DETERMINATION OF MERGER NOTIFICATION

M/21/076

PTSB/CERTAIN ASSETS OF ULSTER BANK

21 July 2022

Coimisiún um Iomaíocht agus Cosaint Tomhaltóirí
Competition and Consumer Protection Commission

CCPC

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1. INTRODUCTION

Introduction

1.1 On 22 December 2021, in accordance with section 18(1)(a) of the Competition Act 2002, as amended (the "Act"), the Competition and Consumer Protection Commission (the "Commission") received a merger notification form (the "Merger Notification Form") of a proposed transaction whereby Permanent TSB plc ("PTSB") would acquire certain assets from Ulster Bank Ireland DAC ("Ulster Bank"), including: Ulster Banks' performing non-tracker mortgage loans; a subset of Ulster Bank's non-performing non-tracker loans; Ulster Bank's performing micro SME business direct loan book; 25 properties in the Ulster Bank branch network; and, Ulster Bank's asset finance loan business (together, the "Target Assets") (the "Proposed Transaction").

The Proposed Transaction

1.2 PTSB, Ulster Bank and NatWest Group plc ("NatWest") (the "Parties") entered into a framework agreement dated 17 December 2021 (the "Framework Agreement") and two mortgage sale deeds dated 17 December 2021 (the "MSDs") which contain the key commercial terms of the Proposed Transaction. In addition to the Framework Agreement and MSDs, the Parties have concluded other transaction documents including: an agreement to govern operational arrangements in relation to the migration of the assets from Ulster Bank to PTSB (the "On-Boarding Agreement"); two business transfer agreements relating to the asset finance business (the "BTAs"); and a contract for sale agreement relating to the transfer of certain properties.

1.3 Under the Framework Agreement, RBS AA Holdings (UK) Limited ("RBS AA"), a subsidiary of NatWest, will acquire a minority equity stake of 16.66% of the total issued ordinary share capital of Permanent TSB Group Holdings plc ("PTSB Group Holdings plc"), the parent company of PTSB.[1] RBS AA will have only investor

[1] The Commission understands from the notification that this stake is a means of PTSB partly paying for the Target Assets and [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂].

protections which are commensurate with the standard rights accorded to minority shareholders to protect their financial interests as investors but no additional rights in respect of the strategic commercial behaviour or control of PTSB Group Holdings plc.

1.4 The MSDs also provide for the transfer of Ulster Bank employees ("Anticipated Employees") to PTSB, under the European Communities Transfer of Undertakings Regulations 2003 (the "TUPE Regulations").

1.5 In sum, the Framework Agreement, the MSDs and the BTAs, together with the On-Boarding Agreement, provide for the transfer to PTSB of Ulster Bank's rights, interests, obligations, and benefits, with respect to the Target Assets.

1.6 Following the implementation of the Proposed Transaction, PTSB will hold the rights, claims, and obligations associated with the Target Assets, and thus have sole control over the Target Assets.

The Undertakings Involved

The Acquirer - PTSB

1.7 PTSB is a public limited company registered in the Republic of Ireland (the "State") under company number 222332.

1.8 PTSB is wholly owned by PTSB Group Holdings plc, the shares of which are listed on Euronext Dublin and the London Stock Exchange. The Minister for Finance holds 74.92% of the ordinary shares of PTSB Group Holdings plc. The relationship between PTSB Group Holdings plc and the Minister for Finance is governed by a relationship agreement.

1.9 PTSB is a provider of retail and SME banking operating exclusively in the State. PTSB provides a range of banking products such as business and personal current accounts, overdrafts, mortgages, business and personal loans, credit cards and home insurance.

1.10 For the financial year ending 31 December 2021, PTSB's turnover was €313 million, all of which was generated in the State.

The Seller - Ulster Bank

1.11 Ulster Bank is a designated activity company registered in the State under company number 25766.

1.12 Ulster Bank is a wholly-owned indirect subsidiary of NatWest. Ulster Bank is a full-service retail and commercial bank. Ulster Bank's business is formed of two distinct divisions: personal banking and commercial banking.

The Target Assets

1.13 According to the Framework Agreement, the Target Assets include the following assets of Ulster Bank:

- Ulster Bank's entire book of performing non-tracker mortgage loans[2];
- A subset of Ulster Bank's non-performing non-tracker mortgage loans. The subset is those that, as at 30 June 2021 or the date falling three months prior to the Principal Completion Date, have nil arrears, the customer is meeting contractual payments and is on a 12-month probation period (together with the book of performing non-tracker mortgage loans, the "Mortgage Book");
- the entire performing micro SME ("microenterprise") Business Direct loan book of Ulster Bank (the "Microenterprise Business Direct Loan Book")[3],[4];

[2] Valued at approximately €7 billion as of 30 June 2021.

[3] Valued at approximately €230 million as of 30 June 2021.

[4] PTSB defines SMEs in line with the EU definition of SMEs contained in Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprise (2003/361/EC). This includes businesses that employ fewer than 250 persons and which has either or, both of the following: (i) an annual turnover not exceeding €50 million; (ii) an annual balance sheet total not exceeding €43 million. This Recommendation defined a microenterprise as "an enterprise which employs fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 2 million".

- the entire asset finance loan business of Ulster Bank (the "Asset Finance Loan Business")[5]; and,
- 25 properties in the Ulster Bank branch network (the "Target Branches").

1.14 The Target Assets do not include other products or services offered by Ulster Bank, such as:

- Ulster Bank current accounts;
- Ulster Bank overdrafts;
- Ulster Bank deposit accounts; or,
- Ulster Bank loans for larger SMEs and corporate customers.

1.15 Regarding Ulster Bank employees, PTSB states the following in the Merger Notification Form:

> *"Certain employees of Ulster Bank will be entitled to transfer to PTSB pursuant to the [TUPE Regulations]".*

Rationale for the Proposed Transaction

1.16 The Parties have stated the following in the Merger Notification Form:

> *"The Proposed Transaction arises in the context of NatWest's decision on 19 February 2021 to begin a phased withdrawal from Ireland. Following a strategic review of Ulster Bank, NatWest concluded that "Ulster Bank in the Republic of Ireland will not be in a position to achieve an acceptable level of sustainable returns over its planning horizon."[6] Accordingly, NatWest announced that it "… intends to begin a phased withdrawal from the Republic of Ireland over the coming years that will be managed in an*

[5] Valued at approximately €400 million as of 30 June 2021.

[6] For more information on NatWest's Press Release on the outcome of strategic review into Ulster Bank in the Republic of Ireland, see: https://otp.tools.investis.com/clients/uk/rbs3/rns/regulatorystory.aspx?cid=365&newsid=1454197

orderly and considered manner."[7] *… From PTSB's perspective, the Proposed Transaction represents a significant opportunity for PTSB, its stakeholders and its customers to grow its position in the Irish banking sector and position it for future growth. The Proposed Transaction would provide PTSB with a larger customer base, [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]. Following the Proposed Transaction, [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]."*

Preliminary Investigation ("Phase 1")

Contact with the Undertakings Involved

1.17 On 31 January 2022, the Commission served two Requirements for Further Information (the "Phase 1 RFIs"): one on PTSB, and a second on Ulster Bank/Natwest, pursuant to section 20(2) of the Act. The service of the Phase 1 RFIs adjusted the deadline within which the Commission had to inform the notifying parties of the determination the Commission had made in respect of the Proposed Transaction in Phase 1.

1.18 Upon receipt of all responses to the Phase 1 RFIs, the "appropriate date" (as defined in section 19(6)(b)(i) of the Act) became 28 March 2022.[8]

1.19 During the Phase 1 investigation, the Commission requested and received, on an ongoing basis, further information and clarifications from the Parties.

1.20 The Commission also conducted market enquiries during the Phase 1 investigation and engaged with third parties in relation to its assessment of the competitive effects of the Proposed Transaction. This engagement included the sending of questionnaires to competitors of the Parties, regulators, and other industry stakeholders.

[7] Ibid.

8 The "appropriate date" is the date from which the time limits for making both Phase 1 and Phase 2 Determinations begin to run.

Third Party Submissions

1.21 During the Phase 1 investigation, the Commission received submissions from 4 third parties in relation to the Proposed Transaction.[9] The submissions were fully considered by the Commission insofar as they expressed competition concerns.

Market Enquiries

1.22 During the Phase 1 investigation, the Commission sent questionnaires to various third parties, including:

(a) 25 mortgage brokers or brokers' associations active in the State;[10]

(b) 6 of the parties identified by PTSB and Ulster Bank as their competitors (the "Competitor Questionnaire").[11]

1.23 The Commission received a response from 20% of the brokers to whom it sent a questionnaire.[12] In the case of each broker which provided a response, the Commission also contacted those brokers by telephone and/or email to clarify and/or seek further detail in relation to their responses.

1.24 The Commission received a response from each of the competitors to whom it sent a questionnaire. In each case, the Commission also contacted those

9 These were: Askaboutmoney.com/Brendan Burgess; Complainant 1; Complainant 2; and, Complainant 3.

10 These were: Association of Mortgage Advisors ("AIMA"); Full Circle Financial Services Limited ("Full Circle"); Michael Cassidy Financial Services Limited ("Michael Cassidy"); Irish Mortgage Corporation Limited ("Irish Mortgage Corporation"); Mortgage Horizons Limited ("Mortgage Horizons"); PHD Financial Services Limited ("Ocean Mortgages"); PFP Financial Services Limited ("PFP Financial Services"); New Star Financial Management Limited ("New Star"); MoneyTree Finance Limited ("Cork Mortgage Broker"); Kevin Condon Financial Brokers Limited ("Mortgage Search"); Munster Mortgage & Finance Company Limited ("Munster Mortgage & Finance"); Murray & Spelman (Financial Services) Limited ("Murray and Spelman Financial Services"); First Choice Financial Services DAC ("Mortgage ABC"); Pangea Ireland Digital Limited ("Pangea Mortgages"); T&M Financial Limited ("Mortgage Plus"); MBL Financial Services Limited ("Mortgage Express"); Paul Murphy ("Phoenix Financial Services"); SEFS Limited ("Southeast Financial Services and Southeast Mortgages"); Cormac Woods Financial Services Limited ("Acorn Financial Services"); Tredagh Life Assurance Pension & Investments Limited ("Capital Masters"); Neptune Magnus Financial Solutions Limited ("Neptune Financial"); Tracy Beirne ("Tracy Beirne Financial Services"); Money Maximising Advisors Limited; True Financial Limited t/a Lowquotes and SafeNET Financial ("Low Quotes"); and, DMP Financial Limited.

11 These were: Allied Irish Banks plc ("AIB"); Avantcard DAC ("Avant"); Bank of Ireland plc ("BOI"); Dilosk DAC trading as Dilosk ICS Mortgages ("Dilosk"); Finance Ireland Credit Solutions DAC ("Finance Ireland"); and, KBC Bank Ireland plc ("KBC").

12 5 out of 25 third parties.

competitors by telephone and/or email to clarify and/or see further detail in relation to their responses.

1.25 During the Phase 1 investigation, the Commission arranged discussions with a number of other existing and potential competitors.[13]

The Phase 1 Investigation

1.26 Having considered all the available information in its possession at the time, the Commission was unable to form the view, at the conclusion of its Phase 1 investigation, that the result of the Proposed Transaction would not be to substantially lessen competition in any market for goods or services in the State.

1.27 On 30 May 2022, the Commission determined, in accordance with section 21(2)(b) of the Act, to carry out a full investigation under section 22 of the Act.

Full Investigation (“Phase 2”)

Contact with the Undertakings Involved

1.28 On 26 May 2022, the Commission served two Requirements for Further Information (the “Phase 2 RFIs”): one on PTSB, and a second on Ulster Bank/NatWest, pursuant to section 20(2) of the Act. The service of the Phase 2 RFIs adjusted the deadline by which the Commission was required to issue its assessment of the Proposed Transaction in Phase 2.

1.29 The parties each provided a full response to the Phase 2 RFIs on 20 June 2022.

1.30 During the Phase 2 investigation, the Commission requested and received, on an ongoing basis, further information and clarifications from the Parties.

Third Party Submissions

[13] These were: Revolut Limited (“Revolut”); N26 GmBH (“N26”); Cedar Lending Services Limited (“MoCo”); Starling Bank Limited (“Starling”); Octopus Capital Limited (“Octopus”); First Citizen Finance DAC (“First Citizen”); and, An Post Designated Activity Company (“An Post”).

1.31 During the Phase 2 investigation of the Proposed Transaction, the Commission received 2 third party submissions in relation to the Proposed Transaction.[14] The submissions were fully considered by the Commission insofar as they expressed competition and consumer harm concerns.

Market Enquiries

1.32 During the Phase 2 investigation, the Commission sent a questionnaire to competitors requesting copies of data they supply to the Banking & Payments Federation Ireland (the "BPFI").[15]

1.33 The Commission received a response from all of the competitors to whom it sent a questionnaire.

1.34 During the Phase 2 investigation, the Commission continued the process initiated during the Phase 1 investigation of seeking the views of and engaging with third parties in relation to their assessment of the competitive effects of the Proposed Transaction, including mortgage brokers, industry or sector competitors, industry stakeholders, and other parties active in the Proposed Transaction. Relevant third-party views are also referenced throughout this Determination.

1.35 In forming its conclusions as set out in this Determination, the Commission has considered all the relevant information available to it at the time of making the Determination, including information provided by the Parties in response to the Commission's RFIs and Information Requests, information obtained from third parties, and other information available in the public domain.

[14] These were: MoCo; and, Complainant 4.

[15] These were: Allied Irish Banks plc ("AIB"); Avantcard DAC ("Avant"); Bank of Ireland plc ("BOI"); Dilosk DAC trading as Dilosk ICS Mortgages ("Dilosk"); Finance Ireland Credit Solutions DAC ("Finance Ireland"); and, KBC Bank Ireland plc ("KBC").

2. INDUSTRY BACKGROUND

Introduction

2.1 The Parties are both active in the provision of banking services in the State. This section firstly provides an overview of the Irish retail banking sector including the role of the Irish Government and the relevant regulatory framework in which the providers of retail banking services in the State operate. The section then focuses specifically on describing the key segments of the market relating to the Ulster Bank assets that PTSB will acquire as a consequence of the Proposed Transaction.[16]

2.2 The Commission's description of the relevant industry background is structured as follows:

(a) Overview of retail banking services;

(b) Mortgage lending in the State; and

(c) Lending to SMEs in the State.

Overview of Retail banking services

2.3 Retail banking comprises all banking services provided to private individuals and small enterprises, typically including:

(a) Deposit and account services: current accounts, savings accounts, cash deposits, cheque collection;

(b) Payment services: ATM services, payment card issuing, credit transfer, direct debit, standing orders and cheques;

(c) Lending: personal loans, small business loans, consumer credit, overdraft facilities, mortgages; and,

[16] See paragraph 1.13 for a description of the Target Assets.

(d) Investment Products: mutual funds, pension funds and securities brokerage and custody services.

Providers of retail banking services in the State

2.4 At present, there are five full service retail banks operating in Ireland. AIB, BOI and PTSB are Irish incorporated banks, while Ulster Bank and KBC are subsidiaries of foreign banking groups, namely, NatWest Group plc and KBC Group N.V., respectively.[17]

2.5 In addition to retail banks, a number of non-bank finance providers also operate in the State, including specialist lenders such as Avant Money, Dilosk and Finance Ireland, as well as An Post and the credit union network. Some retail banking services are provided, such as payment and transaction services, through fintech companies, such as Revolut and N26.

2.6 Figure 1 below sets out the different providers of a retail banking service(s) in the State.

Figure 1: A snapshot of providers of a Retail Banking Service(s) in the State, 2021.

Source: BPFI "Future of Retail Banking in Ireland" Report (2021).[18]

Role of the Government in the Irish banking sector

2.7 In 2009, to assist in addressing the difficulties brought about by the financial crisis, the Government utilised the assets of the National Pension Reserve Fund to invest

[17] See Section 5 for a description of the status of KBC in the State. KBC stopped accepting new applications for KBC products since 15 July 2022.

[18] https://bpfi.ie/wp-content/uploads/2021/09/BPFI-Future-of-Retail-Banking-in-Ireland-Report.pdf.

in Irish banks and contribute to the EU/IMF Programme of Financial Support for Ireland.[19] These include investments in AIB, BOI and PTSB.[20]

2.8 The State holds 70.97% of AIB's shares, an equity stake below 4% in BOI[21] and a 74.92% shareholding in PTSB as at 21 July 2022.[22] Government policy is to return the banking sector to private ownership in a phased manner that maximises the recovery value to the taxpayer. Each of the banks remain separate economic units with independent powers of decision and their respective boards and management teams retain responsibility and authority for determining strategy and commercial policies (including business plans and budgets) and conducting day-to-day operations.

Regulatory framework

2.9 The CBI regulates more than 10,000 firms providing financial services in Ireland and overseas. The objective of the CBI's regulatory role is to safeguard financial and price stability, consumer protection, and market integrity. The financial crisis was caused by an excessive expansion of credit and of the financial system more broadly. Consequently, across the world authorities responsible for promoting financial stability took measures to reduce the risk of such systemic crises reoccurring through the enactment of macro-prudential policies. These regulatory policies are aimed at the promotion of the stability of the financial system as a whole.[23] However, the measures introduced to implement these policies impact on the ability and profitability of banks to engage in mortgage lending in the State.

Capital Requirements

2.10 Following the financial crisis, EU Member States implemented a framework for setting minimal capital requirements for banks. In 2013, the Capital Requirements

[19] https://www.audit.gov.ie/en/find-report/publications/2011/2010-annual-report-chapter-08-national-pensions-reserve-fund.pdf.

[20] https://www.gov.ie/en/organisation-information/f95734-the-shareholding-and-financial-advisory-division/.

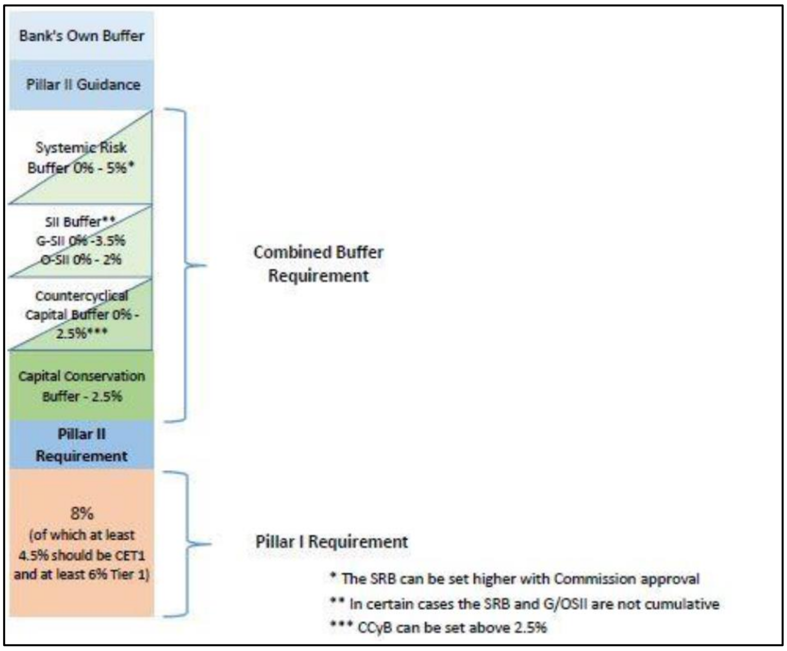
[21] https://www.irishtimes.com/business/financial-services/state-s-bank-of-ireland-stake-falls-below-6-1.4798784.

[22] https://www.gov.ie/en/publication/066a28-banks/.

[23] See the CBI's macro-prudential policies.

Directive ("CRD") and the Capital Requirements Regulations were agreed.[24] Figure 2 below illustrates the range of requirements to which banks may be subject. These requirements are summarised below.

Figure 2: Illustrative Capital Requirements for Banks.



Source: Department of Finance overview of Capital Requirements and Macro-prudential Policy.[25]

<u>Pillar I Requirement</u>

2.11 The Pillar I Requirement is the regulatory minimum amount of capital which banks must hold. This is a total capital ratio of 8% of their risk weighted assets ("RWA"). A minimum of 4.5% of the RWAs must be Common Equity Tier 1 ("CET1") and at

[24] As set out in Capital Requirements Directive IV (Directive (EU) 2013/36) and the Capital Requirements Regulation (Regulation (EU) 575/2013), as amended by the Capital Requirements Directive V (Directive (EU) 2019/878) available at: https://eur lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:176:0338:0436:En:PDF and the Capital Requirements Regulation II (Regulation (EU) 2019/876) available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R0876&from=EN.

[25] Department of Finance overview of Capital Requirements and Macro-prudential Policy https://assets.gov.ie/6056/280119120125-51f2f5d31bb9471cb0ecb8c46ef5cb94.pdf.

least 6% of RWAs should be met with Tier 1 capital. The Pillar 1 requirement applies to all banks uniformly.[26]

Pillar II Requirement

2.12 The Pillar II Requirement is an additional capital requirement that may be applied by competent authorities to banks on a case by case basis. It is based on a bank's specific risks and assesses whether it has sufficient capital to address them.[27]

Combined Buffer Requirements

2.13 The Combined Buffer Requirement is the collective term for the four capital buffers, these are:

(a) Capital Conversion Buffer: A uniform requirement applied to all banks fixed at 2.5% of a bank's total RWA; [28]

(b) Global/Other Systemically Important Institution ("O-SII"): The objective of the O-SSI Capital Buffer is to reduce the probability of a failure of a systemically important institution.[29]

(c) Countercyclical Capital Buffer: A time varying capital requirement designed to make the banking system more resilient and less pro-cyclical by requiring banks to hold more capital during periods of strong capital growth and growing systemic risk; and,

(d) Systemic Risk Buffer: Designed to mitigate long-term, non-cyclical risks which may have serious negative consequences for the real economy.

2.14 The CBI may utilise the macro prudential policy instruments as outlined above to mitigate against the risk of a disruption to the provision of financial services,

[26] Department of Finance overview of Capital Requirements and Macro-prudential Policy https://assets.gov.ie/6056/280119120125-51f2f5d31bb9471cb0ecb8c46ef5cb94.pdf.

[27] Department of Finance overview of Capital Requirements and Macro-prudential Policy https://assets.gov.ie/6056/280119120125-51f2f5d31bb9471cb0ecb8c46ef5cb94.pdf.

[28] RWA density measures how a bank's assets are adjusted for risks associated with those assets.

[29] See the CBI's Systemically Important Institutions.

caused by an impairment of all or parts of the financial system. The CBI's mortgage measures were introduced to achieve the same objective.

CBI Mortgage Measures

2.15 The CBI's mortgage measures were introduced in 2015 in response to the financial crisis, when losses on residential mortgages, following a prolonged period of unsustainable lending standards, were a primary cause of the banking crisis.[30] The CBI's mortgage measures aim to increase both bank and borrower resilience and mitigate the risks of credit-house price spirals emerging, by limiting the Loan-to-Value ("LTV") and Loan-to-Income ("LTI") ratios that apply to new residential mortgage lending.

2.16 LTV limits require borrowers to have a deposit of a certain amount before they will be offered a mortgage. There are different limits in place for different types of borrower, with First Time Buyers required to have a 10% deposit; second-time and subsequent buyers required to a have a 20% deposit; and Buy-to-let buyers required to have a 30% deposit. An LTI limit of 3.5 times a borrower's gross annual income applies to applications for a mortgage for a principal dwelling home.

Measures relating to non-performing loans ("NPLs")

2.17 Following the financial crisis, there was a rapid increase in the number of NPLs held by European banks and financial institutions. A loan is considered non-performing when more than 90 days pass without the borrower paying the agreed instalments, or when there are indications that the borrower is unlikely to repay the loan without realisation of collateral.[31] The European Central Bank (the "ECB") has noted that high levels of NPLs negatively impact the economy[32] by, for

[30] CBI explainer on the Mortgage Measures, available at: https://www.centralbank.ie/consumer-hub/explainers/what-are-the-mortgage-measures.

[31] The European Banking Authority ("EBA") introduced a harmonised definition of NPLs across European countries in 2014. For more information, see EBA Report on NPLs 2019, pg. 10.

[32] See page 4 of the EBA's *Guidance to Banks on non-performing loans,* available at: https://www.bankingsupervision.europa.eu/ecb/pub/pdf/guidance_on_npl.en.pdf.

example, holding up bank capital that could be used for lending, reducing bank profitability and raising funding costs.[33]

2.18 As part of its response to the crisis in the State, the Irish Government created the National Asset Management Agency in 2009, to reduce uncertainty over potential future losses on Irish banks' balance sheets. In 2014, the ECB through the 'ECB Banking Supervision' programme addressed issues concerning asset quality in European banks.[34] Subsequently, it became necessary for banks to deleverage risk and to reduce their levels of NPLs.[35] In order to do so, banks disposed of a large portion of NPLs through loan sales to unconnected third parties.

2.19 More recently, in July 2017, the Council of the European Union adopted an "Action Plan to Tackle Non-Performing Loans in Europe", combining various measures by national governments, bank supervisors and the EU institutions to improve the tools and incentives for banks to proactively address NPLs.[36] In October 2018, the EBA published its "Guidelines on management of non-performing loans" ("EBA Guidelines").[37] The EBA Guidelines set out the need for the development of a non-performing exposure ("NPE")[38] strategy for the reduction of the number of NPEs on a bank's balance sheet for banks with a high NPE level. The gross NPL ratio is used to determine whether a bank has a high NPE level, with a 5% NPL ratio triggering the need to develop NPE strategies.

[33] See the International Monetary Fund ("IMF") discussion *A Strategy for Resolving Europe's Problem Loans*: https://www.imf.org/external/pubs/ft/sdn/2015/sdn1519.pdf.

[34] See page 4 of the ECB's *to Banks on non-performing loans,* available at: https://www.bankingsupervision.europa.eu/ecb/pub/pdf/guidance_on_npl.en.pdf.

[35] See for example https://www.irishtimes.com/business/financial-services/ecb-target-impossible-without-loans-sale-ptsb-says-1.3435544.

[36] See press release from the Council of Europe titled *Council Conclusions on Action Plan to Tackle Non-Performing Loans in Europe*, available at: https://www.consilium.europa.eu/en/press/press-releases/2017/07/11/conclusions-non-performing-loans/

[37] See the EBA Guidelines at: https://eba.europa.eu/sites/default/documents/files/documents/10180/2425705/371ff4ba-d7db-4fa9-a3c7-231cb9c2a26a/Final%20Guidelines%20on%20management%20of%20non-performing%20and%20forborne%20exposures.pdf?retry=1.

[38] Non-performing exposures, as defined in Annex V to Commission Implementing Regulation (EU) 680/2014, are a credit institution's material exposures that are either more than 90 days past due, or where the debtor is assessed as unlikely to pay his or her credit obligations in full without realisation of collateral. Non-performing exposure is essentially an umbrella term which covers a credit institution's total risk positions, of which NPLs are only one example.

Potential consequences of regulatory measures for banks and mortgage lending in Ireland

2.20 While the CBI's bank capital instruments and mortgage measures were introduced to ensure stability and resilience in the financial system, according to market stakeholders such requirements for Irish banks may have additional consequences.

2.21 A BPFI report based on information gathered from the five Irish banks, the ECB and EBA found that RWA density on mortgage loans in Ireland is significantly higher than the average for comparable European countries.[39] This requires banks that are lending for Irish mortgages to hold more equity to issue a mortgage than other European banks, which in turn increases the price of the mortgage for the customer. The BPFI report noted at the end of 2019, Irish mortgage RWA was 37%, whereas the European average was around 13%, meaning that banks that are lending for Irish mortgages are required to hold more capital than banks in other EU countries to counter the risk of unexpected losses.[40] Furthermore, research from the EBA suggests that a one percentage point increase in capital requirements may reduce bank lending by as much as 8%.[41]

2.22 At the Oireachtas Joint Committee on Finance, Public Expenditure and Reform, and Taoiseach, on 23 February 2021, representatives from Ulster Bank stated that Irish banks are required to keep a higher level of capital reserves than is the case in the UK or elsewhere in Europe, and that this impacts on a shareholder's return on capital.[42] Reports from 2021 suggested that Ulster Bank is required to hold equity capital reserves equivalent to about 28% of RWA; this is more than double both the EU average and what is required of Ulster Bank's UK shareholder,

[39] RWA density measures how a bank's assets are adjusted for risks associated with those assets.

[40] Page 5 of the BPFI's "*Irish Mortgage RWA Density Analysis Project*", dated January 2021, available at: https://bpfi.ie/wp-content/uploads/2021/02/Final-BPFI-RWA-Report.pdf.

[41] See page 30 of the EBA's working paper series "*The Real Effects of Bank Capital Requirements*", dated June 2017, available at: https://www.esrb.europa.eu/pub/pdf/wp/esrbwp47.en.pdf?28bb787723d7bf33c385ac16156e3a88.

[42] See page 22 of the Joint Committee on Finance, Public Expenditure and Reform, and Taoiseach on 23 February 2021, available at: https://data.oireachtas.ie/ie/oireachtas/debateRecord/joint_committee_on_finance_public_expenditure_and_reform_and_taoiseach/2021-02-23/debate/mul@/main.pdf.

NatWest.[43] In its announcement in February 2021, NatWest cited the difficulties in generating long term sustainable returns as the rationale behind Ulster Bank's withdrawal from all banking activities in the State.

2.23 It has been reported that the average interest rate on a new mortgage in the State, 2.69% as of December 2021, is the highest in the euro zone and more than double the currency bloc's average rate.[44] An analysis by the stockbroking firm, Goodbody, said the capital charge[45] in the State on a bank home loan equates to 0.5 percentage points of a mortgage interest rate, 2.6 times the EU figure.[46] Irish funding costs, at 0.4 percentage points, are almost a third higher, while loan impairment charges account for 0.2 percentage points locally, compared to 0.12 across the EU.[47]

2.24 Aside from the difference in capital costs for Irish banks versus European banks, it has been observed that the most significant difference is in running costs, including staff, IT spending, levies and other general overheads. An analysis carried out by Goodbody estimated that operating costs account for 1.05 percentage points of the average Irish mortgage interest rate, compared to 0.65 percentage points across the EU.[48] Goodbody believes that the difference arises due to the scale of the Irish economy, rather than relative inefficiency.[49]

Regulatory framework for non-bank lenders

[43] https://www.irishtimes.com/business/financial-services/ulster-bank-set-to-exit-irish-market-after-more-than-160-years-1.4487912.

[44] https://www.centralbank.ie/docs/default-source/statistics/data-and-analysis/credit-and-banking-statistics/retail-interest-rates/interest-rate-statistics-december-2021.pdf?sfvrsn=5

[45] Capital charge represents the cost in a bank's pricing resulting from capital holding requirements.

[46] https://www.irishtimes.com/business/financial-services/more-non-bank-lenders-will-enter-market-mortgage-chief-1.4741009

[47] *Ibid.*

[48] *Ibid.*

[49] "*The cynics might argue that the higher opex cost in Ireland is the result of a less efficient banking system, so is costing customers higher pricing of c.30-35bps, but the reality is that banking is a scale game with a lot of fixed costs (levies, infrastructure, regulatory costs, digital investment etc) which is shared over a smaller pool of assets in an Irish context as a smaller financial system/economy, driving up costs*". Goodbody equity and credit research note, dated 1 July 2021, 'Irish Banks'.

2.25 It worth noting that non-bank lenders are not subject to the same capital requirements as those faced by retail banks set out in paragraphs 2.10 to 2.244 above. Non-bank lenders such as Finance Ireland,[50] Dilosk[51] and Avant Money[52] are registered with the CBI as "retail credit firms," a firm that provides credit directly to individuals.[53] The CBI's retail credit firm authorisation process requires applicants to provide information to the CBI such as business plans, detail on sources of funding and the ability of a lender to withstand shocks to funding sources.[54]

2.26 In addition, "*A Retail Credit Firm is required to have a documented credit risk strategy in place which must be approved by its management body and must take into account the Retail Credit Firm's:*

(a) business model;

(b) overall risk appetite;

(c) financial condition and funding capacity;

(d) credit-granting activities as well as the management of non-performing loans; and,

(e) activities where credit risk can be significant."[55]

2.27 CBI oversight of retail credit firms is also concerned with the sales process, provision of information to consumers and complaints handling. Retail credit firms are subject to the Consumer Protection Code,[56]the Code of Conduct on Mortgage

[50] Finance Ireland on the CBI register.

[51] Dilosk on the CBI register.

[52] Avant Money on the CBI register.

[53] See the CBI's description of retail credit firms, here.

[54] See paragraph 3.7 of the CBI's Authorisation Requirements and Standards for Retail Credit Firms.

[55] See paragraph 4.1 of the CBI's Authorisation Requirements and Standards for Retail Credit Firms.

[56] Consumer Protection Code 2012.

Arrears[57] and the Minimum Competency Code.[58] The CBI's Mortgage Measures, the lending rules relating to LTV and LTI, apply to both banks and non-bank lenders.

2.28 Non-bank lenders in the EU are subject to regulatory oversight from the Alternative Investment Fund Managers Directive[59] which ensures that non-bank lenders: (i) match the liquidity arrangements of their funds with the liquidity profile of their lending activity; (ii) undertake rigorous borrower due diligence and credit underwriting procedures on any loans they originate; (iii) implement risk management systems, including stress testing, to identify, monitor and manage risk arising from their lending activity; (iv) are transparent in their use of leverage to their investors and national competent authorities; and, (v) provide detailed reporting to investors and national competent authorities.[60]

2.29 The differing requirements in holding capital has a material impact on how banks and non-bank lenders operate in the State, with capital requirements estimated to account for an additional 0.5 percentage points on a mortgage interest rate.[61] It appears that some of the capital and operating costs incurred by Irish banks are not incurred by the non-bank lenders, although the latter will also have operating costs and funding costs and, as they operate on a much smaller scale, may also face challenges in achieving sufficient economies of scale to be profitable and sustainable in the longer term.

2.30 It is worth noting, however, that at a European level and separate to the capital requirements imposed by the CBI, an international bank which owns or provides funding to a non-bank lender active in the State, is subject to the same capital

[57] Code of Conduct on Mortgage Arrears 2013.

[58] Minimum Competency Code 2011.

[59] Available at: https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:174:0001:0073:EN:PDF.

[60] See the AIMA's research on non-bank lending in Europe, available at: https://www.aima.org/educate/aima-research/non-bank-lending-in-the-european-union.html.

[61] https://www.irishtimes.com/business/financial-services/more-non-bank-lenders-will-enter-market-mortgage-chief-1.4741009.

requirements set by the EBA as an Irish retail bank. For example, the EBA sets capital requirements for each of AIB, BOI and Bankinter alike.

Mortgage lending in the State

2.31 This section examines mortgage lending in the State, in particular: (i) types of mortgages; (ii) demand for mortgage lending; (iii) an overview of the mortgage lending process and distribution channels; (iv) mortgage switching; (v) an outline of competitors in the provision of mortgage lending; and, (vi) potential barriers to entry, including insights on consumer behaviour where appropriate.

(i) Types of Mortgages

2.32 Mortgage lending refers to the provision of a number of related products offered by mortgage lenders to customers[62] to purchase a property. Typically, as mortgage loans are secured against the value of a property and customers can borrow large sums, mortgages are provided over a longer duration than other personal loans.

2.33 There are several features of mortgage products that may be available to customers from mortgage lenders, including those listed below. However, these are not necessarily mutually exclusive and it is important to note that a borrower could obtain a mortgage from a lender that includes different elements of the features listed below:

(a) Interest only mortgage customers only repay the interest on their outstanding mortgage balance every month, not the capital ("Interest Only");

(b) Repayment mortgage customers pay the interest on their outstanding mortgage balance every month as well as an additional amount representing a portion of the capital;

(c) Fixed rate mortgages keep the customer's monthly repayments at the same amount for a fixed term ("Fixed Rate"), although typically this is the

[62] The terms "customer" and "consumer" are used interchangeably in this Determination.

case for introductory offers only beyond which customers may move to a variable rate mortgage. Of new mortgage lending in 2021, Fixed Rate products were selected by 91.6% of First Time Buyers and 80.4% of second and subsequent buyers;[63]

(d) Variable rate mortgages charge an interest rate on the loan that varies over time ("Variable Rate"). Different types of Variable Rate mortgages include (i) standard variable rate ("SVR") mortgages which are linked to the rates of the ECB. SVRs are the most common Variable Rate product; (ii) tracker mortgages are mortgage loans which specify that the interest rate charged will be set at a specified margin, typically 1-1.3% above the ECB base rate for the lifetime of the loan ("Tracker Mortgages");[64] (iii) capped rate mortgages in which the interest rate is variable but cannot rise above a certain fixed rate; (iv) temporary discounted rates below the SVR offered as incentives to new customers ("Discounted Rate"); and, (v) a LTV rate which is determined by the size of the amount requested to be borrowed compared to the value of the property to be purchased;

(e) Split rate mortgages offer customers the option of splitting their mortgage into partially fixed and variable ("Split Rate");

(f) Buy-to-let mortgages are intended for landlords purchasing a property to be rented out to tenants. Buy-to-let are offered in two forms, business Buy-to-let, aimed at professional landlords operating rental properties as a business; and consumer Buy-to-let, aimed at individual, part-time landlords. Buy-to-let mortgages may be more difficult to obtain than typical residential mortgages, as many lenders will typically offer a lower

[63] See the CBI's New Mortgage Lending - Data and Commentary, available at: https://www.centralbank.ie/financial-system/financial-stability/macro-prudential-policy/mortgage-measures/new-mortgage-lending-data-and-commentary.

[64] Tracker Mortgages are no longer offered to new customers by mortgage lenders. In this Determination, when referring to Variable Rate mortgages, Tracker Mortgages are excluded.

LTV rate than they may for a residential property, and they may also set stricter limits on the maximum value of the property;[65]

(g) Green mortgages offer a lower interest rate to purchasers of energy efficient homes ("Green Mortgages"). [Green Mortgages are available from AIB, Haven,[66] BOI, and PTSB. In most cases, the home being purchased requires a building energy rating ("BER") of B3 or higher to qualify for a Green Mortgage; and,

(h) Some providers offer so-called "High Value Mortgages", where customers seeking to purchase a mortgage in excess of a certain value may be offered a different interest rate for certain fixed term periods. AIB and PTSB currently offer High Value Mortgages for mortgage amounts in excess of €250,000; and BOI currently offers High Value Mortgages for mortgage amounts in excess of €300,000. Typically, the interest rate charged on High Value Mortgages are less than those charged for the corresponding non-High Value Mortgage of the same fixed term.

(ii) Demand for mortgage lending

2.34 Mortgage lenders offer the products outlined in paragraph 2.33 above to different types of customers. For the purposes of this Determination, demand for mortgage lending can be understood to arise from three customer types in particular:

(a) First time buyers are defined by the CBI as "a borrower to whom no housing loan has ever before been advanced. Where the borrower under a housing loan is more than one person and one or more of those persons has previously been advanced a housing loan, none of those persons is a first-time buyer" ("First Time Buyers"); [67]

[65] LTV limits as they relate to Buy-to-let mortgages are described in paragraph 2.16 above.

[66] Haven Mortgages Limited ("Haven") is a wholly owned subsidiary of AIB.

[67] https://www.centralbank.ie/docs/default-source/news-and-media/press-releases/faq---new-regulations-on-residential-mortgage-lending.pdf?sfvrsn=2.

(b) Customers that are in the process of relocating from one property to another may require a new mortgage to ensure that their mortgage is suitable for their new home ("Movers"); and,

(c) Customers that decide to refinance an existing mortgage from one financial institution to another ("Switchers"). Switchers may take this decision, for example, if they can switch to a lower interest rate. In general, switching in the State has tended to be relatively limited, for example, in 2019, less than 3% of mortgages in Ireland were switched, despite CBI estimates that as many as 3 in 5 mortgages could save €1000 within one year of switching.[68]

2.35 However, across all three types of customer, demand for mortgage lending is influenced by common factors. Both the Commission in its 2017 Mortgage Options Paper[69] and the UK's Financial Conduct Authority[70] (the "FCA") in 2015 note that, for consumers, the most important consideration is how much credit they will be able to borrow, as this will determine the property they can purchase. The FCA found this to be the case for First Time Buyers and Movers in particular, whereby the focus on the property itself may inhibit a borrower from engaging fully with the implications of their decisions regarding mortgage features. Beyond this point, consumers' priority shifts to the initial monthly repayment amount. Consumers usually have a target level of repayment in mind which is based on their finances and lifestyle. It is within this context that consumers are concerned with mortgage repayments.

2.36 Because of this set of priorities, consumers may, in effect, exhibit high levels of time-discounting, focusing on up-front costs and benefits more than the lifetime

[68] See the CBI's review of switching activity in the mortgage market from 2020, available at: https://www.centralbank.ie/docs/default-source/publications/economic-letters/economic-letter-12-mortgage-switching.pdf?sfvrsn=4.

[69] See the Commission's Mortgage Options Paper, dated 15 June 2017, which can be accessed at: https://www.ccpc.ie/business/wp-content/uploads/sites/3/2017/06/CCPC-Mortgages-Options-Paper.pdf.

[70] See the ESRO report prepared for the FCA, dated July 2015, which can be accessed at: https://www.fca.org.uk/publication/research/understanding-consumer-expectations-of-the-mortgage-sales-process-esro.pdf.

implications of the mortgage. A 2019 ESRI study[71] found that consumers display steep time discounting and weight short-term financial outcomes substantially more strongly than long-term outcomes. Therefore, as consumers search for low interest rates initially, the length of the repayment term and the complexity of other mortgage product conditions can result in consumers paying more in the long run. This appears to have been confirmed by the Commission's market investigation which suggested that customers tend to focus on the headline rate more than the annual percentage rate of charge ("APRC"),[72] which may be more important in terms of understanding the long-term cost of the mortgage. This effect would seem likely to also apply with respect to cashback mortgages. As discussed further below, customers who avail of cashback tend to pay more over the lifetime of the mortgage, yet it remains a very popular choice among consumers.

2.37 Research undertaken by the Commission in 2016[73] found that, although only 52% were aware of the interest rate they paid on their mortgage, 86% of mortgage holders were aware of their monthly repayment amount. With such focus placed on the monthly repayment, consumers are often flexible on other conditions of a mortgage, such as the repayment term, for instance, in order to achieve a targeted monthly figure. Even though purchasing a home is likely the most important financial decision that most consumers will ever make, consumers' choices are nonetheless predominantly short-term, with behaviour driven by the search for the most favourable initial deal – consumers are focused on the property, not the mortgage.[74]

2.38 When it comes to mortgages:

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[71] See the ESRI's paper into perceptions on switching, dated February 2019, which can be accessed at: https://www.esri.ie/system/files/publications/WP612_0.pdf.

[72] APRC calculates the total amount of interest that will be paid over the entire period of the loan.

[73] See the Commission's Mortgage Holding & Switching: Market Research Findings, conducted by Behaviour & Attitudes, dated 27 March 2017, which can be accessed at: https://www.ccpc.ie/business/research/market-research/mortgage-holding-switching-2016/.

[74] See page 4 of the ESRO report prepared for the FCA, dated July 2015, which can be accessed at: https://www.fca.org.uk/publication/research/understanding-consumer-expectations-of-the-mortgage-sales-process-esro.pdf.

"...Consumers often enter the market without knowing exactly what kind of mortgage they want or need, and therefore are susceptible to outside influence.

... Given the complexity of loan pricing and the variation of loan features, consumers have difficulty understanding alternative mortgage products.

... Given that the mortgage transaction has multiple time and cost dimensions, consumers often are unable to determine what actual risks they face over time.

... While standard economic theory assumes that consumers shop for the best available price and terms, even the most sophisticated borrowers often find it difficult to effectively shop for mortgages".[75]

2.39 Understanding how the mortgage process works and identifying the most appropriate products can be difficult for consumers. This is exacerbated by the introduction of additional elements such as up-front cashback offers and loyalty discounts. The more product attributes that a consumer is required to consider when choosing between products, the more difficult it is for the consumer to accurately assess the options available. When it comes to sourcing a mortgage, the CBI's 2017 Mortgage Switching Research paper[76] noted the general perception that getting a mortgage is a complex and confusing process, with issues such as the level of information required, technicalities, legal fees and stamp duty often cited as concerns.

2.40 Furthermore, consumers' lack of understanding of mortgage products is clear from research surveys carried out by both the Commission and the CBI. In 2017, for the Commission, Amárach Research conducted focus groups examining

[75] See pages 2-4 of Ren S. Essene and William Apgar "Understanding Mortgage Market Behaviour: Creating Good Mortgage Options for All Americans", dated 25 April 2007 https://studylib.net/doc/14810795/understanding-mortgage-market-behavior--creating-good-mor

[76] See the CBI's Mortgage Switching Research, dated April 2017, which can be accessed at: https://www.centralbank.ie/docs/default-source/publications/consumer-protection-research/mortgage-switching-research.pdf?sfvrsn=7.

mortgage switching and found one core theme to be that of consumers' limited knowledge about mortgages and how they work, stating that:

> *"[…]* the lack of knowledge makes them risk averse… They fundamentally believe that mortgages and mortgage switching is complicated".[77]

2.41 The Amárach Research study concluded that this lack of knowledge and confidence is further compounded by consumers' inability to recognise their own power as consumers in the process:

> *"They don't engage with the fact that the lender needs them as much as they need the lender, they don't understand how mortgages work and they seem to believe that the involvement of other players in the process, other than the borrower and lender creates an impenetrable complexity".*[78]

2.42 Research carried out in other jurisdictions produced similar findings. For example, the FCA noted that consumers appear unable to choose effectively between alternative products:

> *"Consumers' lack of understanding of the types of mortgage products available and reported absence of discussions with mortgage advisers around alternatives means that some consumers are finding themselves considering a particular product at the expense of others which may have been better suited to their needs and circumstances. Many found it difficult to fully explain what their chosen product offered ahead of others, and what the benefits of other mortgage products were".*[79]

2.43 While there are different types of customers such as First Time Buyers, Movers and Switchers, research findings consistently suggest that demand for mortgage

[77] See Amárach Research's Mortgage Switching Report for the Commission, dated February 2017, which can be accessed at: https://www.ccpc.ie/business/wp-content/uploads/sites/3/2017/06/Amarach-Mortgages-Study.pdf.

[78] *Ibid.*

[79] See page 22 of the ESRO report prepared for the FCA, dated July 2015, which can be accessed at: https://www.fca.org.uk/publication/research/understanding-consumer-expectations-of-the-mortgage-sales-process-esro.pdf.

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lending is influenced by the fact that all customers regardless of type tend to be risk averse and require knowledge and capability to be able to correctly assess mortgage products. When the product set offered is further complicated by lenders through offers of cashback and loyalty discounts, consumers become even more unsure in their decision making.

(iii) Overview of mortgage lending and distribution channels

2.44 The following paragraphs outline the key features of mortgage lending in the State. Beginning with a snapshot of the mortgage lenders that are active in the State, this section sets out how mortgage interest rates are determined, followed by a description of the various features available in different mortgage products, including an illustrative summary of the products offered by lenders in the State. Finally, the distribution channels used by mortgage lenders in the State are examined.

2.45 In 2007, there were 10 mortgage lenders active in the State. Following the financial crisis, this fell to just 5 by 2013 with the merger of AIB and EBS,[80] the exit of Bank of Scotland (Ireland)[81] and Danske Bank,[82] the winding down of Anglo Irish Bank[83] and Irish Nationwide,[84] and the subsequent liquidation of the Irish Bank Resolution Corporation.[85] Since then, there has been some limited new entry: Pepper,[86] an Australian firm which specialises in asset management and third party loan and servicing activities, began offering private dwelling home mortgages and Buy-to-let mortgages on a limited basis to Irish customers in 2016 before selling its mortgage origination platform to Finance Ireland in 2018;[87] Dilosk

[80] EBS d.a.c. ("EBS") is a wholly owned subsidiary of AIB.

[81] Bank of Scotland (Ireland) Limited.

[82] Danske Bank A/S ("Danske Bank").

[83] Anglo Irish Bank Corporation Limited.

[84] Irish Nationwide Building Society.

[85] See https://www.irishstatutebook.ie/eli/2013/act/2/enacted/en/print.

[86] Pepper Finance Corporation (Ireland) DAC trading as Pepper Money and Pepper Asset Servicing ("Pepper").

[87] See https://www.financeireland.ie/announcements/finance-ireland-announces-entry-into-irish-residential-mortgage-market/.

started offering Buy-to-let mortgage finance in the Irish market in 2017, having previously acquired the ICS Mortgage brand and portfolio in 2013 from BOI, following the European Commission's approval of a restructuring package for BOI;[88] and Avant Money entered in 2020.

2.46 At present there are 6 lenders offering mortgage products in the State. These lenders are AIB (including EBS and Haven), BOI, PTSB, Finance Ireland, Dilosk and Avant Money. On 29 October 2021, Ulster Bank ceased accepting mortgage applications from new customers. Ulster Bank has announced that it will no longer accept new mortgage applications from existing customers from close of business on 10 June 2022, and it will no longer provide a mortgage approval in principle to new customers from 29 April 2022.[89] On 15 July 2022, KBC ceased accepting mortgage applications from new customers and applications for top-ups from existing customers.[90]

How mortgage interest rates are determined

2.47 Mortgage interest rates are ostensibly the most important feature of a mortgage product. In 2015, the CBI published a report titled "*Influences on Standard Variable Mortgage Pricing in Ireland*"[91] which outlined the range of factors affecting the margin that banks charge on Variable Rate products and as a consequence the interest rate consumers pay. These factors include:

(a) The cost of funds – for banks, the gross return on lending must be higher than the cost of funding given the existence of operating costs and the risk of default. In the aftermath of the financial crisis, the predominant source of funding to Irish banks has been the retail channel through deposit funding. Non-bank lenders are funded through capital markets with costs linked to market rates;

[88] See the European Commission's decision on the restructuring of BOI, dated 15 July 2010, available at: https://ec.europa.eu/competition/state_aid/cases/233382/233382_1163194_133_2.pdf.

[89] https://www.ulsterbank.ie/help-and-support/important-customer-notice.html .

[90] Important update from KBC Bank Ireland - KBC .

[91] https://www.centralbank.ie/docs/default-source/publications/correspondence/finance-reports/influences-on-svr-pricing-in-ireland.pdf?sfvrsn=2.

(b) The credit risk associated with lending – the greater the scale of negative equity and indebtedness of borrowers, the higher the risk in lending;

(c) The operational costs of running a bank – outside of funding costs and asset performance, the efficiency with which the bank conducts its operations has a bearing on the overall level of profitability;

(d) The cost of capital – capital acts as a buffer to cover losses on a loan book. The cost of this capital had in the years prior to the 2015 CBI report significantly depended upon: (a) increased requirements in relation to the quality and amount of capital required to be held by banks; and (b) changes in the risk weighting applied to loans arising from loan losses. As this capital is invested by equity holders, a bank needs to generate some return to reward its owners for the risk that they have taken. The greater the amount of capital required, the higher the expected nominal return would be to cover its allocation; and,

(e) The market structure and competitive environment faced by each bank – simply put, the fewer the number of players, the more concentrated the market structure, which is an indicator of a less competitive market structure. Research indicates that less competitive markets are associated with higher lending margins.

2.48 While interest rates and the levels at which they are set are clearly an important feature of mortgage products, lenders have developed other features to try to make their mortgage product offerings more attractive.

Incentives Included in Mortgage Product offerings

2.49 A number of product features are discussed in the following paragraphs that have been introduced by lenders in an effort to make their mortgage product offering more attractive. The most prominent of these in recent years has been cashback offers, which offer customers an upfront lump sum payment of cash based on the total value of their mortgage. There are other products which feature incentives that are not tied to the value of a customer's mortgage.

Percentage Cashback Mortgages

2.50 Percentage cashback mortgages are fixed or variable rate mortgages that pay out a cash lump sum at completion of drawdown of the mortgage ("cashback"), calculated as a percentage of the total value of the mortgage. Some cashback mortgages include additional cashback at later points in the mortgage term (BOI, for example, offer an additional 1% at the end of the fixed term to BOI current account customers)[92] or cashback on monthly payments (see PTSB's 2% cashback on monthly repayments offer).[93]

2.51 The first cashback mortgage offer was introduced in 2015 by BOI, with a 2% offer. PTSB and EBS introduced similar offers in 2016. Since then, BOI has introduced its 1% additional offer at the end of the fixed term offer, EBS has increased its offer to a flat 3% at drawdown, and PTSB has introduced its 2% cashback on repayments to First Time Buyers.

2.52 The benefits of cashback mortgages are up-front. Customers who choose to avail of cashback mortgages can receive a significant sum of money (2% cashback on a €300,000 mortgage is €6,000) immediately upon drawdown. These products may be particularly attractive to customers who may have low levels of funding after drawdown. The Commission's market investigation supports this, suggesting that cashback mortgages tend to be particularly popular with First Time Buyers, who may have used a significant portion or all of their savings to pay down the mortgage deposit.[94]

2.53 Cashback mortgages tend to have higher headline fixed rates than non-cashback mortgages. This does not mean, by itself, that cashback mortgages are worse value than non-cashback mortgages. By way of example, Table 1 shows the five-year and lifetime costs of a €300,000, 30-year, 5-year fixed term loan with an LTV

[92] https://personalbanking.bankofireland.com/borrow/mortgages/up-to-3-cashback-on-your-new-mortgage/

[93] https://www.permanenttsb.ie/mortgages/first-time-buyer-mortgage/

[94] See page 2 of the Irish Mortgage Corporation Call Note, dated 21 December 2021.

of 75%. These costs are inclusive of all of offers (such as cashback or payments for legal fees) and ancillary costs (such as valuation fees).

Table 1: Five-year and lifetime mortgage costs (€300,000, 30-year, 5-year fixed term loan for a First Time Buyer with an LTV of 75%).[95]

	Five-year Cost		Lifetime Cost (re-fix after each 5-year term)		Lifetime Cost (SVR after 5-year term)	
	Cost	**Rank**	**Cost**	**Rank**	**Cost**	**Rank**
AIB	€70,805	7	€424,079	3	€444,281	4
Avant Money	€69,911	5	€418,221	2	€412,738	1
BOI	€67,039	3	€446,482	7	€498,277	8
Dilosk	€82,084	8	€491,266	8	€443,593	3
EBS	€64,633	1	€424,695	5	€471,955	6
Finance Ireland	€69,987	6	€418,617	1	€442,734	2
Haven	€66,741	2	€424,695	4	€449,220	5
PTSB	€68,719	4	€440,573	6	€484,474	7

Source: CCPC website, 12 May 2022.

2.54 However, Table 1 also shows that the three available cashback mortgages (BOI, PTSB, EBS, respectively) are the most expensive over the total lifetime of the mortgage, if the customer rolls off the fixed term onto that lender's SVR. If it is

[95] This should not be interpreted as an overall summary of value for money of different lenders, as certain lenders compete more vigorously at specific term lengths or LTVs. This also excludes specific products such as High Value and Green mortgages, and Switcher incentives.

instead assumed that the customer continually re-fixes for five years at the end of the fixed terms, then Dilosk is the most expensive over the total lifetime, followed by BOI, PTSB and EBS, respectively. So, while the cashback may appear to compensate for the higher headline rate of the mortgage, cashback mortgages appear to offer significantly poorer value for money over the lifetime of the mortgage.

2.55 Switching mortgage providers at the end of the fixed term can make the SVR and the total lifetime cost of a mortgage irrelevant, from that customer's point of view. Customers can even switch from a cashback product to a cashback product and avail of cashback twice. However, due to combinations of switching barriers, consumer inertia or lack of understanding (see paragraphs 2.84 to 2.91) and the possibility of a customer's circumstances making it difficult or impossible to switch, a significant proportion of customers will not switch at the end of the fixed term of a cashback product.

2.56 Therefore, an important difference between cashback products and non-cashback products is that cashback products can be very price-competitive in the short-term, such as over the duration of a fixed rate term. However, as they tend to incorporate higher interest rates (in particular, SVRs) than non-cashback products, they are considerably more expensive over the lifetime of the loan than non-cashback alternatives.

2.57 Cashback mortgages have been criticised recently:

(a) The Irish Independent reported on claims by a consumer advocate that "*[e]xisting customers of EBS are overpaying for their mortgages so the lender can offer cash-back incentives*." The consumer advocate, Brendan Burgess, said that "*cash-back deals were being used to distort the market*".[96]

[96] https://www.independent.ie/irish-news/ebs-accused-of-overcharging-existing-mortgage-holders-to-fund-cash-backs-40591501.html.

(b) The Irish Times reported on a research paper which found that "*[cashback] mortgages might be more expensive than many believe*".[97] The paper also noted that "*[n]ot only do cashback mortgages have higher interest rates in Ireland, but the differential between standard and cashback mortgages is significantly higher in Ireland than in either Canada or the UK.*"[98]

(c) In an appearance by AIB executives before the Oireachtas Finance Committee on June 30 2021, Deputy Jim O'Callaghan proposed that the, "*purpose – whether it is intended or not – of cash-back mortgages appears to be to facilitate the application of higher mortgage rates?*" In response to this, Mr Jim O'Keefe of AIB responded that, "*a significant group of customers, probably 30% to 40% of the market, want cash-back as part of their solution. It works for them. They get it up front. They get the benefit of that. That is what they enjoy*".[99]

Other incentives

2.58 Some lenders offer financial incentives which are not tied to the value of the mortgage. For example, Ulster Bank offers a Legal Fee Contribution of €1,500 to all First Time Buyers, movers and switchers.[100]

2.59 A number of banks offer rewards to mortgage customers who have personal current accounts with them. BOI offer €2000 bonus interest on mortgages purchased with using money saved in their 'MortgageSaver' accounts.[101] AIB waive

[97] https://www.irishtimes.com/business/personal-finance/cashback-mortgages-could-cost-borrowers-30-000-more-1.3734512.

[98] Ibid.

[99] See Joint Committee on Finance, Public Expenditure and Reform, and Taoiseach debate - Wednesday, 30 Jun 2021.

[100] See Ulster Bank Staff monthly update – Ulster Bank Intermediary.

[101] Up to 3% Cashback on your new mortgage - Bank of Ireland.

the maintenance and transaction fees on current accounts used to pay an AIB mortgage.[102]

2.60 EBS offer discounts on home insurance with the drawdown of mortgages on new homes.

2.61 Finally, some lenders offer specific financial incentives to Switchers. AIB offers €2,000 towards legal fees.[103] In December 2021, Finance Ireland and Avant Money both introduced a €1500 contribution to legal fees,[104] with Avant Money's incentive only being available to customers switching from Ulster Bank or KBC from January 1 2022 to March 31 2022.[105] These offers aim to attract Switchers by assisting with one of the main switching barriers, which is legal fees.

Mortgage Lending Channels

2.62 Mortgage products are supplied through a number of channels, though not every product is available through each of these channels. Figure 33 below presents an illustrative overview of the operation of the mortgage market. The market for mortgage lending includes not only lenders (either the traditional retail banks or non-bank lenders) and borrowers, but also independent financial advisors and intermediaries ("brokers"), which are described in further detail below.

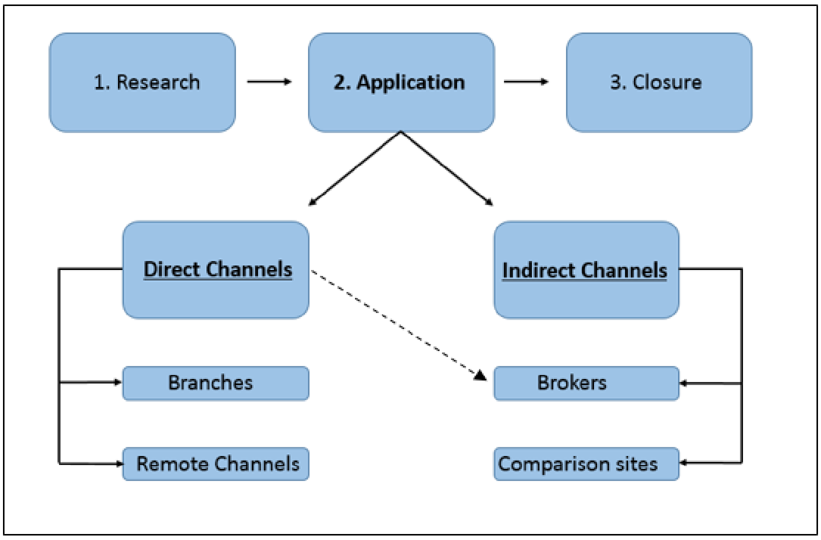
Figure 3: Mortgage Product Distribution Channels

[102] See https://aib.ie/our-products/mortgages/mortgage-benefits#:~:text=If%20you%20have%20an%20AIB,and%20transaction%20fees%20will%20help.

[103] See https://aib.ie/our-products/mortgages/switcher-mortgage#:~:text=We'll%20give%20you%20%E2%82%AC2%2C000%20when%20you%20switch%20your,account%20is%20with%20another%20bank.

[104] https://www.irishtimes.com/business/financial-services/non-bank-lenders-cut-mortgage-rates-in-face-of-kbc-and-ulster-exits-1.4744949

[105] https://mortgage123.ie/switch-mortgage-avant-money/



Source: The Commission's description of mortgage distribution.

2.63 Consumers will interact either directly with a lender, or indirectly through a broker with a number of mortgage lenders in order to obtain approval for the level of credit required to purchase a property. Lenders will compete for that consumer on the basis of price (i.e., the mortgage interest rate, fixed rates or cashback incentives) and non-price elements, for example, the speed of the approval process.

Direct Channels

2.64 When applying for a mortgage directly via lenders, it is up to customers to shop around and identify the various lenders and offers in the market, as well as choose the characteristics of mortgage which they intend to pursue. This can be a complex process as there are multiple lenders, offering multiple different types of product (e.g., cashback or non-cashback), with multiple different choices around elements such as length of fixed term, impact of LTV on rates offered, and more. There are tools available to these customers to assist in the process, including the CCPC's financial tools[106] as well as a number of other independent comparison sites.[107]

[106] See https://www.ccpc.ie/consumers/money-tools/mortgage-comparisons/./.

[107] Such as bonkers.ie and switcher.ie.

2.65 In the direct channels such as in branch or online, traditional retail banks typically cross-sell by offering mortgage products to current customers of other retail banking products. For lenders without an established branch network, brokers act as an important distribution channel, as they reduce overheads for lenders by allowing them to avoid the set-up costs of their own branch network whilst still reaching potential customers.

Indirect Channels - Brokers

2.66 The other route that customers can take is to use the services of a mortgage broker. Mortgage brokers are regulated by the CBI[108] and authorised to: (i) offer a mortgage approval in principle to borrowers; (ii) provide advice to borrowers (including assistance with mortgage applications); and, (iii) conclude mortgage offers with borrowers on behalf of a mortgage lender. Customers may find a mortgage broker in several different ways, for instance, Brokers Ireland provide a search facility[109] of brokers available to customers; lenders may provide customers with a choice of brokers; and comparison websites may suggest products provided through a broker. There are over 400 independent brokers currently operating in the State.

2.67 Brokers have relationships with multiple, sometimes all, mortgage lenders in the State. When a customer comes to a broker seeking a mortgage, the broker will typically advise the customer based on that customer's criteria and the characteristics of mortgages available. Some of the criteria can include:

(a) the total sum of money required;

(b) the LTV;

(c) whether cashback is desirable;

[108] http://registers.centralbank.ie/DownloadsPage.aspx.

[109] Brokers Ireland search facility available at: https://brokersireland.ie/broker/?product=Mortgages&categories=All+Counties.

(d) whether they are interested in fixed rates and the potential length of fixed rate term; and,

(e) ability to overpay during the term of the loan and whether they have plans to move home during the term of the loan.

2.68 Brokers will also advise on the implications of different potential options. For example, if a customer is seeking a cashback mortgage, brokers will make them aware of the long-term implications of that in terms of the total cost of credit.[110]

2.69 Based on these and other criteria, mortgage brokers can recommend a number of options to the customer. If the customer wishes to proceed with any of these options, or with options not recommended, the broker will manage the mortgage application and advise the customer on the documentation required. Finally, the broker may conclude offers with the customer on behalf of the lender.

2.70 There are a number of reasons why a customer may wish to go to a broker. The Commission's market investigation during its review of the Proposed Transaction indicated that bad experiences with banks may be relevant, that the customer may want market-based advice or that they have been recommended to go to a broker.[111] Customers go to brokers to understand the market, including whether newer and non-bank lenders can be trusted. One broker said that customers rarely have issues with recommended lenders once they have discussed them with brokers.[112]

2.71 Brokers may receive a flat commission fee of 1% of the mortgage from the lender, with some mortgage brokers additionally charging borrowers a fee based on a percentage of the mortgage amount or charge at a flat rate. However, in order to be termed as "independent", a broker can only charge a fee to a customer and not accept commission from a lender. It is not the case that all mortgage products in the State are available through all mortgage brokers. Some brokers may be tied

[110] See page 1 of the Irish Mortgage Corporation Call Note, dated 21 December 2021.

[111] See page 1 of the AIMA Call Note, dated 22 December 2021.

[112] See page 1 of the AIMA Call Note, dated 22 December 2021.

to certain lenders and a given lender may not select certain brokers through which to distribute a mortgage product. Part 4.58A of the CBI's 2019 Addendum to the Consumer Protection Code requires mortgage brokers to make available in a manner that is easily accessible to consumers, a summary of the details of all arrangements for any fee, commission, other reward or remuneration paid or provided to the intermediary which it has agreed with product producers.[113]

2.72 All lenders in the market also make their mortgage products available through the broker network, however as noted above not all mortgage products are available to all mortgage brokers in the State. For lenders without an established branch network, brokers act as an important distribution channel, as they reduce overheads for lenders by allowing them to avoid the set-up costs of their own branch network whilst still reaching potential customers. Avant Money, Dilosk and Finance Ireland provide their entire mortgage offering through brokers. Retail banks also distribute mortgage products through brokers. AIB has a dedicated broker-facing subsidiary, Haven, which does not offer mortgages direct to customers. The other banks engage directly with brokers.

2.73 Figure 4 below sets out, for each lender, the percentage of their new mortgage lending which was originated via a mortgage broker. The non-bank lenders rely almost entirely on the broker channel for their lending. KBC originates [✂] through the broker channel, with [✂] % of mortgages lent in 2021 done so via a broker. [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂], it is clear that AIB and BOI have not been. It is worth noting that BOI only began competing in the broker channel again in 2019.

Figure 4: Broker Channel as % of all new mortgage lending, 2017 – 2021.

[✂][✂][✂][✂][✂][✂][✂][✂]

Source: The Commission analysis of lending data.

[113] https://www.centralbank.ie/docs/default-source/regulation/consumer-protection/other-codes-of-conduct/addendum-to-the-consumer-protection-code-2012---september-2019.pdf.

2.74 Following the financial crisis, brokers accounted for minimal levels of new lending, but in 2021 H1, over 40% of mortgages in the State were sold through the brokers network,[114] with the remainder primarily distributed directly through banks (online, by phone or in branch) or non-bank mortgage lenders. This increased to 40.7% in 2021 Q3.[115] Recently, there has been a sharp growth in brokers' share of mortgage origination—by comparison, in 2019 brokers accounted for approximately 27.4% of mortgages.[116] This highlights the growing importance of the broker channel as a distribution network for mortgage providers, and coincides with increases in switching levels (see paragraph 2.78).

2.75 Studies suggest that consumers hold a positive view regarding the role played by mortgage brokers by those who had used them. In the Amárach Research survey, in particular, a view was expressed that brokers are on the side of the consumer more so than mortgage providers and that brokers had an expertise and insight that consumers lacked.[117] Research from the United Kingdom has also illustrated the favourable light in which consumers view brokers, with mortgage seekers perceiving brokers as experts with their best interests at heart and access to the best range of products.[118]

(iv) Switching

2.76 For most consumers, choosing a mortgage is the biggest credit decision they will make in their lifetime. The ability of customers to switch providers to avail of cheaper interest rates, or other incentives, during the lifetime of the mortgage is

[114] See paragraph 2.79 of the Commission's Determination in *BOI/KBC*, available here.

[115] https://www.irishtimes.com/business/financial-services/more-non-bank-lenders-will-enter-market-mortgage-chief-1.4741009#:~:text=Share%20of%20mortgage%20drawdowns%20from,grown%20to%2040.7%25%2C%20AIMA%20says&text=In%20addition%2C%20Bank%20of%20Ireland,market%20share%20a%20year%20earlier.

[116] *Ibid.*

[117] See page 17 of Amárach Research's Mortgage Switching Report for the Commission dated February 2017, which can be accessed at: https://www.ccpc.ie/business/wp-content/uploads/sites/3/2017/06/Amarach-Mortgages-Study.pdf.

[118] See page 14 of the ESRO report prepared for the FCA, dated July 2015, which can be accessed at: https://www.fca.org.uk/publication/research/understanding-consumer-expectations-of-the-mortgage-sales-process-esro.pdf.

hence important for the welfare of consumers and to ensure competitive markets. This has been highlighted by the ESRI in its paper on perceptions on switching.[119]

2.77 In the CBI's review of switching activity in the Irish mortgage market, it was estimated that three in every five eligible[120] mortgages for private dwelling homes could save €1000 within the first year by switching, and more than €10,000 over the remaining term. However, in the last six months of 2019, only 2.9% of mortgage holders switched provider.[121] Similarly, a 2016 CCPC study found that only 6% of mortgage holders had considered switching their mortgage provider over the 5 years prior to January 2016; but only 2% had actually switched.[122]

2.78 Figure 5 below shows the Switcher share of total mortgages from 2016 to 2021. It shows that while the Switcher share of total mortgages has steadily increased in that timeframe, it remains low, having increased from around 9% in 2016 to around 15% in 2021.

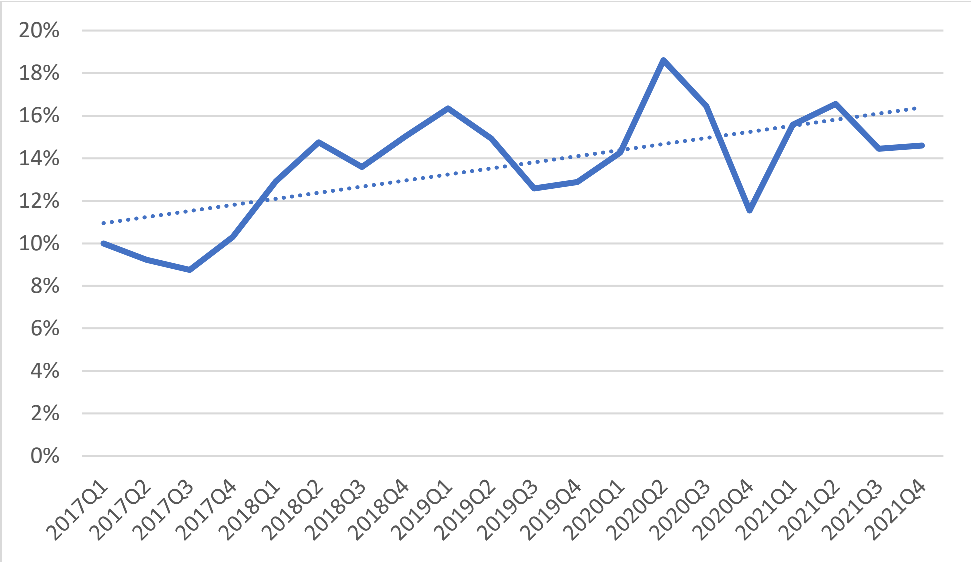
Figure 5: Switcher share of total mortgages, 2016-2021

[119] See page 2 of the ESRI's paper into perceptions on switching, dated February 2019, which can be accessed at: https://www.esri.ie/system/files/publications/WP612_0.pdf.

[120] Eligible mortgages considered were private dwelling home borrowers on a SVR (excluding trackers) or a FR with one year remaining on the mortgage term.

[121] See the CBI's 2020 review of switching activity in the Irish mortgage market, which can be accessed at: https://www.centralbank.ie/docs/default-source/publications/economic-letters/economic-letter-12-mortgage-switching.pdf?sfvrsn=4.

[122] See the Commission's Mortgage Holding & Switching: Market Research Findings, conducted by Behaviour & Attitudes, dated 2016, which can be accessed at: https://www.ccpc.ie/business/research/market-research/mortgage-holding-switching-2016/.



Source: The Commission analysis of lending data

2.79 There is a material cost to consumers' reluctance to switch mortgage providers more regularly, with the average interest rate payable among Switchers estimated to be a full percentage point lower than non-switchers.[123]

2.80 The issue of switching behaviour and consumers' attitudes to switching, both in general and with regard to mortgages, has been the focus of a number of research initiatives on behalf of the CCPC[124] and the CBI.[125]

2.81 As a core part of their financial management, consumers are generally comfortable with the process of switching providers or products in order to make a saving. However, that is generally not the case in respect of mortgages. In 2017, the Commission found switching rates to be much higher in respect of car

[123] See page 4 of the CBI's 2020 review of switching activity in the Irish mortgage market, which can be accessed at: https://www.centralbank.ie/docs/default-source/publications/economic-letters/economic-letter-12-mortgage-switching.pdf?sfvrsn=4.

[124] See https://www.ccpc.ie/business/research/market-research/consumer-switching-behaviour-2017 and https://www.ccpc.ie/consumers/money/mortgages/changing-yourmortgage/switching-lenders-or-mortgage and the CCPC study Mortgage Holding & Mortgage Switching Market Research Findings, conducted by B&A, January 2016.

[125] See https://www.centralbank.ie/docs/default-source/publications/consumer-protection-research/mortgage-switching-research.pdf?sfvrsn=7 and https://www.centralbank.ie/docs/default-source/publications/economic-letters/economic-letter-12-mortgage-switching.pdf?sfvrsn=4.

insurance (28%), electricity supply (15%), gas supply (15%) and broadband provider (14%)[126] compared to 6% in mortgages in 2016.[127]

2.82 In its 2017 examination of mortgage switching, the CBI noted:

> "… there is little or no discussion amongst mortgage holders about switching mortgages. The very idea of mortgage switching seemed remote and those that did so may perhaps had[sic] been prompted by a change in circumstance, or by external events rather than by a positive choice or option". [128]

2.83 Consumers' reluctance to switch mortgage providers may be explained to a great extent by the costs involved in switching, both real and perceived.

Switching costs

2.84 There are a number of real costs to switching mortgages, including legal fees, valuation fees and VAT. In total, these may amount to €2,000.[129] However, the savings from switching mortgage providers can be substantially more than this, and there are also several providers who will offer money (e.g., KBC offer €3,000) to Switchers to cover the costs of the switching fees.

2.85 In addition, as described from paragraphs 2.35 to 2.43, the mortgage market can be complex and consumers may find it difficult or time-consuming to identify the right mortgage, and go through the application process. This is an area in which brokers can be very helpful, if this is a switching barrier for specific consumers.

[126] See the Commission's Consumer Switching Behaviour Research Report, dated 17 March 2017, which is available at: https://www.ccpc.ie/business/wp-content/uploads/sites/3/2017/03/CCPC-Switching-Consumer-Behaviour-Research-2017.pdf.

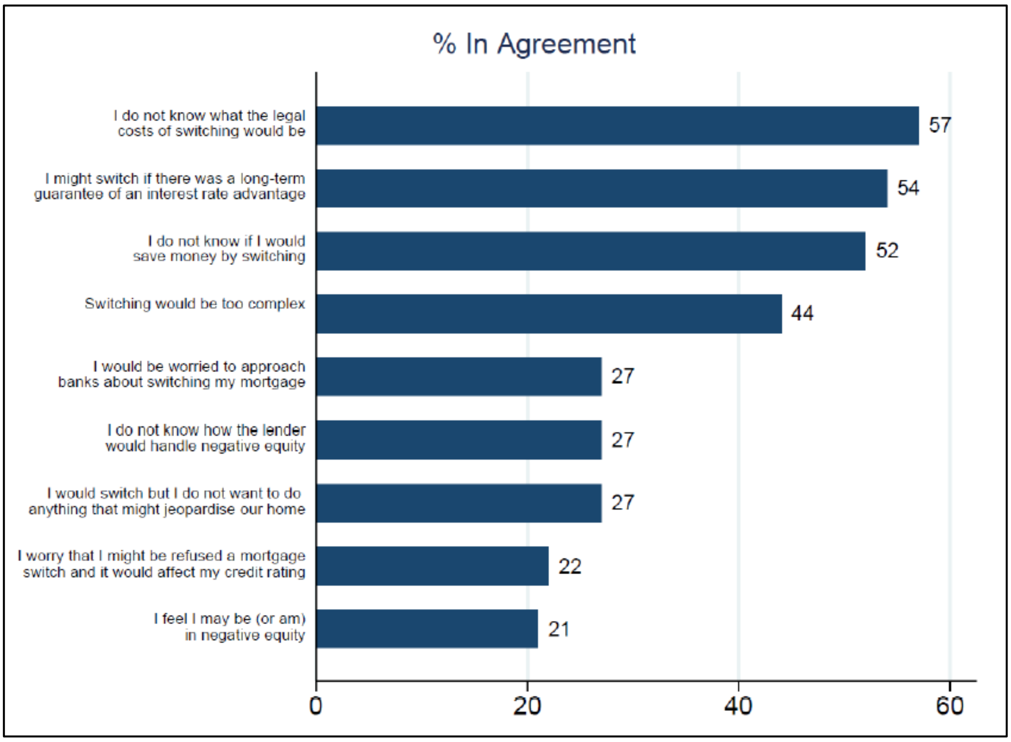
[127] See the Commission's Mortgage Holding & Switching: Market Research Findings, conducted by Behaviour & Attitudes, dated 2016, which can be accessed at: https://www.ccpc.ie/business/research/market-research/mortgage-holding-switching-2016/.

[128] See page 10 of the CBI's Mortgage Switching Research, dated April 2017, which can be accessed at: https://www.centralbank.ie/docs/default-source/publications/consumer-protection-research/mortgage-switching-research.pdf?sfvrsn=7.

[129] https://www.irishtimes.com/business/personal-finance/switching-your-mortgage-will-save-you-more-than-1-000-a-year-1.4484501

2.86 Research carried out by the CBI[130] into the attitudes of consumers to mortgage switching confirms the continued prevalence of perceived difficulties to switching among mortgage holders, many of which are linked to consumers' overall views of the mortgage market as discussed above. The CBI research findings are summarised in Figure 6 below. In particular, the following issues arise: a lack of knowledge of the costs or potential savings of mortgage switching; the perceived level of complexity of the process; and fear or uncertainty about the outcome of the process.

Figure 6: Attitudes to Mortgage Switching



Source: CBI, Room to improve: A review of switching activity in the Irish mortgage market, 2020.

2.87 Summarising these findings, it is possible to identify three broad categories of barriers, or perceived barriers, to switching:

(a) The first is around the **costs and the process of switching**. This is clearly significant with 57% of surveyed consumers citing "I do not know what

[130] See the CBI's 2020 review of switching activity in the Irish mortgage market, which can be accessed at: https://www.centralbank.ie/docs/default-source/publications/economic-letters/economic-letter-12-mortgage-switching.pdf?sfvrsn=4.

the legal costs of switching would be", 44% saying "switching would be too complex" and 27% saying "I would be worried to approach banks about switching my mortgage".

(b) The second is around **a lack of knowledge or understanding of the benefits** of switching, with 54% saying "I might switch if there was a long-term guarantee of an interest rate advantage" and 52% saying "I do not know if I would save money by switching".

(c) The third is about a **perceived or actual inability to be approved for a new mortgage**. 27% of consumers said "I do not know how the lender would handle negative equity", 27% said "I would switch but I do not want to do anything that might jeopardise my home", 22% said "I worry that I might be refused a mortgage switch and it would affect my credit rating" and 21% said "I feel I may be (or am) in negative equity".

2.88 It is therefore clear from this survey that a combination of consumer behavioural barriers and financial barriers contribute to the low levels of switching in Ireland.

2.89 These findings resonate with those of the Commission's research in 2017, which examined the issue of consumers' attitudes towards mortgage switching and found that, at the heart of the issue, there is a significant information gap creating fear and uncertainty among consumers which has limited the incidence of switching.[131] Again, this theme is consistent with a CBI summary of consumer views of barriers to mortgage switching from the same year, where the following observations were cited:[132]

(a) Lack of transparent information on the process or promotion of tools to aid comparison;

[131] See Amárach Research's Mortgage Switching Report for the Commission, dated February 2017, which can be accessed at: https://www.ccpc.ie/business/wp-content/uploads/sites/3/2017/06/Amarach-Mortgages-Study.pdf.

[132] See page 11 of the CBI's Mortgage Switching Research, dated April 2017, which can be accessed at: https://www.centralbank.ie/docs/default-source/publications/consumer-protection-research/mortgage-switching-research.pdf?sfvrsn=7.

(b) The uncertainty around whether mortgage lenders will stay in the market;

(c) The unknown cost of moving a mortgage;

(d) The unknown savings to be made over the long-term;

(e) The unknown cost of legal fees etc.;

(f) Implications a switch might have for their credit rating;

(g) The complexity of the process and the time involved;

(h) Potential difficulties in securing new finance; and,

(i) No long-term guarantee about the actual cost of the mortgage in the event of a switch.

2.90 In addition, the difficulties encountered by consumers in obtaining their first mortgage appears to have a negative impact on consumers' desire to switch, as they would rather avoid having to go through the mortgage application process again.[133]

2.91 It is clear that there is significant customer inertia as a result of the time, complexity and cost of switching. Therefore, mortgage customers are likely to require a significant benefit from switching in order to overcome such barriers.

2.92 To counteract barriers to mortgage switching, since 1 January 2019, the CBI has implemented new measures[134] to make switching easier. Under the new measures, lenders must:

(a) Tell current customers about mortgage options available with the same lender and which offer lower pricing than the pricing the customer would otherwise be on with their current mortgage. The lender must inform

[133] See page 11 of the CBI's Mortgage Switching Research, dated April 2017, which can be accessed at: https://www.centralbank.ie/docs/default-source/publications/consumer-protection-research/mortgage-switching-research.pdf?sfvrsn=7.

[134] https://www.centralbank.ie/consumer-hub/explainers/how-is-the-central-bank-making-mortgage-switching-easier.

current customers of these alternative options no more than 60 days before the customer comes to the end of the introductory fixed rate period of their current mortgage;

(b) Tell customers if they can switch to a cheaper mortgage based on how much equity is in their home;

(c) Clearly explain the pros and cons of any mortgage incentives such as cashback offers;

(d) Give customers a comparison of how much their mortgage costs versus other options offered by their lender if requested;

(e) Give customers all the information needed to switch; and,

(f) Give customers a decision within ten business days of receiving a completed mortgage application.

Evidence since 2019 suggests that these measures have yet to have a significant impact in the mortgage market.

(v) Outline of Competitors

2.93 The section below provides an overview of each of the lenders outlined at paragraph 2.46, separated into: (a) bank lenders; and (b) non-bank lenders, followed by a consideration of potential new entrants to mortgage lending in the State. Finally, consideration is given to potential barriers to entry and expansion.

(a) Bank Lenders

PTSB

2.94 PTSB is a provider of retail and SME banking in the State. PTSB offers a range of banking products such as business and personal current accounts, overdrafts, mortgages, business and personal loans, credit cards and home insurance.

2.95 PTSB is wholly owned by PTSB Group Holdings plc. The shares of PTSB Group Holdings plc are listed on the Euronext Dublin and London Stock Exchanges. The

Government owns 74.92% of the Ordinary Shares of PTSB Group Holdings plc. The relationship between PTSB Group Holdings plc and the Minister for Finance is governed by a relationship agreement. PTSB has no activities outside of the State.

2.96 PTSB reported a loss of €162m in 2020.[135] According to its Chief Executive, PTSB:

> *"saw a strong rebound in activity in the second half of 2020 and this momentum has continued into the first half of 2021. The Bank reported a loss after tax of €5 million in the first half of 2021, trending positively from a loss after tax of €54 million in the first half of 2020 at the beginning stages of the COVID-19 pandemic".*[136]

2.97 PTSB noted a reduction in its net interest margin ("NIM"), from 1.82% in June 2019 to 1.75% in June 2020 and to 1.5% in June 2020. It explained that this drop between 2020 and 2021 was due to the low interest rate environment with lower yields on treasury assets and the cost of carrying excess liquidity.[137]

2.98 PTSB is mainly funded by current accounts and retail deposits, which make up 88% of the total funding profile.

2.99 PTSB reported a "[s]*ignificant improvement in reputation score for the Bank, moving up 24 places to 69th position in the annual Ireland RepTrak Top 100 List*".[138, 139]

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[135] PTSB Annual Report 2020, https://www.permanenttsbgroup.ie/sites/tsb/files/TSB/21641-ptsb-group-holdings-ar-ye2020-v8.pdf.

[136] Page 8, 2021 PTSB Interim Results. https://www.permanenttsbgroup.ie/sites/tsb/files/TSB/ptsbgh-interim-report-2021.pdf.

[137] Pages 5 and 9, PTSB 2021 Interim Report. https://www.permanenttsbgroup.ie/sites/tsb/files/TSB/ptsbgh-interim-report-2021.pdf.

[138] The annual Ireland Reptrak study is the largest and longest running study of reputation in Ireland and is based on the perceptions of over 6,500 members of the public. The study measures the level of trust, respect, admiration and esteem the public has for 100 organisations in Ireland, along with close to 100 other reputation and brand indicators. Page 7, PTSB 2021 Interim Report. https://www.permanenttsbgroup.ie/sites/tsb/files/TSB/ptsbgh-interim-report-2021.pdf

[139] According to PTSB, "*The annual Ireland Reptrak study is the largest and longest running study of reputation in Ireland and is based on the perceptions of over 6,500 members of the public. The study measures the level of trust, respect, admiration and esteem the public has for 100 organisations in Ireland, along with close to 100 other reputation and brand indicators*", see. Page 7, PTSB 2021 Interim Report. https://www.permanenttsbgroup.ie/sites/tsb/files/TSB/ptsbgh-interim-report-2021.pdf.

2.100 PTSB is the third largest mortgage provider in the State, accounting for [15-20]% market share by the stock of mortgages in 2020.[140] PTSB provides current accounts, mortgages, term lending, credit cards, saving accounts, deposit accounts and home insurance through its partnership with Allianz[141], and 'bancassurance' (life assurance and pensions) to its personal banking customers through its partnership with Irish Life. PTSB also provides business banking products.

2.101 PTSB's home loan assets at the end of June 2021 were €12,272m while Buy-to-let assets accounted for €1,535m.[142]

2.102 In 2020, PTSB had an estimated share of mortgage flow of [15-20]%.[143]

2.103 In its Interim Report, of the first half of 2021, PTSB reported that:

> *"new mortgage lending, which represented 90% of total new lending, increased by 45% compared to 30 June 2020 and outperformed the mortgage market which grew by 26%. Mortgage pipeline remains strong and the Mortgage Drawdowns were €764 million in the first half of 2021, reflecting a 45% growth compared to the prior period. The year to date Mortgage Market Share was 17.5% representing year on year growth of 2.2% in the market share".*[144]

2.104 PTSB offers cashback in a similar way to BOI and EBS. PTSB launched its 2% cashback offer in 2016, after BOI first launched it in 2015.[145]

[140] See paragraph 17 of the Merger Notification Form.

[141] Allianz p.l.c ("Allianz").

[142] Page 21, PTSB 2021 Interim Report.

[143] See BPFI data.

[144] Page 9, PTSB 2021 Interim Report. https://www.permanenttsbgroup.ie/sites/tsb/files/TSB/ptsbgh-interim-report-2021.pdf

[145] https://www.rte.ie/news/business/2016/0108/758535-ptsb-mortgage-offer/

2.105 In 2021, PTSB introduced a new 4-year fixed rate mortgage product for new personal customers, with rates from 2.25%.[146] In April 2022, it launched green mortgage products.

2.106 In 2021 PTSB announced plans to launch a new online based mortgage application service.[147]

AIB

2.107 AIB is a financial services group operating predominantly in the State. It was established in 1966 from the amalgamation of three Irish banks. In December 2010, the Irish government took a majority stake in the bank. As at 21 July 2022 the government's stake in AIB was 70.97%.

2.108 According to its annual report for 2021, AIB generated worldwide revenues of approximately €2.379 billion in 2021 (of which €2.197 billion was generated in the State).[148] AIB provides retail banking products and services such as mortgages, consumer lending, certain business lending, asset-backed lending, wealth management, daily banking and general insurance.[149]

2.109 In the first half of 2021, AIB announced a profit after tax of €274m and operating profit of €373m.[150] AIB reports that it has a digitally active customer base of 1.78m

[146] Page 10, PTSB 2021 Interim Report.

[147] "*We also recently announced a partnership with Irish fintech CreditLogic, which will see Permanent TSB provide a new digital application platform for mortgage applicants. This partnership with CreditLogic will allow our customers to complete their entire mortgage application process online through a special app designed for exceptional ease of use and security. This new online based mortgage application service will launch later this year*." Page 10, PTSB Interim Report 2021

[148] See AIB's 2021 Annual Report https://aib.ie/content/dam/frontdoor/investorrelations/docs/resultscentre/annualreport/2021/aib-group-plc-2021-annual-financial-report-3-march-2022.pdf.

[149] See AIB's response to Question 1 of the BOI/KBC Competitor Questionnaire.

[150] https://group.aib.ie/content/dam/aib/group/Docs/Press%20Releases/2021/aib-group-plc-AIB-announces-half-year-profit-afte-tax-of-%E2%82%AC274m.pdf.

customers.[151] AIB's products and services include retail banking services, mortgages, wealth management and insurance and corporate banking.[152]

2.110 In 2011, EBS, a major Irish building society, became a subsidiary of AIB. AIB has more than 200 AIB branches located throughout the State,[153] while EBS operates through 68 EBS branches nationwide.[154] AIB has noted that, before the pandemic, "*in the order of 50,000 customers would visit our branch network in the Republic of Ireland on an average day*" and that AIB's branch network is very important and "a key differentiator" for AIB.[155]

2.111 As well as offering mortgages through its AIB and EBS brands, AIB also supplies mortgages through its Haven brand. Through these brands AIB distributes mortgages through the broker network, and directly through its branches, digitally, and by telephone.

2.112 In August 2021, AIB reported that:

> *"The mortgage market in Ireland performed strongly in H1 2021 with total drawdowns of €4.4bn up 26% on H1 2020. A solid rise in mortgage lending is expected with market estimates revised to c. €10bn for 2021. New mortgage lending in our ROI business was €1.1bn in the first six months. With a strengthened proposition, momentum continues in our applications and approvals data, giving us confidence in our full year performance"*.[156]

2.113 AIB has noted how it provides advice to customers, including through its branches:

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151 https://group.aib.ie/content/dam/aib/group/Docs/Press%20Releases/2021/aib-group-plc-AIB-announces-half-year-profit-afte-tax-of-%E2%82%AC274m.pdf.

152 See AIB's response to Question 1 of the BOI/KBC Competitor Questionnaire.

153 Branch Locator (aib.ie).

154 https://offices.ebs.ie/index.html.

155 https://www.oireachtas.ie/en/debates/debate/joint_committee_on_finance_public_expenditure_and_reform_and_taoiseach/2021-06-30/3/.

156 https://group.aib.ie/content/dam/aib/group/Docs/Press%20Releases/2021/aib-group-plc-AIB-announces-half-year-profit-afte-tax-of-%E2%82%AC274m.pdf.

"When people come to the big financial decisions they will make in their lives such as the mortgage, life insurance and savings for the future, we will have people right across the group and across the country employed giving that advice. We will continue to have a really strong physical presence in branches that we serve. I believe that the very best brand ambassadors we have are, without question, the people who wear the AIB uniform and who serve on the front line in every single part of the country".[157]

2.114 For its mortgage offer, the AIB brand appears to focus on headline rates, currently offering variable and fixed rate mortgages. AIB also offers a green mortgage with a lower fixed rate for a high energy rated home.[158] In August 2021, AIB reported that its "*green mortgage product represented 16% of new ROI mortgage lending*".[159] For Switchers, AIB offers to pay €2,000 to the customer within two months of switching.[160] AIB offers free banking for mortgage customers that have a current account with AIB.[161]

2.115 EBS's mortgage proposition primarily comprises a fixed rate and cashback offering. In particular, EBS offers a 3% cashback offering, with 2% cashback on drawdown and 1% cashback after five years.[162]

2.116 In July 2021, EBS announced that it would reduce its three and five-year fixed-rate mortgages by 0.15% to 2.75%. This change would apply to both new and existing

157 https://www.oireachtas.ie/en/debates/debate/joint_committee_on_finance_public_expenditure_and_reform_and_taoiseach/2021-06-30/3/.

158 https://aib.ie/our-products/mortgages/mortgage-interest-rates.

159 https://group.aib.ie/content/dam/aib/group/Docs/Press%20Releases/2021/aib-group-plc-AIB-announces-half-year-profit-afte-tax-of-%E2%82%AC274m.pdf.

160 https://aib.ie/our-products/mortgages/switcher-mortgage#accd-pane-1_vvavomiie.

161 https://aib.ie/our-products/mortgages/switcher-mortgage#accd-pane-1_vvavomiie.

162 3% Back in Cash – Mortgage Cash Back – EBS

customers; to First Time Buyers, Movers and Switchers; and to all LTV ratios.[163] This was the first rate cut by EBS since November 2019.[164]

2.117 As noted above, Haven operates exclusively through brokers. Haven offers a four-year fixed green mortgage, for properties with BER Rating of A1- B3, across all LTV bands with rates from 2.15%.[165]

2.118 Customers who switch their mortgage to Haven receive a €2,000 cash offer towards legal costs.[166] Haven has recently offered €5,000 cashback on certain fixed rate mortgages of €250,000 or more.[167]

2.119 In responding to questions from the Oireachtas Joint Committee on Finance, Public Expenditure, and Reform, Jim O'Keeffe, AIB CEO, explained the differentiation in pricing by AIB and EBS. He stated that:

> *"The AIB brand itself for a considerable number of years has laid out price as key. This is both for front book and back book*[168] pricing and not just competitive pricing. Therefore, on the EBS side, we price differently and have always done so. This is not just because of the cash-back, but also because of the type of proposition we have there. Even within the grouping, when one compares others with AIB's front book and back book pricing, we will find that AIB stacks up favourably. Looking at other cash-back providers, they go well beyond what EBS provides. It is not just an EBS issue in that regard. We are meeting the customer demands. Customers are looking for cash-back. EBS is our channel to market for

[163] https://www.bonkers.ie/blog/mortgages/ebs-cuts-its-fixed-mortgage-rates/.

[164] https://www.bonkers.ie/blog/mortgages/ebs-cuts-its-fixed-mortgage-rates/.

[165] https://www.havenmortgages.ie/mortgage-centre/haven-green.

[166] https://www.havenmortgages.ie/useful-information/why-choose-haven.

[167] https://www.havenmortgages.ie/useful-information/why-choose-haven.

[168] Front book refers to customers newly or recently acquired whereas back book refers to previously acquired customers.

cash-back. On the AIB side, that is where we come to market in terms of pricing, especially on the new to bank”.[169]

BOI

2.120 BOI Group is one of the largest financial services groups in Ireland and provides a broad range of banking and other financial services. In the State, BOI is active in retail banking, wealth and insurance and corporate banking. BOI is the main operating entity and the licensed bank of the BOI Group. Its parent company, BOI Group, is listed on Euronext Dublin.[170]

2.121 BOI Group had gross lending of €5.7 billion to the Irish economy in 2021.[171]It serves 2 million consumer and business customers across a broad range of segments and through digital, branch and phone banking channels.[172] According to its annual report for 2021, BOI generated revenues of approximately €2.74 billion in 2021.[173]

2.122 The Government announced in June 2021 that it planned to sell down part of its 13.9% shareholding in BOI over the following six months. As of 17 July 2022, the Government’s shareholding in BOI was below 4%.[174]

2.123 Following a review of its network, on 1 March 2021 BOI decided to close 103 branches in the Republic of Ireland and Northern Ireland.[175] BOI intends to continue to operate 182 branches across the island of Ireland.[176]

[169]https://www.oireachtas.ie/en/debates/debate/joint_committee_on_finance_public_expenditure_and_reform_and_taoiseach/2021-06-30/3/.

[170] See: https://live.euronext.com/en/product/equities/IE00BD1RP616-XMSM

[171] Annual-Report-for-the-Year-Ended-31-December-2021.pdf (bankofireland.com).

[172] See: Bank of Ireland Overview (bankofireland.com)

[173] See: Bank of Ireland Annual Report 2021.

[174] https://www.irishtimes.com/business/financial-services/state-s-bank-of-ireland-stake-falls-below-6-1.4798784.

[175]https://www.rte.ie/news/business/2021/0301/1199958-bank-of-ireland/#:~:text=Bank%20of%20Ireland%20said%20it,service%2C%20Bank%20of%20Ireland%20said.

[176] Page 4, https://investorrelations.bankofireland.com/app/uploads/BOI-Annual-Report-2020.pdf.

2.124 BOI notes that, "*Customers are increasingly banking digitally and 2020 has seen an accelerated shift in this direction. At Bank of Ireland, c.70% of sales of key banking products are now originated digitally*".[177]

2.125 In *M/21/021 – Bank of Ireland/Certain Assets of KBC* ("BOI/KBC"), the CCPC noted that BOI focuses on selling direct to its customer base, in common with the other major banks.[178]

2.126 BOI operates through a number of distribution channels, including through brokers, its branch network, by telephone and online. BOI also serves mortgage customers through mobile mortgage managers, who arrange flexible appointments at the location of a customer's choosing.[179]

2.127 BOI's mortgage offering is primarily focussed on fixed rate mortgages with cashback incentives. The cashback offer comprises 2% cashback at drawdown of a mortgage and 1% cashback after five years. BOI also offers green mortgages, and offers a fixed payment of €2,000 to First Time Buyers once they have saved €5,000 in a BOI MortgageSaver account.

2.128 In *BOI/KBC*, the parties submitted that a lender's funding model is a key variable in its pricing strategy and competitive position in the market.[180] In relation to this, they stated that BOI is self-reliant and is funded entirely from its own customer base (with a loan/deposit ratio of 86% as at 31 December 2020).

2.129 On 16 April 2021, KBC and BOI announced that they had entered into a memorandum of understanding whereby BOI would acquire substantially all of KBC's performing assets and liabilities. On 22 October 2021, KBC and BOI entered into a binding agreement in this regard. As such, BOI's share of mortgage stock is expected to grow significantly from [20-25]% in 2021 to [30-35]% in 2022.

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[177] Page 9, https://investorrelations.bankofireland.com/app/uploads/BOI-Annual-Report-2020.pdf.

[178] See paragraph 2.106 of the Commission's Determination in *BOI/KBC*, supra

[179] https://personalbanking.bankofireland.com/borrow/mortgages/mobile-mortgage-manager/

[180] See paragraph 2.109 of the Commission's Determination in *BOI/KBC*, supra 114.

(b) Non-Bank Lenders

2.130 There are currently three non-bank lenders active in the provision of mortgages in the State – Dilosk (trading as ICS Mortgages), Finance Ireland and Avant Money. Each is a relatively recent entrant into the supply of residential mortgages in Ireland. In general, these lenders tend to focus on low headline rates, distribution through brokers, and a fast response on mortgage applications.[181] These providers do not supply the range of products offered by full-service banks (e.g., they do not offer current accounts); do not have physical branches; and have relatively new IT platforms.

2.131 The chart below shows the share of mortgage business by non-bank lenders. These providers collectively have very low shares of the stock of mortgages but they have seen substantial growth in the share of mortgage origination recently, from a very low base. The total share of these lenders in mortgage origination was [15-20]% in 2021 Q4, compared to [0-5]% in 2020 Q1.[182]

Figure 7: Recent entrants' share of total lending, 2017 – 2021

[✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]

Source: The Commission analysis of lending data

2.132 Some market participants expect this trend to continue – for example, one broker, Irish Mortgage Corporation, expects the collective share of the non-bank lenders to increase to 20% in 2022.[183] The Commission understands from speaking with various non-bank lenders that they have few capacity constraints.

[181] According to AIMA, the non-bank lenders need to have these qualities to succeed as they either primarily or only distribute their products through the broker channel, so must be able to provide the best products, rates and service to receive business. See page 2 of the AIMA Call Note, dated 22 December 2021.

[182] See BPFI Data.

[183] See page 2 of the Irish Mortgage Corporation Call Note, dated 21 December 2021.

2.133 The increased market share of non-bank lenders may also be attributed to a growth in the broker market share, which made up 41% of the mortgage market in November 2021, up from 25% just two years prior.[184]

2.134 In certain markets abroad, non-bank lenders are commonplace in the supply of mortgages. For example, in the United States, non-bank lenders accounted for 68.1% of mortgage origination in 2020.[185] In Europe, non-bank lenders in the Netherlands have recently financed a significant portion of new mortgages, at 28%.[186]

2.135 Unlike retail banks, non-bank lenders typically do not rely directly on deposits to fund their lending services, instead seeking funding on capital markets from large institutional investors together with securitising the mortgages which they originate. For example, shareholders in Finance Ireland include investment management firm PIMCO[187] and the Ireland Strategic Investment Fund, which is controlled by the National Treasury Management Agency.[188] Meanwhile, Dilosk is reported to have raised €1.3bn through five transactions issuing bonds on capital markets since it was established in 2013.[189] The most recent of such transactions was in October 2021, when Dilosk raised €325 million of funding across 20 institutional investors through the sale of bonds backed by its own owner-occupied and Buy-to-let mortgages assets.[190] In addition, some non-bank lenders may receive funding from an overseas parent company. For instance, Avant Money is a subsidiary of the Bankinter Group.[191]

[184] See page 2 of the AIMA Call Note, dated 22 December 2021.

[185] https://www.wsj.com/articles/nonbank-lenders-are-dominating-the-mortgage-market-11624367460.

[186]https://www.ecb.europa.eu/pub/financial-stability/fsr/focus/2017/pdf/ecb~8341bea69d.fsrbox201705_07.pdf.

[187] PIMCO Europe GmbH Irish Branch, through its investment fund PIMCO BRAVO Fund II.

[188] See Finance Ireland's Investors.

[189] https://www.independent.ie/business/irish/dilosk-founders-lift-stake-above-50pc-as-lender-eyes-further-growth-41139877.html.

[190] See Dilosk news story dated 21 October 2021, available at: https://www.dilosk.com/news/dilosk-dac-raises-euro325-million-in-fifth-public-bond-issuance/.

[191] See paragraph 2.154.

2.136 As securitisation markets can endure periods of interruption, such as at the beginning of the Covid-19 pandemic, non-bank lenders have looked to diversify their funding models. One way of doing so is through "forward flow funding". Forward flow funding arrangements may involve the outright purchase by a funder of loans originated by a mortgage provider. A non-bank lender may secure such funding from an international bank, which provides non-bank lenders with an additional line of credit. A forward flow funding arrangement provides a non-bank lender with access to liquidity as they build out a mortgage origination and underwriting process.

2.137 As non-bank lenders do not hold customer deposits, they typically rely on the residential mortgage-backed securitisation ("RMBS") market, where they issue bonds backed by income from mortgages, to fund their growth.[192]

2.138 Dilosk's Chief Executive, Fergal McGrath, said that:

> *"buyers of the bonds "take some comfort in" the Central Bank of Ireland's mortgage limits, which are under review, having been introduced in 2015, adding that they were "good for the long-term stability of the market".*
>
> *"My personal view is that house prices in Ireland would be higher if we hadn't the rules in place. They've created a level playing field among all lenders," he said, adding that the limits restricts (sic) lenders from loosening credit standards to grab market share".*[193]

Dilosk

2.139 Dilosk DAC, trading as Dilosk and ICS Mortgages, is a specialist lender. It provides residential mortgage loans with a focus on Buy-to-let and owner-occupied mortgages.[194]

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192 https://www.dilosk.com/news/dilosk-aims-to-double-mortgage-market-share-to-10/.

193 https://www.dilosk.com/news/dilosk-aims-to-double-mortgage-market-share-to-10/.

194 See Dilosk's response to Question 1 of the BOI/KBC Competitor Questionnaire.

2.140 Dilosk reported that its consolidated loans rose to €566 million at the end of 2020 from €251 million a year earlier. Dilosk's group net profit fell to €672,822 in 2020 from €5.72 million in 2019.[195]

2.141 In September 2014, Dilosk acquired the ICS brand, mortgage distribution platform and a book of performing mortgages from BOI. Dilosk subsequently acquired €160 million of mortgages from GE Capital and acquired approximately €180 million of Irish loans from Leeds Building Society in 2018. It currently manages about €1.12 billion of mortgages.[196] It has been offering Buy-to-let loans since 2016. In October 2019, Dilosk entered into the market for owner-occupier mortgages. At the time of its entry, it offered the lowest variable rate in the market (2.70%) for properties with an LTV of less than 50%; and also offered 3 and 5 year fixed rates starting at 2.55% and 2.60%.[197]

2.142 In August 2021, Dilosk further reduced its fixed rates.[198] Currently, it offers variable rate mortgages from 2.45% and 3 year and 5 year fixed rate mortgages from 1.95%. In addition, Dilosk allows customers to overpay an additional 20% off their mortgage in any 12-month period without penalty.[199] According to the brokers, Full Circle, this may allow it to pick up some of KBC's available 2021 market share by attracting Switchers from KBC.[200] Dilosk is now looking to target First Time Buyers.[201]

195 https://www.irishtimes.com/business/financial-services/first-citizen-reports-2020-loss-as-it-weighs-mortgage-market-entry-1.4752363?mode=sample&auth-failed=1&pw-origin=https%3A%2F%2Fwww.irishtimes.com%2Fbusiness%2Ffinancial-services%2Ffirst-citizen-reports-2020-loss-as-it-weighs-mortgage-market-entry-1.4752363.

196 https://www.dilosk.com/news/dilosk-aims-to-double-mortgage-market-share-to-10/.

197 https://www.dilosk.com/news/ics-mortgages-enter-the-owner-occupier-market/.

198 https://www.dilosk.com/news/ics-mortgages-cuts-interest-rates/.

199 https://www.icsmortgages.ie/mortgages.

200 See pages 1-2 of the Full Circle Call Note, dated 16 November 2021.

201 See page 2 of the Irish Mortgage Corporation Call Note, dated 21 December 2021.

2.143 Dilosk has a share of 5% in mortgage origination.[202] It aims to double its share to 10% within three years.[203] Dilosk says that it saw an "instant uptick" in inquiries in early 2021 after Ulster Bank and KBC announced plans to withdraw from the State.[204]

2.144 Dilosk raised €325 million in October 2021, refinancing a portfolio of mortgages on the international bond markets. This transaction was its fifth such deal and brings the level it has raised on bond markets since 2015 to more than €1.3 billion.[205]

2.145 Dilosk does not operate a branch network but is active through the broker channel and through its own direct-to-customer offering.

2.146 In May 2022, similarly to Avant Money and Finance Ireland, Dilosk increased interest rates on all of its fixed-rate mortgage products. Dilosk stated that this increase was made due to the increase in its cost of funding, which impacted its NIM.[206]

2.147 In May 2022, Dilosk became party to a funding proposal in relation to the *BOI/KBC* transaction. This funding proposal involves BOI committing to offer €500 million in funding RMBS securitisations to Dilosk.[207]

Finance Ireland

2.148 Finance Ireland is another recent entrant into the Irish residential mortgage sector. It began offering commercial mortgages in 2013 but entered into the supply of residential mortgages when, in October 2018, it acquired the mortgage

[202] https://www.dilosk.com/news/dilosk-aims-to-double-mortgage-market-share-to-10/.

[203] https://www.irishtimes.com/business/financial-services/dilosk-aims-to-double-mortgage-market-share-to-10-1.4703892?mode=sample&auth-failed=1&pw-origin=https%3A%2F%2Fwww.irishtimes.com%2Fbusiness%2Ffinancial-services%2Fdilosk-aims-to-double-mortgage-market-share-to-10-1.4703892.

[204] https://www.dilosk.com/news/dilosk-aims-to-double-mortgage-market-share-to-10/.

[205] https://www.dilosk.com/news/dilosk-aims-to-double-mortgage-market-share-to-10/.

[206] See page 2 of the Dilosk Call Note, dated 17 June 2022.

[207] https://www.ccpc.ie/business/wp-content/uploads/sites/3/2021/04/2022.05.23-BOI-KBC-Determination-Short-Non-Confidential.pdf.

origination business of Pepper Money, including a c.€200M Irish residential mortgage loan portfolio, consisting of approximately 900 performing mortgage loans originated by Pepper Money.[208]

2.149 Finance Ireland, which was established in 2002, is active in the markets for lending to Auto Finance, SME Finance, Agri Finance and Commercial Real Estate Finance.[209] It is owned primarily by two shareholders: PIMCO, an investment management firm; and Ireland Strategic Investment Fund, a sovereign investment fund with a mandate to invest on a commercial basis to support economic activity and employment in Ireland. According to its financial statements for 2020, Finance Ireland generated revenue of approximately €48.5 million.

2.150 Finance Ireland is an online-only mortgage provider and operates exclusively through the broker channel.[210] It offers a range of variable and fixed-rate mortgages. Variable rate mortgages range from 2.75% to 3.22% depending on the LTV. Finance Ireland's fixed rates include 3.45% for a three-year Fixed Rate with an LTV less than 50%.[211] In 2021 Finance Ireland introduced long-term Fixed Rates of 10, 15 and 20 years.[212]

2.151 In December 2021 Finance Ireland announced a reduction in its long-term Fixed Rates and a Switcher incentive of a €1500 contribution towards the legal fees incurred when switching.[213]

2.152 In its first full year of business in 2019, Finance Ireland's retail mortgage division saw new loans written rise from €219 million to €283 million. The figure for 2020 equated to about 3.3% of €8.4 billion of lending in the Irish home loans market.[214]

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[208] https://www.financeireland.ie/announcements/finance-ireland-announces-entry-into-irish-residential-mortgage-market/

[209] https://www.financeireland.ie/announcements/finance-ireland-announces-entry-into-irish-residential-mortgage-market/.

[210] https://www.financeireland.ie/products/residential-mortgages/overview/.

[211] https://www.financeireland.ie/products/residential-mortgages/mortgage-rates/.

[212] See Finance Ireland's response to Question 2 of the BOI/KBC Competitor Questionnaire.

[213] https://www.rte.ie/news/business/2021/1201/1264301-finance-ireland-mortgage/.

[214] https://www.irishtimes.com/business/financial-services/finance-ireland-profits-fell-in-2020-as-covid-triggered-13-7m-loans-charge-1.4689043?mode=sample&auth-failed=1&pw-

It had a 3.5% market share in mortgage origination in the year ending 2020.[215] In October 2021, Finance Ireland's Chief Executive said that the group currently had a 6% share of the Irish mortgage market, with strong underlying activity being helped by the decisions of Ulster Bank and KBC to withdraw from the State earlier in 2021.[216]

2.153 Along with Dilosk, in May 2022, Finance Ireland became party to a funding proposal in relation to the *BOI/KBC* transaction. This funding proposal involves BOI committing to offer €500 million in funding RMBS securitisations to Finance Ireland.[217] In June 2022, Finance Ireland increased its interest rates on its fixed-rate mortgage products, in a similar manner to Dilosk and Avant Money.

Avant Money

2.154 Avant Money is a new entrant into the Irish mortgage market, having commenced mortgage operations in late 2020. It also offers personal loans and credit cards, having operated previously as MBNA and Avantcard in respect of these products. Avant Money is not funded by retail deposits in the State. It is owned by Bankinter, a Spanish financial services company based in Spain. Bankinter is the fourth largest Spanish bank by market capitalisation and reported net interest income of €1.28 billion in 2021.[218]

2.155 Avant Money provides products to First Time Buyers, Switchers and Movers.[219] Avant Money operates through an online only model and does not have any branches in the State, offering mortgages to customers exclusively through

origin=https%3A%2F%2Fwww.irishtimes.com%2Fbusiness%2Ffinancial-services%2Ffinance-ireland-profits-fell-in-2020-as-covid-triggered-13-7m-loans-charge-1.4689043

[215] See Finance Ireland's response to Question 24 of the BOI/KBC Competitor Questionnaire.

[216] https://www.irishtimes.com/business/financial-services/finance-ireland-profits-fell-in-2020-as-covid-triggered-13-7m-loans-charge-1.4689043?mode=sample&auth-failed=1&pw-origin=https%3A%2F%2Fwww.irishtimes.com%2Fbusiness%2Ffinancial-services%2Ffinance-ireland-profits-fell-in-2020-as-covid-triggered-13-7m-loans-charge-1.4689043

[217] https://www.ccpc.ie/business/wp-content/uploads/sites/3/2021/04/2022.05.23-BOI-KBC-Determination-Short-Non-Confidential.pdf.

[218] See: https://www.bankinter.com/file_source2/webcorporativa/accionistas-inversores/informacion-financiera/informes-anuales/2021/Informe%20Anual%20Integrado%202021_en.pdf.

[219] See Avant Money's response to Question 1 of the BOI/KBC Competitor Questionnaire.

brokers. Similar to other non-bank lenders, it has offered lower rates than retail banks. Irish Mortgage Corporation, a broker, noted that Avant Money can approve a mortgage application very quickly, turning around an application in 2.2 days.[220]

2.156 Avant Money holds a 4% share in mortgage origination in the State.[221]

2.157 In April 2021 Avant Money introduced a 10-year fixed product and in June 2021 full fixed for life products. Avant Money's One Mortgage product is the first and only product in the State to offer a fixed rate for the entire term of a 30-year mortgage. It also provides customers with the flexibility to overpay up to 10% of the balance each year and potentially to move home without any early redemption fee.

2.158 In December 2021 Avant Money reduced the rates of its long-term fixed rate products and introduced a temporary Switcher incentive of a €1500 contribution to professional fees. This switcher incentive was specifically aimed at KBC and Ulster Bank mortgage customers.[222]

2.159 In May 2022 Avant Money announced interest rate increases to a majority of their mortgage products, including medium and long-term fixed rates and One Mortgage rates.

Potential Entrants

2.160 There are a number of providers of financial services who might be considered as well placed to enter the market for the provision of mortgage products.

<u>MoCo</u>

2.161 MoCo[223] is a new entrant to the Irish residential mortgage market. [✂]

[220] See page 2 of the Irish Mortgage Corporation Call Note, dated 21 December 2021.

[221] See page 2 of Irish Mortgage Corporation Call Note, dated 21 December 2021.

[222] Avant Money offering €1,500 cashback to mortgage switchers | bonkers.ie.

[223] Trading as Cedar Lending Services Limited, as defined in supra 1.13.

[✂].[224]

2.162 Mortgages provided by MoCo will be underwritten, but users will be able to submit and complete the entire mortgage process digitally, without any physical paperwork and no branch network.

<u>An Post</u>

2.163 An Post is authorised by the Minister for Finance to provide payment services and is regulated by the CBI in the provision of these services. An Post has a network of over 900 post offices offering a range of financial services, including cash lodgements and withdrawals as well as foreign exchange. An Post has typically taken a partnership approach in establishing financial products and services, for example, partnering with Mastercard[225] on foreign exchange services[226] and with AvantCard for credit cards and personal loans.[227]

2.164 An Post intends to enter the mortgage market, and it informed the Commission that [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂].[228]

<u>[✂][✂][✂]</u>

2.165 [✂].

Potential Barriers to Entry and Expansion

2.166 The following section assesses potential barriers to entry or expansion in the supply of mortgage lending in the State. Research, as well as evidence provided to

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[224] See MoCo's response to Question 1 of the BOI/KBC Questionnaire.

[225] Mastercard International Incorporated ("Mastercard")

[226] https://www.anpost.com/Money/Foreign-Currency/Currency-Card.

[227] https://www.checkout.ie/a-brands/avantcard-post-partner-offer-personal-loans-credit-cards-65329.

[228] See page 2 of the An Post Call Note, dated 10 November 2021. See also https://www.irishtimes.com/business/financial-services/an-post-in-talks-with-non-bank-start-up-moco-to-offer-mortgages-1.4664431.

the Commission by third parties, indicates that there are high barriers to entry and expansion in the mortgage market. Such barriers may include: regulatory requirements; low profitability; product distribution issues; data inequality; and balance sheet exploitation. Each of these is discussed in greater detail below, after a brief overview of findings on barriers to entry from the Commission's 2017 research into the mortgage market.[229] The Commission's conclusions on potential barriers to entry and expansion in the mortgage market are outlined in Section 5.

Findings of the Commission's Mortgage Market Options Paper

2.167 As part of the Commission's 2017 mortgage study, a public consultation sought views on perceived barriers to entry into the Irish market and enquired whether there are any unique features of the Irish context that make entry less attractive and what could be done to attract and facilitate entry. Most respondents to the consultation identified lack of scale, legacy issues of NPLs and poor access to collateral (i.e., the difficulties and timelines faced by lenders when attempting to repossess properties on which mortgages are not being, nor are likely to be, repaid) as unique barriers to entry in the State. Other issues raised included the conveyancing process and the extent of current regulation.[230]

2.168 Dr Edward Shinnick's contribution to the Commission's public consultation[231] offered a comprehensive summary of the various views offered by several respondents:

> *"In addition to the potential barriers to entry posed by regulation, other forms of non-regulatory entry barriers and sunk costs may also exist. These include:*
>
> • *Access to finance*
>
> • *Consumer inertia resulting in low switching rates*

[229] For more information, see: Options for Ireland's Mortgage Market, 2017.

[230] See page 38 of the Commission's Mortgage Market Options Paper, available here.

[231] See page 2 of Dr Edward Shinnick's response to the public consultation, available here.

- *Information asymmetries and high switching costs*
- *Size of the domestic market*
- *Costs of establishing a branch network for retail banking, and*
- *Legal and institutional barriers."*

2.169 This section considers some of the potential barriers to entry raised above, in addition to issues that came to the attention of the Commission in correspondence with third parties in assessing the Proposed Transaction.

State Involvement in the Banking Sector

2.170 As summarised in paragraphs 2.7 and 2.8 above, following the financial crisis the Irish Government became and continues to be a shareholder in each of AIB, BOI and PTSB. Government involvement in the banking sector could be considered a negative feature from the perspective of new entry into the Irish market. However, respondents to the Commission's 2017 public consultation noted that while it may be a challenge, it was not a significant barrier to entry because of the Government's commitment to unwind its shareholding and because the Government's bailouts were seen as a necessary response to the financial crisis.[232]

Regulatory Environment

2.171 With regard to the current regulatory regime and its impact on the functioning of the market and on potential entry as a whole, respondents to the public consultation provided mixed views. While there appears to be general support for the idea that robust regulation is required and that conduct regulation and the macro-prudential measures are necessary, there are some differences regarding the impact that regulation is having on lenders. PTSB and BOI support the current regulatory regime while two lenders (anonymised in the Commission's paper)

[232] See page 41 of the Commission's Mortgage Market Options Paper, available here.

responded expressing the view the regulatory regime is more onerous in Ireland compared to other jurisdictions.[233]

2.172 Both Dilosk and Finance Ireland informed the Commission that there is a perception that the regulatory process of applying for a banking licence is both a lengthy and onerous one.[234]

2.173 One of the anonymous lenders noted that:

> *"regulatory policies and practices in Ireland are more onerous due to proprietary Irish mortgage regulation, specifically:*
>
> *• Macro-prudential Measures;*
>
> *• Code of Conduct on Mortgage Arrears;*
>
> *• S149 of CCA 1995 - this is also unique to the Irish market.*
>
> *Additionally, the small nature of the Irish market and its highly contended [sic] nature means that regulatory costs which are relatively fixed are significant relative to income*."[235]

Operating Costs

2.174 Paragraphs 2.20 to 2.24 above highlighted the potential consequences for retail banking providers in the State of regulatory requirements such as the CBI's bank capital instruments and mortgage measures. In summarising the previous discussion, operating costs such as requirements on retail banks to hold capital may impact on potential new entrants in the following manner:

[233] See page 44 of the Commission's Mortgage Market Options Paper, available here.

[234] See Dilosk's response to Question 11 of the BOI/KBC Competitor Questionnaire, dated 12 July 2021 and Finance Ireland's response to Question 13 of the BOI/KBC Competitor Questionnaire, dated 12 July 2021.

[235] See page 45 of the Commission's Mortgage Market Options Paper, available here.

- *"Retail banks operating in the State are required to hold more capital than counterparts in Europe, for example, as demonstrated by the proportion of RWA;*

- *The capital charge on a bank home loan in the State is 2.6 times higher than in the EU; and*

- *Aside from capital requirements, operating costs for retail banks in the State are higher than elsewhere, accounting for 1.05 points of the average Irish mortgage rate, compared to 0.65 points across the EU".*[236]

Low profitability

2.175 In the Merger Notification Form, the Parties stated that the rationale for the Proposed Transaction and ultimately Ulster Bank's withdrawal from the Irish banking sector concerns the challenge faced by Ulster Bank in achieving and acceptable level of sustainable returns within a reasonable timeframe.[237]

2.176 Market participants may encounter difficulty in generating sustainable returns upon entry for a number of reasons, including regulatory and legal costs, origination costs and commission paid to brokers. Additionally, third parties expressed to the Commission that purchasing a back book of mortgages can help when entering the market, in order to quickly establish a flow of income. As noted in paragraph 2.141 above, Dilosk acquired a back book of mortgages from BOI in 2014.

2.177 In the absence of a back book of mortgages, new entrants may encounter difficulties in covering their costs in the short to medium term before generating a profit.

Repossession Policies

[236] https://www.irishtimes.com/business/financial-services/more-non-bank-lenders-will-enter-market-mortgage-chief-1.4741009

[237] See paragraph 10 of the Merger Notification Form.

2.178 Uncertainty over repossession policies were cited as a potential barrier to entry in response to the Commission's 2017 public consultation. One lender stated that:

> *"repossession policies and practices are a barrier to entry to the Irish market for the following reasons: access to loan security is uncertain; the timing to security realisation is protracted; associated capital and operating costs are significant. … The time to resolution in Ireland is also* typically much more protracted than elsewhere. In Ireland, this ranges from 18 to 72 months. By contrast, the UK range is 9 to 12 months, with Northern Ireland and Denmark at 6 months."[238]

2.179 Similarly, in response to the BOI/KBC Competitor Questionnaire, Dilosk informed the Commission that the length of time to foreclose on a borrower in arrears acts as a potential barrier to new entrants.[239]

Barriers to Switching

2.180 As discussed in paragraphs 2.84 to 2.91 above, mortgage holders face significant barriers to switching mortgage products. These barriers can be broadly summarised as: (i) the cost and process of switching; (ii) lack of knowledge or understanding of benefits of switching; and, (iii) perceived or actual inability to be approved for a new mortgage. The reluctance or inability of consumers to switch mortgage products may place new entrants at a material disadvantage to incumbent lenders.

2.181 A new entrant offering mortgage products may find customers via two routes. Firstly, a new entrant can generate customers by originating new mortgage lending, for example to First Time Buyers. Secondly, a new entrant can build its customer base through second-time and subsequent borrowers that switch from their mortgage provider to the new entrant. However, with low rates of switching, as has historically been the case in the State, a new entrant may face difficulty in

[238] See page 57 of the Commission's Mortgage Market Options Paper, available here.

[239] See Dilosk's response to Question 11 of the BOI/KBC Competitor Questionnaire, dated 12 July 2021.

growing its customer base and thereby generating a sustainable return on its investment.

Data Inequality

2.182 Incumbent banks with substantial back books of loans have access to large volumes of data on customers. The data includes information on customer history of loan repayments, credit conditions, income and property valuations. The greater volumes of this data that a lender can generate and analyse, the more accurate a lender may be in calculating risk. The Commission understands that lower risk lending may lead to lower pricing by lenders.

Lending to SMEs in the State

2.183 The Target Assets include the Microenterprise Business Direct Loan Book.[240] This section provides an overview of the provision of lending to SMEs in the State, focusing on, in particular: (a) Customers of Business Lending; (b) provision of commercial lending; (c) Pricing; (d) Barriers to entry and switching costs; and (e) Countervailing Buyer Power.

Customers of Business Lending

2.184 Given that the business lending to be acquired by PTSB is lending to microenterprises,[241] the Commission has focussed on providing a background assessment of this particular segment of the business lending market.

2.185 The purpose of a loan, i.e., the reason it is required, can broadly be divided into working capital requirements and investment funding. Working capital loans are used to finance a business's day-to-day operations and include the following: overdrafts, short term working capital loans, and invoice finance. Investment funding includes capital expenditure finance, and finance for acquisition or funding organic growth.

[240] See paragraph 1 of the Merger Notification Form

[241] Defined as enterprises that employ fewer than 10 persons and whose annual turnover or annual balance sheet total does not exceed €2 million

2.186 The purpose of the loan can influence the term of the loan required, with term lengths of less than one year generally considered short-term. Secured loans, those which are backed by an asset, such as property, generally have lower interest rates and/or fees in comparison to unsecured lending (for example, overdrafts).

2.187 Both the form of security required to secure the loan, together with the purpose of the loan, influence the type of loan a business will seek and may be offered. The size of the business and the sector in which it operates may also influence both the type of loan a business will seek and be offered. Market intelligence indicates that businesses typically use more than one lending product.

2.188 The Department of Finance has indicated that a low demand for credit has been a consistent feature of the Irish SME environment in recent years as evidenced by its SME Credit Demand Survey. The SME Credit Demand Survey Report April - September 2021 shows that credit demand for SMEs has been on a downward trend from 2012 to date, with only 17% of surveyed businesses seeking credit in the assessed 2021 period. Predicted credit demand among the surveyed businesses was also low, with only 7% predicting that they would seek bank finance in the next six months. A key reason provided for this low level of demand for credit is that small businesses use their own funds instead of loans where possible.

Provision of Commercial Lending in the State

2.189 This section provides an overview of the banks active in commercial lending to SMEs in the State, followed by an overview of the role of non-banks in commercial lending.

Banks Active in Commercial Lending in the State

2.190 Focusing initially on banks active in the State, the Commission observes that they typically compete across a wide spectrum of lending products. For the purposes of this analysis it is useful to consider the differences in their customer focus:

(a) **Pillar Banks**, consisting of Bank of Ireland, AIB and Ulster Bank, cover lending to all types of businesses regardless of turnover size; and

(b) **Retail Banks**, consisting of Permanent TSB and KBC, primarily cater to retail (i.e., non-business) customers but also serve SMEs, with a focus on the smaller sized businesses.

2.191 A brief overview of the main banks providing commercial lending in the State, other than PTSB and Ulster Bank, is provided below.[242]

<u>AIB</u>

2.192 An overview of AIB is provided in paragraphs 2.107 – 2.119 above.

<u>BOI</u>

2.193 An overview of BOI is provided in paragraphs 2.120 – 2.129 above.

Non-Bank Lenders Active in Business Lending in the State

2.194 There are a variety of non-bank lenders active in business lending to SMEs in the State. Non-bank lenders do not provide the full range of products and services available from a licensed bank. Non-bank lenders offering financing to SMEs in the State include Dunport, Bain Capital Credit, Muzinich, Beechbrook, Finance Ireland and Proventus.

2.195 Generally, non-bank lenders provide funding at higher interest rates than those of the pillar banks, and provide funding to customers that banks may not be interested in due to, perhaps, risk appetite.[243]

2.196 In *M/21/040 – AIB/Certain Assets of Ulster Bank* ("AIB/UB"), the Commission was informed that the products and services acquired by business customers from non-bank lenders often sit alongside services acquired from a customer's

[242] A description of the Parties is provided in Chapter 1.

[243] CBI, 'Behind the Data: the role of non-bank lenders in financing Irish SMEs', citing Cherneko et al, 2019; Tsuruta, 2010; Denis and Mihov, 2003; Carey at al. 1998 "*There is evidence that banks and non-bank lending can have different risk profiles*". Available at https://www.centralbank.ie/statistics/statistical-publications/behind-the-data/the-role-of-non-bank-lenders-in-financing-irish-smes

relationship bank, which works for some customers, but does not work for all customers.[244] This means that businesses, even if they acquire lending from a non-bank lender, will almost always have a relationship with a bank for at least some of their financial services.

2.197 Non-bank lenders are, however, considered an important source of finance to SMEs in Ireland, having granted new loans totalling a value of €1.6 billion to Irish SMEs in 2020.[245] Non-bank lenders provide increased choice for borrowers, particularly in market segments underserved by other lenders.[246] The CBI states that non-bank lenders' *"...position as a key part of the SME funding ecosystem was demonstrated by the inclusion of non-bank lenders in the government's COVID-19 Credit Guarantee Scheme, as well as by participation in the range of SBCI loan schemes over the past decade."*[247]

Pricing

2.198 Pricing of business loans for larger loan amounts is often determined on the basis of the features of the individual loan and the customer. However, for smaller loan amounts that would typically be lent to microenterprises, there is more standard pricing.

2.199 In *AIB/UB*, the Commission found that business lending products provided by non-banks are generally more expensive than those provided by banks, which may arise due to non-banks having a higher cost of funds, or due to the types of customers to whom they lend.[248] However, non-banks consider themselves to

[244] See the Commission's Determination in *M/21/040 – AIB/Certain Assets of Ulster Bank*, which is available at: https://www.ccpc.ie/business/wp-content/uploads/sites/3/2021/08/M.21.040-AIB-Certain-Assets-of-Ulster-Bank-Phase-2-Determination-Public.pdf.

[245] CBI, 'Behind the Data: the role of non-bank lenders in financing Irish SMEs.' Available at: https://www.centralbank.ie/statistics/statistical-publications/behind-the-data/the-role-of-non-bank-lenders-in-financing-irish-smes

[246] Ibid.

[247] Ibid.

[248] As indicated above in paragraph 2.195.

have quicker turn-around times on decisions, and potentially a higher risk appetite, than pillar banks.[249]

Barriers to Entry and Expansion

2.200 In its previous determination, the Commission identified substantial barriers to entry in respect of the supply of business lending as a full-service bank serving a broad range of customer sizes and sectors and supplying a broad range of business banking and lending products.[250]

2.201 These barriers include, but are not limited to: (i) switching costs; (ii) legal and institutional barriers; (iii) regulatory and capital requirements; (iv) low profitability; and, (v) information asymmetries. These barriers appear to be less substantial for those providers specialising in certain products, or sectors, or certain customer types. Each of these barriers to entry are briefly discussed below.

Switching Costs

2.202 Switching refers to customers changing providers. In banking, business customers will frequently incur costs, whether pecuniary or the opportunity costs of their time, when they initially establish a relationship with their banking service provider. They will often, thereafter, remain 'loyal' to that institution in order to avoid incurring the same costs again, or just due to a degree of inertia.[251]

2.203 However, customers' perception of switching costs also plays an important role. Ulster Bank recognised that customers tend to expect the switching process to be difficult.[252] Also, considering the importance of the banking relationship to some customers, the loss of that relationship may be considered as a further reason not to switch, particularly for those customers which consider that they have built a beneficial relationship with a dedicated relationship manager. An Ulster Bank SME

[249] See Determination in AIB/UB, supra 245.

[250] Ibid, page. 25.

[251] Donatella Porrini and Giovanni B. Ramello, 'Competition in Banking: Switching Costs and the Limits of Antitrust Enforcement' (2005) Law and the State: A Political Economy Approach, 358.

[252] See Determination in AIB/UB, supra 245.

customer survey found that a small amount of SME's switched their main business operating account in the past 5 years.[253]

Regulatory and Capital Requirements

2.204 As a consequence of the global financial crisis, authorities responsible for promoting financial stability took measures to reduce the risk of such systemic crises reoccurring through the enactment of macro-prudential policies. These regulatory policies are aimed at the promotion of the stability of the financial system as a whole.[254] These included the implementation of a framework for setting minimal capital requirements for banks. It has been reported that, due to the requirement to hold more capital, these policy measures impact upon the profitability of banks engaged in business lending in the State.[255]

2.205 Non-bank lenders are not subject to the same capital requirements as those faced by banks. Non-bank lenders in the EU are subject to regulatory oversight from the Alternative Investment Fund Managers Directive ("AIFMD").[256] However, against this non-bank lenders do not have access to the low-cost deposit funding.

Low Profitability and Market Vulnerability

2.206 Market participants may encounter difficulties in generating sustainable returns for a number of reasons. Average Return on Equity ("ROE") in 2019 for Irish banks, according to a report by Goodbody Stockbrokers in May 2021, was lower than their European counterparts. For continental European banks, the average ROE was 6% while, for the same time period, it was around 3% for AIB, 2% for Ulster

[253] See Determination in AIB/UB, supra 245.

[254] See the CBI's macro-prudential policies.

[255] See the Banking and Payments Federation Ireland Report entitled *"Irish Mortgage RWA Density Analysis Project"* by Kevin McConnell, dated January 2021.

[256] See Directive 2001/61/EU of the European Parliament and of the Council on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulation (EC) No 1060/2009 and (EU) No 1095/2010. Available at: Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010Text with EEA relevance (europa.eu). See also the AIMA's research on non-bank lending in Europe, available at: https://www.aima.org/educate/aima-research/non-bank-lending-in-the-european-union.html.

Bank, and 4% for Bank of Ireland.[257] The net interest margins earned by the main Irish banks had been steadily decreasing in the period up to 2021 although recent market movements suggest that this may not be a long- term trend.

2.207 In addition, the CBI has noted that Ireland has been particularly vulnerable to shocks in global financial conditions, particularly the sudden repricing of risk in global financial markets.[258]

Information Asymmetry

2.208 Incumbent banks are able to form judgements as to the creditworthiness of potential business borrowers based upon information they have accumulated on the past financial performance of the borrower's business; how the business is managed; how it has previously responded to shocks; the repayment history for previous loans; and how its current account cash flows vary over time. New entrants have limited access to such information, which may make the task of calculating risk significantly more difficult, particularly in relation to SME lending. This has been identified as contributing to the higher financing costs that SMEs typically face as compared to larger business borrowers.[259]

Countervailing Buyer Power

2.209 In the Commission's previous determination, it found that there appears to be little countervailing buyer power in business lending for the majority of customers. Larger corporate customers may have a degree of negotiating power, but this would be very limited for smaller businesses.

[257] See the report by the Banking and Payments Federation of Ireland, *'The Future of Retail Banking in Ireland',* dated September 2021. Available at: https://bpfi.ie/wp-content/uploads/2021/09/BPFI-Future-of-Retail-Banking-in-Ireland-Report.pdf

[258] Financial Stability Review 2021:I (centralbank.ie)

[259] See paragraph 27 on page 9 of the OECD report entitled, 'New Approaches to SME and Entrepreneurship Financing: Broadening the range of instruments', dated 2015.

3. RELEVANT PRODUCT AND GEOGRAPHIC MARKETS

Introduction

3.1 In this section, the Commission identifies the potential product and geographic markets that are relevant for the assessment of the likely effects of the Proposed Transaction. It summarises the general principles that apply to market definition, the activities of the notifying parties, the views of the notifying parties and third parties and then sets out the Commission's view of the potential relevant product and geographic markets.

3.2 Market definition provides a framework for assessing the competitive effects of a merger; it is a means to an end. The boundaries of a market do not determine the outcome of the analysis of the competitive effects of the merger, as there can be constraints on the merging parties from outside the relevant market, segmentation within the relevant market, or other ways in which some constraints will be more significant than others.[260] The Commission expects to take such factors into account in its assessment of competitive effects.

Horizontal Overlap

3.3 In the Merger Notification Form, the Parties have submitted that there is a horizontal overlap between PTSB and Ulster Bank in the State with respect to the provision of the following products[261]:

(a) Mortgages; and

(b) SME Lending.

3.4 The Parties have submitted that, as PTSB has no activities in asset finance/leasing, the Proposed Transaction does not give rise to an overlap between PTSB and Ulster Bank in asset finance/leasing. Although PTSB previously provided asset

[260] See paragraph 2.3 of the Guidelines for Merger Analysis, adopted by the Commission on 31 October 2014 (the "Merger Guidelines").

[261] See page 19 of the Merger Notification Form

finance/leasing services, origination of these services was wound down from 2010 and the portfolio was sold in 2012.

3.5 With respect to bank branches, the Parties have submitted that PTSB is acquiring the buildings and not the associated business. The Parties noted that the geographical overlap between Ulster Bank's branches and PTSB's existing branches is limited to 5 out of the 25 branches being acquired.

3.6 The Commission's assessment of data obtained from the Parties and from other sources is consistent with the Parties' assessment with respect to the minimal significance of overlaps in the provision of asset finance/leasing and in the acquisition of bank branches. There is no overlap in the provision of asset finance/leasing, as PTSB is not active in this market. In relation to the Target Branches, as described above, only 5 of the 25 Target Branches overlap geographically with an existing PTSB branch. The Commission assessed each of these overlaps, and found that the branches of a number of competitors were also present in these areas, which would continue to constrain the current and new PTSB branches. In light of this, the Commission does not propose to come to a definitive view on the definition of these potential product markets. The analysis of asset finance/leasing and bank branches is not considered further in this Determination.

Relevant principles

3.7 The role of market definition is explained in the Commission's Merger Guidelines. Market definition is a conceptual framework within which relevant information can be organised for the purpose of assessing the competitive effects of a merger.[262]

3.8 According to the Merger Guidelines:

> *"The relevant product market is defined in terms of products rather than producers. It is the set of products that customers consider to be close*

[262] See paragraph 2.1 of the Merger Guidelines.

substitutes. In identifying the relevant product market, the Commission will pay particular attention to the behaviour of customers, i.e., demand-side substitution. Supply-side substitution (i.e., the behaviour of existing and/or potential suppliers in the short term) may also be considered".[263]

3.9 The relevant market contains the most significant alternatives available to the customers or consumers of the merging parties. Identifying the precise relevant market involves an element of judgement, with appropriate weight being given to factors on both the demand and supply side.[264]

3.10 The Merger Guidelines note that:

"Whether or not a product is a close substitute of a product supplied by one or more of the merging parties will depend on the willingness of customers to switch from one product to the other in response to a small but significant and non-transitory increase in price (or an equivalent decrease in quality). This will involve an assessment of the characteristics and functions of the products in question".[265]

3.11 The standard economic test for defining the relevant market is the small but significant non-transitory increase in price (''SSNIP'') test. The SSNIP test seeks to identify the smallest group of products and geographic areas within which a hypothetical monopolist could profitably impose a SSNIP without a sufficient number of consumers/service purchasers switching to alternative products to render the price increase non-profitable. However, the Commission notes that the SSNIP test is just one of the tools used in defining the relevant product market. A substantial emphasis should also be placed on product characteristics, price and intended use as well as observed substitution patterns between various products that can potentially be included in the same product market.

[263] See paragraph 2.8 of the Merger Guidelines.

[264] See paragraph 2.2 of the Merger Guidelines.

[265] See paragraph 2.9 of the Merger Guidelines.

3.12 It may not be possible to draw a clear line around the fields of rivalry. That being so, it is fallacious to regard as relevant to the competition analysis only those products defined as falling within the relevant market and to disregard any competitive pressure from those products defined as falling outside it. The Commission may therefore consider segmentation within the relevant market or factors outside the relevant market that impose competitive constraints on firms in the relevant market.[266]

3.13 Ultimately, the Commission's definition of the relevant market or markets depends on the specific facts, circumstances, and evidence of the merger under investigation.[267]

Relevant Product Markets

Previous decisions

3.14 The Commission has recently considered several mergers in the financial sector.[268] These previous merger determinations concerned various segments of the financial sector, including investment and wealth management services, corporate finance advisory services, and capital market services. The Commission has specifically considered the provision of mortgages and SME lending in previous merger determinations.[269] Outside its merger review remit, the Commission carried out a review of the Irish mortgage market in 2017.[270]

3.15 The European Commission has considered mergers in the financial sector in several Member States. Generally, the European Commission has left the precise definition of relevant financial sector markets open in its merger considerations. For example, it has considered whether individual retail banking products

[266] See paragraph 2.1 of the Merger Guidelines.

[267] See paragraph 2.6 of the Merger Guidelines.

[268] See for example M/21/046 – Bank of Ireland/Davy (Wealth Management and Capital Markets) and M/21/012 – AIB/Goodbody.

[269] See the Commission's Determination in *BOI/KBC,* supra 114*;* and its Determination in *AIB/UB,* supra 245.

[270] See the Commission's Mortgage Options paper, dated 15 June 2017, available at: https://www.ccpc.ie/business/wp-content/uploads/sites/3/2017/06/CCPC-Mortgages-Options-Paper.pdf.

represent separate relevant product markets or whether several retail banking products may form part of a single relevant product market, and in both cases did not come to a definitive conclusion.[271]

3.16 In considering the provision of mortgages, the European Commission has recognised that the weakness or absence of demand-side substitution suggests that mortgages should be treated separately from other financial products. However, the exact product market definition has generally been left open.[272]

3.17 The European Commission has also considered whether banking markets should be segmented according to customer size. According to the European Commission's investigation in M.4844 - Fortis/ABN AMRO Assets, smaller customers have different needs as to product complexity and transaction size. They also have less in-house knowledge about banking products, less access to foreign banks or to capital markets (as an alternative funding source), lower bargaining power and typically hold fewer banking relationships. The investigation also found that banks treat customers differently based on their size as to product standardisation, marketing approach, and risk assessment.[273]

3.18 When considering different markets for corporate lending to smaller commercial customers (such as SMEs) and to larger corporate clients, the European Commission found "that there is no obvious single parameter by which companies can be designated as SMEs or LCCs, and which would be applicable to all market players in a given market."[274] However, in carrying out market inquiries as part of their analysis of a merger, the European Commission has found that "it appears that the turnover represents a good proxy to determine whether a customer is part or not of the LCCs segment".[275]

[271] See for example Case M.3894 – Unicredit / HVB and Case M.4844 – Fortis / ABN Amro.

[272] See for example Case M.7007 - RZB/ RBSPK/ RWBB and case COMP/M.3894 - UNICREDITO / HVB.

[273] See paragraph 14 of *COMP/M.4844 – Fortis/ABN AMRO Assets*.

[274] See paragraph 26 of *M.8414 DNB / NORDEA/LUMINOR GROUP*, citing *COMP/M. 2567 – Nordbanken/Postgirot, COMP/M.3894 – Unicredito / HVB, COMP/M.4844 – Fortis/ABN AMRO Assets.*

[275] See paragraph 30 of *M.8414 DNB/NORDEA/LUMINOR GROUP*.

3.19 The European Commission has acknowledged that size thresholds might be case specific. Past decisions of the European Commission and national competition authorities show that, in fact, large differences in thresholds exist between business lending markets in different Member States. For instance, while the European Commission decided on a threshold of €250 million for the purpose of identifying LCCs (Large Corporate Customers) in M.4814 Fortis/ABN AMRO Assets (the Netherlands), a considerably lower one of €20 million was found to be more likely to be applicable in M.8414 DNB/NORDEA/LUMINOR GROUP (Baltics) given the specific characteristics of business lending in the concerned Member States. Some national competition authorities have used the EU definition of an SME (i.e. around €50 million) to subdivide the market.[276]

3.20 Ultimately, the European Commission did not, in any of the above-mentioned cases, need to conclude on whether these candidate markets (whether segmented by product or by size) constituted separate product markets.

Views of the Parties

3.21 In the Merger Notification Form, PTSB proposed that the definition of the relevant product and geographic markets can be left open as, in its view, the Proposed Transaction does not give rise to a substantial lessening of competition.[277] Notwithstanding, the Parties have proposed that there are separate markets for:

(a) The supply of mortgages on a national basis; and

(b) SME lending in the State.[278]

The provision of mortgages

[276] See Greece: *562/VII/2013 National Bank of Greece S.A.|Eurobank Ergasias S.A.* – LCCs are companies with a turnover of over €50 million (Greece); Norway: *V2003-61 DnB Holding ASA/Gjensidige NOR ASA* – LCCs are companies with turnover of over 300 million NOK (€30 million in today's exchange rate); Denmark: *4/0120-0401-0044 Nordea Bank Danmark A/S/Fionia Bank A/S* – SMEs with a turnover of less than €47 million were categorised under "retail banking" along with private customers; UK: *ME/3862/08 Lloyds TSB Group plc.|HBOS plc*. - The exact definition of SME (small and medium sized enterprises) varies, but the OFT has previously classed firms as SMEs where they have an annual turnover of up to £25 million (currently €29.97 million as of 12 April 2022).

[277] See Page 25 of the Merger Notification Form

[278] The Parties have defined SMEs as businesses that employ fewer than 250 persons and which has either or, both of the following: (i) an annual turnover not exceeding €50 million; (ii) an annual balance sheet total not exceeding €43 million.

Views of the Commission

3.22 The Commission has taken the Parties' core overlap in the provision of mortgages as the starting point for its assessment of the relevant product market(s) and has considered whether this definition should be:

(a) Wider to include other banking products, or

(b) Narrower to distinguish between:

(i) Different types of mortgage.

(ii) Different customer groups.

(iii) Different sales channels.

*(a) Should the market be **wider** than the provision of mortgages?*

3.23 The market would be wider than the provision of mortgages if it could be shown that there are demand side substitutes for a mortgage, such that a customer would consider other products to have sufficiently similar functionality to constitute a significant alternative to a mortgage.

3.24 The Commission's view is that other financial products cannot be seen as functional substitutes for a mortgage; a small but significant change in the price of mortgages would not result in customers switching from mortgages to other financial products to fund property purchases, as a mortgage customer would be unlikely to find other sources of funding to be a substitute for a mortgage. This is due to the characteristics of a mortgage as a loan secured on a property, such as the duration and terms and conditions of the loan, compared with alternative sources of funding that are typically shorter term and of smaller value. Therefore, there is not demand-side substitutability between mortgages and other financial products.

3.25 Although other financial products cannot act as a substitute for mortgages, the Commission has considered whether the purchase of a range of financial products from the same provider might suggest that there is a wider market for general financial or banking services. The Commission notes that customers will often seek a basket of financial products from the same provider. This may include a range of products such as current and deposit accounts, mortgages, credit card and insurance products.

3.26 There is considerable cross-selling in the financial sector. Being a customer's main current account provider is often an advantage when seeking to sell other financial products to that customer, including mortgages and deposit accounts. As discussed in Section 2, all of the full service retail banks have mortgage offers that are linked, or could be linked, to other banking products.

3.27 The Commission's view is that while cross-selling between mortgages and other products takes place, particularly where a customer buys a mortgage from a full-service bank, this is not sufficient to suggest a wider product market of a basket of financial services. Customers can and do purchase standalone mortgages, and all providers offer standalone mortgages that are not linked to other financial products. However, the Commission does recognise potential linkages between various financial products falling outside the market for the supply of mortgages.

3.28 The Commission has considered the extent to which a supplier of other financial products would switch to supply mortgages, such that supply-side substitutability would suggest a wider product market. The Commission's view is that a supplier of other financial products would not be able to switch to supply mortgages quickly and at minimal cost. The Commission notes, amongst other factors, high barriers to entry (including regulatory barriers) that would make switching of supply unlikely. The reactions and behaviour of actual and potential competitors will be considered in the analysis of competitive effects in Section 5 rather than as part of the market definition.

3.29 On the basis of the information provided above, the Commission's view is that the relevant product market is not wider than the supply of mortgages. The Commission's view is consistent with the Parties' view and precedent from EU decisional practice discussed above.

*(b) Should the market be **narrower** than the provision of mortgages?*

3.30 The Commission has considered whether the market for the provision of mortgages should be further segmented by:

(a) Different types of mortgage;

(b) Different customer groups; and

(c) Different sales channels.

<u>(a) Different types of mortgage</u>

3.31 In Section 2, the Commission has described the various types of mortgage available in the State.

3.32 In summary, types of mortgage can be categorised as:

(a) Interest only;

(b) Repayment;

(c) Fixed rate;

(d) Variable rate;

(e) Split rate; and,

(f) Cashback.

3.33 In examining types of mortgage available from a demand-side perspective, the Commission's view is that a small but significant change in the price of one type of mortgage could result in customers switching to a different type of mortgage. Where customers switch mortgage, they can and do switch between different types of mortgage.

3.34 The possible exception to this is the case of tracker mortgages. Tracker mortgages are linked to the ECB's interest rate, and as a result, have been historically substantially lower interest rates than other mortgage products. However, tracker mortgages are no longer sold in the State. Customers with a variable or fixed rate mortgage cannot switch to a tracker mortgage. However, tracker mortgage customers can switch to variable or fixed rate mortgage.

3.35 The Commission considers that there is no need to come to a definitive view on whether tracker mortgages belong in the same product market as all other types of mortgage. In any case, the Commission notes that Ulster Bank's tracker mortgages are not included within the Proposed Transaction.

3.36 From a supply-side perspective, all mortgage lenders offer a range of different types of mortgage. The Commission outlined in Section 2 the propensity for some lenders to prioritise certain types of offer. For instance, cashback offers are primarily (but not always) offered by the retail banks and not by non-bank lenders. While some lenders may focus on the provision of one type of mortgage rather than another, there is no evidence that would suggest that particular types of mortgage would constitute separate product markets.

(b) Different customer groups

3.37 The Commission has considered whether the mortgage market should be segmented by type of customer.

3.38 The Commission has considered whether different customer types require different mortgage products, and the extent to which this indicates separate markets defined by customer type. In Section 2, the Commission noted different regulatory requirements that are applied to different types of customer. For example, the level of deposit required differs according to whether the customer is a First Time Buyer, a second or subsequent time buyer, or is purchasing a Buy-to-let mortgage. The Commission also noted in Section 2 that market research findings describe some differences in the characteristics of different types of mortgage seeker which may impact on their choice of mortgage. For instance, there is some evidence that cashback mortgages are particularly popular with First Time Buyers.

3.39 Demand may also differ between business customers acquiring Buy-to-let mortgages in order to offer rental properties as a business, and consumer Buy-to-let mortgages which are aimed at individual consumers. Typically, a business customer seeking funding to offer rental properties as a business would not be likely to find a residential mortgage to be a good substitute because the characteristics, terms and pricing of the loan product would be significantly different. Business Buy-to-let mortgages are generally not available to residential mortgage-seekers. There may be limited substitutability at the margins, if for example a consumer started to acquire mortgages for a number of properties.

3.40 The Commission has considered whether the market should be segmented in terms of new customers (which would correspond to mortgage origination, or the front book) and existing customers (which would correspond to mortgage stock or the back book). The Commission's view is that the products demanded by each type of customer would be similar, and would be unlikely to warrant the finding of separate markets.

3.41 The Commission's view is that there is limited or no demand-side substitutability between customer types. A First Time Buyer clearly cannot switch to become a second time buyer, and a purchaser of an owner-occupier mortgage cannot switch to become a Buy-to-let purchaser.

3.42 However, from a supply-side perspective, the Commission notes that almost all mortgage lenders offer almost all types of mortgage to all types of customer. The exception to this is in the provision of Buy-to-let mortgages to business customers, where the mortgage is sought as an input to a property rental business. The Commission's view is that business Buy-to-let is functionally different to the provision of other types of mortgage and is akin to an investment product. This functional difference on the demand side is also evident on the supply side. A supplier of residential Buy-to-let mortgages would not necessarily be able to switch to supply business Buy-to-let mortgages. This is supported by the presence in the market of specialist providers such as Capitalflow who offer business Buy-to-let mortgages alongside other business lending products, and do not offer mortgages to other customer groups. Amongst other mortgage providers, only those that offer a range of investment products to large corporate clients will offer both business Buy-to-let and consumer Buy-to-let. In the State, mortgage providers offering both business Buy-to-let and residential mortgages are BOI and AIB.

3.43 The Commission's view is that the product market includes the provision of mortgages to all types of customer with the exception of customers purchasing business Buy-to-let mortgages.

(c) Different sales channels

3.44 The Commission has considered whether it is appropriate to segment the mortgage market by distribution channel, particularly in relation to mortgage products which can be sold either directly to customers by retail banks or non-bank providers, or through mortgage brokers or white label offerings.[279] Mortgage brokers typically offer mortgages from a range of providers and offer customers independent advice on suitable mortgages, which is required by law to be impartial. Mortgage brokers may receive commission from mortgage providers for each product sold.

3.45 The Commission's investigation has shown that there is no distinction between the mortgage products available to customers based on the distribution channel used by the customer to secure their mortgage. From a demand side perspective, there are little to no barriers to customers' ability to substitute between mortgage brokers and direct providers when securing a mortgage. Similarly, the distribution channel does not affect the range and cost of products available to customers seeking to secure a mortgage, as the vast majority of products offered directly by retail banks and non-bank providers to customers are also available through mortgage brokers.

3.46 While non-bank mortgage providers access the mortgage market primarily or, in some cases, exclusively through the mortgage broker channel, rather than by directly selling to customers, there is no evidence of a demand-side distinction

[279] White label mortgages are those offered by a mortgage lender using the name and brand of another company.

that supports the assessment of the provision of mortgage products via the broker channel as a distinct customer segment from the provision of mortgage products directly by retail banks and non-bank providers to customers.

3.47 The Commission has also considered whether mortgage lending by bank and non-bank lenders would be likely to constitute separate product markets. For example, the Commission noted in Section 2 that consumer research indicated that some customers would choose to acquire a mortgage only from a bank. The Commission's view is that the mortgage products offered by bank and non-bank lenders are sufficiently similar to suggest that they belong in the same product market. As noted above, bank and non-bank lenders offer a similar range of mortgage products. While bank and non-bank lenders may place a different emphasis on aspects of their offer – for example, offering cashback – the underlying offers are similar. A customer acquiring a mortgage from a bank could readily switch that mortgage to a non-bank lender and, vice versa. The Commission's view is that mortgages provided by bank and non-bank lenders are in the same relevant product market.

3.48 The Commission's view is that there is no need to further segment the market by: type of mortgage; customer group; sales channel; or lender.

Conclusion on a relevant product market for the provision of mortgages

3.49 The Commission's view is that the relevant product market is that for the provision of mortgages to all types of customer (with the exception of customers purchasing business Buy-to-let mortgages), and that there is no reason to find a wider product market, nor to further segment the market. The Commission notes that this is consistent with the Parties' view in the Merger Notification Form.

SME lending in the State

Views of the Commission

3.50 The Commission notes that the Parties have defined SMEs as businesses that have (i) an annual turnover not exceeding €50 million; and/or (ii) an annual balance sheet total not exceeding €43 million. This is aligned with the European

Commission definition of SME.[280] The European Commission further distinguishes microenterprises, which are defined as enterprises which employ fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 2 million.[281]

3.51 The Proposed Transaction is limited to lending to: "*The entire performing micro-SME/business direct ("Business Direct") loan book…*"[282] which the Commission understands means lending to SMEs with an annual turnover of less than €2 million. This is consistent with the Commission's approach in *AIB/UB*, which did not include loans to businesses with an annual turnover of less than €2 million.[283] Therefore, although the Parties define a market for SME lending which would include lending to SMEs with an annual turnover of up to €50 million, those SMEs with a turnover between €2 million and €50 million would form part of the *AIB/UB* transaction, and so would not be included in the Proposed Transaction. The Proposed Transaction is therefore limited to SMEs with a turnover of less than €2 million, which would be those SMEs falling within the European Commission's definition of microenterprises.

3.52 In its Determination of *AIB/UB*, the Commission found that the demand and supply side characteristics of lending to businesses of different size categories differ to such an extent that they may be considered distinct markets.[284] In the *AIB/UB* Determination, the Commission indicated that there are differences in the borrowing needs of businesses dependent on their size. These differences were found in: the general characteristics; customer usage patterns; relative pricing levels between the different lending offerings towards different sizes of business; and the observed set of competitors. These differences are most notable at the very low end of business size, which is analogous to businesses with an annual

[280] https://ec.europa.eu/growth/smes/sme-definition_en

[281] https://ec.europa.eu/growth/smes/sme-definition_en

[282] See para 1(c) of the Merger Notification Form

[283] See Determination in AIB/UB, supra 245.

[284] See Determination in AIB/UB, supra 245.

turnover of less than €2 million (i.e. microenterprises), and the very high end of business size, with an annual turnover greater than €250 million.

3.53 In its market investigation in *AIB/UB*, the Commission found that microenterprises often have banking needs that are more similar to retail customers than larger business customers.[285] In this investigation, the Commission also found that from the lender's perspective, it tends to be less expensive to provide business lending services to microenterprises than to businesses with larger turnovers, but microenterprises consistently pay the highest interest rates of any of the business size groups investigated by the Commission.[286]

3.54 In addition to the pillar banks, microenterprises are served by a different set of lenders that do not target larger businesses, such as the credit unions. The Commission notes that there is some interest from new entrants, who currently have a main focus on personal banking, in expanding into the provision of funding to microenterprises, meaning that barriers to expansion from retail consumer lending into microenterprise lending may be lower compared to lending to larger businesses.[287] In contrast, the Commission has received no evidence of intent of expansion into the provision of lending to microenterprises from lenders which currently target larger businesses.

3.55 In summary, the Commission's view is that demand for lending to microenterprises is distinct from demand for lending to larger businesses, including larger SMEs, and is analogous to the type of demand for consumer retail lending.[288] There are a range of suppliers of lending for businesses with a turnover of less than €2 million. For all of these reasons, the Commission finds that lending to microenterprises constitutes a distinct product market.

[285] See paragraph 3.45 of the Commission's Determination in *AIB/UB*, supra 245.

[286] See paragraph 3.40 of the Commission's Determination in *AIB/UB*, supra 245.

[287] See paragraph 3.41 of the Commission's Determination in *AIB/UB*, supra 245.

[288] Note that businesses with an annual turnover <€2 million meet the EC's definition of microenterprises. https://ec.europa.eu/growth/smes/sme-definition_en

3.56 For the purposes of this Determination, the Commission does not need to come to a definitive view on the precise relevant market since its conclusion on the likely competitive impact of the Proposed Transaction is unaffected by whether the precise relevant product market(s) is defined with reference to microenterprises with a turnover of less than €2 million, or with reference to SMEs with a turnover of less than €50 million.

Relevant Geographic Markets

Views of the Parties

3.57 In the Merger Notification Form, the Parties stated that the markets for the provision of mortgages and the market for SME lending were national in scope.[289]

Views of the Commission

3.58 The Commission's view is that the market for the provision of mortgages and the market for lending to microenterprises are national in scope. The Commission has seen no evidence to suggest that a finding of narrower, subnational markets would be warranted. No mortgage provider or lender has claimed to the Commission that it operates at a regional or sub-national level. The branch networks of pillar banks cover all sections of the State, while mortgage brokers provide widespread geographic access to non-bank lenders. Furthermore, mortgage products and lending products for microenterprises are being increasingly accessed online. Online access is available across all of the State.

3.59 Given differences in competitive conditions between jurisdictions, the Commission considers that a finding of a wider cross-border market would not be appropriate. Providers of mortgages in the State must follow relevant Irish mortgage regulation.[290] This appears to prevent mortgage providers without established Irish operations from selling mortgage products in the State.

Overall conclusion on relevant market definition

[289] See Page 27 of the Merger Notification Form

[290] Such as Macro-prudential Measures, the Code of Conduct on Mortgage Arrears, and S149 of CCA 1995.

3.60 Having regard to the evidence available to it, the Commission considers that the relevant markets for the competitive assessment of the Proposed Transaction are:

(a) The market for the provision of mortgages to all types of customer (with the exception of customers purchasing business Buy-to-let mortgages) in the State; and

(b) The market for lending to microenterprises in the State.

4. RELEVANT COUNTERFACTUAL

Introduction

4.1 Under section 22(3) of the Act, the Commission must consider whether a merger or acquisition gives rise to a substantial lessening of competition ("SLC"). The SLC test requires an assessment of the effects of a merger or acquisition on the state of competition in a relevant market. In assessing the likely effects of a merger on competition, the Commission, as in the present case, typically compares the situation that may be expected to arise following the merger with that which would have prevailed without the merger. The market situation without the merger is often referred to as the "counterfactual".

4.2 The Merger Guidelines state that:

> *"The term 'counterfactual' refers to the state of competition without the merger or acquisition. In other words the "actual" situation is the merger being put into effect and the "counterfactual" is the situation in the absence of the merger being put into effect. The counterfactual provides the reference point, or the point of comparison, for assessing competitive effects arising from a merger."*[291]

4.3 In other words, a counterfactual is a hypothesis as regards the facts by reference to which an alleged effect on competition is to be tested. It involves considering what would have happened if the proposed merger had not taken place.

4.4 Paragraph 1.15 of the Merger Guidelines states the following:

> *"the Commission will expect the merging parties to substantiate any counterfactual they propose with objective evidence supported, where necessary, by independent expert analysis. Such evidence and analysis should obviously be consistent with the parties' own internal pre-merger assessments of the likely counterfactual."*

[291] See paragraph 1.12 of the Merger Guidelines.

4.5 Inevitably there is a degree of uncertainty as regards hypothetical future events, and the Commission will consider all the evidence adduced by the parties in the context of an assessment as to whether there is likely to be an SLC in the future.[292] The Commission must ultimately ask itself whether it is satisfied on the balance of probabilities that there will be an SLC caused by the merger. The Commission is, however, not under an obligation to make findings of fact (whether on the balance of probabilities or otherwise) in respect of each item of evidence. Nor is it obliged to find that any particular potential event is more likely than not to occur before it can take it into account in its overall assessment of the probability of an SLC.

4.6 Paragraph 9.8 of the Commission's Merger Guidelines states: "[i]n particular, documents prepared prior to, or unrelated to, the proposed transaction will provide useful evidence of intentions to exit." This means that the Commission places more weight on documents produced prior to the merger or acquisition (that is, the proposed transaction) being in contemplation. This is because such documents could indicate an intention to exit regardless of any particular asset sale being achieved. However, once the merger or proposed transaction is under contemplation, it becomes very difficult for the Commission to distinguish between an intention to exit in the absence of the merger from an intention to exit due to the merger.

4.7 To establish the relevant counterfactual, it is necessary to: (a) establish the competitive situation that would prevail in the absence of the merger; and (b) distinguish between: (i) merger-specific competitive effects, and (ii) non-merger-specific competitive effects, if any, that would occur irrespective of the merger being put into effect.[293]

4.8 The Commission recognises that competitive conditions can and do change over time and that it is important to take into account the potential for change in the market in order to consider as fully as possible the level and intensity of competition without the merger. It is equally important to distinguish between

[292] See paragraph 1.14 of the Merger Guidelines.

[293] See paragraph 1.13 of the Merger Guidelines.

competitive conditions and other developments that would have happened irrespective of the merger (which should be taken into account as part of any counterfactual analysis) and those which are directly related to or the result of the merger (which are irrelevant to the counterfactual analysis[294]).

4.9 The Commission generally adopts the prevailing conditions of competition as the counterfactual against which it assesses the impact of the merger.[295] However, this may not always be the case, e.g., non-merger specific competitive effects may in some circumstances occur irrespective of the merger or acquisition. One particular example where the pre-merger situation would not be the relevant counterfactual is where the target firm is a 'failing firm'.[296]

4.10 In coming to its view of the appropriate counterfactual in this case, the Commission has fully considered the available evidence and taken into account the Parties' views. It is for the Commission to determine whether a counterfactual is sufficiently realistic to be useful, and to decide how much weight to place on it.

4.11 In coming to its view of the appropriate counterfactual in this case, the Commission has not ignored developments that occurred after the notification of the Proposed Transaction. Rather, post-notification developments that are unrelated to the Proposed Transaction have been taken into account by the Commission in both the merger scenario and the counterfactual. However, post-notification developments that are causally related or attributable to the Proposed Transaction have not been taken into account by the Commission.

4.12 As part of its assessment of the relevant counterfactual in this case, the Commission has assessed:

[294] See, for example, the European Commission's decision in Case M.7278, *General Electric/Alstom*, 8 September 2015, in which the Commission found that "*recent deterioration of Alstom's financial situation in so far as it would not have occurred in the absence of the proposed merger cannot be taken into account*", at section 8.10.3.6, available at https://ec.europa.eu/competition/mergers/cases/decisions/m7278_6808_3.pdf.

[295] See paragraph 1.12 of the Merger Guidelines.

[296] See paragraph 1.14 of the Merger Guidelines.

(a) whether the Target Assets would exit the relevant markets identified in Section 3 in the absence of the Proposed Transaction; and, if so,

(b) whether there is a credible alternative purchaser of some, or all, of the Target Assets which may lead to a less anti-competitive alternative outcome than the Proposed Transaction.

4.13 In this section the Commission sets out its views on (a) and (b) under the following subsections:

(a) The Parties' views on the appropriate counterfactual;

(b) The Commission's assessment of the appropriate counterfactual and, in particular, whether:

(i) the Target Assets would have exited the market in the absence of the Proposed Transaction; and

(ii) there is a credible alternative purchaser of some, or all, of the Target Assets which may lead to a less anti-competitive alternative outcome than the Proposed Transaction in each of the following product and geographic markets:

a. the provision of lending to microenterprises in the State; and,

b. the provision of mortgages of all types of customers (with the exception of customers purchasing business Buy-to-let-mortgage) in the State.

(c) The Commission's conclusion on the appropriate counterfactual.

The Parties' views of the appropriate counterfactual

4.14 The Parties submitted that the appropriate counterfactual for the Proposed Transaction is Ulster Bank's exit from the State, with the Target Assets being either 'run down' in a Wind Down scenario[297] or sold to a purchaser or purchasers other than PTSB.[298]

4.15 The Parties submitted that "*Ulster Bank will exit the Irish market irrespective of the Proposed Transaction: Thus, the Proposed Transaction does not result in an exit of Ulster Bank from the market*".[299] A detailed view of Ulster Bank's timeline of decision-making regarding exiting the State is set out below. The Parties stated that this exit would result in Ulster Bank discontinuing the provision of products and services to mortgage customers, Micro SMEs, Asset Financing customers and Bank Branches in the State, stating the following:

> *"in any counterfactual, the businesses associated with the Target Assets will over time come to be operated by other entities. In particular, the non-tracker performing mortgage book, Business Direct, and asset finance loan business would in due course no longer be serviced by Ulster Bank regardless of whether the Proposed Transaction proceeds."*[300]

4.16 With regard to the Target Assets being 'run down' in a Wind Down scenario or sold off,[301] the Parties submitted that neither of these scenarios would yield a less anti-competitive outcome for competition or consumers. In this regard, the Parties put forward the following key arguments:[302]

(a) Ulster Bank is exiting the State and therefore inevitably going to cease providing services to customers in the State, even in the absence of the Proposed Transaction;[303]

[297] "Wind Down" refers to a Target Asset ceasing to accept or originate new business, and continuing to service its current contracts until they expire, after which they will not be renewed.

[298] See paragraph 162 of the Merger Notification Form.

[299] See paragraph 17 of the Merger Notification Form.

[300] See paragraph 105 of the Merger Notification Form.

[301] See paragraph 162 of the Merger Notification Form.

[302] See paragraph 100 of the Merger Notification Form.

[303] See paragraphs 104-138 of the Merger Notification Form.

(b) The combination of the four elements comprising the Target Assets is unique to the Proposed Transaction with PTSB and will ensure the overall market withdrawal is done in an orderly and considered manner;[304] and,

(c) There is no realistic and credible less anti-competitive alternative possible sale of the Target Assets, either as a whole or individually as part of an alternative transaction.[305]

4.17 With regard to the Target Assets being sold in the absence of the Proposed Transaction, the Parties submitted that the Mortgage Book is deemed [✂].[306] The Parties argued that a "*counterfactual scenario in which [the] asset perimeter would be broken up, would result in a high probability of a worse outcome for competition and customers*".[307]

4.18 The Parties also asserted that a Wind Down scenario would not be as beneficial to customers, staff and stakeholders as the Proposed Transaction. According to the Parties, during the period of time in which the assets would be 'run down', Ulster Bank would not be competing in any of the relevant product or geographic markets. [✂]. Additionally, with regard to the Target Branches:

304 See paragraphs 139-149 of the Merger Notification Form.

305 See paragraphs 150-160 of the Merger Notification Form.

306 See paragraph 161 of the Merger Notification Form.

307 See paragraph 164 of the Merger Notification Form.

*“[✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]
[✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][
✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂].”*[308]

4.19 In summary, the Parties submitted that the relevant counterfactual is that, in the absence of the Proposed Transaction, Ulster Bank would exit the State, ceasing to provide products and services to mortgage customers, microenterprise customers, Asset Financing customers, as well as ceasing to operate Bank Branches, in the State, with the Target Assets being either ‘run down’ in a Wind Down scenario or sold off. The Parties submitted that a less anti-competitive outcome would not arise in either scenario (that is, regardless of whether the Target Assets were ‘run down’ in a Wind Down scenario or sold off).

The Commission’s assessment of the appropriate counterfactual

4.20 The Commission’s assessment of the relevant counterfactual begins by considering whether, absent the Proposed Transaction, Ulster Bank had, or would have, taken concrete steps to cease its operations in the State with respect to the Target Assets. The Commission then considers whether there may be an alternative purchaser for some, or all, of the Target Assets which may lead to a less anti-competitive alternative outcome, relative to the Proposed Transaction, in the relevant product markets discussed in Section 3.

4.21 The Commission notes the Parties’ argument that the Proposed Transaction will allow Ulster Bank to exit the market in an orderly and considered manner, as stated in paragraph 4.16 above. For the purposes of merger review, the Commission analyses the Proposed Transaction based on whether any alternative purchasers of the Target Assets offer a less anti-competitive outcome than the Proposed Transaction. As such, the possibility of the Proposed Transaction potentially giving rise to market exit in an orderly and considered manner is not a relevant test and has not been further considered in this Determination.

[308] See paragraph 147 of the Merger Notification Form.

(a) Ulster Bank's intentions to cease its operations in the State, with respect to the Target Assets, absent the Proposed Transaction

4.22 The Commission has assessed the intentions of Ulster Bank and NatWest with respect to Ulster Bank's operations in the State on the basis of an in-depth analysis of internal documents of Ulster Bank and NatWest, which were produced prior to the Proposed Transaction being in contemplation.

4.23 Information reviewed by the Commission of a meeting held in March 2019 (the "March 2019 Meeting") shows that, since at least 2018, the board of RBS (as NatWest was then known[309]) (the "RBS Board"), was not satisfied with the performance of Ulster Bank in the State and did not think it likely that Ulster Bank could provide their desired level of return. In the March 2019 Meeting, the RBS Board acknowledged that Ulster Bank "*faces challenges in returning above its cost of capital*" and that "[✂]."[310]

4.24 Also, in the March 2019 Meeting, the RBS Board commented that, "*We have considered a wide range of exit options (see Q4);* [✂]." However, the RBS Board further decided that, "*From a risk perspective beginning a wind-down before* [✂][✂][✂][✂][✂][✂][✂][✂][✂] *might be premature and produce unintended consequences*."[311]

4.25 Based on its risk assessment, at the March 2019 Meeting the RBS Board decided [✂]. In the March 2019 Meeting the RBS Board

[309] RBS was renamed as NatWest in 2020.

[310] See page 1 of NatWest internal document [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]. In this context a wind-down refers to the exit of Ulster Bank as a whole without a sale to third parties and not specifically a Wind Down as defined in paragraph 4.14 of this Determination.

[311] See [✂][✂][✂][✂][✂][✂][✂][✂].

decided to continue with a strategy that was started in 2018 following the appointment of a new CEO to Ulster Bank, Jane Howard, whereby the (then) newly appointed chief executive officer of Ulster Bank [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] (the "CEO Strategy").

4.26 The Commission understands that, at the time of the March 2019 Meeting, Ulster Bank [✂].[312]

4.27 According to the minutes of the March 2019 Meeting, the RBS Board requested views on strategic options [✂]. The CEO Strategy was reviewed in a meeting of the NatWest Executive Committee held on [✂][✂][✂][✂][✂][✂][✂][✂][✂].[313]

4.28 At the April 2020 Meeting, the outlook for Ulster Bank's performance in the State remained unchanged. In that meeting, the NatWest Executive Committee resolved that "[✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]*, it is now the right time to re-consider our long-term future in the State."*[314] [✂][✂][✂][✂][✂], the NatWest Executive Committee [✂][✂][✂][✂][✂]decided to commence the review of Ulster Bank's operations in the State. The Commission understands that the NatWest Executive Committee decided to focus on two possible options to facilitate an exit, namely: (1) the wind-down of Ulster Bank and (2) a merger with [✂][✂] with a view to exit over time, either through a sale or initial public offer ("IPO").

4.29 In particular, regarding the wind-down option, the NatWest Executive Committee decided that *"consideration needed to be given to the implication of a wind-down*

[312] See [✂][✂][✂][✂][✂][✂][✂].

[313] See [✂][✂][✂][✂][✂][✂][✂].

[314] See [✂][✂][✂][✂][✂][✂][✂].

from a NWH capital perspective."[315] Regarding the option of a merger with [✂][✂], the NatWest Executive Committee acknowledged that "*improved returns may not be achieved* [✂][✂][✂] *and that more will be determined after engagements with* [✂][✂]*."*[316] In summary, in the [✂][✂][✂] Meeting, the NatWest Executive Committee decided the following:[317]

> *"a) that it was the right time to re-consider the long-term future in [the State];*
>
> *b) to focus on a narrowed scope of inorganic options alongside the "new" status quo (wind-down and [merger] with [✂][✂]) as set out in the paper; and,*
>
> *c) that a further update should be provided in June 2020" ([✂][✂][✂][✂][✂]).*

4.30 The Commission is of the view that the April 2020 Decision crystallised NatWest's long-term intention to cease its operations in the State. This is because, unlike in [✂][✂], where a strategy was pursued to try and stabilise Ulster Bank's long-term position in the State, in April 2020 the NatWest Executive Committee resolved to focus on options that would facilitate the exit of Ulster Bank from the State. This signifies a change in Ulster Bank's long-term strategy in the State.

4.31 The Commission considers that, based on the [✂][✂][✂] Meeting, the NatWest Executive Committee planned to discuss [✂][✂][✂] in June 2020. This discussion happened in meetings held on 10 and 11 June 2020 ("June 2020 Meetings").[318]

4.32 The Commission understands that, in the June 2020 Meetings, the NatWest Executive Committee accepted the financial outlook presented by the Project [✂][✂] team, indicating that Ulster Bank could not produce acceptable returns in

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[315] *ibid*.

[316] *ibid*.

[317] See page 2 of NWH & Sub Groups Board Meeting.

[318] See document [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂].

the State. Specifically, according to the minutes of the June 2020 Meetings, "*Even under assume [sic] materially lower impairments we will not be close to achieving cost of equity returns through the plan period…* [✂]."[319] This led the NatWest Executive Committee to consider the following options for a managed exit: (1) a wind-down of Ulster Bank (termed the 'Gradual Case'); (2) a merger with [✂][✂]; and, (3) a merger with [✂][✂][✂][✂].[320] According to the minutes of the June 2020 Meetings *"the Directors recognised that a wind-down of UBIDAC was likely to be the most favourable"*[321] (the "Withdrawal Decision").[322]

4.33 [✂].

4.34 The Commission has not, at this point, found any evidence or information that Ulster Bank and NatWest implemented further strategies to ensure that Ulster Bank would continue to compete in the State. In the Commission's view, the

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[319] See [✂][✂][✂][✂][✂][✂][✂][✂].

[320] See [✂].

[321] See [✂][✂][✂][✂][✂][✂][✂].

[322] Note that UBIDAC is used in internal documents to refer to Ulster Bank.

minutes of the June 2020 Meetings show that NatWest had decided to consider only options which would eventually lead to Ulster Bank's exit from the State.

4.35 On 18 September 2020, NatWest confirmed to the media that it was carrying out a review of Ulster Bank's operations in the State.[323] An internal Ulster Bank document dated [✂][✂][✂][✂] discusses a number of potential inorganic exit options, including combinations with [✂][✂][✂][✂] and sales to [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂].[324] [✂][✂][✂] are listed as a likely interested party "[✂][✂][✂][✂][✂][✂][✂]" and who are likely to respond to those actions by "[✂] [✂][✂][✂][✂][✂][✂][✂]".[325]

4.36 The Commission understands that, in a meeting held in October 2020, the NatWest Executive Committee, with the [✂][✂][✂][✂][✂], continued to review options [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂].[326]

4.37 In that meeting in October 2020 new additional options for the wind-down of Ulster Bank were discussed, namely: (a) a wind-down with some loan sales up to [✂][✂][✂] to bring capital repatriation forward by 1 year to [✂][✂] (termed the 'Central Case'); and (b) a wind-down with a larger sale of assets up to [✂][✂] to bring capital repatriation forward to [✂][✂] [✂][✂][✂][✂][✂][✂][✂][✂][✂].[327]

4.38 The NatWest Executive Committee also accepted recommendations of the [✂][✂][✂][✂] that sufficient work had been done to make an explicit statement

[323] See article here: https://www.irishtimes.com/business/financial-services/natwest-confirms-review-of-ulster-bank-as-covid-19-bites-1.4358311.

[324] See document [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂].

[325] [✂][✂][✂].

[326] See [✂].

[327] See [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂].

in time for the Q3 2020 results and that work should commence to start engagements with stakeholders, including the Government, regulators, customers, and employees, as part of the [✂] [✂] [✂] [✂] [✂] (the "[✂][✂] 2020 Decision").[328]

4.39 In [✂][✂][✂], NatWest and Ulster Bank continued to assess Ulster Bank's exit options [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]. At this time, it did not conclude that [✂].[329] Another document dated [✂][✂][✂] prepared by [✂][✂][✂][✂] advises that a combination with "[✂] [✂][✂][✂][✂][✂][✂][✂][✂]",[330] but nevertheless advised NatWest and Ulster Bank to "[✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]".[331]

4.40 The Department of Finance stated, in a call with the Commission, that in [✂][✂][✂][✂] Ulster Bank met with the Minister and [✂]. This indicates that in [✂][✂][✂], the intentions regarding exit had not changed and that Ulster Bank and NatWest continued to implement the strategy of the [✂][✂][✂] Decision.

4.41 The Commission is of the view that the board documents of the meetings of the NatWest Executive Committee prior to [✂][✂][✂] demonstrate NatWest and Ulster Bank's intentions to cease Ulster Bank's operations in the State.

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[328] Ibid.

[329] See slide 8 of 2020-09-23 Aslan NWG & NWH Board Paper.

[330] Note that Pegasus is used in internal documents to refer to PTSB.

[331] See slide [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂].

4.42 [✂]. The Commission is not aware of any evidence of a decision or discussions, after the [✂][✂][✂][✂] Meeting, towards sustaining Ulster Bank operation in the State long-term.[332] Instead, in the June 2020 Meetings, the NatWest Executive Committee continued to discuss [✂][✂][✂][✂] for Ulster Bank.

[✂] confirming to the media, in September 2020, that NatWest was carrying out a review of Ulster Bank's operations in the State; [✂].

4.43 In the light of the above, the Commission is of the view that there is sufficient evidence to conclude that Ulster Bank's intention to cease operations in the State is not causally related or attributable to the Proposed Transaction, since the formation of that intention preceded Ulster Bank's contemplation of the Proposed Transaction. Therefore, the Commission is of the view that there is sufficient evidence to show Ulster Bank's intentions to cease its operations in the State, absent the Proposed Transaction.

4.44 The Commission also understands, as detailed in the paragraphs below, that the NatWest Executive Committee took further steps specifically in relation to the Target Assets in the context of its intention to exit the State. The Commission now sets out its assessment of Ulster Bank and NatWest's intention specifically with respect to the Target Assets.

4.45 By [✂][✂][✂][✂][✂] NatWest had resolved to pursue [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂].[333] An internal NatWest document from [✂][✂][✂][✂] proposes in next steps to

[332] See [✂].

[333] See document [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]. MD5 Hash 16dcfa61adf269022b866a91a3fd7f92.

“[✂]… *At that juncture, there will be a decision point around whether to progress in discussions in Phase II to work towards an agreed Memorandum of Understanding*”.[334],[335]

4.46 In the minutes of a meeting held in [✂][✂][✂][✂], the NatWest board considered factors such as [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂] in identifying and evaluating the following potential exit options:[336]

(a) a deposit-led transaction to transfer a large part of the Ulster Bank balance sheet to [✂][✂][✂][✂][✂][✂] [✂];

(b) [✂]); and,

(c) discussions with [✂].

4.47 In this meeting, the NatWest board resolved that, “*We are therefore prioritising the investigation of* [✂]”[337] for the following reasons:

[✂][

[334] See slide 20 in document [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂] dated [✂][✂][✂][✂]. MD5 Hash 84113c837a24929b793b719100a633a9 [✂][✂][✂][✂][✂][✂][✂].

[335] [✂][✂][✂] refers to “[✂]” [✂] [✂] [✂] [✂][✂][✂][✂][✂][✂]).

[336] See page 2 of document [✂]. MD5 Hash 3cd3cb075def4c0263a4aace68663378 (“[✂][✂][✂][✂][✂][✂]”).

[337] See [✂][✂][✂][✂][✂][✂][✂][✂].

✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][
✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][
✂][✂][✂][✂][✂][✂][✂][✂][✂][✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂]
[✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂]
[✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂]
[✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂]
[✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂]
[✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂]
[✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂]
[✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂]
[✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂] [✂].[338]

4.48 This meeting also shows that the NatWest board considered the [✂].[339,340]

4.49 In [✂][✂][✂][✂], the NatWest Executive Committee also resolved to establish the [✂][✂] Executive Steering Group ("[✂][✂] ESG"), a committee of the boards of NatWest Group and NatWest Holdings that had full authority to consider all matters and take all decisions in connection with the [✂][✂][✂][✂] strategy, including, but not limited to, approving any proposed transaction.[341]

[338] See [✂][✂][✂][✂][✂][✂][✂]

[339] See [✂][✂][✂][✂][✂][✂].

[340] 'NWG' refers to NatWest Group. [✂][✂][✂][✂][✂][✂][✂].

[341] See document [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂].

4.50 A letter dated [✂][✂][✂][✂] from the PTSB CEO to [✂][✂][✂] , Head of Corporate Development at NatWest, [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]. The letter stated:

> *"[✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂] [✂]".[342][sic]*

4.51 On 19 February 2021, following completion of its strategic review of Ulster Bank, the NatWest board announced that Ulster Bank in Ireland would not be in a position to deliver an acceptable level of returns, and therefore, NatWest would commence a phased withdrawal of Ulster Bank's banking activities and associated services within the State (the "Withdrawal Announcement").[343] This Withdrawal Announcement was made following approval by the Ulster Bank shareholders of the Withdrawal Decision on 19 February 2021. [344]

4.52 [✂]. A non-binding MOU was announced on 23 July 2021 and a binding agreement was entered into on 17 December 2021.[345]

Conclusion of the Commission's assessment of Ulster Bank's intentions to cease its operations in the State, with respect to the Target Assets, absent the Proposed Transaction

[342] See page 1 of document [✂].

[343] See paragraph 204 of the Merger Notification Form.

[344] See document [✂] dated 19 February 2021. MD5 Hash 17ca0cd8f300fbb73e963dfe75ecb59c.

[345] See paragraph 140 of the Merger Notification Form.

4.53 As stated above in paragraph 4.6, the Commission places more weight on documents produced prior to the Proposed Transaction being in contemplation. The Commission is satisfied that Ulster Bank had taken a concrete decision to exit the State at [✂] [✂] [✂] [✂] [✂] (i.e. the Withdrawal Decision) and that there is sufficient evidence to substantiate that this decision was not causally related or attributable to the Proposed Transaction. The Commission is of the view that this contemplation by NatWest and Ulster Bank would be to [✂]

4.54 Accordingly, the Commission is of the view that the relevant counterfactual is that Ulster Bank would cease its operations in the State in respect of the Target Assets absent the Proposed Transaction.

4.55 In the following section, the Commission sets out its assessment of whether the Target Assets could have been sold to a potentially less anti-competitive alternative purchaser.

(b) Is there is a credible alternative purchaser of some, or all, of the Target Assets which may lead to a less anti-competitive alternative outcome than the Proposed Transaction in each of the identified product markets?

4.56 In general terms, when considering if there were alternative less anti-competitive purchasers, the Commission seeks to identify who the alternative purchaser(s) might have been and takes this into account when determining the counterfactual. The Commission does not restrict its analysis to alternative purchasers who were willing to pay the same or similar price that was agreed in the merger, but rather if there was an alternative purchaser willing to acquire the firm at any price above liquidation value.

4.57 The Commission considered three types of alternative buyers:

(a) Another pillar bank (i.e., AIB or BOI);

(b) A credit serving firm (i.e., a firm that does not provide lending but manages book for yield), which would not contribute to new mortgage origination or SME lending in the State or exert a competitive constraint on other players in those markets; and,

(c) Non-bank lenders, including those currently or potentially active in the relevant market.

4.58 As stated by the Parties in the Merger Notification Form, and as seen by the Commission in internal Ulster Bank documents [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂] as potential alternative purchasers of the Target Assets. However, the Parties argued that an acquisition of the Target Assets by either of [✂][✂][✂] would yield a less favourable competitive outcome, stating the following:

> *"[✂]."*[346]

4.59 [✂]. An acquisition of the Target Assets by [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]. As such, the Commission considers that it is possible that a sale of the Target Assets to [✂]. Therefore, it would be inappropriate for the Commission to adopt a sale of the Target Assets to [✂][✂][✂] as the most likely counterfactual in the absence of the Proposed Transaction.

[346] See paragraph 98 of the Merger Notification Form.

4.60 Similarly, [✂][✂][✂][✂][✂][✂] contacted Ulster Bank in relation to a potential acquisition of the Target Assets.[347] With regard to the Mortgage Book and Microenterprise Business Direct Loan Book, [✂].[348] In this way, the Commission considers that such a sale is likely to have the same effect as a Wind-Down by Ulster Bank as, in both situations, Ulster Bank would cease to provide mortgage products and lending to microenterprises in the State, with no existing or new competitors in either relevant market being created or substantially strengthened. As such, the Commission considers that it is possible that a sale of the Target Assets to [✂][✂][✂][✂][✂] would raise competition concerns similar to, or greater than, those that may arise in relation to the Proposed Transaction. Therefore, it would be inappropriate for the Commission to adopt a sale of the Target Assets to [✂][✂][✂][✂][✂] as the most likely counterfactual in the absence of the Proposed Transaction.

4.61 In the next section, the Commission sets out its analysis of potential alternative less anti-competitive purchasers for the Target Assets in relation to each of the identified potentially relevant markets identified in section 3.

An alternative purchaser which may lead to a less anti-competitive alternative outcome than the Proposed Transaction in the provision of lending to microenterprises in the State

4.62 NatWest and Ulster Bank submitted that the relevant counterfactual for the Microenterprise Business Direct Loan Book is a Wind-Down, stating that the book would be "[✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]" in the absence of the Proposed Transaction.[349]

[347] Such as [✂].

[348] See paragraph 153 of the Merger Notification Form.

[349] See paragraph 157 of the Merger Notification Form.

4.63 The Commission engaged with one potential alternative purchaser of Ulster Bank's microenterprise lending business during its investigation of the Proposed Transaction – [✂][✂][✂]. In this engagement, [✂][✂][✂] informed the Commission that it would be interested in acquiring some or all of Ulster Bank's microenterprise lending assets. No other firm contacted by the Commission during its review of the Proposed Transaction demonstrated any serious interest in acquiring these assets.

4.64 The Commission considers that, in the absence of the Proposed Transaction, there are credible potential purchasers of Ulster Bank's whole Microenterprise Business Direct Loan Book, and that NatWest and Ulster Bank would have had an incentive to sell these loans to an alternative purchaser. The Commission is, therefore, of the view that the counterfactual for Ulster Bank's lending to microenterprises is the sale to a potentially less anti-competitive purchaser.

An alternative purchaser which may lead to a less anti-competitive alternative outcome than the Proposed Transaction in the provision of mortgages to all types of customer (with the exception of customers purchasing business Buy-to-let mortgages) in the State

4.65 According to the Parties, as stated in the Merger Notification Form, absent the Proposed Transaction, Ulster Bank would still exit the State, thereby ceasing its provision of mortgages in the State, and NatWest would [✂][
✂][✂][✂][✂][✂][✂][✂]. As the Parties state in the Merger Notification Form:

> *“[✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]
> [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][
> ✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][
> ✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][
> ✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][
> ✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][*

✂][✂]”.[350]

4.66 Internal documents submitted to the Commission show that NatWest [✂].[351]

4.67 The Commission's engagement with multiple potential purchasers, and the assessment of the information and evidence provided by those third Parties and the Parties, indicates that potential alternative purchasers of some of the Target Assets could be identified.

4.68 However, it is likely that the appetite and interest of a potential alternative purchaser would be limited to a proportion of the portfolio of the Mortgage Book. No firm contacted by the Commission expressed serious interest in acquiring all of the Mortgage Book. The highest figure identified to the Commission was around [✂][✂].

4.69 In particular, in their engagement with the Commission throughout the course of its review of the Proposed Transaction, [✂][✂][✂][✂][✂] have repeatedly expressed their interest in acquiring a portfolio of the Mortgage Book.

4.70 The Commission notes that the selling of a proportion of the Mortgage Book to a potential new entrant, e.g., [✂][✂], is likely to be more competitive than the selling of a proportion of the Mortgage Book to an existing competitor. The Commission has therefore taken a conservative approach and adopted the view that the counterfactual for Ulster Bank's mortgage lending is the sale of a proportion of the Mortgage Book to a new entrant.[352]

[350] See paragraph 153 of the Merger Notification Form.

[351] See document [✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂][✂]. MD5 Hash 2a386ce066eb903923334f5ccc1fd46a. ('Caspian Inbound').

[352] If the Commission's analysis showed no SLC when adopting this conservative counterfactual, then the use of a less conservative counterfactual, such as the sale to an existing competitor with a small share, should also show no SLC.

The Commission's conclusion on the appropriate counterfactual

4.71 On the basis of the above, the Commission considers that the Parties have substantiated their submission with supporting evidence which pre-dates the Proposed Transaction that, absent the Proposed Transaction, Ulster Bank would have exited the State.

4.72 The Commission considers that there were alternative (and potentially less anti-competitive) purchasers in respect of Ulster Bank's performing mortgage book and book of lending to microenterprises.

4.73 Therefore, the Commission has reached the view that the appropriate counterfactual is that, absent the Proposed Transaction, Ulster Bank would have exited the State and that it would have proceeded with: (i) a sale to a potentially less anti-competitive alternative purchaser of its whole book of lending to microenterprises; and (ii) a sale to a potentially less anti-competitive alternative purchaser of a proportion of the Mortgage Book.

5. COMPETITIVE EFFECTS – UNILATERAL EFFECTS

Introduction

5.1 In this section, the Commission sets out its analysis of the likelihood of unilateral effects arising from the implementation of the Proposed Transaction in: (i) the market for lending to microenterprises in the State; and, (ii) the market for the provision of mortgages in the State.

5.2 As set out in paragraph 4.73, the Commission considers the appropriate counterfactual to be that, absent the Proposed Transaction, Ulster Bank would have exited the State and that it would have proceeded with a sale to an alternative purchaser in respect of: (i) its microenterprise lending assets; and (ii) a proportion of the Mortgage Book. Therefore, this section assesses the competitive effects of the Proposed Transaction compared to this counterfactual.

The Likelihood of Unilateral Effects

5.3 The Commission's competitive assessment can be broadly categorised as a unilateral effects assessment. Unilateral effects, as explained in paragraph 4.8 of the Commission's Merger Guidelines, occur when "*a merger results in the merged entity having the ability and the incentive to raise prices at its own initiative and without coordinating with its* competitors."

5.4 In addition, the EC Horizontal Merger Guidelines state the following in respect of "Non-coordinated effects":

> *"A merger may significantly impede effective competition in a market by removing important competitive constraints on one or more sellers, who consequently have increased market power. The most direct effect of the merger will be the loss of competition between the merging firms. For example, if prior to the merger one of the merging firms had raised its price, it would have lost some sales to the other merging firm. The merger removes this particular constraint. Non-merging firms in the same market can also benefit from the reduction of competitive pressure that results*

from the merger, since the merging firms' price increase may switch some demand to the rival firms, which, in turn, may find it profitable to increase their prices. The reduction in these competitive constraints could lead to significant price increases in the relevant market.

[…]

A number of factors, which taken separately are not necessarily decisive, may influence whether significant non-coordinated effects are likely to result from a merger. Not all of these factors need to be present for such effects to be likely".[353]

5.5 In this regard, the Commission has assessed whether the Proposed Transaction would result in unilateral effects because the Proposed Transaction will likely result in an increase in prices, a loss of service quality and/or a loss in innovation.

How the Commission considers KBC in its competitive assessment of the Proposed Transaction

5.6 As noted in Section 2 above, on 16 April 2021 KBC and BOI announced that they had entered into a memorandum of understanding whereby BOI would acquire substantially all of KBC's performing assets and liabilities. As a consequence of this, KBC would exit the State. On 22 October 2021, KBC and BOI entered into a binding agreement in this regard.

5.7 This transaction was notified to the Commission as BOI/KBC[354] on 16 April 2021. On 23 May 2022, having taken into account proposals made by BOI in accordance with section 20(3) of the Act, and in light of those proposals (which form part of the basis of its determination), the Commission determined under section 22(3)(a) of the Act that this transaction could be put into effect.[355]

[353] See paragraphs 24, 25, and 26 of the European Commission's Horizontal Merger Guidelines, available here.

[354] See https://www.ccpc.ie/business/mergers-acquisitions/merger-notifications/m-21-021-bank-of-ireland-certain-assets-of-kbc/

[355] See the Commission's Determination in *BOI/KBC,* supra 114.

5.8 On 31 May 2022, KBC announced the following:[356]

> *"We are now providing notice that after 15 July 2022 we will no longer be accepting new applications for all KBCI products including Current Accounts, Mortgages, Personal Deposits, Personal Loans, Home, Car and Life Insurance and Personal Credit Cards."*

5.9 On 15 July 2022, this came into effect and, since that date, KBC no longer accepts new applications for any KBC products. The Commission therefore considers that other mortgage providers no longer have to consider the risk that customers choose KBC over them, or that their customers may switch to KBC. This is particularly important given the role of switching as a competitive constraint in the market for the provision of mortgages in the State. On this basis, the Commission considers that KBC is no longer active in the mortgage market in the State and no longer poses any competitive constraint on other providers in this market.

5.10 The transaction between KBC and BOI is, as of the date of this determination, still subject to Ministerial approval.[357] Therefore, KBC's mortgage assets have not, as of the date of this determination, been transferred to BOI. Nonetheless, for the purposes of this determination, the Commission will treat KBC's stock of existing mortgages as having been acquired by BOI.

Assessment of Unilateral Effects

5.11 In this section, the Commission sets out its analysis of unilateral effects arising from the implementation of the Proposed Transaction in each of the markets defined in Section 3, namely:

A. the market for lending to microenterprises in the State; and,

B. the market for the provision of mortgages in the State.

[356] See *Latest News Updated 31st May 2022 - Updates For Our Customers,* which is available at: https://www.kbc.ie/important-update-from-kbc-bank-ireland

[357] That transaction is to be effected using the statutory transfer mechanism available for the transfer of a banking business under Part III of the Central Bank Act 1971 and a transfer order issued by the Minister for Finance.

(A) The market for lending to microenterprises in the State

Views of the Parties

5.12 In the Merger Notification Form, the Parties argued that the Proposed Transaction will not give rise to a substantial lessening of competition in the market for lending to microenterprises in the State for two reasons:

(a) Following the Proposed Transaction, PTSB will have a *de minimis* increase in market share; and,

(b) PTSB will continue to be constrained by other competitors in this market.[358]

The impact of the Proposed Transaction on market structure and concentration

5.13 Table 2 below sets out market shares and an HHI delta, based on information provided by the Parties.

Table 2: SME lending market structure, 2020[359]

	PTSB	Alternative Provider	Others[360]	HHI[361] delta
Counterfactual	[0-5]%	[0-5]%	[95-100]%	/
Post-Proposed Transaction	[0-5]%	[0-5]%	[95-100]%	[0-100]

[358] See paragraphs 332 to 336 of the Merger Notification Form.

[359] The market shares provided by the Parties are for lending to SMEs with a turnover of up to €50 million. The Commission has not seen evidence suggesting that the share of lending to microenterprises with a turnover less than €2 million would be significantly different.

[360] Including AIB and BOI.

[361] The Herfindahl-Hirschman Index, or "HHI", is a measure of market concentration that takes account of the differences in sizes of firms in the market. It is calculated by summing the squares of the shares of each firm in the market. The purpose of HHI is described in paragraph 16 of the European Commission's Horizontal Merger Guidelines (available here) as follows: "*The HHI gives proportionately greater weight to the market shares of the larger firms. Although it is best to include all firms in the calculation, lack of information about very small firms may not be important because such firms do not affect the HHI significantly. While the absolute level of the HHI can give an initial indication of the competitive pressure in the market post-merger, the change in the HHI (known as the 'delta') is a useful proxy for the change in concentration directly brought about by the merger*".

Source: The Commission, based on information provided by the Parties.

5.14 The Commission's investigation confirmed that these share estimates are an accurate representation of the market structure of that market, and that, based on the Commission's market enquiries, there appears to be many other competitors active in this market in the State such as BOI, AIB, Capital Flow, GRID Finance, and Finance Ireland. PTSB currently has a minimal share of this market, with its share rising from [0-5]% to [0-5]% following implementation of the Proposed Transaction.

5.15 Paragraphs 3.9 to 3.10 of the Commission's Merger Guidelines set out that the Commission utilises the Herfindahl-Hirschman Index ("HHI") as a measure of market concentration. The Commission's Merger Guidelines state that the Commission will have regard to the following HHI thresholds:

> *"A post-merger HHI below 1,000 is unlikely to cause concern.*
>
> *Any market with a post-merger HHI greater than 1,000 may be regarded as concentrated and highly concentrated if greater than 2,000.*
>
> *Except as noted below, in a concentrated market a delta of less than 250 is unlikely to cause concern and in a highly concentrated market a delta of less than 150 is unlikely to cause concern."*

5.16 The Commission notes that the HHI delta arising from the Proposed Transaction of [0-100] is far below the level of 150 set out in the Merger Guidelines for a concentrated market, and as such is unlikely to raise concern.[362]

5.17 Furthermore, there will remain a number of competing firms active in the microenterprise lending market, including banks such as AIB and BOI, and non-bank lenders such as Finance Ireland and Capital Flow and others (a CBI report

[362] The Commission recognises that this HHI calculation assumes that the alternative provider has zero market share. GRID Finance, who expressed an interest in purchasing the lending assets, already offers microenterprise lending in the State. The Commission does not have reliable market share data for GRID Finance. However, the Commission has seen no evidence to suggest that the share of GRID Finance is such that it would lead to an HHI delta greater than 150.

estimated that there were 63 non-bank lenders lending to Irish SMEs in 2019 and 2020[363]).

Conclusion on the market for lending to microenterprises

5.18 In the light of the assessment set out above, the Commission considers that the Proposed Transaction will not lead to a substantial lessening of competition in the market for lending to microenterprises in the State.

(B) The market for the provision of mortgages in the State

Views of the parties

5.19 In the Merger Notification Form, the Parties argued that the Proposed Transaction will not give rise to an SLC in the market for the provision of mortgage products in the State for eight key reasons:[364]

(a) PTSB will receive a limited increase in mortgage stock after the Proposed Transaction;

(b) PTSB will receive a limited increase in mortgage flow after the Proposed Transaction;

(c) PTSB will continue to face strong competition from existing mortgage lenders;

(d) The Parties are not each other's closest competitors and Ulster Bank is not a maverick;

(e) The Proposed Transaction will allow PTSB to compete more aggressively and effectively in the mortgage market;

(f) The Irish mortgage market is dynamic with new emerging lending models;

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[363] See: *The role of non-bank lenders in financing Irish SMEs*, *Central Bank of Ireland*, which is available at: https://www.centralbank.ie/statistics/statistical-publications/behind-the-data/the-role-of-non-bank-lenders-in-financing-irish-smes. While lending to microenterprises is a subset of lending to all SMEs, this may indicate that the market for lending to microenterprises comprises a large number of firms.

[364] See paragraph 166 of the Merger Notification Form.

(g) Switching in the mortgage market is becoming more common; and,

(h) There are relatively low and decreasing barriers to entry and expansion for non-bank lenders in the mortgage market.

The impact of the Proposed Transaction on market structure and concentration

Market structure and concentration

5.20 Paragraph 3.1 of the Commission's Merger Guidelines states that "*A central element in assessing the competitive impact of a merger is identifying its effect on market structure*." Market structure can be characterised by the number, size and distribution of firms in a market. A merger or acquisition will have an impact on market structure as the merging parties which were two firms pre-acquisition become one firm post-acquisition.

5.21 The Commission has used two ways to measure the structure of the market. Mortgage 'stock' measures the number of existing mortgage customers of each provider. Mortgage 'flow'[365], on the other hand, measures new business acquisition by mortgage providers. Mortgage stocks and mortgage flows are not different markets. They are different ways of measuring the same market. Today's mortgage flow is tomorrow's mortgage stock. Mortgages are not inert financial assets but rather active consumer contracts and so these two aspects are intrinsically linked. With this in mind, the Commission has measured the HHI in terms of both mortgage stocks and mortgage origination/mortgage flow.

Mortgage stock

5.22 The Commission has considered the impact of the Proposed Transaction compared to a counterfactual of the acquisition of a portfolio of €1 billion of mortgages, a proportion of the Mortgage Book, by a new entrant. This is set out in Table 3 below.

Table 3: *Market structure (stock), acquisition by new entrant, H2 2021*[366]

[365] In this determination, the Commission uses the terms *"mortgage flow"* and *"mortgage origination"* interchangeably.

[366] KBC's share of stock has been assigned to BOI in light of the Commission's decision to clear *BOI/KBC* with commitments.

	AIB	BOI	PTSB	UB	Dilosk	Finance Ireland	Avant	New entrant	HHI
Proposed Transaction	[30-35]%	[35-40]%	[20-25]%	0	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[3200-3300]
Acquisition by new entrant	[30-35]%	[35-40]%	[20-25]%	0	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[3100-3200]

Source: The Commission, based on information provided by the Parties and third parties active in the mortgage market

5.23 As is clear from Table 3, there is minimal difference between the Proposed Transaction and the counterfactual, with an HHI delta of [0-100]. The Commission notes that the HHI delta arising from the Proposed Transaction of [0-100] is below the level of 150 set out in the Merger Guidelines and such is unlikely to cause concern.

<u>Mortgage flow</u>

5.24 Solely for the purposes of this determination, the Commission has adopted the following assumptions regarding the potential share that could be obtained by a new entrant purchasing a proportion of the Mortgage Book.

- First, MoCo provided the Commission with projections of its share of mortgage flow in the State following their entry. MoCo estimated a share of [0-5]% in its first year[367]. The Commission has assumed that a new entrant would obtain a share of [0-5]%, in line with the MoCo forecasts.

- Second, in MoCo's view, [✂]. The Commission has assumed that the acquisition of 1.2 percentage points of

[367] At the time of writing this Determination MoCo had not yet started selling mortgages.

Mortgage Book could further increase MoCo's share of mortgage flow from [0-5]% to [0-5]%.

- Third, that the MoCo share of [0-5]% reduces other suppliers' share of flow pro-rata.

- Fourth, the implicit assumption that the new entrant only enters mortgage lending if it purchases a proportion of the Mortgage Book.

5.25 In the Commission's view the assumptions adopted for the purposes of this Determination are a conservative approach to estimating the potential impact of the Proposed Transaction. This is because these assumptions are, when combined, likely to lead to an overestimate of the projected market share of the new entrant and therefore an overestimate of the difference between the Proposed Transaction and the counterfactual.[368]

Table 4: Market structure (flow), 2021 H2

	AIB	BOI	PTSB	Dilosk	Finance Ireland	Avant Money	MoCo	HHI
Proposed Transaction	[35-40]%	[25-30]%	[20-25]%	[5-10]%	[5-10]%	[5-10]%	[0-5]%	[2400-2500]
Counterfactual	[30-35]%	[25-30]%	[20-25]%	[5-10]%	[5-10]%	[5-10]%	[0-5]%	[2300-2400]

Source: The Commission, based on information provided by the Parties, and other mortgage providers active in the market to the BPFI.

As seen in Table 4, the HHI delta arising from these assumptions is [100-200]. The Commission notes that the HHI delta arising from the Proposed Transaction of [100-200] is below the level of 150 set out in the Merger Guidelines and such is unlikely to cause concern. Furthermore, this HHI delta is based on a conservative

[368] For example, assuming that the new entrant will only enter if it purchases the €1bn of assets is a conservative approach. Furthermore, it is unlikely that purchasing 1.2 percentage points of mortgage stock leads to an increase of 1.2 percentage points in mortgage flow. The additional mortgage stock could provide the entrant with increased economies of scale, but this is unlikely to translate into a 1.2 percentage point increase in flow.

approach to estimating the difference between the Proposed Transaction and the counterfactual.

Direct effects of the Proposed Transaction on Ulster Bank customers

Third Party submissions received by the Commission

5.26 As noted in paragraphs 1.21 and 1.31, the Commission received 6 complaints from third parties over the course of its review of the Proposed Transaction. These submissions expressed concerns about potential adverse effects of the Proposed Transaction on Ulster Bank mortgage customers.

5.27 Four of the submissions were made by Ulster Bank mortgage customers. They detailed the following concerns:[369]

(a) Transferring Customers[370] will be treated as existing customers of PTSB rather than new customers, which may limit the options available to those customers;

(b) Mortgage interest rates offered by PTSB are not as competitive as those offered by Ulster Bank;

(c) Ulster Bank customers would be charged a breakage free for switching their mortgage away from Ulster Bank before the expiry of their fixed term in order to avoid their mortgage being transferred to PTSB; and,

(d) Transferring Customers who can currently overpay their mortgage by 10% of the outstanding balance per annum without penalty may no longer have this facility following transfer to PTSB, and resulting in an increase in the lifetime cost of their mortgage.

5.28 The Commission also received a third-party submission from founder of the consumer information website askaboutmoney.ie, Brendan Burgess. This

[369] See complaints from Complainant 1, Complainant 2, Complainant 3 and Complainant 4.

[370] 'Transferring Customers' refers to those Ulster Bank customers who will be transferred to PTSB upon implementation of the Proposed Transaction.

submission raised concerns that PTSB is not as customer friendly as Ulster Bank.[371] It recommends that to protect Transferring Customers, PTSB should cease its current price discrimination between its new and existing mortgage customers, discontinue offering cash back, cover the switching fees of those Transferring Customers who seek to switch their mortgage away from PTSB, treat Transferring Customers as new rather than existing business, and that a new unit be set up within PTSB to deal specifically with Ulster Bank customers.[372]

5.29 The Commission fully considered the concerns raised in submissions made to it during its review of the Proposed Transaction.

5.30 The Commission raised the concerns contained in third party submissions with the Parties. On 28 June 2022, PTSB responded to the concerns expressed in the third party submissions in writing.

5.31 The Commission further engaged with the Parties in respect of the concerns raised in third party submissions. The Commission sought, and received, information from PTSB regarding how it intends to address the concerns set out in third party submissions made to the Commission.

5.32 In particular, PTSB submitted the following to the Commission:

(a) First, PTSB will uphold the contractual obligations, terms, and conditions set out in the mortgage contracts; and has specific obligations under the MSDs between it and Ulster Bank.

(i) In particular, this means that the 10% overpayment facility referred to in paragraph 5.26(d) above will be retained

(ii) PTSB has also committed to maintain certain discounts available to Transferring customers – namely the 'Ulster Bank Loyalty'; 'UFirst'; and, 'Ulster Bank Staff Rate' discounts.

[371] See complaint from Brendan Burgess.

[372] Ibid.

(b) Second, PTSB currently offers the same fixed rates to new and existing mortgage customers for mortgages not exceeding €250,000. [✂].

(c) Third, PTSB's interest rate offerings are, for certain products, lower than Ulster Banks. PTSB also noted that former Ulster Bank customers would be free to switch to another mortgage provider following their transfer to PTSB should they wish to do so.

Conclusion on the market for the provision of mortgages in the State

5.33 In light of the evidence available to it and its assessment set out above, the Commission considers that the Proposed Transaction will not lead to a substantial lessening of competition in the market for the provision of mortgages in the State.

Conclusion on unilateral effects

5.34 In light of its analysis as set out in this Determination, the Commission has determined that the Proposed Transaction will not substantially lessen competition in any market for goods or services in the State.

5.35 The views set out by the Commission upon reaching its determination in AIB/UB[373] remain relevant. International evidence shows that higher concentration in business banking services is likely to have a detrimental effect on competition, leading to poorer outcomes for business borrowers in terms of pricing, innovation and service.

5.36 However, Ulster Bank had decided to exit the markets under consideration before it embarked on the Proposed Transaction.[374] The exit of Ulster Bank will lead to a high level of concentration in the markets in which it currently competes, and the Commission is concerned that there will not be sufficient competition following

[373] See Determination in AIB/UB, supra 245.

[374] See Chapter 4.

Ulster Bank's exit. This concern arises whatever the mechanism for Ulster Bank's exit; it is not a consequence of the fact that the exit will be achieved by means of the Proposed Transaction.

5.37 The Commission's assessment of the Proposed Transaction is based on the difference in competitive conditions arising following the Proposed Transaction as compared with the competitive conditions that would arise absent the Proposed Transaction. The Commission has concluded, based on the evidence available to it, that the relevant counterfactual for the assessment of the Proposed Transaction is that, absent the Proposed Transaction, Ulster Bank would in any event have exited the market. Both scenarios therefore involve the exit of Ulster Bank from the State.

5.38 In both scenarios, the competition from Ulster Bank is lost. Both scenarios involve a high level of concentration in the relevant markets. And both scenarios raise serious concerns about the adequacy of competition in these markets. However, there is no appreciable difference in competitive conditions between the two scenarios. Hence, the Commission has concluded that the exit of Ulster Bank by means of the Proposed Transaction will not result in a substantial lessening of competition, when compared with the alternative of an exit of Ulster Bank by winding down its services or selling its assets, or a proportion of those assets, to an alternative purchaser. This conclusion does not diminish in any way the high level of concern that the Commission has about the inadequacy of competition that will arise following the exit of Ulster Bank.

6. COMPETITIVE EFFECTS – COORDINATED EFFECTS

6.1 Coordinated effects can occur where a proposed transaction changes the nature of competition in the relevant market by making it more likely that the merged entity and some or all of its competitors will coordinate their behaviour by, for example, raising prices and/or decreasing output. Thus, the key question is whether a proposed transaction would materially increase the likelihood that firms in the markets for: (i) lending to microenterprises in the State; and (ii) the provision of mortgages to all types of customer (with the exception of customers purchasing business Buy-to-let mortgages) in the State, would successfully coordinate their behaviour or would strengthen existing coordination between firms in this market.

6.2 On the basis of the information in the possession of the Commission in its review of the Proposed Transaction, no plausible coordinated effects theory of harm was identified given the relevant counterfactual. Therefore, no further discussion of coordinated effects is carried out for the purposes of assessing the likely effects of the Proposed Transaction in the identified relevant markets.

7. VERTICAL RELATIONSHIP

7.1 The Parties have stated in the notification that there is no vertical relationship between PTSB and Ulster Bank. The Commission has not identified any vertical relationship between the Parties. On this basis, the Commission considers that the Proposed Transaction does not raise any vertical competition concerns in the State.

8. EFFICIENCIES

8.1 Paragraphs 8.1 and 8.2 of the Commission's Merger Guidelines state that:

> *"A merger may generate various efficiencies for the merged entity. The Commission's analysis of efficiencies goes beyond the impact of efficiencies on the merged entity and focuses on whether verifiable efficiencies mitigate adverse competitive effects and prevent an SLC".*
>
> *"The onus rests on the parties to show that claimed efficiencies are (i) merger-specific, (ii) verifiable and (iii) benefit consumers sufficiently to prevent an SLC".*

8.2 The Commission has not received any submission from the Parties on efficiencies which meets the criteria set out in paragraph 8.2 of the Commission's Merger Guidelines.

9. CONCLUSION

9.1 In light of the information and evidence available to it and in light of its analysis as set out in this Determination, the Commission has formed the view that the Proposed Transaction, will not substantially lessen competition in any market for goods or services in the State.

9.2 Before making a determination in this matter, the Commission, in accordance with section 22(8) of the Act, has had regard to any relevant international obligations of the State, and concluded that there were none.

10. ANCILLARY RESTRAINTS

10.1 No ancillary restraints were notified.

11. DETERMINATION

The Competition and Consumer Protection Commission, in accordance with section 22(3)(a) of the Competition Act 2002, as amended, (the “Act”) has determined that the result of the proposed acquisition, whereby Permanent TSB plc would acquire certain assets, consisting of the entire Ulster Bank Ireland DAC (“Ulster Bank”) performing non-tracker mortgage book (including undrawn facilities), non-performing loans within Ulster Bank’s non-tracker mortgage book, the entire performing micro-SME/ business direct loan book, 25 properties and Ulster Bank’s entire asset finance business, will not be to substantially lessen competition in any market for goods or services in the State and, accordingly, that the acquisition may be put into effect. Before making a determination in this matter, the Commission, in accordance with section 22(8) of the Act, had regard to any relevant international obligations of the State, and concluded that there were none.

For the Competition and Consumer Protection Commission

Jeremy Godfrey
Chairperson
Competition and Consumer Protection Commission

CCPC

Coimisiún um Iomaíocht agus Cosaint Tomhaltóirí

Competition and Consumer Protection Commission