COMPETITION ENFORCEMENT AND ADVOCACY IN THE FINANCIAL SECTOR IN SPAIN*

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The CNMC is responsible for enforcing the competition law in all sectors of the Spanish economy, the financial sector included. In fact, the CNMC's Action Plan for 2018 contains a special reference to the financial sector as a specific sector of interest from the dual competition perspective, antitrust enforcement and competition advocacy.

The relevance of the financial sector is more qualitative that quantitative[1]. Payments, credit and insurance services are inputs for other sectors of the economy, especially important for innovative SMEs. It is the "life blood" of any economy. An efficient financial sector is key to provide access to quality and affordable financing for other sectors to develop and grow. This is key for the productivity and competitiveness of the economy.

The competition authorities' interest on this sector is also due to other factors. The financial sector is an industry with several market failures: information asymmetries, externalities, economies of scale and scope, network and learning effects, creating systemic risks. To correct these market failures and improve consumer's welfare, some public intervention is necessary, in particular through regulation. Additionally, the relevance of the financial sector as an input for the rest of the economy brings stability aspects in question. Regulation can also reduce stability concerns. In any case, as some experts

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1 The financial sector represents 4% of Spanish GDP (this share has reduced with the crisis, as it was 6% before). It is a 5% of EU GDP.

have stated as well, those regulations have to take into account the intensity of competition. Because competition, as in any other sector, can have a positive impact on efficiency and even on stability in the financial sector.

Over the last 10 years, since the beginning of the crisis until now, market concentration increased sharply in the financial sector in Spain, specifically in the banking sector. The number of banks and saving entities has clearly reduced between 2008 and 2018 and this market concentration process during the crisis and after has been more intense in Spain than in the rest of the EU. In terms of the European Central Bank figures[2], the share in total assets of the 5 bigger banks increased from 42% in 2008 to 63.7% in 2017 (higher than Italy –43%–, France –45%– or Germany –30%–). CNMC's analysis show that, in Spain, in terms of credits and deposits, this share could be higher and close to 80% in some local markets.

This concentration process has been due on one hand, as it has happened historically, to the financial restructuring due to and during the crisis and after. On the other hand, there are as well other structural factors with an incidence on the restructuring process. Concentration is also the response to an already mature business, to enormous regulatory requests to enter the activity and provide services and to competition from new non-traditional incomers that do not need physical presence.

It is interesting to follow all this restructuring process through the competition merger control. Mergers in the financial sector over the last 5 years (for some experts, the last 3rd wave of mergers that started in 2014) attains around 7% of total mergers cleared under merger control in Spain[3]. The competition analysis has been very detailed, separating banking from insurance sectors and analyzing quite a number of markets in each sector. In banking for instance, following the national and EU precedents, retail (credit, deposit and branches), corporate, investment banking and factoring markets

2 *Structural Indicators for the EU Banking Sector*, European Central Bank.

3 For example, in the insurance sector: C/0647/15, *Segurcaixa Adeslas/Sociedad de Profesionales/Igualatorio de Asturias*; C/0861/17, *Santa Lucía/Unicaja Banco/Aviva Vida/Unicorp Vida/Caja España Vida*; C/0928/18, *Grupo Catalana Occidente/Sociedades Adquiridas*; C/0960/18, *Sanitas/Néctar*; C/0568/14, *Mapfre/Bankia/Aselval/Laietana Vida/Laietana Generales*; C/0530/13, *Segurcaixa Adeslas/Cajasol Seguros Generales/Ican Salud*; C/0629/14, *Caser/CMV/CMP*; C/0963/18, *Santa Lucía/Pelayo/Pelayo Vida*; C/0765/16, *Catalana Occidente/Grupo Previsora Bilbaina/Grupo Funerario Arroita*; C/0717/15, *VidaCaixa/Barclays Seguros – Negocio Adquirido*; C/0683/15, *Pelayo/Agromutua – Activos*; C/0698/15, *GACM/RACC Seguros*. And in the banking sector: C/0873/17, *Banco Santander/Santander Elavon Merchant Services-SEMS*; C/0942/18, *Banco Santander/Wizink Activos*; C/0535/13, *Apollo/Evo Banco*; C/0587/14, *Banco Popular/Citibank-Activos*; C/0940/18, *Varde/Wizink*; C/0611/14, *BBVA/Catalunya Banc*; C/0911/17, *Servired/Sistema 4B/Euro 6000*; C/0732/16, *Credit Mutuel-Targobank*; C/0901/17, *Bankia-BMN*; C/603/14, *CaixaBank/Barclays*; C/515/13, *Banco Sabadell/Lloyds España*.

were reviewed. Also life and non-life insurance and reinsurance markets. All these markets have different geographic scopes (supranational or international scope in corporate, investment and factoring; national – or within EU scope – in insurance and national and regional – province level – in retail banking in deposits, credits and branches).

Except from one big operation in 2017, analyzed and cleared by the European Commission[4], the CNMC gave the green light to mergers in banking with not substantial share additions at national level. The CNMC has actually verified in those analysis that things have been changing rapidly in this sector. As regards the assessment of entry barriers in the markets considered, the CNMC has stated that, there are still legal barriers (legal requests that banks have to fulfil to enter in activity and provide services); and that branches are not significant entry barriers anymore. In fact, the development of alternative channels – ATM and phone, mobile and on-line banking – has allowed the entrance of new incomers operating only via internet[5]. In the meantime, the new incomers without branches have the possibility to arrange collaboration agreements to use others operators' networks, in particular with third operators not present in the financial services markets. Obviously, the CNMC has also considered in these merger assessments that Fintech and big data companies are lessening entry barriers.

The merger of the management companies for domestic card payment system in Spain (SERVIRED, SYSTEM 4B, EURO 6000) was also reviewed by the CNMC at the beginning of this year. CNMC took into account that the effect of it was the convergence to the most common model within the EU, where there is a single card payment system with a payment application of its own in which financial entities that intermediate card payments are integrated. CNMC authorized it subject to commitments – now under monitoring for a 5+3 year period –, to keep access opened to new members and to preserve the competitive capacity of their members in the market of card payment services in Spain. Additionally, commitments were offered as well in the market for issuance, acquisition and processing of card payments, to avoid hindering the selection of alternative payment applications and to prevent the flow of sensitive information.

What has been said so far clearly reflects that the industry is undergoing a deep process of transformation. There is a complex interplay of exhaustive

4 Case M.8553 – *Banco Santander/Banco Popular Group*.

5 ING Direct, OpenBank and Activobank.

regulations, increasing potential competition and growing market concentration in Spain. All considered, as a competition authority, CNMC has been following this process with close attention to preserve competition and to avoid antitrust conducts.

In fact, in 2015, the multilateral ATM's interbank rate agreement, prior authorized in 2007 by the former Spanish Competition Authority – Tribunal de Defensa de la Competencia – under the previous regime, broke up as from the withdrawal of one of the main banks followed by others. The effect of that was the proliferation of bilateral ATM agreements between medium size entities that gave rise to a complex scenario followed by a new piece of legislation to avoid double payments to users. The CNMC closely monitored the process and published a state of the play report in 2016.

Besides, concerning antitrust enforcement, the CNMC adopted at the beginning of this year a decision[6] imposing fines (up to 91 mll€) on the main 4 Spanish banks for an infringement of article 1 LDC and 101 TFEU, consisting on financial derivative price agreements in derivatives hedging syndicated loan interest rates in project finance. All of those four main banks participated jointly in a relevant part of total syndicated loans contracted in between 2006-2016.

The file started with a complaint from a renewable energy company that had a syndicated loan with the four banks. Normally, in syndicated loans[7], interest rates are variable[8] and, to ensure the return of the loan, the banks requested the borrower to buy from them an interest rate financial derivative to counteract interest rates fluctuations. The four banks provided the financial derivative, which was normally a collar or a *swap*.

During the investigation, it was proved that the banks agreed on advance on the collar floor rate level or the swap fixed rate, behind the borrower's back, through phone calls and e-mails, and more than 100 b.p. -1 percentage point – higher than the market rates, without any proved objective or technical justification. They pass it on to the borrower as if it was at "zero cost" or at "market conditions". On the contrary, with those rates, the value of the financial derivative for the borrower of the syndicated loan at the time of purchase was negative for him. The undertaking should have received a premium from

6 S/DC/0579/16, *Derivados Financieros*.

7 The European Commission has launched in 2017 a study on EU loan syndication and its impact on competition in credit markets.

8 6/3 month Euribor/Libor + spread.

the banks, as the hedging included an implicit and, to the CNMC, non-licit spread favorable to the banks that made the derivative very negative to the undertaking from the outset.

The CNMC adopted this decision in February 2018 and it is now under jurisdictional review.

Based on this experience in merger and antitrust, and bearing in mind the indicated restructuring and transformation process, the CNMC decided to study FINTECH in its action plan 2018, to advocate it as a source of competition in the financial sector that can bring along greater access to financing, especially to SMEs, benefiting the whole economy.

So concerning advocacy in the financial sector, after some months of public consultations, the CNMC Board adopted in the last week of September a report on Fintech that has become public recently.

Fintech – ICTs in the financial sector – is a disruptive innovation. The key element at the center of this process is the improved forms of information and data use, information being the most important input in the financial services markets. The better use of data (DLTs, new payment services, financial, advice and asset management, crowdfunding, Insurtech) allows new incomers into the markets, many of them smaller than incumbents and offering just a specific service in a market niche, also greater consumer involvement, disintermediation and new business models and services based on platforms. A completely new picture of the industry structure.

New stakeholders will compete with new strategies completely adapted to consumer needs. New technologies allow banks to be profitable at a lower scale, since fixed costs are much lower thus reducing the need of physical branches and legacy infrastructure. This is the main reason of the advent of alternatives to the one-stop shop model, unbundling the provision of financial services and allowing the emergence of niche competitors. On the other hand, costs and assets are less specific, and firms from other sectors (e.g. TechFins with know-how in data management) can compete in the financial sector. Both tendencies put consumer at the center, with a bigger customization of financial services. This customer centricity is a driver of competition.

Based on a detailed analysis, the CNMC study highlights three main conclusions:

1) FINTECH can foster competition in the financial sector and hence in the rest of the economy. This importance of advocating for competition

in the financial sector is obvious when we see how financial instruments are a catalyst for competition in other sectors. This is the case of crowdfunding, which provides cheaper and broader access to credit, reducing the credit rationing for small, nascent and innovative firms or projects. In the same vein, wider options in payments can allow firms to internationalize their business, and do business in a global and more competitive environment.

2) Fintech eliminates or, at least, reduces market failures that are behind financial regulation such as information asymmetries and systemic risk, because of customer centricity, smaller players competing and unbundling services provision.
3) These new market realities demand regulators and policy makers to reassess current regulation that maybe has become inefficient for these new realities and is preventing competition and innovations to develop.

On the basis of the former conclusions, the CNMC's study on Fintech recommends:

1) Ensure good regulations and reassess the rational of some restrictions in existing laws (entry requirements, physical presence); Intervention has to base on necessity, proportionality and non-discrimination principles.
2) Try to regulate activities instead of entities and avoid whenever possible reserves of activities (key to take advantage of scope and network economies).
3) Take advantage of Regtech to reduce regulations (compliance and supervision can be less costly and more efficient for operators and regulators).
4) Consider regulatory sandboxes (or temporary regulatory exemptions for innovative models and assess their impact on the market before adopting a final regulatory response).
5) Open banking and insurance (access to inputs on fair and reasonable terms under principles of technological neutrality and non-discrimination).

The digitalization/digitisation of the economic activity, poses evidently some challenges to the competition authorities. There is in particular the issue of data – or big data – and competition; and digital platforms and

competition[9]. Dynamic competition is worth stressing because it plays a key role to ensure the health of the digital economy preserving innovation. That is why it is so relevant to make sure that regulation is not hindering innovation changes in financial markets.

Besides, there is the question of how competition authorities can take into account this innovation defense in the different markets and how mergers can affect. One very important element is that big players do not foreclose access to their data when firms in other related markets need it to develop new products. Regulation has provided an answer to this potential problem. The Payment System Directive 2 (PSD2) has tried to address those challenges from a broad perspective, trying to ensure the application of general principles, such as interoperability and technological neutrality, and it has made mandatory that banks grant access to financial data of their customers when they give their consent and some security requirements are fulfil.

It is likely that Competition Authorities will have to react faster but Competition Authorities should keep on conducting the competition analysis on a case-by-case basis. Existing antitrust tools are robust and forward-looking, capable of evolving with the times and able to cope with the challenges of the digital economy.

9 See *CNMC's contribution on the "Implications of digitisation for competition policy" for the conference on "'Shaping competition policy in the era of digitisation"* (under DG COMP call for contributions, July 2018).