ANTICIPATED ACQUISITION BY LONDON STOCK EXCHANGE GROUP PLC OF QUANTILE GROUP LIMITED

Issues Statement

16 June 2022

The CMA has excluded from the published version of the issues statement, information which the inquiry group considers should be excluded having regard to the three considerations set out in section 244 of the Act (specified information: considerations relevant to disclosure). The omissions are indicated by [✂]. Some numbers have been replaced by a range. These are shown in square brackets.

The reference

1. On 17 May 2022, the Competition and Markets Authority (**CMA**), in exercise of its duty under Section 33(1) of the Enterprise Act 2002 (the **Act**), referred the anticipated acquisition by London Stock Exchange Group plc (**LSEG)** of Quantile Group Limited (**Quantile**) (the **Merger**) for further investigation and report by a group of CMA panel members (the **Inquiry Group**). LSEG and Quantile are together referred to as the Parties and, for statements referring to the future, the **Merged Entity**.

2. In exercise of its duty under Section 36(1) of the Act, the CMA must decide:

   (a) whether arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation; and

   (b) if so, whether the creation of that situation may be expected to result in a substantial lessening of competition (**SLC**) within any market or markets in the United Kingdom (**UK**) for goods or services.

3. In answering these questions, we will apply a 'balance of probabilities' threshold to our analysis. That is, we will decide whether it is more likely than not that the Merger will result in an SLC.[1]

[1] Merger Assessment Guidelines (CMA129) – 2021 revised guidance (March 2021) (**MAGS)**, paragraph 2.36.

Purpose of this Issues Statement

4. In this Issues Statement, we set out the main issues that we are likely to consider in reaching our decision on the SLC question (paragraph 2(b) above), having had regard to the evidence available to us to date, including the evidence obtained in the CMA's phase 1 investigation. This does not preclude the consideration of any other issues which may be identified during the course of our investigation.

5. The CMA's phase 1 Decision (the **Phase 1 Decision**) contains much of the detailed background to this issues statement.[2] We are publishing this issues statement to assist parties submitting evidence to our phase 2 investigation. This statement sets out the issues we currently envisage being relevant to our investigation and we invite parties to notify us if there are any additional relevant issues which they believe we should consider.

6. At phase 2, while we are not precluded from considering any other issues which may be identified, we intend to focus our investigation on the areas in which the CMA found in the Phase 1 Decision that the Merger gives rise to a realistic prospect of an SLC – that is, as a result of vertical effects in relation to multilateral compression for over-the-counter interest rate derivatives (**OTC IRDs**) in the UK.[3,4]

7. We intend to use evidence obtained during the phase 1 investigation. However, we will also be gathering and considering further evidence on these and any other issues which may be identified during the course of the investigation.

Background

The Parties

8. LSEG is an international financial markets infrastructure and data business headquartered in London. LSEG has three main business activities in Europe:

[2] CMA, ANTICIPATED ACQUISITION BY LONDON STOCK EXCHANGE GROUP PLC OF QUANTILE GROUP LIMITED, Decision on relevant merger situation and substantial lessening of competition, 3 May 2022 (the **Phase 1 Decision.**)
[3] Multilateral compression is a risk-reduction technique by which a group of market participants contract with a multilateral compression provider to identify and replace multiple offsetting derivative contracts with fewer deals of the same net risk to reduce the notional value of their portfolio. By reducing the notional value of the portfolio, a customer reduces the capital that needs to be held, lowering the cost of engaging in those trades.
[4] CMA, Phase 1 Decision, paragraph 118.

(a) capital markets: LSEG offers access to capital for domestic and international participants, and electronic platforms for secondary market trading of equities, exchange-traded funds, fixed income and FX.[5]

(b) data & analytics: LSEG offers information and data products such as real-time and non-real-time data, pricing and reference services, indices, analytics and risk management services.[6]

(c) post trade: LSEG provides clearing and bilateral services as well as financial resource optimisation and reporting solutions. Amongst others, LSEG holds a majority shareholding in LCH Group, a multi-asset class global clearing house.[7]

9. The turnover of LSEG in the financial year 2021 was £7,165 million worldwide, of which approximately £[✂] million was generated in the UK.[8]

10. Quantile is a provider of portfolio compression and margin optimisation services for financial institutions dealing with derivatives instruments. Quantile was founded in 2015 and is headquartered in London. The turnover of Quantile in the financial year 2021 was £[✂] million worldwide, of which approximately £[✂] million was generated in the UK.[9]

Business activities and relevant overlap

11. LSEG's post-trade division mainly offers centralised risk management (ie insuring each party to a trade against counterparty risk in the post trade segment). Its LCH business acts as a central counterparty (**CCP**) for various types of trades. Quantile provides (i) portfolio compression services for cleared trades; and (ii) margin optimisation services for cleared and uncleared trades.[10] Multilateral compression providers for OTC IRDs rely on cooperation by LSEG's clearing house, LCH, to implement their multilateral compression proposals for trades cleared at LCH.[11]

[5] LSEG operates trading venues such as LSE, Turquoise and Tradeweb.
[6] LSEG owns FTSE Russell (a provider of financial indexing, benchmarking and analytic services) and Refinitiv (a financial markets data and infrastructure provider, which provides data and insights, trading platforms, and open data and technology platforms that enable customers to execute critical investing, trading and risk decisions).
[7] LSEG also operates UnaVista, a regulated technology platform that helps firms to reduce operational and regulatory risk through a range of regulatory reporting, reference data and analytics solutions.
[8] CMA, Phase 1 Decision, paragraph 25, and end note i.
[9] CMA, Phase 1 Decision, paragraph 26.
[10] CMA, Phase 1 Decision, paragraph 39, and end note ii.
[11] CMA, Phase 1 Decision, paragraph 9.

The Merger

12. On 6 December 2021, LSEG entered into a share purchase agreement to buy the entire issued and to be issued capital of Quantile.

13. The Merger is not yet complete and is conditional upon clearance by the CMA. The Parties informed the CMA that the Merger is not subject to review by any other competition authority.[12]

Our inquiry

14. Below we set out some specific areas that we intend to investigate in order to help parties who wish to make representations to us. However, these will not be the only areas for our assessment. For example, we will also consider the rationale for the Merger and any other relevant issues.

Jurisdiction

15. We shall consider the question of jurisdiction in our inquiry. A relevant merger situation exists where the following conditions are satisfied:[13]

    (a) Two or more enterprises have ceased to be distinct; and

    (b) Either:

        (i) the value of the target enterprise's UK turnover exceeded £70 million in its last fiscal year (the turnover test); or

        (ii) the enterprises ceasing to be distinct have a share of supply in the UK, or in a substantial part of the UK, of 25% or more in relation to goods or services of any description (the share of supply test).

16. The CMA found in its Phase 1 Decision that it had jurisdiction to review the Merger on the basis that it is or may be the case that:[14]

    (a) each of LSEG and Quantile should be considered an enterprise and that these enterprises will cease to be distinct as a result of the Merger.

    (b) the Parties have a combined share of supply of more than 25% with an increment of more than [10-20%] either by revenue or volume in the supply

[12] CMA, Phase 1 Decision, paragraphs 27 to 28.
[13] Section 23 of the Act.
[14] CMA, Phase 1 Decision, paragraphs 30 to 34.

of portfolio compression services in the UK in 2021.[15] Therefore, the CMA found that the share of supply test in of the Act is met.

The counterfactual

17. The application of the SLC test involves a comparison of the prospects for competition with the merger against the competitive situation without the merger. The latter is called the 'counterfactual'. The counterfactual is not a statutory test but rather an analytical tool used in answering the question of whether a merger gives rise to an SLC.[16]

18. For anticipated mergers the CMA generally adopts the prevailing conditions of competition as the counterfactual against which to assess the impact of the merger. In its phase 1 decision, the CMA found no evidence supporting a different counterfactual.[17]

19. We currently intend to adopt the prevailing conditions of competition as the most likely counterfactual to the Merger but welcome any evidence on this part of our assessment.

Assessment of competitive effects of the Merger

Theory of harm

20. The term 'theory of harm' describes the possible ways in which an SLC could arise as a result of a merger. The theory of harm provides the framework for our analysis of the competitive effects of a merger.[18] Identifying a theory of harm in this issues statement does not preclude an SLC from being identified on another basis following receipt of additional evidence or further analysis. We welcome views on the theory of harm described below.

21. Subject to the evidence we obtain during our investigation, we intend to assess whether the Merger may be expected to result in an SLC as a result of vertical effects in relation to multilateral compression for OTC IRDs in the UK.

22. Vertical effects may arise when a merger involves firms at different levels of the supply chain, for example a merger between a firm and an upstream supplier or a downstream customer. In certain circumstances vertical mergers can weaken rivalry, for example when they result in foreclosure of the merged firm's

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[15] CMA, Phase 1 Decision, paragraph 32.
[16] MAGs, paragraph 3.1.
[17] CMA, Phase 1 Decision, paragraphs 35 to 37.
[18] MAGs, paragraph 2.11.

competitors. This would weaken the constraints that the merged entity faces and, as a result, harm competition and therefore customers.[19]

23. In assessing a foreclosure theory of harm, the CMA's approach is to consider whether three cumulative conditions are satisfied:

(a) Ability: Would the merged entity have the ability to use its control of inputs (input foreclosure) or to restrict rivals' access to a customer (customer foreclosure) to harm the competitiveness or incentive to compete of its rivals?

(b) Incentive: Would it have the incentive actually to do so, ie would it be profitable?

(c) Effect: Would the foreclosure of these rivals substantially lessen overall competition?[20]

24. In the Phase 1 Decision, the CMA found there was a realistic prospect of an SLC as a result of input foreclosure effects. This could be through total foreclosure, whereby the Merged Entity ceases to approve rival providers of multilateral compression services for OTC IRDs cleared at LCH. Alternatively, it could be through partial foreclosure whereby the Merged Entity increases prices, reduces quality or otherwise worsens the terms now or in the future to Quantile's rivals (and indirectly to their customers). For example, partial foreclosure mechanisms could include (i) LCH arranging for the timing and frequency of compression runs to be scheduled in Quantile's favour; (ii) LCH providing data or information to Quantile that gives it an advantage over rival multilateral compression providers; (iii) LCH changing the order of compression files so that Quantile files are always processed first; or (iv) LCH increasing ACSP fees or changing the fee structure in a way that disadvantages Quantile's rivals.[21]

25. In relation to the ability to engage in foreclosure:[22]

(a) the CMA found that LCH has significant market power in the provision of clearing services for OTC IRDs with a stable share of supply of around 90% (by notional cleared) between 2018-2021.

(b) Feedback from clearing house customers confirmed that switching from one clearing house to another is difficult. Around 75% of OTC IRDs are

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[19] MAGs, paragraph 7.2.
[20] MAGs, paragraph 7.10.
[21] CMA, Phase 1 Decision, paragraph 69.
[22] CMA, Phase 1 Decision, paragraph 12.

cleared and the CMA considers that LCH has significant market power in the provision of clearing services for OTC IRDs.

(c) The CMA therefore found that multilateral compression providers who wish to offer their services in relation to OTC IRDs need the ability to offer to compress trades cleared at LCH.

(d) Based on third-party feedback, the CMA found that LCH retains a margin of discretion in granting Approved Compression Service Provider (**ACSP**) status to a multilateral compression provider and that LCH could engage in foreclosure strategies either by declining to grant status, or by providing lower quality services to competing compression providers that do obtain such status.

(e) Finally, the CMA found there is no legal impediment for LCH to deviate from its current (open access) governance model.

26. In relation to the Merged Entity's incentive to engage in foreclosure, the CMA found that:[23]

(a) partial foreclosure strategies aimed at Quantile's rivals in multilateral compression would be unlikely to significantly harm the Merged Entity, especially strategies that could be justified by LCH.

(b) any costs of engaging in total or partial foreclosure for the Merged Entity are likely to be limited. One cost is the risk of retaliation by customers, which the Parties argued would constrain their conduct. Based on the available evidence, including third-party feedback, the CMA found that, although customers would disapprove of the Merged Entity's behaviour, they would not be able to move a significant number of OTC IRD trades from LCH to another clearing house, given switching is difficult. Furthermore, the available evidence does not show that customers would switch part of their spend on other LSEG services to alternative providers of those services. Based on the available evidence, the CMA found customer switching would be limited and would not be enough to offset the benefits from foreclosure.

(c) the foreclosure strategies aimed at Quantile's rivals in multilateral compression would benefit the Merged Entity substantially, allowing it to gain market power in multilateral compression.

[23] CMA, Phase 1 Decision, paragraph 13.

27. With regard to the effect of any foreclosure strategy, the CMA found that multilateral compression for OTC IRDs is already concentrated, with TriOptima and Quantile being the main providers. The CMA therefore found that foreclosure is likely to have a negative impact for customers as a loss of choice and competition may increase prices and reduce quality and innovation.[24]

28. We will consider whether the Merger may be expected to result in an SLC as a result of vertical input foreclosure in the provision of multilateral compression for OTC IRDs in the UK.

29. To assess this vertical theory of harm, we shall consider evidence on the ability and incentive of the Merged Entity to pursue foreclosure strategies such as those identified at paragraph 24 and the effect that this could have on competition. We intend to consider evidence in relation to:

    (a) Ability: (i) whether LCH has market power in the supply of clearing services for OTC IRDs; (ii) whether restricting Quantile's rivals access to OTC IRDs cleared at LCH would harm rivals' competitiveness due to the importance of such inputs for the provision of multilateral compression services; and (iii) whether there are any other constraints on the Parties' ability to pursue foreclosure strategies, for example due to regulatory requirements or LSEG's governance with respect to the provision of open access.

    (b) Incentive: (i) quantitative evidence on margins and switching patterns; and (ii) qualitative evidence on firms' business plans and overall strategies, including further evidence on whether the risk of retaliation by customers would constrain the Parties' conduct.

    (c) Effect: drawing on the evidence considered under (a) and (b) above, the pre-existing position of the Merged Entity downstream, and whether a sufficient number of rivals with sufficient scale will be unaffected.

30. As noted in paragraph 20 above, the identification of a theory of harm does not preclude an SLC being identified on another basis following further work by the CMA, or the receipt of additional evidence. For example, the CMA may consider whether the proposed transaction may lead to a strengthening of LSEG's and/or LCH's market position in other ways. The CMA remains open to the investigation of such issues should this be appropriate.

[24] CMA, Phase 1 Decision, paragraph 14.

Market definition

31. Where the CMA makes an SLC finding, this must be 'within any market or markets in the United Kingdom for goods or services'.[25] The CMA is therefore required to identify the market or markets within which an SLC exists. An SLC can affect the whole or part of a market or markets. Within that context, the assessment of the relevant market is an analytical tool that forms part of the analysis of the competitive effects of a merger and should not be viewed as a separate exercise.[26]

32. At Phase 1, the CMA found that the Parties and their competitors provided multilateral compression services to global customers; and with respect to the geographic frame of reference, the CMA did not see any evidence that market conditions differ significantly between the UK and the rest of the world. In the Phase 1 Decision, the CMA therefore considered the impact of the Merger on the supply of multilateral compression services for OTC IRDs globally.[27]

33. We will use the frame of reference adopted in the Phase 1 Decision as a starting point for our analysis and our view of market definition will be drawn largely from the findings of our competitive assessment. Where relevant, we will consider out-of-market constraints and/or any differences in the degree of competitive constraints on the Merged Entity from different suppliers.

Countervailing factors

34. We will consider whether there are countervailing factors which are likely to prevent or mitigate any SLC that we may find. Some of the evidence that is relevant to the assessment of countervailing factors may also be relevant to our competitive assessment.

35. In the Phase 1 Decision, the CMA found that entry or expansion in multilateral compression services for OTC IRDs would not be timely, likely or sufficient to mitigate any SLC arising.[28]

36. We will consider evidence on entry and/or expansion by third parties and whether such entry or expansion would be timely, likely, and sufficient to prevent any SLC from arising as a result of the Merger.[29] We will also consider

[25] Section 36(1)(b), the Act.
[26] MAGs, paragraph 9.1.
[27] CMA, Phase 1 Decision, paragraph 57.
[28] CMA, Phase 1 Decision, paragraph 197.
[29] MAGs, paragraphs 8.30 and 8.31.

evidence from the Parties, to the extent relevant, in relation to efficiencies arising from the Merger.[30]

Possible remedies and relevant customer benefits

37. Should we conclude that the Merger may be expected to result in an SLC within any market or markets in the UK, we will consider whether and, if so, what remedies might be appropriate.

38. In any consideration of possible remedies, we may in particular have regard to their effect on any relevant customer benefits (**RCBs**) that might be expected to arise as a result of the Merger and, if so, what these benefits are likely to be and which customers would benefit.[31]

Responses to this Issues Statement

39. Any party wishing to respond to this Issues Statement should do so in writing, by no later than **30 June 2022** by emailing your written submission to LSEG_Quantile@cma.gov.uk.

[30] MAGs, paragraph 8.2. At phase 2, in order to form a view that claimed efficiencies will enhance rivalry such that an anticipated merger may not be expected to result in an SLC, the CMA must expect that the following criteria will be met: The merger efficiencies must (a) enhance rivalry in the supply of those products where an SLC may otherwise arise; (b) be timely, likely and sufficient to prevent an SLC from arising; (c) be merger-specific; and (d) benefit customers in the UK (paragraph 8.8). Evidence of claimed efficiencies must also be verifiable (paragraph 8.7).

[31] Merger Remedies (CMA87) (December 2018), paragraphs 3.4 and 3.15 to 3.24.