Anticipated acquisition by London Stock Exchange Group Plc of Quantile Group Limited

Summary of provisional findings

Notified: 9 September 2022

Overview

1. The Competition and Markets Authority (**CMA**) has provisionally found that the anticipated acquisition by London Stock Exchange Group Plc (**LSEG**) of Quantile Group Limited (**Quantile**) (the **Merger**) may not be expected to result in a substantial lessening of competition in the supply of multilateral compression of over-the-counter interest rate derivatives (**OTC IRDs**) in the UK as a result of input foreclosure.

2. This is not our final decision, and we invite any interested parties to make submissions on these provisional findings by no later than 5pm on Friday 30 September 2022. Please make any response to these findings by email to LSEG_Quantile@cma.gov.uk. We will take all submissions received by this date into account in reaching our final decision.

Who are the businesses and what services do they provide?

3. The Merger relates to the provision of post-trade services, ie services that are performed after a trade is agreed.

4. LSEG operates a business, LCH Ltd (**LCH**), that acts as a clearing house for various types of trades. Trades are first agreed and then are 'cleared' (so that each party can be sure the trade will go ahead – removing the risk that the other party to the trade might fail (ie the counterparty risk)). The activities of LCH in clearing OTC IRDs are the most relevant to our assessment of the Merger.

5. Quantile provides a range of optimisation services for financial institutions dealing with derivative instruments, including multilateral compression

services for OTC IRDs cleared at LCH. Multilateral compression is a capital and risk management technique by which market participants replace multiple offsetting derivative contracts with fewer contracts of the same net risk to reduce the notional value of their portfolio. This reduces market participants' overall regulatory capital costs by minimising the positions (or line items) which give rise to capital costs.

6. LSEG and Quantile are each a **Party** to the Merger; together they are referred to as the **Parties** and, for statements relating to the future, the **Merged Entity**.

What evidence have we looked at?

7. In assessing this Merger, we looked at a wide range of evidence that we considered in the round to reach our provisional findings.

8. We received several submissions and responses to information requests from the Parties and held a site visit and hearings with each of them. We also examined the Parties' internal documents, which show (among other things) how they run their businesses and the Parties' plans for the future of their businesses.

9. We gathered evidence from customers and competitors via written questions and discussions to understand better the competitive landscape and get their views on the impact of the Merger. This included evidence from 13 of the 14 SwapClear Banks. The SwapClear Banks are a group of large global banks and broker dealers who were involved in the development of LCH's IRD clearing service and are important customers of LCH in clearing services and Quantile and its competitors in multilateral compression services. They are also important customers of LSEG.

10. Finally, we considered evidence from the Parties and third parties received during our phase 1 investigation of the Merger.

What would have happened absent the Merger?

11. To determine the impact that the Merger may have on competition, we have considered what would have happened absent the Merger. This is known as the counterfactual.

12. For an anticipated merger such as this, we generally adopt the prevailing conditions of competition as the counterfactual against which to assess the impact of the Merger and, in this case, we have found no evidence to support a different counterfactual. Our provisional conclusion is, therefore, that the counterfactual is the prevailing conditions of competition.

The effects of the Merger

13. The Parties do not compete directly with each other, but providers of multilateral compression services need to work with clearing houses in order to offer their services to end customers (banks and other traders). Our investigation focused on whether, following the Merger, LCH might reduce access to Quantile's rivals, thereby harming competition in multilateral compression.

14. In light of high and stable shares of supply, network effects and barriers to switching, we have provisionally found that LCH has market power upstream in the provision of clearing services for OTC IRDs. The evidence we have seen shows that LCH's involvement is essential for providers wishing to offer multilateral compression of trades cleared at LCH, which account for a substantial part of all OTC IRDs. This means that LCH controls key inputs to downstream providers of multilateral compression services. We consider that there are a range of ways that LCH could potentially disadvantage Quantile's rivals such as limiting the days on which they could access LCH to carry out compression runs or limiting the support available to those rivals when they seek to introduce improvements to their service offerings.

15. We considered whether there are regulations or other restrictions on LCH's ability to disadvantage Quantile's rivals. The evidence shows that neither the applicable regulatory framework nor LCH's internal governance arrangements would prevent LCH from engaging in foreclosure strategies. On this basis, our provisional view is that the Merged Entity would have the ability to engage in foreclosure strategies.

16. We considered the Merged Entity's incentive to foreclose Quantile's rivals by analysing the benefits and costs of foreclosure. There are currently just two providers of multilateral compression of OTC IRDs cleared at LCH: Quantile and TriOptima. This means that if TriOptima were to lose sales as a result of foreclosure by LCH, Quantile would be well placed to capture those sales and increase its profits. In assessing LSEG's incentive to foreclose Quantile's rivals, we have considered the magnitude of the potential gains to Quantile as compared to any potential consequential losses to the Merged Entity.

17. We have received evidence that Quantile and LCH's customers value having access to more than one provider of multilateral compression services at LCH. Access to more than one provider increases operational resilience and enables customers to obtain better services through competition. Customers would lose these benefits if TriOptima were foreclosed.

18. In terms of revenues, the supply of multilateral compression services is small compared to the other services provided by the Merged Entity to the same customers. This means that losing a small proportion of these other revenues would be sufficient to offset any potential gain from foreclosure related to multilateral compression.

19. The main potential cost of foreclosing would be the response of TriOptima's customers, who are also major customers of the Merged Entity. These customers would be harmed if TriOptima were foreclosed and therefore might take action to prevent foreclosure. These customers told us that they would be able to detect and deter any attempt at foreclosure by LCH.

20. The first mechanism to which customers pointed for preventing foreclosure was raising complaints with LCH (and LSEG) through a number of direct and indirect channels. While customers indicated that they believed LCH would respond to such complaints, we consider that LCH would only respond to such complaints where they are likely to impact LCH's profitability. We have given more weight to the evidence on customer switching described in the second mechanism below, as this directly impacts the revenues and profitability of the Merged Entity, and therefore the incentives to engage in foreclosure.

21. The second mechanism that customers pointed to for preventing foreclosure was switching certain business away from the Merged Entity. We considered both the possibility that customers could switch clearing business away from LCH and the possibility that customers could switch other types of business away from the Merged Entity.

22. With respect to clearing, while some customers indicated that it would be possible to switch away from LCH for clearing OTC IRDs, most customers told us that this would not be possible. Switching away from LCH was seen as difficult and requiring collective action over the medium term.

23. With respect to other types of business, customers highlighted broader interactions with LSEG and Quantile in relation to other services, including the option not to support new services. However, switching away from other (new or existing) LSEG or Quantile services would require customers to switch away from their first choice of provider or to choose not to adopt new services which might benefit them.

24. Nevertheless, some customers told us that they would be motivated to incur the cost of these responses because of the importance of having a second multilateral compression provider at LCH.

25. The value of the business that the same customers have with the Merged Entity is much larger than the value of the compression services provided by each of Quantile and TriOptima. As a result, the prospect of even a relatively low proportion of switching by these customers would offset any potential gains from foreclosure and would be a significant risk to the Merged Entity. Based on the evidence from customers, we judged that, the likely response would be sufficient to more than offset the benefits of foreclosing. On this basis, our current view is that the Merged Entity would not have the incentive to engage in foreclosure strategies.

Provisional conclusion

26. We have provisionally found that the anticipated acquisition by LSEG of Quantile may not be expected to result in a substantial lessening of competition as a result of vertical effects in the supply of multilateral compression services for OTC IRDs in the UK.