

## Completed acquisition by ICAP plc of EBS Group Limited

The OFT's decision on reference under section 22(1) given on 20 June 2006.  
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**Please note that square brackets indicate figures or text which have been deleted or replaced at the request of the parties for reasons of commercial confidentiality.**

### **PARTIES**

1. **ICAP plc (ICAP)** is a holding company for a number of trading subsidiaries whose operations together comprise the world's largest inter-dealer broker (IDB) business.<sup>1</sup> ICAP is active in the wholesale markets for over-the-counter (OTC)<sup>2</sup> derivatives, fixed income securities, precious metals, money market products, foreign exchange, energy, credit and equity derivatives.
2. **EBS Group Limited (EBS)** is a provider of electronic IDB services primarily to the spot foreign exchange trading community. Prior to the transaction it was owned by a number of leading financial institutions. In the financial year ended 31 December 2004, EBS achieved total worldwide turnover of US\$206.2 million. EBS's UK turnover in 2005 was [less than £70] million.

### **TRANSACTION**

3. On 21 April 2006 ICAP notified the proposed acquisition of the entire share capital of EBS to the OFT. On 5 June 2006 ICAP completed the acquisition of EBS for a combination of cash and an issue of new ICAP shares. The statutory deadline expires on 4 October 2006.

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<sup>1</sup> Inter-Dealer Broker: IDBs provide specialist intermediary services to financial institutions and commercial banks active in wholesale financial markets.

<sup>2</sup> OTC relates to any market which does not fulfil trades at a nationally recognised exchange. An OTC market is conducted directly between counterparties or through brokers via telephone or computer networks.

## **JURISDICTION**

4. As a result of the transaction, ICAP and EBS have ceased to be distinct. The share of supply test in section 23(2) of the Enterprise Act 2002 (the Act) is met in relation to the supply of spot foreign exchange or precious metals IDB services. The OFT therefore believes that it may be the case that a relevant merger situation has been created.

## **MARKET DEFINITION**

5. As noted above, the merging parties overlap in the supply of foreign exchange and precious metals IDB services. Each of these is considered below.

### **Product market**

Foreign exchange - background

6. ICAP claims that the foreign exchange market is commonly acknowledged to be among the largest and most liquid markets in the world. It is estimated that average daily worldwide turnover in what the parties describe as the 'traditional' foreign exchange markets reached US\$1.9 trillion in April 2004, with the UK the most active trading centre, accounting for [25 – 35] per cent of total turnover.
7. There are a number of different foreign exchange transactions, including spot trades, outright forwards and exchange swaps, each of which have discrete characteristics, intended functions and transaction costs. For the purposes of this investigation, we have focused on spot foreign exchange transactions, the only type of foreign exchange transaction in which the merging parties overlap.
8. Spot foreign exchange can be executed by dealers through two distinct channels: principals may trade directly with each other ('direct dealing'), or the transaction may be mediated by an IDB, who seeks to match the 'bid and ask' quotes of the market participants (seller and buyer). In this way, IDBs provide specialist intermediary services to financial institutions and commercial banks, thereby creating liquidity in the exchange of currencies by banks, and are paid a commission for their services.

Spot foreign exchange - electronic v voice broking

9. Within the IDB channel, there are two distinct brokerage methods. Voice broking is conducted with a broker in person, quoting prices and transacting deals over the telephone, and communicating directly with the relevant counterparty. Electronic brokerage involves the setting up of an electronic marketplace on which

traders can buy and sell spot foreign exchange. Since 1992, and the introduction by Reuters of an electronic brokerage service in relation to spot foreign exchange trading, the position of voice broking has eroded rapidly in spot foreign exchange, and notably in relation to the brokerage of particularly liquid currency pairs.

10. In Collins Stewart/Prebon the OFT considered voice and electronic broking in combination and as separate segments.<sup>3</sup> In obtaining evidence in relation to the current investigation, responding customers (with one exception), along with most competitors, viewed voice broking and electronic broking as complementary rather than substitutable. Third parties suggested that voice broking could not compete with the greater liquidity, speed of execution and transparency provided by electronic broking. Moreover, the relatively low marginal cost of supplying electronic broking services relative to voice broking means that voice brokers cannot compete with electronic broking on price alone. There appear to be significant differences between voice and electronic broking in both the structure and level of commission charges.
11. Third parties claimed that voice broking accounts for a relatively small proportion of their total business, and this is confirmed by figures provided by ICAP. Voice broking appears to be used predominantly for currency pairs that are not traded enough for electronic broking platforms to enable sufficient liquidity<sup>4</sup>; for more complicated currency exchanges; or in cases where a trader wishes to remain anonymous and/or avoid negative price effects of trading large volumes on the electronic marketplace.
12. The OFT has found little evidence of supply-side substitution between voice and electronic broking. While there are examples of brokerage firms participating in both voice and electronic broking, the resources required for each differ substantially. Voice brokers are required to establish relationships with traders, and expend significant effort and expertise to execute a trade, while an electronic system requires significant development costs but has very low marginal costs. The current transaction itself illustrates the difficulty of supply side substitution, with internal documents suggesting that ICAP could only enter the market for electronic broking of spot foreign exchange by way of acquisition, despite its presence through its existing voice broking business.

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<sup>3</sup> Anticipated acquisition by Collins Stewart Tullett plc of Fulton Prebon Group Holdings plc (7 October 2004) paragraph 17.

<sup>4</sup> In this case 'liquidity' refers to the ease with which an asset (e.g. foreign exchange) can be brought or sold quickly without substantially affecting the asset's price. A platform will be highly liquid if a large pool of buyers and sellers generate a large volume of transactions such that individual transactions will have little impact on the asset price.

## Precious metals

13. EBS is the leading electronic broker of spot trades in precious metals, in particular gold and silver. While ICAP is active in the voice broking of precious metals, primarily gold, its spot business is of only minimal significance, with on average fewer than one spot trade per day generating annual revenues for ICAP of [less than £250,000] in 2005 (inclusive of gold, silver, platinum and palladium).
14. Spot precious metal transactions, like spot foreign exchange transactions, can be executed through direct dealing by principals, or through the use of intermediary services offered by an IDB (voice or electronic). The characteristics of voice and electronic broking are substantially similar to those described in relation to spot foreign exchange trading, although the introduction of electronic IDBs occurred in July 2000. Voice brokerage remains well suited to the execution of large block trades, where there is little liquidity in the market (e.g. trading of platinum and palladium) and/or where a price is not available from an electronic broker.
15. The evidence available in this particular case, therefore, leads the OFT to conclude that there is little, if any, competitive constraint between voice and electronic broking, both in relation to spot foreign exchange and precious metals broking.

## Wholesale supply of electronic broking

16. A competitor suggested that the OFT should consider the frame of reference to be the supply of electronic broking of all OTC financial instruments. Users of IDB services are traders within large banks and financial institutions. These banks and financial institutions trade in a range of OTC financial instruments and it was claimed by the third party in question that many customers view and manage their relationship with IDBs as a single entity. The third party cited ICAP press releases announcing the transaction as referring to the 'market' for electronic brokerage services.
17. The OFT explored whether this single view was corroborated by customers, questioning a number of financial institutions about the structure of their dealing in OTC financial instruments and their procurement of IDB services. These customers said that, despite the fact that they deal in a range of financial instruments, they typically have separate 'business franchises' for dealing different classes of financial instruments. Some of these franchises negotiate independently with IDBs for their services. Moreover, many customers said that it is individual traders that are on the whole responsible for choosing how to execute their trade – and they typically concentrate on one financial instrument, with only sporadic trading in related instruments.

18. In terms of supply-side substitution, while a number of the IDBs provide electronic broking services in relation to a range of OTC financial instruments, third party competitors agreed that this would be of only little assistance if an existing electronic IDB wished to move into electronic broking of spot foreign exchange. While an existing electronic broker would have the technology available to quickly move into electronic broking of another financial instrument, the key barrier to entry - liquidity - would exist regardless of any existing electronic service (see barriers to entry section below). Some indication of the lack of supply-side substitution is the pervasiveness of entry by acquisition, rather than expansion by existing providers of electronic IDB services.
19. As a result, the OFT believes that there is little in the way of either demand- or supply-side substitution to support considering the provision of electronic broking services across different financial instruments in the same product scope; for the purposes of this investigation, the OFT has considered electronic broking services in the context of individual OTC financial instruments.

#### **Geographic market**

20. The majority of products in the financial trading markets are international in nature, being freely traded across geographic boundaries and time zones. The market characteristics suggest that the markets for voice and electronic broking services of spot foreign exchange and precious metal trades are at the very least EEA-wide, and possibly worldwide, in scope. However, we do not consider it necessary to conclude on geographic scope for the purposes of this decision as it does not affect the competition analysis in this case.

#### **UNILATERAL EFFECTS**

##### **Shares of supply - spot foreign exchange**

21. ICAP provided us with share of supply figures in relation to a number of possible frames of reference. A broad overview of the shares of supply for spot foreign exchange trading is set out in Table 1:

**Table 1: Share of supply, London daily spot foreign exchange, 2005**

	<b>US\$ billions</b>	<b>per cent</b>
<b>VOICE BROKING AND DIRECT TRADES</b>		
Direct trades	[ ]	[25 – 30] per cent
Inter-dealer brokerage		
• ICAP	[ ]	[0 – 5] per cent
• Collins Stewart	[ ]	[0 – 5] per cent
• GFI	[ ]	[0 – 5] per cent
• Other	[ ]	[0 – 5] per cent
<b>Sub-total</b>	[ ]	[30 – 40] per cent
<b>ELECTRONIC BROKING</b>		
Single bank dealer-to-client platforms (SDPs) (e.g. Citibank, Deutsche Bank, ABN Amro)	[ ]	[25 - 30] per cent
Multibank dealer-to-client platforms (e.g. FXAll, Currenex, FX Connect, Lava, Hotspot)_	[ ]	[5 – 10] per cent
Inter-dealer brokerage		
• EBS	[ ]	[15 - 20] per cent
• Reuters	[ ]	[10 -15] per cent
• Other	[ ]	[0 – 5] per cent
<b>Sub-total</b>	[ ]	[60 – 70] per cent
<b>TOTAL</b>	[ ]	100.0 per cent

Source: ICAP Best Estimates

22. Shares of supply figures for IDBs are set out in Tables 2 and 3:

**Table 2: Electronic IDB shares of supply, London daily spot foreign exchange market, 2005**

Company	Estimated Daily Transaction Volume (US\$ billions)	per cent
EBS	[ ]	[55 – 60] per cent
Reuters	[ ]	[35 – 40] per cent
Others (electronic)	[ ]	[0 – 5] per cent
<b>Total</b>	[ ]	<b>100 per cent</b>

Source: ICAP Best Estimates

**Table 3: Voice IDB shares of supply, London daily spot foreign exchange market, 2005**

Company	Estimated Daily Transaction Volume (US\$ billions)	per cent
ICAP	[ ]	[35 – 40] per cent
Collins Stewart Tullett	[ ]	[20 – 25] per cent
GFI Group	[ ]	[0 – 5] per cent
BGC Partners	[ ]	[0 – 5] per cent
Traditional	[ ]	[0 – 5] per cent
Others (voice)	[ ]	[30 – 35] per cent
<b>Total</b>	[ ]	<b>100 per cent</b>

Source: ICAP Best Estimates

23. As discussed above, there seems to be limited or no competitive interaction between voice and electronic brokerage services, and hence between ICAP and EBS. Even if, in an abundance of caution, voice and electronic broking of spot foreign exchange trading were considered a single relevant market, the ICAP adds only [0 – 5] per cent to EBS' [45 – 50] per cent share. Evidence obtained from the parties and third parties suggests that Reuters was EBS' primary competitor prior to the merger.

24. Reuters offers a similar electronic IDB service to EBS in relation to foreign exchange. EBS and Reuters have traditionally attracted liquidity in different currency pairs (i.e. EBS is the key provider of the major G10 currencies and Reuters is the key provider for GBP and Commonwealth currencies). However, the potential for a movement in liquidity from one to the other exists, albeit typically in a dynamic context. Examples of such movement were provided by third parties. These included a shift of liquidity to EBS upon entry into the market, a shift of

liquidity back to Reuters when it appeared that EBS' successful entry was threatening Reuters' position and further shifts to Reuters when the EBS system had gone offline. These examples suggest that the two systems act as a competitive constraint on each other – a constraint that is not expected to change post-merger.

25. Accordingly, the OFT takes the view that the totality of the share data do not give cause for prima facie competition concerns in relation to merger effects in spot foreign exchange trading.

**Shares of supply - precious metals**

26. EBS is the sole electronic broker of spot precious metal trades, with daily volumes of between [ ] and [ ] ounces.<sup>5</sup> The main voice brokers of precious metal trades are GFI, Tradition, ICAP and Prebon-Premex. Their daily brokerage volumes are set out in Table 4.

**Table 4: IDB share of supply: voice brokers**

<b>Voice broker</b>	<b>Daily volumes (Ounces)</b>	<b>Share (per cent)</b>
GFI	[ ]	[30 – 40]
Traditional	[ ]	[30 – 40]
ICAP	[ ]	[10 – 25]
Prebon-Premex	[ ]	[10 – 15]

Source: ICAP Best Estimates

27. As was the case with brokerage of spot foreign exchange, there seems to be limited or no competitive interaction between voice and electronic brokerage, and hence between ICAP and EBS. No concerns were raised by any third parties in relation to IDB services in precious metals. Even if, in an abundance of caution, we assume there was some level of competitive interaction prior to the transaction, three precious metal voice brokers remain following the transaction, two of whom had a greater share of supply than ICAP pre-merger. Therefore, the OFT does not believe that the merger will have a material effect on customers: as such, any lessening of competition is not considered to be substantial.

**Entry and expansion**

28. In Collins Stewart/Prebon the OFT concluded that there were some barriers to entry in relation to IDB services, although they were not considered to be insurmountable. In relation to voice broking, third parties confirmed that the

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<sup>5</sup> Parties estimates.

primary barrier to de novo entry is establishing relationships between brokers and dealers. This suggests that an existing voice broker, already possessing the infrastructure to support a new financial instrument desk, could expand relatively easily into voice broking other OTC financial instruments.

29. As regards entry into electronic broking of spot foreign exchange or precious metals, expansion by an existing electronic IDB into the electronic broking of other OTC financial instruments is considered to be easier than de novo entry. However, the evidence obtained by the OFT in relation to the investigation suggests that even entry by existing electronic brokers is not straightforward. Documents provided by the merging parties suggest that acquisition, rather than expansion, would be the more likely means of entry for ICAP into electronic IDB market for spot foreign exchange, despite the breadth of electronic services it already provided.
30. The main reason for this view appears to be the need to obtain sufficient liquidity on an electronic platform; given the importance of liquid electronic market places, there is a significant disincentive on any individual customer to be the first to switch to a new provider. ICAP maintains that liquidity will move easily between IDBs. However, the OFT's view, and that of many third parties, is that liquidity is likely to remain with incumbent providers (Reuters and EBS in the case of spot foreign exchange), in the absence of the following:
- **Sponsored entry:** major banks and financial institutions (many of whom were shareholders of EBS prior to the transaction) have in the past sponsored electronic IDB entry in relation to a number of OTC financial products. ICAP cites the creation of EBS itself, which was started by a consortium of leading financial institutions, as well as BrokerTec, MTS Group and Eurex Bonds. It maintains that financial institutions will retain the ability to act collectively to support new entry and/or constrain ICAP/EBS, whether by directly creating a new entrant or by moving liquidity to alternative trading platforms. Customer corroboration lends particular weight to this view.
  - **Innovative entry:** a number of third parties suggested that, despite the prominence of the two incumbents, the emergence of new technology was such that there were opportunities for new electronic trading platforms to 'leap-frog' incumbents by providing a differentiated service. HotSpot, Lava and CME are all interbank electronic spot foreign exchange trading platforms that offer alternative pools of liquidity customers could access. Although small compared to EBS/Reuters it was submitted to us that they may well grow in the future. Lava, owned by Citigroup, has recently launched an interbank foreign exchange trading system in direct competition to Reuters and EBS, incorporating a number of features not available on EBS or Reuters.

31. In summary, the evidence obtained by the OFT suggests that the most significant barrier to successful de novo entry into the electronic IDB market (or expansion by an existing electronic broker) is liquidity. While obtaining enough liquidity to attract traders is difficult, the OFT was presented with a number of examples where customers sponsored entry or diverted liquidity in order to encourage an existing competitor. This, along with the possibility of entry through technological innovation, suggests that successful entry is possible, and increasingly likely the greater the degree of customers dissatisfaction with the terms of supply by incumbents.

### **Countervailing buyer power**

32. The merged entity will provide IDB services to a client base comprising some of the world's largest commercial banks and financial institutions. Such customers are sophisticated, resourceful, highly cost-sensitive and believe that they are in a strong negotiating position when dealing with IDBs. This is consistent with the discussion on sponsored entry (effectively an example of countervailing buyer power above), and the OFT's finding in Collins Stewart/Prebon, where it was observed that banks use a wide range of brokers and switch frequently. It was also noted that, whilst customers value the benefits of trading through brokers they also have an option to switch to trading directly (or to an exchange, depending on the financial instrument).
33. A number of customers the OFT approached expressed their preference for having two IDBs in relation to electronic foreign exchange broking (although this was not the case for precious metals, given the relatively small size of the market). This would ensure that in the event, for example, of EBS going offline there would be a fallback broking option. It was noted that when this had happened in the past liquidity had quickly shifted to the alternative electronic broker. Moreover, the ability to sponsor entry by quickly shifting large amounts of liquidity gives the large banks a source of buyer power vis-à-vis the IDBs (see barriers to entry above).
34. We also have evidence that customers are conscious of the benefits of competition between IDBs. Some third parties suggested to us that, even though EBS was owned by a consortium of commercial banks and financial institutions, these same banks and financial institutions had continued to support Reuters to ensure that there was effective competition in relation to electronic broking of foreign exchange.
35. [ ]

36. Overall, the evidence provided to the OFT suggests that customers of the merged entity are sophisticated, resourceful, cost-sensitive, and have good knowledge of IDB services. They retain a strong preference for retaining a choice between electronic IDBs where possible, and have taken an active role in supporting entry and encouraging competition. We do not believe that this will change as a result of the merger.

#### **Conclusion on unilateral effects**

37. Given the very limited competitive constraint between ICAP and EBS pre-merger, the small incremental share of supply, together with the presence of buyer power, and the possibility of sponsored entry in particular, the OFT does not consider that competition concerns will arise from this merger in relation to IDB services for spot foreign exchange. This conclusion holds true even if, for the sake of argument, voice and electronic broking were considered sufficiently substitutable to be treated as one relevant product market.

#### **NON-HORIZONTAL ISSUES**

38. Some non-horizontal concerns were raised by third parties. One competitor noted that ICAP now offered electronic trading platforms across the full range of OTC financial instruments, and suggested that ICAP had an incentive to bundle/tie their various IDB services, and/or cross-subsidise their various products. Another competitor suggested that ICAP's voice brokers would obtain an information advantage over other voice brokers, as ICAP could make pricing information obtained from the acquired EBS platform available to its voice brokers. Each of these concerns is discussed below.

#### **Tying/bundling**

39. One third party argued that, as a result of the merger, ICAP would be able to offer a complete electronic brokerage portfolio across OTC financial instruments. It was submitted that this would enable ICAP to tie or bundle the broking of less desired financial instruments to instruments where ICAP has high liquidity, and therefore potential market power. This competitor also submitted that EBS is a 'must-have' electronic platform for spot foreign exchange, and that ICAP could leverage this market power into other IDB markets. It was also suggested that such a practice has already been adopted by ICAP in respect of US Treasury Bonds following ICAP's acquisition of the BrokerTec electronic IDB platform.
40. Mergers between firms that do not supply directly competing products rarely lead to a substantial lessening of competition solely as a result of their conglomerate

effects: on the contrary, portfolio effects are generally pro-competitive since they tend to lower customers' buying costs (as customers can now buy the same range of services by dealing with fewer suppliers). But it cannot be excluded that a conglomerate merger may be anti-competitive – where it directly affects market structure by substantially increasing the feasibility of anti-competitive strategies and/or eliminating the competitive constraint imposed by firms in a neighbouring market, and if competitors unable to offer the same portfolio of products cannot provide a sufficient competitive constraint on the merged parties.

41. Customers have told us that trader preference is the key determinant in deciding which electronic brokerage system is used, and that decisions are based on liquidity rather than brokerage agreements. This is consistent with providing traders with the freedom to use the IDB that provides the best option for the particular trade, rather than the lowest commission rate. It is also consistent with our description of the separate 'business franchises' model by which many of the customers operate, whereby different business divisions, specialising in the trading of different asset classes, are treated as individual profit centres (see market definition section above). One customer suggested that a bundling/tying strategy would be slightly simplistic for what is a large and varied market, and it would not suit the customer's way of doing business.
42. Since trader preference is only affected by the liquidity of the particular financial instrument that they are charged with trading, it is not expected that offers of discounts on commissions on other financial instruments will induce switching to a particular electronic broker in any one financial instrument. As discussed above, it is of note that even within spot foreign exchange, EBS and Reuters have attracted liquidity in relation to different currency pairs that both parties have told us have been difficult to shift.
43. ICAP has told us that it does not, nor has it considered, offering cross-product customer discount terms. This was supported by ICAP's customers, none of whom suggested that bundling/tying would be a concern post-merger, despite the fact that the concern was specifically mentioned to some of them. Based on this evidence, the OFT believes that the theory that the transaction may substantially lessen competition through the use by ICAP/EBS of bundling/tying practices lacks credibility on the facts in this case.

### **Cross subsidisation to aid predatory pricing**

44. It has also been suggested to us that, as a result of the transaction, ICAP/EBS will be able to engage in predatory pricing in order to prevent successful entry or induce exit in one or more markets of IDB services, cross-subsidised from those areas of business where market power may exist. It was argued that if EBS does possess market power, the merger increases ICAP's ability to engage in such cross-subsidisation.
45. Leaving aside the question of whether EBS has market power, it should be noted that this is already a strategy that ICAP could have pursued across the platforms that it owned prior to the merger - and no evidence of it so doing has been provided to the OFT. Second, the importance of liquidity on electronic platforms relative to brokerage commissions is inconsistent with the assumption that predation will generate shifts in volumes in any case. As stated above, liquidity is typically the key determinant in choice of broker, rather than commission.
46. In addition, for this to be a competition concern, the OFT would need to consider that recoupment of lost profits would be feasible at some point in the future: there does not appear to be an incentive for cross-subsidisation if it is unlikely to result in greater profits in the longer term, i.e. whereby the short-term losses of predation are absorbed in the expectation of greater longer term gain. In this case, even if predation is successful in inducing market exit or preventing entry, prospects for recoupment seem remote, due to the ability of customers to sponsor entry, and the buyer power that the threat of such entry can provide. (See sections on barriers to entry and buyer power, above). As discussed above, it is of note that EBS customers have acted collectively to shift liquidity in the past to encourage competition.

### **Access to information**

47. Two competitors of the merging parties raised concerns regarding the ability of ICAP to allow its voice brokers to see the prices generated on EBS without generally making this information available to its competitors, which they claim would give it such a significant advantage such as to foreclose the market for voice broking of spot foreign exchange. While there is no evidence that co-ownership of both voice and electronic IDB services has resulted in such access to information in relation to the trading of other financial instruments, it was submitted by one third party that the volatility of spot foreign exchange prices meant that knowledge of 'real-time' foreign exchange pricing was particularly important.
48. The weight of third party views expressed to the OFT undermine the validity of

this concern. While one third party competitor did suggest that access to such information would give ICAP a substantial advantage over other voice brokers, another competitor told us that any advantage would not be of such a serious concern as to significantly affect the competitive dynamic. None of the customers raised this concern with the OFT of their own volition, so we directly sought customer views.

49. In response, customers suggested that, while access to EBS might provide some information advantage, the spot foreign exchange market was sufficiently transparent that such an advantage would not be significant. In particular, traders on either side of the voice IDB will have access to electronic broking platforms and prices thereon to inform their pricing decisions, effectively providing the IDB with 'emulated' access to the EBS system. It was also submitted that there are a variety of additional methods available to voice brokers to help them determine the appropriate bid/sell price.
50. The merging parties submitted that no voice broker has ever requested access to the EBS system. ICAP also submitted that it does not intend to allow its own voice brokers access to the EBS system, and that such a practice would undermine the integrity of the EBS system.
51. Based on the evidence discussed above, and in particular the views of customers, we do not consider that any information advantage gained by ICAP will be sufficient to provide such an overriding advantage as to raise a realistic prospect of a substantial lessening of competition in relation to spot foreign exchange voice broking.

### **THIRD PARTY VIEWS**

52. The OFT received a number of comments from third parties. Customers of ICAP and EBS were generally supportive of the merger, thus supporting the argument that it is pro-competitive. It is relevant to note that the former EBS shareholders (i.e. the vendors for this transaction) are all significant customers of EBS. EBS provided evidence describing the shareholders' consideration of the transaction, and the consequences of selling EBS to ICAP. Moreover, customers' views were largely consistent, whether or not they were shareholders of EBS.
53. Some competitors raised concerns. In addition to those discussed above, the primary concerns also raised regarded the share element of the transaction consideration, as well as any additional commitments that the former shareholders of EBS may have made in relation to supporting the EBS platform following the transaction.

54. As previously noted, the transaction included a share option for each of the EBS shareholders to acquire ICAP shares in lieu of cash consideration. Two third parties suggested that, given the EBS shareholders are all major users of ICAP's IDB services, the share option would encourage those customers to use ICAP to the exclusion of other IDBs. However, we note that the exercise of the share option has resulted in EBS shareholders only owning around five to six per cent of the total ICAP shares in issue. Split between the 13 banks and financial institutions that were the shareholders of EBS prior to the acquisition, this level of shareholding would suggest that little incentive arises to support ICAP to the detriment of competition in various IDB markets. This is supported by the fact that Reuters has competed strongly in spot foreign exchange broking despite EBS, its major rival, being owned by some of Reuters' customers.
55. Some third parties also stated that they would have concerns if the EBS vendor shareholders had entered into volume commitments (or similar arrangements) to support ICAP following the merger. It was noted that such commitments were agreed in relation to ICAP's acquisition of BrokerTec as a way of establishing BrokerTec in the IDB market for US Treasury and Agency Securities. Following objections to the US Department of Justice, these volume commitments were reduced and certain non-compete clauses removed. Some third parties argued such clauses would tie the majority of EBS' actual or potential customer base, especially for spot foreign exchange broking, to EBS, thus excluding competition from other brokerage providers.
56. The OFT directly queried both of the merging parties on this aspect of the transaction. While there is in place an agreement that EBS will not increase fees from those agreed with any of the vendor shareholders at the time of the merger, no volume commitments or non-compete clauses were included as part of the transaction. This is confirmed not only by the transaction documents but by the internal documents produced by EBS in anticipation of the sale process. [ ]

## **ASSESSMENT**

57. The transaction combines the world's largest IDB with a significant provider of electronic IDB services in relation to spot foreign exchange and precious metals. The parties therefore overlap in the supply of spot foreign exchange and precious metals IDB services.
58. Evidence obtained by the OFT suggested that the parties were not direct competitors pre-merger, despite both providing IDB services in relation to spot foreign exchange and precious metals. ICAP provided only voice broking of these financial products, while EBS' services were solely electronic. Customers viewed the two methods of broking as largely complementary, predominantly using voice

broking in limited circumstances when electronic broking was unsuitable for a particular transaction. Similarly, customer evidence also suggested that we should not view the provision of electronic broking services across different financial instruments in the same product scope.

59. Even if voice broking and electronic broking could be considered substitutable to the point of forming a single relevant market, the OFT found that any competitive interaction between the merging parties pre-merger was very limited. This factor, the small incremental share of supply, the presence of buyer power, and the possibility of sponsored entry in particular suggested that no horizontal concerns will arise from this merger in relation to IDB services for spot foreign exchange and precious metals.
60. The OFT also carefully considered a number non-horizontal issues raised by third parties. In relation to alleged bundling/tying practices, the evidence obtained by the OFT suggested that such strategies were not expected to induce traders (and hence their banks and financial institutions) to switch to a particular electronic broker.
61. In relation to the possibility of cross-subsidisation, we found that there was no evidence that ICAP had pursued this strategy in the past, notwithstanding its broad portfolio of electronic broking services prior to the merger. We found that, even if predation was successful in inducing market exit or preventing entry, recoupment seemed remote given the threat of sponsoring entry that the sophisticated and well-resourced customer base can wield.
62. Finally, we considered whether ICAP would seek to obtain an advantage over other spot foreign exchange voice brokers by allowing its voice brokers to access the information contained on the EBS system. We found that, while ICAP voice brokers may gain some benefit from any information that can be obtained from the EBS system, this was not seen by customers to be important enough to give it an overriding advantage so as to foreclose the market for voice broking of spot foreign exchange.
63. Consequently, the OFT does not believe that it is or may be the case that the merger has resulted or may be expected to result in a substantial lessening of competition within any market or markets in the United Kingdom.

## **DECISION**

64. This merger will therefore not be referred to the Competition Commission under section 22 (1) of the Enterprise Act.