
<b>The Mortgage Works</b>		[30-40]%
<b>Paragon</b>		[10-20]%
<b>Shawbrook</b>		[5-10]%
<b>Together</b>		[0-5]%
<b>Vida</b>		[0-5]%
<b>Total</b>	<b>7756</b>	

Source: CMA estimate for 2018 using the Parties' and third parties' data which includes data from almost all of the key competitors listed by the Parties in their submissions and internal documents.

110. Although the Parties have only a moderate estimated share of supply in BTL mortgage lending to portfolio landlords, the Parties are two of the largest lenders active in lending to these customers. However, customers in this frame of reference are likely to be differentiated for example by complexity based on the number of properties in their portfolio, or by also being a limited company or by having a portfolio of properties including HMOs.<sup>71</sup> Consequently, the shares of supply calculated may not fully capture the closeness of the Parties and the competition that could be lost post-Merger.
111. The Parties submitted that the CMA's share of supply estimates had failed to capture the full market, as a result of omitting a number of building societies active in lending to portfolio landlords, as well as loans made by the commercial desks of mainstream banks. The CMA considers that the estimated shares of supply are a helpful starting point for considering competition in this frame of reference, and the Parties failed to identify any specific competitor that would be of a large enough scale within this frame of reference to significantly alter the shares of supply. The CMA obtained

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<sup>71</sup> Because of the intersections between the frames of reference, some customers will be included under more than one frame of reference.

evidence from almost all of the 'key' competitors identified by the Parties in their submissions and referenced in their internal documents.

### *Closeness of competition*

112. The Parties submitted that although they both offer a range of products to portfolio landlords, there are differences in their offering, such as OSB offering a bespoke underwriting process compared to an automated process, and OSB offering mortgages at higher LTV thresholds than Charter Court does.
113. The CMA observed some evidence to suggest that the Parties may be amongst a more limited group of competitors that are able to supply BTL mortgages to landlords with larger portfolios, indicating they may be closer competitors than the shares of supply show. In particular, some internal documents suggested that only the Parties, Aldermore, Fleet and Paragon consistently lend to customers with larger portfolios.<sup>72</sup>
114. The evidence shows that the Parties are relatively close competitors in BTL lending overall (as described at paragraph 68 onwards), and within BTL lending to portfolio landlord customers. However, the CMA did not observe any evidence of the Parties being closer competitors to each other for portfolio landlords than they each are to a number of their competitors (particularly Aldermore and Paragon). For example, one Charter Court document [redacted].<sup>73</sup>

### *Alternative lenders*

115. The Parties submitted that there are a substantial number of competitors and that their combined market share of under [20-30]% is strong evidence of a lack of competition concerns. They submitted that there are competitors with similar offerings to them with similarly sized shares of supply to each of the Parties pre-Merger, and that The Mortgage Works is clearly the largest lender and a strong constraint. They submitted that there are at least 11 lenders offering BTL mortgages to portfolio landlords with more than 10 properties, even at higher LTV thresholds,<sup>74</sup> and that 8 of these lenders have entered since 2015.
116. The evidence indicates that several competitors are able to match the Parties both on the criteria of the product (eg lending at a higher LTV or to larger portfolio landlords), as well as the price, with OSB tending to be more expensive than both Charter Court and some of its competitors. Almost all of

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<sup>72</sup> See for example documents 127, 137, 163, 235, and 245 of the Parties' response to the s.109 notice.

<sup>73</sup> H.15 BDRRC Commentary August 2018.

<sup>74</sup> See the lenders highlighted green in Table 1 above.



the competitors who responded to the CMA were active in supplying BTL mortgages to portfolio landlords, and they indicated that expanding their operations within this segment would be relatively quick and easy to do. For some (ie less complex) customers, The Mortgage Works is likely to act as a strong constraint on the Parties, given its strong share of supply and ability to offer lower rates than the Parties. For some (ie more complex) customers, there still remains several lenders who will, individually and collectively, constrain the Parties, particularly due to the distribution model in BTL lending (described at paragraph 95). Intermediaries who responded to the CMA indicated that there was a range of lenders active in BTL mortgages to portfolio landlords, and none expressed concerns about the impact of the Merger in this segment.

### *CMA conclusion*

117. For the reasons set out above, the CMA believes that the Parties have a relatively modest share of supply with evidence of several competitors with a similar offering to the Parties who compete closely with them to win customers. Accordingly, the CMA found that the Merger does not give rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in relation to the supply of BTL mortgages in GB to portfolio landlords.

### ***Horizontal unilateral effects in the supply of BTL mortgage lending in GB to expat landlords***

118. Of the Parties, only OSB is currently active in supplying BTL mortgages to expat landlord customers. However, as explained above in paragraph 122, Charter Court has in the recent past considered entry into this area on a number of occasions.
119. Unilateral effects can arise from the elimination of potential competition. One way in which this can occur is where the merger involves an incumbent supplier and a potential entrant that could have increased competition against the incumbent.<sup>75</sup>

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<sup>75</sup> [Merger Assessment Guidelines](#), paragraph 5.4.13 – 5.4.15.

120. The CMA, consistent with its established guidance,<sup>76</sup> assessed whether the Merger gives rise to a realistic prospect of an SLC as a result of horizontal unilateral effects from a loss of actual potential competition by reference to:
- (a) Whether Charter Court would be likely to enter the supply of BTL mortgages to expat customers in the absence of the Merger; and
  - (b) Whether such entry and expansion would lead to greater competition.

*Potential entry by Charter Court in the supply of BTL mortgages to expat customers*

121. Charter Court submitted to the CMA that [X] and provided documents discussing [X].
122. These documents show that Charter Court, [X], appears to have chosen to [X] as well as different strategic priorities within Charter Court. However, the CMA notes at the point in time when the Merger was first discussed between the Parties, [X]. For example, [X].<sup>77</sup> In addition, the relative timing of this decision ([X], when the Merger had been under consideration since June 2018) limits the weight that the CMA can place on [X].
123. The CMA observes that [X], raising the question of whether Charter Court might have entered in the supply of BTL mortgages to expat landlords in the foreseeable future absent the Merger. On the other hand, given its strength and experience across a range of products in the BTL segment and its continued consideration of this segment, the CMA considers there is evidence to suggest it might enter. The CMA has not ultimately had to conclude on whether potential entry by Charter Court into supplying BTL mortgages to expat landlords may have occurred absent the Merger as no competition concerns arise (see assessment from paragraph 124 onwards).

*Effect on competition of potential entry of Charter Court*

124. The CMA gathered evidence from OSB and third parties in order to estimate OSB's share of supply in BTL mortgages to expat landlords. The CMA estimated that OSB has a share of supply of up to [40-50]% and found many of the Parties' competitors were not active in supplying customers in this frame of reference. This is supported by the table provided by the Parties (and shown at paragraph 45), which shows that 10/21 lenders listed are active in supplying expat customers, fewer than in other customer segments.

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<sup>76</sup> [Merger Assessment Guidelines](#), paragraph 5.4.15.

<sup>77</sup> Para 3.2, Document 2 (Change Management Committee - Minutes of 24 January 2019).

125. The Parties submitted that the CMA's share of supply estimate for OSB will overstate its competitive position because: (i) other available data indicates that the CMA's estimated total market size for BTL lending to expat landlords is too small and so OSB's share is overstated; (ii) the estimate does not capture all of the alternative lenders active in supplying expat landlords; and (iii) there are additional competitors who have the capability to enter.
126. The Parties provided evidence that just two intermediaries brokered enough loans to account for the total market size the CMA has estimated (with many more intermediaries active in the market) suggesting that the CMA has understated the overall size of the market. The Parties also provided evidence that OSB originates just a small amount of these loans, and so cannot have a share of supply of [40-50]%. The CMA acknowledges that, due to the 'bottom-up' methodology used to calculate OSB's share, the CMA's estimate is likely to overstate OSB's position.
127. In addition, the Parties submitted that BTL mortgage lending to expat landlords is already highly competitive with many alternatives to OSB. The Parties provided evidence showing that [redacted] to expat landlord customers as indicated by [redacted] on the rankings of a broker sourcing system – OSB's BTL mortgage offer was ranked [redacted], with eight alternative lenders and their various products ranked [redacted].<sup>78</sup> These alternative lenders include State Bank of India, Foundation Home Loans, Saffron Building Society, Landbay and Axis Bank.
128. The CMA was able to confirm the presence of Foundation Home Loans, Aldermore, Shawbrook and Vida Homeloans in this frame of reference but was not able to collect data from a number of the other competitors active, increasing the likelihood of OSB's estimated share of supply being overstated.
129. The Parties submitted that there are other competitors, aside from Charter Court, who have recently started supplying these customers, or are capable to start doing so. They highlighted Paragon's recent decision to start supplying BTL mortgages to expat customers, announced in November 2018.
130. The CMA asked the Parties' competitors whether they had plans to start supplying BTL mortgages to expat customers, and what their procedures would be to do so. Competitors typically commented that it would take a few months to investigate and assess the risks of the customer segment, and then a few months to implement the decision. The CMA asked competitors whether they had plans to start lending to expat landlords, and one commented that

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<sup>78</sup> Each mortgage lender has multiple products listed, with positions 1-8 occupied by one lender, 9-15 by the second lender, and so on. OSB's products were ranked [redacted].

they did, and their proposition for expat landlord customers was ‘*currently under development*’ and they saw it as a ‘*market opportunity*’. One or two competitors commented that they saw expat customers as more risky than other segments, and that it may be outside their current risk appetite or would involve increased due diligence costs. No intermediaries told the CMA that there were fewer BTL mortgage options for expat landlord customers, and none expressed concerns about the impact of the Merger in this segment.

131. On balance, the CMA considers that there are sufficient lenders active in supplying BTL mortgages to expat landlord customers, and that, consistent with other customer segments, competitors (particularly those already active in specialist BTL lending and with higher risk appetites) have the ability to enter or expand their offering in a given segment relatively quickly and easily. On this basis, the CMA considers that BTL expat landlord customers are already well served by a variety of lenders who are already competing strongly such that any entry by Charter Court would not lead to greater competition than is already present in this segment for these customers.

#### *CMA conclusion*

132. For the reasons set out above, the CMA believes that, although it cannot rule out potential entry by Charter Court into supplying BTL mortgage lending to expat landlords, any such entry by Charter Court would not lead to greater competition owing to the current levels of competition and variety of lenders active. Accordingly, the CMA found that the Merger does not give rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in relation to the supply of BTL mortgages in GB to expat landlord customers.

#### ***Barriers to entry and expansion***

133. Entry, or expansion of existing firms, can mitigate the initial effect of a merger on competition, and in some cases may mean that there is no SLC. In assessing whether entry or expansion might prevent an SLC, the CMA considers whether such entry or expansion would be timely, likely and sufficient.<sup>79</sup>
134. The Parties listed a number of new or recent entrants across the frames of reference considered by the CMA, including Fleet, Vida Homeloans, Landbay and Zephyr.

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<sup>79</sup> [Merger Assessment Guidelines](#), from paragraph 5.8.1.

135. The Parties also submitted that mainstream lenders such as high-street banks are well-positioned to enter. The CMA observed that The Mortgage Works, BM Solutions and Godiva are present across a number of the BTL customer segments considered. The Mortgage Works has also recently started lending to limited company landlords, with the Parties' internal documents noting it as a potential constraint going forward (see paragraph 104).
136. As described elsewhere, the CMA recognises there is dynamism within BTL lending, with some customer segments being relatively new, and lenders entering and expanding in different customer segments over time (indeed, as the Parties did – see paragraphs 93 and 106). The CMA has considered this evidence within the competitive assessment as part of the competitive constraints that the Parties face. However, the CMA has not had to conclude on barriers to entry and expansion as the Merger does not give rise to competition concerns on any basis.

## **Decision**

137. Consequently, the CMA does not believe that it is or may be the case that the Merger may be expected to result in an SLC within a market or markets in the United Kingdom.
138. The Merger will therefore **not be referred** under section 33(1) of the Act.

**Andrea Gomes da Silva**  
**Executive Director, Markets and Mergers**  
**Competition and Markets Authority**  
**30 July 2019**

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<sup>i</sup> The data related to property valuations indicated approximately 1,700 HMO mortgage applications are placed each month with just two valuation firms (not in total).