EU loan syndication and its impact on competition in credit markets

Final Report

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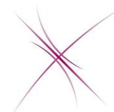

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Final report

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Luxembourg: Publications Office of the European Union, 2018

Catalogue number: KD-04-19-330-EN-N
ISBN 978-92-76-01894-0
doi: 10.2763/738938

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Executive Summary

This is Europe Economics' final report on "EU loan syndication and its impact on competition in credit markets". This research was undertaken for DG Competition of the European Commission.

The European Commission's interest in the syndicated loan market is primarily motivated as to whether it is working well and efficiently, given its role as a source of finance. The aim of this market study, then, is to undertake an assessment of the loan syndication market in terms of its effectiveness and functioning, and to identify potential competition concerns.

Introduction to the study and our approach to the research

Debt is a critical source of finance for the European economy. The syndicated loan market is a major contributor of debt finance, particularly in terms of large-scale debt. We introduce and describe the European loan syndication market further below.

Our study focuses primarily on a sample of six Member States, namely France, Germany, the Netherlands, Poland, Spain and the United Kingdom. These countries — in particular the UK, France and Germany — are the most significant in terms of the location of borrowers, lenders and investors. The study focuses on specific segments of the syndicated loan market: those connected with Leveraged Buy-Outs (LBOs), project finance and infrastructure finance:

- LBOs: LBOs are primarily M&A transactions, where the buyer uses the debt markets to contribute towards acquiring the target's equity. The core of European leveraged lending comes from borrowers sponsored by private equity funds. In Europe, all such private equity-related activity, including refinancing and recapitalizations, are referred to as LBOs.[1]
- Project finance: In broad terms, project finance entails the financing of large-scale long-term projects that tend to require a great deal of debt and equity capital. Syndicated loans tend to be particularly prominent in this type of investment, as they allow the diversification of the risks of a single project (which can be considerable) across multiple banks.
- Infrastructure: Infrastructure loans are considered here to be a subset of project finance loans, with similar financing requirements. The key distinction is the nature of projects that are financed; this broadly includes projects in the areas of utilities, transport, and telecommunications. As in the case of project finance in general, the size and complexity of these projects renders them highly suitable for syndicated loan financing.

We adopted a multi-strand strategy to conducting this research. In particular:

- We developed a conceptual framework to analyse potential competition concerns in the syndicated loan market. Our academic adviser, Professor Alper Kara, Professor of Finance at the University of Huddersfield, helped us to identify relevant academic material, and we worked with Euclid Law, who specialise in competition law, to incorporate competition law considerations into our framework.
- We complemented this with desk-top research, with one of our main research tools being the Thomson Reuters Loan Connector database (which incorporates the Deal Scan database).
- We conducted primary research with lenders in the market. Mr Simon Hood, who worked in the loan market for 30+ years was very helpful in connecting us to lenders and, more generally, assisting our engagement with the loan syndication market and its participants. Overall we conducted over 43 interviews with 37

[1] See e.g. Standard & Poor's (2010) "A Guide to the European Loan Market".

lenders, achieving good coverage across the different countries of interest and diversity in terms of lender type (including leading investment banks, regional commercial banks, and institutional investors, amongst others). We also interviewed debt advisers and Credit Rating Agencies.

- We conducted primary research on borrowers and sponsors. Sponsors (such as private equity funds) are important actors in the LBO and Project Finance / INFRA segments, often taking an active role alongside the borrowers in securing debt finance. We worked with YouGov plc to develop a computer-assisted telephone interview programme that successfully reached 100 market participants. Again, this covered all of the countries of interest and was evenly divided between borrowers and sponsors (i.e. 50 each).

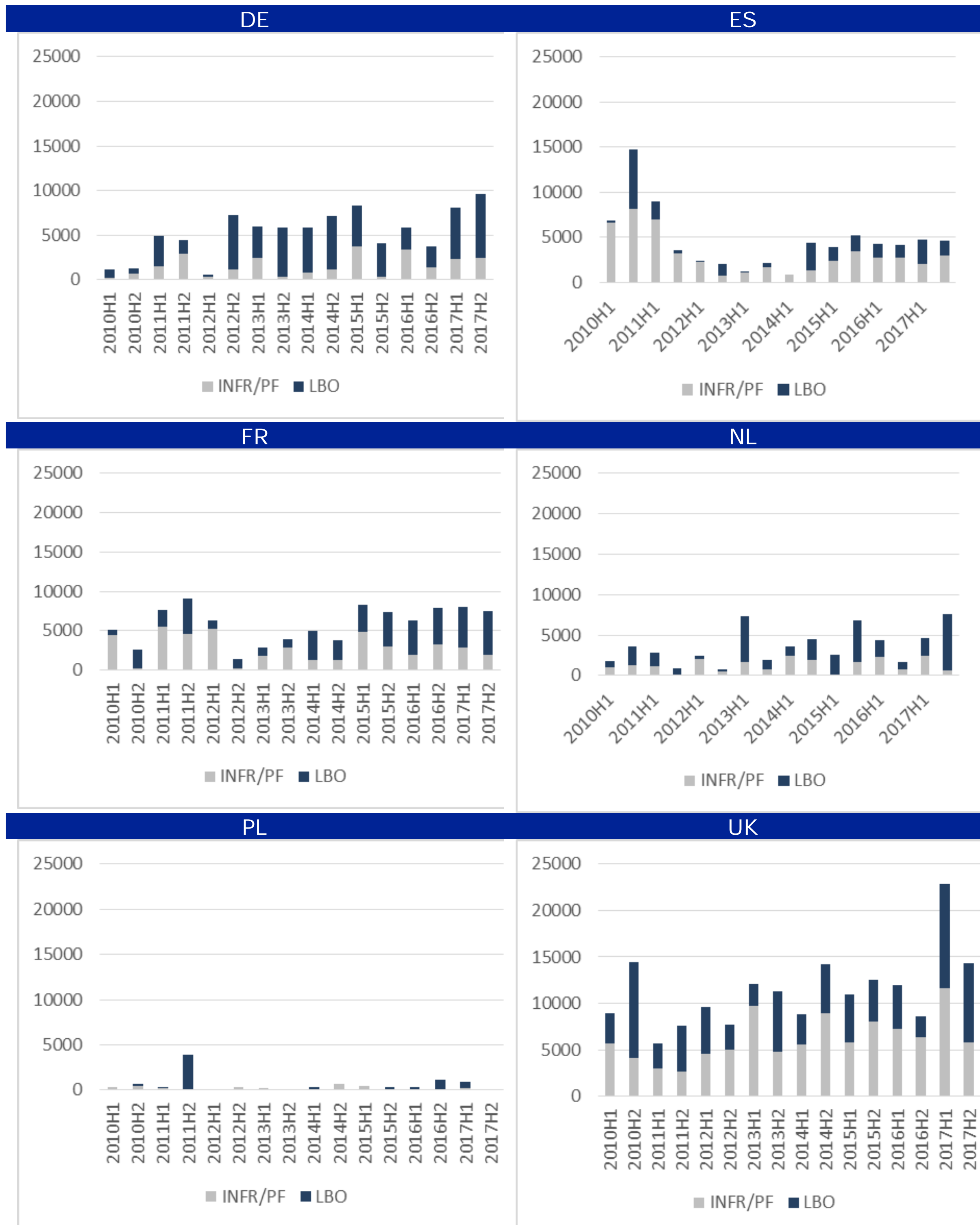
Finally, we brought together these various evidence sources in order to assess the merits of the various hypotheses generated through our conceptual framework so that we could form conclusions about the functioning of the loan syndication market.

The loan syndication market

Debt is a critical source of finance for the European economy. A syndicated loan facility is in turn an important source of large-scale lending where several lenders come together to share credit risk in order to provide loans to a borrower in a single loan facility agreement. Syndicated lending offers an alternative form of debt financing to bilateral lending or corporate bonds, providing benefits to borrowers and lenders alike by addressing a number of typical issues raised in lending markets such as market matching problems, information asymmetry and moral hazard. Syndicated loans are a significant source of capital in Europe, with about $800 billion (about €720 billion) raised in 2017 across all Europe. LBOs, project finance and infrastructure are just some of the purposes to which this capital is put with almost 60 per cent being for various corporate purposes (e.g. refinancing). Corporate M&A is also an important motivation. In 2017, the LBO-related borrowing in the six countries of particular interest to this study was about €58 billion (i.e. about 7 per cent of the total market for syndicate debt for all purposes in all Europe), whereas PF/INFRA-related borrowing was about €35 billion (about 4 per cent).

The evolution of the amounts borrowed by the purpose of the loan and by Member State is set out below. A decline in Spain was experienced particularly strongly post-Euro crisis, but also evident in the Netherlands and Poland. The largest markets – i.e. borrowers located in Germany, France and the UK - exhibit much more consistent deal flow than the others. Poland is clearly a much smaller market than the others, with perhaps only 1-2 transactions “live” at any one time. Overall, the six countries of interest to this study account for about three-quarters of the EU’s LBO, Project and Infrastructure syndicated lending in Europe.

Figure 1: Total value of deals by Member State (biannual, €m)



Source: Europe Economics (using Thomson Reuters Loan Connector).

Nature and features of the syndicated loans markets

We have researched two segments within the syndicated lending space, i.e. LBOs and PF/INFRA.

Nature of LBO and PF/INFRA segments

Both LBOs and PF/INFRA projects have significant needs for debt financing. The main substitutes for syndicated lending are bilateral loans, corporate bonds and private debt placement. Whilst these alternative funding options are generally readily available, a borrower/sponsor can still differentiate between these different products, and have preferences between them.

Our analysis of the market shares of individual lenders at a national level does not indicate any of the markets as being highly concentrated. However, it is worth noting that the PF/INFRA segment is more heterogeneous than the LBO one, in that there are credit risks (say related to a particular type of infrastructure construction, such as specific forms of renewable energy) where knowledge could be less well distributed than our HHI-based analysis might suggest.

On the other hand, there is evidence of "home bias" in that the top ranked lenders tend to be lenders with a parent in that country. This is not experienced evenly, being more prominent in PF/INFRA than in LBOs. We consider it unlikely that this "home bias" is a signal of competition being undermined by restricting the pool of potential Mandated Lead Arrangers (MLAs), at least in the west European markets covered by this study, where non-local banks can be readily accessed. In Poland, on the other hand, the low deal frequency and use of a non-mainstream currency (relative to the £ and €), may make the pool of potential MLAs relatively small. This appears to be more of a concern in the PF/INFRA segment.

Availability of banks/ MLAs

Our research shows that borrowers and sponsors are generally considered to have sufficient sophistication either to assess and negotiate the price and terms of the loan in-house or else to appoint advisers to assist them in that. In terms of the availability of lenders, the number of lenders participating in both LBO and PF/INFRA segments is large. However, far from all of these lenders would have the wherewithal to compete effectively for any given MLA mandate. In the LBO segment there are at least 12–15 credible MLAs in the west European markets of interest here but in Poland, there are fewer, with estimates of the number being as low as 6–8. PF/INFRA is somewhat different, at least in terms of the composition of players. However, we consider that the number of capable MLAs is at least as large as in the LBO space. A point emphasised in the lender fieldwork, though, is that the PF/INFRA segment is more heterogeneous, with the result that in at least some parts of it, MLA choice (e.g. toll roads) would be more restricted and, as with LBOs, the Polish market has less choice.

Although the study has been focused on six Member States, we are able to make some tentative observations about the LBO and PF/INFRA segments outside of these countries. There is some degree of differentiation between west Europe and the rest of the EU, with the former likelier to have choice from more lenders to act as an MLA. This may mean that Poland is a good proxy for at least other non-west European countries, particularly where the Euro is not the currency borrowed in.

Market features that could facilitate collusion

It is also the case that any collusion by lenders ahead of submitting bids in an RFP process would obviously invalidate the anticipated competitive outcomes. Whilst sponsors/borrowers generally seek to control the debt origination/syndication process, there are areas where the control would be reduced. We consider that some of these could potentially facilitate collusive outcomes, in particular:

- The use of market soundings by MLAs. This would be particularly problematic where the sounding crossed the boundary between generic sounding and deal specific-sounding and where the sounding was with an MLA (or even an entity connected to

an MLA). The main safeguard here is that lenders emphasised that internal policies meant that any deal-specific soundings would require client consent, and that this would need to be demonstrable to compliance teams. In its strongest form, such consent should be specific as to who is contacted.

- The provision of ancillary services where this provision is restricted to the syndicate, or some sub-set of it, e.g. an obligation – or strong expectation – that purchase would be from the MLAs, especially if not all MLAs were able or willing to provide or quote for that service.
- In the case of a general syndication (e.g. in an underwritten deal), since it is the bookrunners that deal directly with the potential participating lenders there is scope for this to underpin tacit reciprocity in the market. We note, however, that there are several safeguards that can help to counter any such attempts (i.e. borrower/sponsor-driven white lists, direct feedback loops between investors and sponsors, regular feedback from the bookrunners and approval by borrowers/sponsors of final syndicate member allocations).
- The borrowers/sponsors will also have curtailed bargaining power where a borrower is in financial difficulties and faces default. The options available to a borrower may be very limited in such an instance.

Overall, these are particular market features whose presence would indicate greater cause for concern, and which form part of our analytical framework for assessing the market. We also consider those markets (specifically Poland amongst the countries we have considered) with fewer potential MLAs should be monitored most closely. This may also apply to other countries within the EU where borrowing is not in the £ or € and to smaller markets more generally (particularly those less well connected to the main locus of the syndication market in Europe, i.e. the City in London).

Assessment of competitive dynamics of the syndicated loans process

We developed a coherent framework to assess the implications of how the syndicated loans market works in terms of the competitive dynamics of that market. This framework drew upon past academic work and insights into competition policy and competition law (namely Article 101 and Article 102 of the Treaty on the Functioning of the European Union (TFEU), including the Horizontal Guidelines for Articles 101 and 102[2]) from our legal collaborators. The key issues examined in the framework were:

- Horizontal information sharing – for example this may lead to the disclosure of strategic information (such as strategic market practices to be adopted) which may serve to coordinate the pricing policies of the lenders, thereby facilitating a collusive outcome on the market in terms of price in particular, but also quantity, quality etc.
- Cooperation may also lead to overt agreements between lenders to collude, for example to share markets or customers, or to rig bidding processes. This would not be necessary to the syndicated loan process but possibly facilitated by it.
- Vertical market power held by individual MLAs and/or the lenders may lead to sub-optimal loan terms.
- Syndication may confer market power to a syndicate in certain circumstances, which may lead to sub-optimal outcomes and may increase the negative impacts of collusive behaviour (for example if lenders agree to increase loan prices on refinancing where the borrower has limited alternatives).
- Misaligned incentives between lenders within a syndicate, and between lenders and borrowers, may give rise to more general sub-optimal market outcomes.

[2] European Commission (2011) "Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements" (2011/C 11/01). We draw mainly on the general information sharing guidelines, see in particular paragraphs 55 to 102 and also on the Agreements for Commercialisation guidelines, see paragraphs 225 to 256.

The extent to which information sharing and any potential market power would be able to restrict competition through facilitating collusion and abuse of dominance depends on a number of market characteristics and the nature of the information exchanged. These include for example the level of concentration in the market and market shares of the participants, the availability of substitutes for the borrowers/sponsors and their sophistication, the extent of market transparency and the frequency of interaction and information exchange. In addition, Article 101(3) states that cooperative agreements that do have the potential to limit competition may be exempt from Article 101(1) by virtue of being efficiency enhancing and indispensable to the pro-competitive benefits of the agreement. Our competition framework therefore developed a range of hypotheses for how the various issues and market features set out above might manifest themselves in the loan syndication market. We then analysed the evidence gathered through our fieldwork and desk research against each of these hypotheses. We note that the analysis of competition law issues in relation to Articles 101 and 102 is based on our own judgement, and that the European Commission has not taken a position on what is falling within/outside the scope of these Articles as regards syndicated lending.

We summarise below, in **Table 1,** the main findings stemming from this work, describing those areas where we have identified potential risk, and also discussing the evidence for particular safeguards present in syndicated lending that may limit market participants experiencing these risks in practice. Our analysis works through the different stages of process and by loan segment, and our assessment is limited to whether the market features and the various processes within loan syndication are more or less *conducive* to potential competition law problems, rather than establishing specific cases of competition law violation.

Table 1: Summary of key competition risks and presence of safeguards in syndicated lending, by stage of process and by segment

Stage in process	Findings and conclusions on safeguards and risks
Competitive bidding process for appointing individual banks to the lead banking group	LBO segment The boundary between generic and specific market sounding (as can be conducted by syndication desks) needs careful definition to ensure compliance (banks require explicit borrower/sponsor consent to conduct deal-specific soundings in a form whereby this would need to be demonstrable to compliance teams). In its strongest form, such consent should be specific as to who is contacted. There is evidence of generic market soundings by MLAs with investors prior to submitting bids, and whilst these discussions should not involve details of specific transactions information about specific lenders' appetite etc. may still be communicated back to the origination desks. This risk may be exacerbated where there is no significant functional separation between the syndication and origination desks. Soundings (even generic soundings) with other MLAs (as opposed to exclusively with institutional investors without connections to MLAs) could be abused so as to facilitate collusive action, even potentially enabling a group of MLAs (particularly one with fewer substitute MLAs) to achieve, and sustain, some degree of collective bargaining power. In the markets considered in this study, we consider this risk to be relatively low in the LBO segment. In addition, although the bidding process is set up to keep lenders apart, the prevention of information sharing is governed by NDAs, which can be difficult to enforce. Therefore although the process set up by the borrower/sponsor in LBO loans reduces the risk of anti-competitive information sharing, the risk remains that this may happen. Equally, once an NDA is signed, it is evident to the counter-party that the breach of that agreement is problematic (i.e. it puts banks on clear notice of borrower/sponsor expectations). PF/INFRA segment Similar safeguards exist in the PF/INFRA segment, in that the borrower/sponsor controls the formation of the lead banking group, keeping banks separate until the finalisation of terms and seeks to protect information flows with NDAs. However, given the more bespoke nature of PF/INFRA loans, the availability of information to assist in banks forming their views is likely to be lower. Therefore whilst there is no evidence to suggest that banks in this segment are more likely to engage in market sounding or breach NDAs, it follows that there is a heightened risk relative to the LBO segment that interactions between lenders would cross over the general/specific sounding boundary in the bidding stage, making this an area of increased potential concern. The use of a single MLA to set up a syndicate and negotiate with other banks is more likely to take place in PF/INFRA loans (although it is still not common). Whilst the fieldwork indicates that borrowers/sponsors retain control of this process, there remains the possibility that information sharing may occur such that the negotiations of the syndicate could be coordinated and the price and terms of the loan move against the borrower. The necessity of such information exchange would need to be assessed on a case-by-case basis, but this remains a risk area. This risk would be heightened further if the bank acting as MLA in such a case was also (through a separate arm) acting as an adviser to the borrower/sponsor or there was some other limitation on replacement of that bank as MLA. However, the appointment of a single MLA in the PF/INFRA segment is rare.
Post-mandate to loan agreement	Both segments The scope for lenders discussing loan terms so as to move against the borrower at the post-mandate stage is low, given that in both LBO and PF/INFRA segments the process widely adopted is for the loan terms to be agreed bilaterally between the borrower/sponsor and individual lenders, and that joint discussions between lenders post-mandate should be limited to agreeing the loan documentation and syndication strategy. Borrowers/sponsors also aim to build in latency when obtaining loan commitments from the lead banking group.

Stage in process	Findings and conclusions on safeguards and risks
	There is some evidence that the loan process may not always work in the borrower/sponsor's favour in terms of it agreeing the overall price to the highest common denominator rather than negotiating a common price. This may however simply reflect the relative attractiveness of the credit itself. Our evidence indicates this is not at all common in practice. However, in the PF/INFRA segment there have been cases where the borrower/sponsor does bring lenders together at an earlier stage to discuss loan terms, e.g. in a club deal, and so this safeguard does not apply across the board. The exercise of control of the borrower/sponsor in these cases will therefore be more important i.e. by monitoring the discussions that take place. Whilst evidence gathered throughout the report indicates that borrowers/sponsors are sophisticated in this regard, some risk does remain than lenders may engage in discussions outside of the borrowers' mandate. This risk would be heightened should the borrower/sponsor be less sophisticated than the norm, e.g. if a municipal authority, without prior experience in the syndicated loans market, was acting as borrower. The evidence of the multiple interactions between lenders on transactions over time leads us to conclude that there is a definite risk that lenders can observe each other's behaviours and strategies, which may enable them to engage in some coordination on future loan transactions. We do not have direct evidence that this happens in practice. Given that fact that in most cases the discussions that occur at this stage do not involve detailed information about pricing and hold strategies the amount of information that lenders are able to observe is likely to be limited. Whilst this remains a risk area, we consider it relatively low risk.
The allocation of ancillary services across banks, and the pricing of such services	In the majority of cases from our lender and borrower/sponsor fieldwork, the allocation of ancillary services is decided as part of the initial agreement of loan terms, or as a competitive process after the loan has closed. In both cases the borrower/sponsor would be able to choose between banks' offers and maintain competitive pressure. However a small minority of borrower/sponsors identified that the MLAs make the provision of ancillary services by them a condition of the loan (the rest negotiate ancillary services as part of the initial loan agreement process, or after the loan close). Whilst competition law precedent (e.g. Spain's CNMC) has not concluded that it is unlawful for lenders to specify that ancillary services be purchased from them, we do consider such a feature as raising the risk of a borrower/sponsor achieving a sub-optimal economic outcome. We further note that all of the respondents that cited such provision being a condition of the loan were from Spain. Where this feature occurs, we consider this an area of at least moderate concern. In the PF/INFRA segment it is more common for ancillary services directly related to the loan to be allocated by the borrower/sponsor to lending banks at the initial stage of agreeing overall loan terms. The fact that the banks know who is to be providing the services provides them with scope to discuss and collude on pricing (i.e. makes it easier for them to subvert the proper, agreed process). Restrictions placed by lenders on who can provide hedging services will be more problematic in markets where there is a limited number of lenders in the syndicate with the ability to provide such services, thus restricting borrower/sponsor choice. We do not have evidence of this occurring in practice, but note that smaller national markets (such a Poland in our sample) or else in more bespoke PF/INFRA deal will be more at risk. Ancillary services <u>not directly</u> related to the loan (e.g. further financing, investment services) can be negotiated as part of the loan negotiation, with both "right of first refusal" and "right to match" clauses being used. These have been found by the UK regulator as to have no client benefit – unless related to the replacement of bridging finance - and have been banned in the UK, but their use may be continued outside the UK (representing a continued risk to optimal outcome for borrowers/sponsors).

Stage in process	Findings and conclusions on safeguards and risks
The use of debt advisors which are also involved in the syndicated loan	The use of advisors who are also part of the syndicate is widespread among borrowers and sponsors, and in some cases with there being no other source of external advice. This issue is more common in the PF/INFRA segment (but it is not non-existent in the LBO segment) and could represent a non-negligible fraction of transactions. Our lender fieldwork shows that where an advisory role is provided by a lending bank, this is functionally separate from the lending role, and adherence to such protocols should mitigate the risk of sub-optimal outcomes to borrowers of not having a demonstrably independent advisor. There is (limited) evidence that some lenders do bundle – at the request of the borrower/sponsor – the advisory role with a lending role in PF/INFRA. The risks here would be heightened where the advisor is appointed directly without a competitive process and combines the lending role with the advisory role, whereby the borrower/sponsor may not receive the best loan outcome. A different form of concern would be where the advising bank attempted to influence the borrower/sponsor towards a strategy or debt structure that suited its lending arm, i.e. subverting the Chinese wall between the advisory and lending functions, and with this not being fully apparent to the borrower/sponsor. Based upon the description of their policies for managing such situations given to us by lenders, this would represent a significant breach of such internal protocols. Where such controls were weak, this would be an area of high concern.
Coordination by lenders on the sale of the loan on the secondary market	There is no evidence of co-ordinated activity to manipulate prices in the secondary market in our work, and the safeguard relating to hold levels is widely upheld in practice (indeed, it is a key part of the process). The features of the secondary (i.e. post closure trading) loan market - which remains a caveat emptor market with implicitly sophisticated buyers - should limit any attempt by sellers to manipulate the price of the debt, unless they are able to simultaneously identify a group of unsophisticated buyers of that debt. The economic benefit to lenders from any coordination may therefore be limited, reducing the plausibility of this risk. There is widespread evidence of borrower/sponsor restrictions on secondary trading. The lenders described restrictions imposed by PF/INFRA sponsors/borrowers as potentially including: no small transfers; an embargo during the construction period and the transfer being subject to borrower approval (except in case of default). Whilst such restrictions may be reasonably motivated (e.g. restricting the dispersion of deal-specific information), these do limit – at least at some level - the development and efficiency of the secondary market. Given that secondary market pricing data are also used in the primary market (albeit not exclusively relied upon), this could also affect have (minor) knock-on effects to the development and efficiency of the primary market, at least in the PF/INFRA segment.
Refinancing in conditions of default	Competition policy training is undertaken by lenders' restructuring teams. These are functionally separate teams which take over the loan discussions from the origination teams in the case of a default risk, such that discussions between banks regarding the potential restructuring are not undertaken by teams involved in loan origination. Discussions between lenders are only possible under such policies at the instigation of the borrower. The discussions and negotiations of potential restructuring in the event of a default are performed collaboratively among the members of the syndicate. Whilst this may be efficiency enhancing, as time is often pressurised, it equally enhances the risk of banks acting in a coordinated manner. We note that the bank restructuring teams that we interviewed had undertaken some form of competition policy training, but clearly any subversion of the proper process would be problematic. The extent to which the proper process had been subverted would need to be assessed on a case by case

Stage in process	Findings and conclusions on safeguards and risks
	basis. Our fieldwork shows a majority of instances where refinancing discussions involved lenders from outside of the original syndicate. The willingness of the market to provide the new finance can be seen as a limit upon any bargaining power that the existing group of lending banks may have. However, there is evidence of a non-trivial number of instances where the existing syndicate is the only option, i.e. there is scope to exert such market power. We do emphasise, however, that we do not have evidence for its abuse. In relation to the risk of the syndicate tying ancillary services to the refinancing, the fieldwork shows again that other, non-syndicate members are often involved in these discussions, which would provide market discipline against such coordinated tying behaviour. However, it is also apparent that in a substantial minority of cases such negotiations took place only with the syndicate members. There may be mitigating or efficiency enhancing circumstances, but it is also clear that such distressed circumstances can create the opportunity to price such ancillary services on non-competitive terms, and thus this is also an area deserving future monitoring.

Critical safeguards

We now draw upon the above analysis to identify the most important safeguards to ensure competitive outcomes in the loan syndication process.

- *Banks' duty of care to clients. There are two important safeguards here.*
    - Borrowers may source debt advice from the same lender that they wish to act as MLA (or, at least, consider acting an MLA). The critical safeguard here would be the adequate training and policies for the relevant staff at the potential MLAs. In particular, the training would need to cover topics such as the identification and management of conflicts of interest, and provide clarity as to duty of care to provide neutral advice to clients.
    - MLAs should ensure that there are not alternative options that could be put to the borrower, including inviting other lenders not previously involved in the process to participate (subject to obtaining borrower or sponsor consent), or considering a re-structuring of the loan, before aligning loan pricing or terms upwards to a highest common denominator. If the particular lender asking for the higher price is needed for the purposes of the joint bid (e.g. as explicitly required by the borrower), the price should be set at an acceptable level. The borrower (and its advisors, if relevant) can promote a beneficial outcome through ensuring a competitive bidding process (i.e. approaching more banks), building latency into the process and maintaining bilateral negotiations with individual lenders (or lender consortia) through to mandate award.
- *Avoidance of unwarranted information exchange.* In loan origination banks (and any other market players capable of forming the lead banking group) may need to exchange pricing information for the potential syndication while remaining competitors in the origination. The key safeguard would be that there are enforceable (and enforced) protocols around how – and in what form – any deal-relevant information obtained by the syndication function from other potential participants (who may also be competitors in the origination) may be transferred to the same bank's origination function in order to avoid anticompetitive alignment of prices.
- *Promotion of unbundled price competition.* Ancillary services not directly related to the loan (e.g. future M&A advisory services) can be negotiated as part of the loan negotiation, with both "right of first refusal" and "right to match" clauses being

used. In the absence of market power, such a bundled offering may be pro-competitive but these have been found by the UK regulator as to have no client benefit – except when related to the replacement of bridging finance - and have been banned in the UK. It is advisable for syndicates to limit the cross-sale of ancillary services in order to avoid the risk of impairing competitive conditions in neighbouring markets to that of syndicated loans, and this should be kept outside the loan syndication process when these services are not directly linked to the loan.

Final remarks

The European secondary loan market is notably smaller than that in the USA. The USA's secondary market has been shown to have beneficial impacts on the US primary market.[3] Whilst we do not have evidence to indicate that trading in the European secondary market is inefficient and, whilst noting that the data are very limited, such beneficial impacts on the primary market are less clearly apparent in Europe.

An area of inefficiency in the loan syndication market, not directly related to the competition policy risks discussed above relates to the slowness and expense of Know Your Customer (KYC) rules applied by lenders and more generally to settlement processes. We found evidence to suggest that there is something of a coordination problem here amongst market participants and this could also be an area for future regulatory attention.

[3] See Kamstra, Mark, Roberts, Gordon, Shao, Pei (2014) "Does the Secondary Loan Market Reduce Borrowing Costs?" *Review of Finance*, Volume 18, Issue 3, Pages 1139–1181.

1. Overview of the Study and of our Methodology

This is Europe Economics' report for the study "EU loan syndication and its impact on competition in credit markets". The aim of this study is to undertake an assessment of the loan syndication market in terms of its effectiveness and functioning, and to identify any potential competition concerns.

Introduction and motivation for this research

Debt is a critical source of finance for the European economy. The syndicated loan market is a major contributor of debt finance, particularly in terms of large-scale debt. We introduce and describe the European loan syndication market in Chapters 2 and 3.

The European Commission's interest in the syndicated loan market is primarily motivated as to whether it is working well and efficiently, given its role as a source of project and infrastructure finance. The aim of this study, then, is to undertake an assessment of the loan syndication market in terms of its effectiveness and functioning, and to identify any potential competition concerns.

This study is intended to have both a geographic and a product focus within the overall European syndicated loan market. We focus on six Member States as set out in the Tender Specifications, namely France, Germany, the Netherlands, Poland, Spain and the United Kingdom (although we discuss syndicated lending more generally across the EU and globally where relevant). These countries — in particular the UK, France and Germany — are the most significant in terms of the location of borrowers, lenders and investors.

In addition, we focus upon the leveraged (specifically relating to Leveraged Buy-Outs, or LBOs) and the Project / Infrastructure segments within the Syndicated Loan market. (We expand upon what is included within these segments in the following chapter).

Research methodology

We adopted a multi-strand strategy to conducting this research. In particular:

- We have reviewed the available academic literature, as well as market research and consultancy reports. The purpose of this review was to assist in the development of a conceptual framework to analyse competition in the syndicated loan market. Our academic adviser, Professor Alper Kara, Professor of Finance at the University of Huddersfield, helped us to identify relevant academic material.
- Our collaborator, Euclid Law, provided analysis of the competition policy and legal elements within our conceptual framework for assessing the state of competition in the market. Euclid's analysis of relevant competition cases, including an overview of the available case law, is provided in Appendices 5a–5g.
- We conducted desk-top research to describe the market and to conduct in-depth analysis into specific topics, such as secondary trading in syndicated loans. One of our main research tools here was the Thomson Reuters Loan Connector database (which incorporates the Deal Scan database).
- We conducted primary research with lenders in the market. The aim of the stakeholder engagement was to probe further into the mechanics of how the market works, as well as to investigate any other relevant areas of interest. The main strand of this was a series of stakeholder interviews with lenders. Mr Simon Hood,

who worked in the loan market for 30+ years, was helpful in connecting us to lenders and, more generally, assisting our engagement with and understanding of the loan syndication market and its participants. The questions asked, and the motivation for asking them, are summarised at Appendix 6.

- Overall we conducted 43 interviews with 37 lenders. (Many lenders have discrete teams working in the origination of LBO and PF / INFRA loans, i.e. 'origination desks', which we sometimes interviewed separately for logistical reasons. In the lenders we interviewed, syndication activity was embodied separately from origination — again, this could result in a separate interview. Similarly, we also wished to investigate some aspects of the loan market – such as what happens in the event of a restructuring – that are almost universally handled by separate units within lenders). In addition, we engaged with Credit Rating Agencies and debt advisory firms in order to round out this engagement (but we exclude these from the interview numbers set out here). We break down the lenders that we spoke to as follows:

Table 2: Lender engagement

Location of ultimate headquarters / stakeholder type	Banks	Non-banks (debt funds, institutional investors and CLO managers)	Total
Europe	24	4	28
Non-Europe	7	2	9
Total	31	6	37

- We also conducted primary research with borrowers and sponsors. Sponsors (such as private equity funds, infrastructure funds and construction firms) are important actors in the LBO and Project Finance / INFRA segments. The questions asked, and the motivation for asking them, are included at Appendix 6. We worked with YouGov plc to develop a computer-assisted telephone interview (CATI) programme that successfully reached 100 market participants.

Table 3: Borrower/sponsor engagement

Location / stakeholder type	Borrowers	Sponsors	Total
France	10	10	20
Germany	10	10	20
Netherlands	5	5	10
Poland	3	4	7
Spain	11	10	21
UK	11	11	22
Total	50	50	100

- Finally, we brought together these various evidence sources in order to assess the merits of the various hypotheses generated through our conceptual framework so that we could form conclusions about the functioning of the loan syndication market.

Structure of this report

The report presents the work undertaken across the following sections:

- Chapter 2 presents a background to syndicated lending, including an overview of the actors involved in the market and the processes involved in organising a syndicated loan.
- Chapter 3 describes the loan syndication market, starting with the global market and then narrowing our focus, first to Europe, and then - in more detail – considering the Member States and loan types of specific interest here.
- Chapter 4 sets out our framework for considering the economic and potential competition issues in the market. This drove the subsequent fieldwork and the analysis in this research. As part of this, a case law assessment has been carried out. We then present our economic and competition analysis, assembling the evidence relevant to considering the various hypotheses identified in our conceptual framework. This is ordered by the stages of the process as identified in Chapter 2.
- Chapter 5 contains our conclusions, including tables summarising the key findings from Chapter 4. The latter are also summarised as part of the report's executive summary.
- Appendix 1 sets out a glossary of terms.
- Appendix 2 sets out details of how we defined the segments of interest and cleansed the data extracted from Thomson Reuters Loan Connector.
- Appendix 3 sets out some background on the execution of loan transfers.
- Appendix 4 presents additional background material on past regulation that has impacted upon the syndicated loan market.
- Appendices 5a–5g review relevant competition case law across various European countries.
- Appendix 6 contains details on the fieldwork conducted, and the motivation for it.

2. Introduction to Loan Syndication

This section sets the context for the study by discussing the relevance of loan syndication and the key processes involved. The aim of this section is to inform the reader of how the loan syndication process works and the key actors involved. Therefore, whilst we identify potential competition concerns (related to both competition law and also sub-optimal market functioning) arising from the processes and relationships between the counterparties, these are analysed in detail in Chapter 4. We begin by presenting a glossary of the main actors involved in the loan syndication market. A fuller description is included later in this section.

Table 4: Glossary of actors in the syndicated loan market

Actor	Definition
Borrower / sponsor	A loan transaction would be initiated by a borrower or a sponsor. Borrowers are directly responsible for the project / the direct recipient of the funds (e.g. a special purpose vehicle). Sponsors are the equity providers to a transaction and are often involved in raising finance instead of the borrower.
Advisor	Debt advisors can be used by borrowers/sponsors to drive the loan process. These can be independent advisors, or located within banks also providing lending.
Mandated lead arranger (MLA)	MLAs are banks mandated by the borrower/sponsor to provide the primary arrangement and initial underwriting or provision of funds for the loan.
Bookrunner	In an underwritten deal the bookrunner(s) control the general syndication phase of selling the loan down to participant investors. A "lead left" bookrunner is a single bookrunner appointed to run the whole general syndication phase.
Coordinator	A coordinator bank can be appointed (normally in a club deal) to facilitate the transaction and to liaise with the other lenders.
Participant lenders	These participate in the loan through the general syndication or sell-down phase, and include smaller banks and non-bank lenders like institutional investors, debt funds or hedge funds.
Credit ratings agencies	Ratings agencies can be asked to provide private and public ratings for syndicated loans.

Background on the loan syndication market

Debt is a critical source of finance for the economy. A syndicated loan facility is in turn an important source of large-scale lending where several lenders come together to share credit risk in order to provide loans to a borrower in a single loan facility agreement. Syndicated lending offers an alternative form of debt financing to bilateral lending or corporate bonds, providing benefits to borrowers and lenders alike by addressing a number of typical issues raised in lending markets such as market matching problems, information asymmetry and moral hazard.

Lenders' incentives for engaging in syndicated lending include the ability to earn fees and the ability to gain exposure to certain markets and borrowers that might not be possible on a bilateral basis while at the same time limiting their risk exposure. Borrowers benefit from increased access to capital and lower financial transaction costs than would be achievable through bilateral loans with the individual lenders.

Syndicated loans are a significant source of capital in Europe, with about $800 billion (about €720 billion) raised in 2017. This is comparable in scale to the primary corporate bond market: Euro area non-financial corporations had gross corporate bond issuance of €650 billion in 2017.[4] We deepen the analysis of the syndicated loan market in Chapter 3.

However, syndicated loans may present drawbacks to borrowers, for example if they limit the borrower's ability to influence certain aspects of the functioning of the syndicate, or if intra-syndicate dynamics affect loan pricing and other terms to the detriment of the borrower. A borrowers' choice of a syndicated loan will be determined by the benefits and drawbacks offered by this form of lending, and also by the availability and suitability of other forms of financing.

We consider in detail the economic and competitive dynamics of the market in Chapter 4. In this chapter, we are primarily interested in how the market works, but draw out emerging features to be analysed and tested in light of our competition framework in chapter 4. This chapter includes the following sections:

- Definition of LBO, Project and Infrastructure finance loans.
- Introduction to the main parties in the syndication loan market.
- Description of the syndicated loan process including formation of the lead banking group, the general syndication phase and provision of ancillary services, and post closure including secondary trading and refinancing/restructuring.

Defining LBOs, Project and Infrastructure finance

A clear understanding of the process of loan syndication is important to articulating how this market works and where any competition concerns may arise. We focus on three loan market segments: leveraged buyouts (LBOs), project finance (PF) and infrastructure finance (INFRA).

- LBOs: LBOs are primarily Mergers and Acquisitions (M&A) transactions, where the buyer uses the debt markets to contribute towards acquiring the target's equity. More specifically, an LBO "consists in taking a firm private by purchasing its shares and allocating them to a concentrated ownership composed of management, a general partner, and other investors (the limited partners or LBO fund). Due to the dearth of equity of the owners, the new entity is highly leveraged."[5] A target company that is put up for sale to private equity firms for the first time is a primary LBO. A secondary LBO entails a company being sold from one private equity firm to another (and a tertiary LBO is one that is put up for sale for the third time). The core of European leveraged lending comes from borrowers owned by private equity funds. In Europe, all such private equity-related activity, including refinancing and recapitalizations, are referred to as LBOs.[6]
- Project finance: In broad terms, project finance entails the financing of large-scale long-term projects that tend to require a great deal of debt and equity capital, ranging up to billions of euros. Syndicated loans tend to be particularly prominent in this type of investment, as they allow the diversification of the risks of a single project (which can be considerable) across multiple banks. The loan structure relies primarily on the project's future cash flows for repayment, while the project's assets, rights and interests are typically held as collateral. More specifically, a bankruptcy-remote[7] special purpose vehicle (SPV) is usually set up, whose assets

[4] See European Central Bank Statistical Warehouse.
[5] See J. Tirole, The Theory of Corporate Finance, Princeton University Press, 2006.
[6] See e.g. Standard & Poor's (2010) "A Guide to the European Loan Market".
[7] A bankruptcy-remote firm is a company within a corporate group and whose bankruptcy has as little economic impact as possible on other entities within the group.

are primarily the project's assets, while the liabilities are primarily the project debt and the equity within the SPV. Project sponsors (i.e. equity investors) are usually multinational companies, state-owned firms, and/or governmental bodies that own jointly the SPV and its project financing contractual agreements. Sponsors contribute equity and technical expertise. Debt is, however, a major source of financing.[8]

- Infrastructure: Infrastructure loans are considered in this report to be a subset of project finance loans, with similar financing requirements. The key distinction is the nature of the projects that are financed. We later describe in more detail how we have defined infrastructure for the purposes of our data analysis, but this broadly includes projects in the areas of utilities, transport, and telecommunications. As in the case of project finance in general, the size and complexity of these projects renders them highly suitable for syndicated loan financing.

In describing the key parties involved and the loan syndication process, we draw primarily on our lender and borrower/sponsor fieldwork reflecting the current market in LBO, PF and INFRA financing, augmented by a review of academic papers[9] [10] and various industry guides for completeness.[11] [12] [13] [14] [15] Since different sources and market participants use varying terminology and descriptions of process flows, we have necessarily developed our own synthesis for the LBO, PF and INFRA segments, drawing out key differences in processes where relevant. The motivating ideas behind this are the identification of which actors are important and the scale and direction of information flows between actors.

Types of syndication

One way of distinguishing between different deals is with respect to the distribution method adopted.

- Club deal – this is where the loan is directly (individually) marketed to a group of banks by the borrower/sponsor who then commit to providing the full loan without further syndication. The borrower takes responsibility for identifying a number of banks (likely including, at least, its relationship banks), and then leads the bringing together of those banks interested in providing the finance. (Traditionally club deals have been for smaller scale lending with fewer banks involved, but increasingly more sophisticated borrowers and sponsors are using this method with a larger group and larger amounts of debt.) In a club deal the lenders tend to agree to take on the loan from the outset, without the intention of reducing their commitments through any subsequent syndication. In many cases there would not be an MLA per se as the "arranging" would be done by the borrower, and the amount required is committed by the banks identified. In some cases, however, an arranger or advisor may be involved.
- Fully underwritten – this is where the loan is fully underwritten by the arrangers / initial banking group, these negotiate terms and sign the loan agreement before then going out to the market to engage further lenders (with potentially other rounds of negotiation within the syndicate).

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[8] Beyond syndicated loans debt can also be provided by stand-alone banks, public bonds, private placement, special project finance firms and investment banks.
[9] Godlewski, Christophe J. (2007) "What Drives the Arrangement Timetable of Bank Loan Syndication?"
[10] Sufi, Amir (2006) "Information Asymmetry and Financing Arrangements: Evidence from Syndicated Loans" Journal of Finance. Available at SSRN: https://ssrn.com/abstract=596202 or http://dx.doi.org/10.2139/ssrn.596202.
[11] European Central Bank (2017) "Guidance on Leveraged Transactions ".
[12] AFME (2015) "Guide to infrastructure financing".
[13] Loan Market Association (LMA) (2013) "Guide to Syndicated Loans & Leveraged Finance Transactions".
[14] Standard & Poor's (2017) "Syndicated Loans: The Market and the Mechanics".
[15] S&P (2013) "A Guide to the European Loan Market"(2013).

- Best efforts – this is where the arrangers / initial banking group agree to take on only a portion of the loan, other participant banks are sought and then terms are negotiated among the syndicate before the signing of the deal.

The distribution methods account for much of the variation between the processes adopted in LBO and PF/INFRA loans, as we discuss in more detail the following sections (in particular, "LBO structure and distribution" and "PF/INFRA structure and distribution"). The main distinctions in distribution method are between underwritten deals (which will have a general syndication phase, i.e. the banks in the initial group take some market risk) – and which are most prevalent in the LBO segment - and club deals (where the initial group of banks tend to continue to hold the entirety of the loan) – which are more characteristic of the PF/INFRA segment. Best efforts deals do also take place, say where certainty of funds is not time-critical (such as in a refinancing deal), and follow a broadly similar process to underwritten deals.

Before looking more closely at the loan process, we now introduce the key parties involved.

Main parties in syndicated loan transactions

- *Borrowers and sponsors*. Borrowers and/or sponsors are responsible for initiating the transaction through a need for loan financing. Borrowers would be the party directly responsible for the project / the direct recipient of the funds, for example a special purpose vehicle or a corporation responsible for delivering the underlying project. Sponsors are the equity providers to a transaction and are often involved in raising finance instead of the borrower (i.e. a transaction would involve either the borrower *or* the sponsor). In an LBO transaction, the sponsor would be a private equity firm. In project or infrastructure transactions, the sponsors' identities are more heterogeneous but could include large construction firms, as well as infrastructure funds (which may also be managed by a private equity firm), or state bodies. In the markets of interest to this study both borrowers and sponsors are generally (but not always) highly sophisticated and typically drive the decision-making in the transactions. Current market conditions, with considerable appetite for investing in loans (particularly LBO debt), have strengthened sponsors' bargaining power. Private equity firms (particularly the larger ones) may have dedicated in-house, debt-raising teams.
- *Advisors.* Borrowers/sponsors will sometimes use debt advisors to drive the transaction forward. Advisors are typically independent boutique firms, but in some cases (and generally much more so in the PF/INFRA market) the role can also be filled by advisors located in banks that also have lending capabilities (we return to this topic below). Advisors have extensive experience in loan transactions and can advise on the structure and terms of the loan, as well as manage the negotiations with, and appointment of, the Mandated Lead Arrangers.
- *Mandated lead arrangers (MLAs).* MLAs are banks mandated by the borrower/sponsor to provide the primary arrangement and initial underwriting for the transaction (or the full provision of funds in the case of a club deal). The MLAs will receive the majority of fees available.[16] MLAs will not necessarily participate on a pro rata basis – smaller underwriting share takers, often relationship banks, can also be called 'joint lead arrangers'.
    - Depending on the nature of the transaction, MLAs can be large global banks (i.e. on large international transactions) and also smaller banks (e.g. arranging smaller, local deals).

[16] Whilst some sources differ in terminology, the term "mandated lead arranger" is commonly used, for instance by the Loan Market Association (LMA, a global trade association focused on the syndicated loan market) and industry databases.

- A range of different titles can be assigned to the MLAs, the primary one being that of "bookrunner(s)" in an underwritten (or best efforts) deal. In an underwritten deal, the bookrunner(s) control the general syndication process in terms of distributing, or selling down, the loan to market participants. In a best efforts transaction the bookrunner(s) use best efforts to attract sufficient commitments to achieve the overall requirement of the borrower. In some cases only one bookrunner is appointed, but, more generally, multiple MLAs share the role. It is considered the most important role as it involves the interaction and negotiation of the sell-down with participant investors (i.e. the market) and involves the most direct interaction with the sponsor/borrower. It is also considered desirable by MLAs to be in control of the management of their own underwriting risk. The fees earned in the role are also important. We discuss these further in Chapter 3.
- Due to the prestige attached to this role, there has been substantial 'title inflation' where more banks are termed bookrunner than actually run the book. In such transactions the term 'active' bookrunner(s) can be used to describe those MLAs with this actual bookrunner role – whereas a 'passive' bookrunner would be the other MLAs who would take on a more administrative role (e.g. ratings advisor – who would be responsible for liaising with credit rating agencies). The other titles commonly seen in the European market are the facility agent (which relates to post-closure of the loan and involves such tasks as funds administration, interests calculation, covenants enforcement, information sharing and re-negotiation management)[17] and security agent.[18] These roles are additional to the MLA role in that they involve more administrative activities than simply providing loan funding in the initial lending group. These roles are active after the closure of the loan agreement.
- Lead left bookrunner. In some of the largest transactions, a 'lead left' active bookrunner can be appointed as a single bank from within the MLAs to lead the whole syndication process and receive the majority of the available fees – e.g. if the sponsor/borrower or advisor prefers to have a single story in the market regarding the loan. A 'lead right' bank may also be appointed to stay up to date with the process and step in to fulfil the lead role if the 'lead left' loses confidence in the deal or otherwise underperforms.
- Coordinator. The role of the coordinator can be used in a club deal (when, as they are arranged by the borrower/sponsor or their advisor, there will not be the need for an actual MLA as is the case in an underwritten or best efforts deal). The coordinator role is assigned to a bank to facilitate the transaction and liaise with the other lenders to ensure communication and consensus on documentation. The borrower/sponsor or advisor would decide whether to appoint a coordinator in a club deal or whether to manage all interaction with the lenders themselves.

Within MLAs there are also different functions (also referred to in practice and in this study as 'teams' or 'desks'), which we define briefly here:

- *Origination function.* The origination function is responsible for the initial stages of the loan process, such as identifying the loan or holding initial

[17] Godlewski, Christophe J. (2007) "What Drives the Arrangement Timetable of Bank Loan Syndication?"
[18] The Facility Agent is responsible for the administration of the loan e.g. disbursements, repayments etc.; while the security agent is responsible for holding the security for the loan on behalf of the lenders.

discussions with the borrower about his borrowing needs (e.g. in the case of a relationship bank); bidding for a role in the loan; and negotiating all the key terms – such as price and hold levels – with the borrower and other banks in the lead banking group or club. Depending on the lender's business model, the origination team may sit within a product team or a specific regional team, or may be a central function.

  - *Syndication function.* The syndication function is responsible for syndicating the loan, i.e. selling it down to participating lenders and investors. This team has the main contact with the potential investors in the market, and is responsible for any market soundings to keep up to date with investor sentiment and market appetite for certain loan types. Although the syndication function is more relevant to the later stages of the loan process when the loan is to be sold down in the market, it can still play a role in the origination stage by advising the origination team on current market pricing, loan terms and hold levels, based on what it believes will be acceptable to the market at the syndication stage.

- *Participant lenders*. These parties are only relevant to those syndicated loans with a general syndication or sell-down phase (i.e. they would not be present in a club deal which has no formal syndication phase). These enter the transaction after the MLAs have been mandated and the loan structure and terms agreed with the borrower/sponsor. They can include smaller banks and/or non-bank investors such as debt funds (e.g. investing in Collateralised Loan Obligations, CLOs), hedge funds or institutional investors (i.e. pension funds and insurers).[19] Large ticket holders among the participants (e.g. relationship banks or large non-bank investors like debt funds) are sometimes called 'arrangers'. These may be appointed before the general syndication phase but would not have taken any underwriting risk.[20] Institutional investors would participate in the Term Loans, whilst banks (usually the lead banks) would also participate in the revolving credit facility.
- *Credit ratings agencies.* Ratings agencies provide (private, or increasingly public) ratings for syndicated loans,[21] driven largely by institutional investors' demand, e.g. those investing via CLOs. (Our fieldwork shows that banks and non-bank lenders would undertake their own internal credit rating process).

Deal structure and distribution methods

We describe here the structure of syndicated loans across LBOs, PF and INFRA loan purposes, and the ways such loans are distributed among lenders. The description of the structures is similar across these loan segments, although we draw out differences where relevant. Distribution methods vary more between LBO and PF/INFRA loans, which we describe separately.

Deal structure

A deal will generally be divided into different tranches, i.e. different forms of credit which may be priced differently and which would appeal to different types of lender/investor. Tranches constitute the key unit of reference for syndicated loans as each tranche might be activated in a different period of time, be granted a different loan amount, have a different number of lenders or be traded in the secondary

[19] Non-bank lenders are increasingly active in the syndicated loan market, in particular for LBO loans, as syndicated loans become an established asset class for institutional investors seeking alternative investments and higher returns. We discuss this in more detail in our report.

[20] This refers to the practice of 'early-birding' whereby investors are brought onto the side of the initial negotiations ahead of the general syndication phase. This can be to provide views on market appetite of the emerging terms, and/or so be allocated a share to support the subsequent marketing of the loan. We discuss this in more detail later in this section.

[21] Ratings are provided for the loan instrument directly, or for the borrower — with the rating of the loan then derived from the rating for the borrower.

market. The number of tranches in a deal is typically a good proxy for the size of the loan, i.e. the larger the number of tranches, the bigger the loan.

Each tranche can have a different priority level in being repaid if the company decides to liquidate. More than 98 per cent of the tranches within our data sample are classified as "Senior", meaning that together they represent a company's first level of liabilities, typically secured by a lien against collateral.[22] This applies in all segments. This means that the interest and capital payments to such senior creditors rank ahead of others (subordinated creditors) both on an ongoing basis and, in particular, in default by the borrower. In the latter case, such senior creditors gain some degree of control over the process and, if the worst comes to the worst, such senior creditors will achieve much better recovery of outstanding debts than subordinated creditors. This makes the debt lower risk than otherwise, but with a commensurately relatively lower return for lenders.[23] We discuss refinancing and restructuring further in Chapter 3.

Linked to this seniority feature, a further sub-categorisation of tranches relates to the loan facility provided. More than 70 per cent of the tranches in our sample are classified as either a Revolver Credit Facility (more than 1 year) or a Term Loan (these can also be further sub-categorised as Term Loans A or B in more complex financing structures). The revolving facility is a form of senior bank debt that acts like a continuous credit source for companies and is generally used to help fund a company's working capital needs. A company will draw down the revolver up to the credit limit when it needs cash and repays the revolver when excess cash is available.[24] This is a feature of the vast majority of LBOs, but is less common in PF/INFRA. In the latter, when the project is still in the construction phase, there will be little or no working capital to finance and no cash flow being generated. Therefore, in such cases, cash needs to be derived from structural sources of finance (such as a VAT facility, a loan to finance the build-up of VAT balances prior to any reimbursement by the relevant tax authorities).

A Term Loan allows the borrower to draw funds within a predetermined (usually short) time period. The repayments can be done either through a lump-sum payment of via a scheduled series of repayments. There are some differences in terms of typical debt structure between PF/INFRA on the one hand and the LBO segment on the other. In particular, the LBO segment will distinguish between types of Term Loan (specifically A, B) which have different characteristics and can appeal to different types of investor. (To a degree, Term Loan A and Term Loan B are broadly recognisable debt products within the LBO segments). In an LBO, a Term Loan A is typically amortized evenly over 5 to 7 years whereas Term Loan B usually involves nominal amortization over 5 to 8 years, with a large bullet payment in the last year. Term Loan B allows borrowers to defer repayment of a large portion of the loan, but is more costly to borrowers than Term Loan A.[25] PF/INFRA loan durations may be similar, but can equally be adjusted dependent upon the nature of the underlying transaction (as a general rule of thumb,

[22] Other debts will be subordinated to the senior debt. However, the senior tranches may not rank equally (i.e. some may be 'more senior' than others). This would be mediated by an inter-creditor agreement.

[23] If a company goes bankrupt, senior debtholders are the most likely to be repaid, followed by junior debt holders, preferred stock holders and common stock holders, possibly by selling collateral held for debt repayment.

[24] Revolving credit facilities differ across a number of other features such as, e.g. the presence of borrowing limits and the methodology underpinning their calculation (e.g. as a percentage of a collateral); the duration of the facility and the conditions under which this can be reset at its expiry date; whether or not the borrower is allowed to borrow in a different currency, etc. Typically the credit rating of the borrower plays an important role in determining the features available with the facility.

[25] Nandy, Debarshi K. and Shao, Pei (2010) shows that institutional loan tranches are typically designated as term loan B or higher, while bank loans are either various lines of credit facilities or term loan A.

there is greater scope for heterogeneity between different PF/INFRA deals here than between different LBOs).

The table below shows the number of deals by loan purpose and number of tranches per deal. It shows that most of the deals in our sample are composed of less than four tranches (i.e. 60 per cent of deals have 1-2 tranches and 32 per cent have 3-4 tranches) as well as that the average size of deals increases along with an increase in the number of tranches per deal.

Table 5: Number of deals by loan type and number of tranches per deal across the sample (2010-2017)

Tranches per deal	LBO	Project Finance	Infrastructure	Total	Average loan size (€mm)
1	190	100	355	645	188
2	112	63	194	369	259
3	205	34	99	338	307
4	140	29	49	218	357
5	51	7	20	78	638
6	24	5	9	38	677
7	20		4	24	876
8	3		2	5	1,020
9	2		2	4	1,592
10	1	1		2	892
Total	748	239	734	1,721	

Source: Europe Economics (using Thomson Reuters Loan Connector).

Distribution method

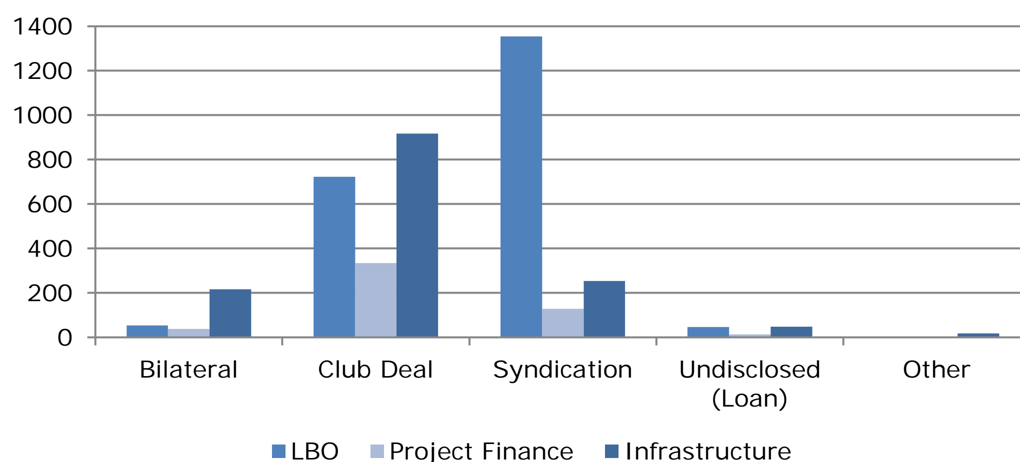
Each loan (and underlying tranches) can be characterised by a different distribution method, i.e. club deals, underwritten deals and best efforts deals, as described above.[26] [27] The distribution methods account for much of the variation between LBO and PF/INFRA loans, as we discuss in the following sections.

As we have noted already underwritten deals are most prevalent in the LBO segment and club deals are more characteristic of the PF/INFRA segment. This is supported in Figure 2 below. The standard syndication (whether underwritten or best efforts) approach to distribution applies to most LBO tranches. The use of bilateral tranches (i.e. involving a unique lender) is used only marginally (largely in Infrastructure deals).

[26] Loan Connector gathers data on distribution methods that aligns in part to these loan types – "club deal" refers to a loan that is taken on entirely by an initial banking group appointed by the borrower, with no further syndication; whereas "syndication" refers to loans that are syndicated among a wider group of participant lenders. However, no distinction is made between underwritten or best efforts deals.

[27] Loan Connector also notes where tranches are distributed bilaterally (i.e. to a single lender). Deals that are exclusively bilateral, i.e. comprising only bilateral tranches, all with the same lender, have been excluded from our sample. However, some bilateral tranches are still included in the sample if (a) they are part of deals including also non-bilateral tranches or (b) the deal include only bilateral tranches but with different lenders. An example of deals of this sort might include for instance Infrastructure deals composed of two tranches, one of which is uniquely financed by a European financial institution (e.g. European Investment Bank) and the other by another standard bank. Deals of this sort maintain a "syndicated" nature and are therefore included in the analysis.

Figure 2: Number of tranches by distribution method and loan type across the sample (2010-2017)



Source: Europe Economics (using Thomson Reuters Loan Connector).
Note: Other distribution methods include: sole lender, private placement, and undisclosed (bond).

LBO structure and distribution

LBO deals are usually sponsored by private equity groups. The presence of a sponsor could mean that the lender would assess not only the credit quality of the borrower (the target company), but also the expertise and reputation of the sponsor (with whom the banks may even have an existing relationship). Huang et al. (2014) examine how private-equity sponsors' relationships with banks influence their portfolio companies' loan syndicate structure.[28] This study found that a stronger relationship between the borrower's private equity sponsor and its lead bank enabled the bank to retain a significantly smaller share of the loan and form a larger and less concentrated syndicate. A stronger sponsor-bank relationship also attracts foreign bank participation. This would suggest that relationship banking in the LBO scenario could benefit competition in increasing the pool of eligible participants to include a more diverse syndicate.

A private equity firm may insist that syndication takes place after signing of the loan agreement, so that it takes a credit risk at signing only with the underwriters; this is often acceptable, the banks recognising that the borrower is paying substantial fees and that the process of negotiating the loan documentation may be easier with fewer parties involved, and also that the private equity house may be a regular source of business. Another reason for the difference in timing is that the private equity house may not want the market to know that it is seeking financing. The bidder needs to present a debt commitment letter to the board of the target to show that financing is in place for the bid. At the same time, the vendor may not want information about the bid to leak out to the market ahead of time and, hence, does not want the arranger to start book-running before the target receives the bid.[29]

The key distinguishing feature of LBO transactions from PF/INFRA is that they almost always take the form of an underwritten loan with a formal syndication or sell down phase. This is driven by timing considerations and the certainty of funds required – the need of the sponsor to have committed funds when bidding for a target within a

[28] Huang, Rongbing and Ritter, Jay R. and Zhang, Donghang (2014) "Private Equity Firms' Reputational Concerns and the Costs of Debt Financing". http://dx.doi.org/10.2139/ssrn.2205720
[29] Max Bruche, Frederic Malherbe, Ralf R Meisenzahl (2017) "Pipeline Risk in Leveraged Loan Syndication" Federal Reserve Board, Working paper 2017-048.

narrow time window. An LBO transaction starts well before lenders are involved.[30] In many LBOs, the company that will be the subject of the LBO is first put up for auction by the vendors. It is common for target companies to be marketed to private equity firms, who would lead an LBO, and act as sponsors for the syndicated loan.[31]

Most of the LBO tranches have a maturity of 5-10 years, with tranche structures carefully mapped to the cash flows of the company that is the target of the LBO.

Table 6: Distribution of tranches across maturities (2010-2017)

	< 1 year	1-5 years	5-10 years	>10 years	missing	Total
LBO	38	290	1,610	11	231	2,180

Source: Europe Economics (using Thomson Reuters Loan Connector).
Note: missing column refers to tranches with missing tranche maturity date.

As described later, the borrower/sponsor will incur underwriting fees in underwritten loans, which is the trade-off for the speed and certainty of funds. Underwritten loans are followed by a general syndication phase where (part of) the underwriters' loan shares are sold off to other participants. There is a high demand from institutional investors for LBO loans (at least for Term Loan elements within the funding package) and thus a general syndication may result in a lower overall price (notwithstanding the underwriting fees paid) than if the underwriters held onto their shares with no further syndication.

PF/INFRA structure and distribution

In the current market the majority of PF/INFRA loans are club deals. This reflects strong, sophisticated sponsors/borrowers able to put together the club and the fact that the timing of most projects is long enough not to necessitate underwritten deals. By having a club deal the borrower/sponsor avoids underwriting fees, i.e. effectively the MLAs are disintermediated. As such, club deals can be considered 'normal' for this segment. Although the prudential capital requirements under CRD IV have reduced the attractiveness of holding on to long-term debt, many of the bank lenders in PF/INFRA deals adopt a 'take and hold' strategy and thus do not need to materially reduce their exposure through later downstream distribution. Again drawing on the lender interviews, those banks closer to the originate-to-distribute model will aim to sell-down post-close (at least if the ticket size is large) but will retain a greater fraction of the allocation than in an LBO. Institutional investors will generally hold on to the assets acquired trough to maturity.

In some circumstances, such as if a sponsor is in competition for a green- or brown-field site where timing is more pressurised then an underwritten deal may be considered, although this is the exception rather than the norm.

There are some other specific features which can apply to project finance and infrastructure projects. The structure of a project differs from that of a corporation, and so does the structure and the features of a syndicate providing funding. Most large project finance loan packages are associated with specific construction projects. Such loan packages are often complex, international financial deals involving a vehicle

[30] Stapled finance would be an exception to this. Here the seller of a company could arrange a financing package with a bank or with a syndicate. The company would then be auctioned with the financing offer "stapled" to it. This is most often used where an eventual sale to a private equity house is anticipated. See Aslan, H. and Kumar, P. (2014) "Stapled Financing, Value Certification, and Lending Efficiency". http://business-school.exeter.ac.uk/documents/Seminars_by_visitors/Stapled_AslanKumar_October2014.pdf.
[31] When the vendor is itself a private equity firm, the subsequent LBO would often be termed a secondary LBO (in contrast to the 'primary' LBO executed by the first private equity firm).

company owned by multiple sponsors, and are arranged to fund development of large, tangible-asset-based projects. The loans can often be guaranteed by third parties (though the entire package rarely is — only individual loan tranches), and the projects can be located in relatively risky countries.[32]

Where an asset (e.g. a toll road or a wind power plant) is being built there may be an intention to refinance once that asset is operational. This is partly because fewer lenders (particularly institutional investors) have the necessary appetite for projects with construction risk – but also institutional investors tend to prefer tranches/deals where the commitment is made on day one (i.e. all the money is put to work on day one, rather than subsequently drawn down). (This is also reflected in reduced appetite for revolving credit facilities in LBOs). This means there is less appetite amongst institutional investors during the construction phase than in the operational phase. This is why the financing of the construction of PF/INFRA is sometimes characterised as being a 'bank market'. However, some institutional investors have emerged recently with revised (i.e. lower) expectations around yield in what continues to be a low real interest rate regime and displaying willing to take on such construction risks (indeed, we understand that some deals are currently being structured such that particular tranches can be marketed directly to such investors, who may be more willing to write large ticket debt). This is facilitated by growing access to internal expertise at such investors (e.g. they have hired individuals or teams with the relevant skills as a pre-condition to increasing such investments). The evolution of the participation of non-bank investors is addressed in more detail in Chapter 3.

Infrastructure and Project Finance loans tend to have a longer time-to-maturity period than LBO tranches, corresponding to long project timelines. In particular, more than half of the Infrastructure loans have more than 10 years.

Table 7: Distribution of tranches across maturities (2010-2017)

	< 1 year	1-5 years	5-10 years	>10 years	missing	Total
Project Finance	16	175	76	191	61	519
Infrastructure	45	271	184	731	221	1,452

Source: Europe Economics (using Thomson Reuters Loan Connector).
Note: missing column refers to tranches with missing tranche maturity date.

Debt advisory activity

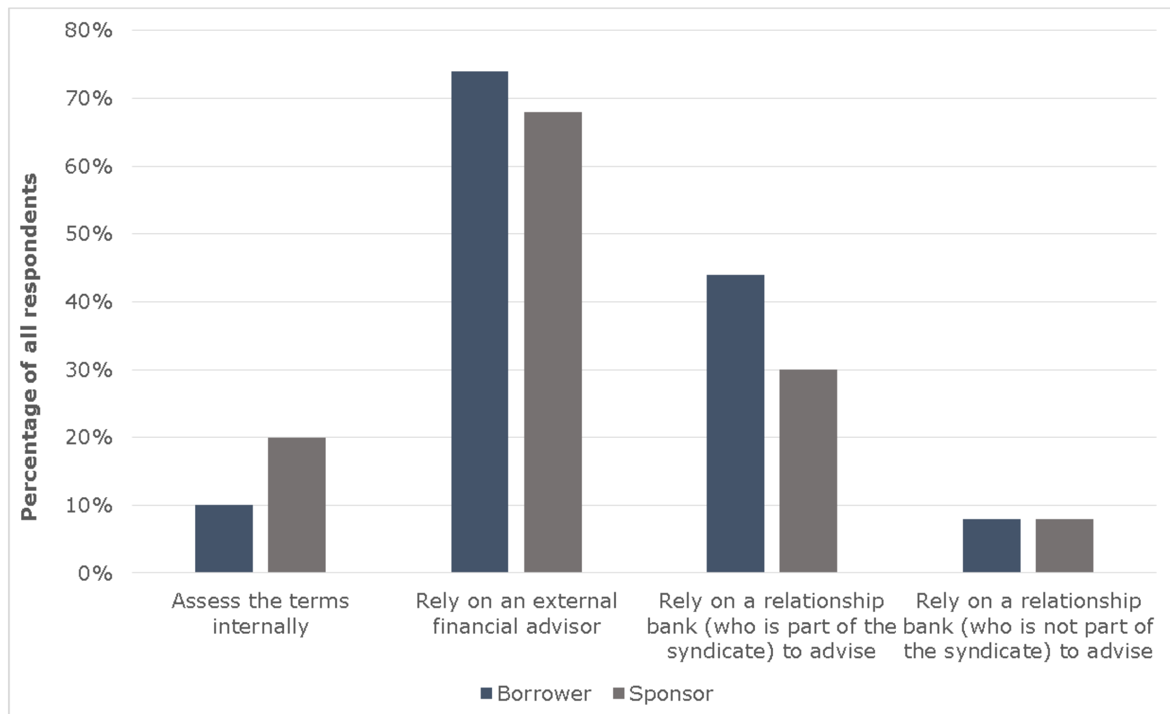
A feature of all of the market segments is the presence of debt advisors, acting on behalf of the borrowers/sponsors. Advisors have extensive experience in loan transactions and essentially drive the transaction on behalf of the borrower/sponsor, often taking on certain of the traditional activities of the lead arranger such as advising on the structure and term of the loan, and managing the information flows to, negotiations with and appointment of MLAs.

Advisors can enhance the efficiency and competitiveness of a syndicated loan transaction, providing the borrower/sponsor with a sophisticated and experienced agent (e.g. able to negotiate bilaterally with competing banks and avoid the need for lender cooperation at the pre-mandate phase, and also to put pressure on loan tenor, terms and pricing) and reducing reliance on a lending bank who may have conflicts of interest (insofar as the advisor itself is independent of the lending group). The presence of an advisor also adds resources, which can mean that staff at the borrower are less distracted from quotidian activities by the demands of the process. Advisors also contribute to the 'bargaining power' of borrower/sponsors.

[32] Kleimeister and Megginson (2000) "Are Project Finance Loans Different from other Syndicated Credits?"

Our lender fieldwork suggests that a diminution in the role of lead arrangers has been facilitated by the increased use of advisors, as well as increased investment by borrowers and sponsors in internal debt financing teams. The use of advisors is common, with both lenders and borrowers reporting their presence on deals. For example, our borrower/sponsor fieldwork indicates that in assessing the terms of the loan, the minority rely only on their internal capabilities (10 and 20 per cent across borrowers and sponsors respectively selected this option), whilst the rest rely on advisors.[33]

Figure 3: Borrower and sponsor assessment of loan terms



Source: Europe Economics and YouGov fieldwork. B29/S31 "Do you usually receive any external aid in assessing the terms of the loan?"

As can be seen in the chart above, the most common method across borrowers and sponsors is to rely on an external financial advisor (74 and 68 per cent across borrowers and sponsors respectively) or a relationship bank that is not involved in the syndicate (eight per cent of borrowers and sponsors). Relatively more borrowers would also rely on a relationship bank that is part of the syndicate compared to sponsors (44 per cent compared to 30 per cent). We note that this fieldwork question did not ask about the role of advisors more generally in the syndication process (e.g. in appointing the lead banking group and negotiating terms), but can be taken as a good indication of advisor involvement.

The appointment of advisors may itself be done through a competitive process, or an advisory firm or relationship bank may be appointed directly. We do not have sufficient evidence to comment on which approach is most common, but discuss the potential risks associated with the appointment of the advisor in Chapter 4.

[33] Fieldwork question B29/S31: "Do you usually receive any external aid in assessing the terms of the loan?" We note that this question does not ask about the use of advisors throughout the syndication processes (e.g. in setting up the initial banking group).

LBO loans

Our borrower/sponsor fieldwork shows that in terms of assessing the loan terms, borrowers and sponsors in LBO loans are less reliant on the advice of relationship banks who are part of the syndicate compared to those in PF/INFRA loans – 32 per cent of LBO respondents compared to 48 per cent of PF/INFRA respondents.

In terms of overall advisory services, in the LBO segment advisors are largely characterised as being independent, even boutique-based.

PF/INFRA loans

However, in the PF/INFRA market segment it is not uncommon for the advisors to be a discrete unit within a lending bank. This is supported by our lender fieldwork and borrower/sponsor fieldwork (where 48 per cent of PF/INFRA respondents have used a syndicate bank to help assess loan terms). The banks have adopted various strategies for providing both advisory and loan services, with most maintaining clear separation between advice and lending decisions. For example, the advisory unit would generally have no balance sheet capacity, and would be 'wall-crossed' from the origination and syndication desks once mandated.

However, our lender fieldwork shows that some banks appear to be more relaxed about bundling these offerings to clients. There can be an expectation from the client that a substantial portion of the lending would come from the bank providing the advisory services, particularly if raising the necessary funds for the deal proves difficult. For this reason, at least, such bundling can be an attractive feature to some borrowers/sponsors. (It could even be argued that, at least in current market conditions, such a pro-bundling strategy could result in adverse selection problems for the bank).

The case where a syndicate bank is also acting as an advisor poses a risk of a conflict of interest, whereby the advising bank may be able to influence the borrower/sponsor towards its own preferred loan terms. We explore this risk in Chapter 4.

Types of loan process in LBO and PF/INFRA segments

The process of loan syndication is complex, with many variations depending on the deal circumstances and distribution method used. The greatest variations exist around the following key stages:

- The formation of the lead banking group,
- the formation of the general syndicate, and
- post-closure (including secondary trading).

In the sections below we describe the process steps under each of the three key stages, drawing out the differences between LBO and PF/INFRA loans where relevant.

Formation of the lead banking group

There are various means by which a syndicated loan may be originated and formed. We describe here the typical process, and draw out separately key differences between LBO and PF/INFRA deals below. For our purposes, the "lead banking group" is the group of banks initially appointed by the sponsor/borrower, usually the MLA(s) and the main capacity providers. This could be in circumstances where further syndication is anticipated (such as an underwritten or best efforts deal for LBOs), or in some circumstances the entire syndicate (a club deal for PF/INFRA, where generally no further formal syndication occurs after the appointment of the lead banking group).[34]

The process of forming the lead banking group typically consists of the following steps:

- The borrower/sponsor or advisor issues an invitation to potential lead banks (MLAs) to participate in the loan, usually through a competitive request for proposal (RFP).
- The banks bid for mandates, either individually or in consortia.
- The borrower/sponsor or advisor negotiates key terms with each bank/consortium and develops a final term sheet.
- The banks agree and sign the final terms.
- The borrower/sponsor or advisor mandates banks and assigns roles where relevant (e.g. bookrunner) and authorises the MLAs to meet and agree a common set of loan documentation.

The process of appointing the lead banks in LBO and PF/INFRA loans is driven by the sponsor/borrower (sometimes assisted by a debt advisor, as discussed under ancillary services), who will have in mind a set of lenders to approach based on prior transactions, ongoing relationships, or the lenders' product/geographic expertise. The past experience of the borrower/sponsor, as well as publicly available deal information and the lenders' own strategic marketing efforts (i.e. attempts to signal interest in working with a particular sponsor, such as offering views on the structure of the financing or options for the client to consider), inform this initial selection. The borrower/sponsors (or their advisors) in the LBO, PF and INFRA loan markets are generally sufficiently sophisticated and experienced to drive this selection process. In some cases a bank will be approached by a sponsor due to its relationship with the underlying borrower or target, e.g. if it is currently providing commercial banking services.

Typically the sponsor/borrower[35] would issue a Request for Proposal (RFP) to individual banks, through which the banks would compete individually to lend or underwrite the loan (depending on whether a club or underwritten deal) and/or compete for fee-paying roles. An alternative scenario suggested in the literature (e.g. Rhodes (2009) "Syndicated lending: Practice and Documentation") is where the RFP invites (or consents) to a bank consortium / consortia being created for the purpose of the bidding stage. The consortium could be requested to pitch its expertise / strategy jointly, whilst potentially to bid separately across the individual banks on pricing elements. Multiple consortia may compete for the lending mandate. There is limited evidence from our fieldwork that this happens in practice – none of the lenders indicated that they participate in such consortia, although some borrowers did state that they can accept bids from pre-formed consortia as well as from individual banks.[36]

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[34] The LMA's guide to Syndicated Loans notes that this group of initially appointed banks can also be known as co-arrangers.

[35] Where an advisor is used, the advisor may undertake the majority of liaising with the lenders.

[36] Fieldwork question: B6 "Which procedure(s) do you usually follow when the MLA(s) are appointed in this transaction?" to which 40 per cent of borrowers said they issue a competitive RFP for funding from

This may be preceded by a short, more informal stage where views on general appetite and structuring ideas are sought from banks, usually (but not always) relationship banks. This input could be provided by the origination desks in the lending teams within such banks or even by relationship bankers. The influence of these initial discussions may limit the competitive outcome of the RFP process if relationship banks are able to unduly influence the proposed loan structure or set of candidate lead banks in their favour. This impact will depend on the sophistication of the borrower/sponsor in developing the RFP (and if these are not highly sophisticated, whether independent advice has been sought), selecting the candidate banks to approach and assessing the competing bids, and the number of other candidate lead banks who would participate in the RFP process. We explore the competitive implications of this in Chapter 4.

At this stage all banks are competing individually and all discussions are bilateral between each bank and the borrower/sponsor. Banks typically would not know the identity of their competitors, but might be aware of approximately how many there are. The request for proposal is accompanied by a non-disclosure agreement (NDA), which requires the banks not to discuss any or all aspects of the proposal as a pre-condition to the sharing of some information about the transaction. We describe these information flows in more detail under the LBO and PF/INFRA sub-sections in this chapter.

The RFP process means that the key terms of the loan (fees, margins, documentation, flex provisions etc.) would be negotiated and agreed bilaterally between the borrower/sponsor and the competing banks, and the borrower/sponsor would use the competitive bidding process to secure the most attractive terms overall and use this as the basis for inviting banks to form the core lending group. In its ultimate form, this can involve the production of a 'grid' by the borrower/sponsor (or their advisers) that summarises the key terms (potentially over several pages), and requests the competing banks to complete the most important economic elements (i.e. margin, fees, etc.) We describe this process further below.

The exchange of grids is not a one-off: once received back from the potential MLAs, the borrower/sponsor may seek to cherry-pick its preferred terms into a revised grid – which would again be sent back to the banks involved in the RFP. At this stage of the process banks may decline to participate (and others may then be invited to participate) based on the borrower/sponsors' initial invitation – for example if the borrower/sponsor invites banks to participate at the best (lowest) price offered by one or more of the banks, some banks may not be willing to participate at that price. Whether the borrower/sponsor will be able to achieve that price will depend on whether enough banks are willing to provide the level of financing that the borrower requires. The price may need to increase if particular bank(s) required cannot commit to certain hold levels other than at a particular price (which is why it is valuable to have some redundancy in the banks involved in the process, to avoid pricing at the highest common denominator amongst the banks). This dynamic is an essential element of the formation of the single price which is inherent in the multi-bank loan process. If views are very different across the pool of lenders it may result in a change to the structure of the loan to better meet the borrower's objectives (e.g. a given level of debt at the lowest possible price).

The borrowers/sponsors seek to build in some redundancy contacting more banks than they wish to appoint as MLAs. That said, in our borrower/sponsor fieldwork, where the

individual banks and 49 per cent they use an RFP for funding from individual banks and consortia. A further 4 per cent used a public approach. Altogether then 93 per cent use RFP (or an equivalent approach).

RFP process was used most borrowers and sponsors indicated that they would not typically approach more than 4-5 potential MLAs. This is below the levels indicated in the lender fieldwork, where approaches to 10+ banks were cited as common (such broader-scale approaches were not unknown in the borrower/sponsor fieldwork, but these did not appear standard). When we compare these numbers with the number of actual MLAs recorded per Loan Connector, there is a further apparent mismatch in that the number of lead arrangers appointed does not differ significantly from the borrower/sponsor fieldwork's views on those approached. One explanation, at least in the LBO space where underwritten deals are most common, is that loan syndication process can be subject to title inflation, whereby those lenders listed as MLAs at the end of transaction include banks which have not truly played the economic role of an MLA. Equally, the banks approached to act as an MLA for an underwritten transaction may be characterised in two ways: those able to act as underwriters and successfully distribute debt – i.e. the MLA function - and those that are essentially being asked to provide balance sheet capacity. Ultimately, the number of banks approached bears some relation to how much is being raised and the expected likelihood of receiving offers from those banks approached.

Another way of thinking about this is what happens when an MLA underperforms. The majority (54 per cent) of borrowers and sponsors had not experienced any such issues across their syndicated lending transactions, with others able to replace the MLA or for other MLAs to rescue the situation. Four respondents in each of LBO and PF/INFRA (i.e. 8 per cent of the sample) identified a lack of suitable alternatives as the reason for non-replacement of the MLA. We need to exercise some caution in interpretation here, however, in that within the context of a transaction (certainly an LBO) there are time constraints meaning that a suitable alternative may not be identifiable in time.

In some LBO transactions, specifically public-to-private or P2P deals, sponsors may be unwilling or unable to go to more than a couple of potential MLAs. (Debt advisers we interviewed were clear, however, that only approaching one would be highly unusual even then). In most LBO deals, however, there is likely to be some form of auction process whereby the target for the LBO is itself being marketed. In such a case the banks do not get paid for helping with losing bids – fees are payable only post-mandate. In this case, then, any attempt at collusion has to cover all banks possibly approached by at least one private equity sponsor - otherwise it could be self-defeating as more costly debt would limit the bid being made by the private equity sponsor.

LBO tranches tend to end up with – on average - a larger number of MLAs than PF/INFRA. There is not a straightforward interpretation to this finding, although on average larger deals than Infrastructure, they tend to be below the size of PF deals (under our definition). LBOs will often be underwritten (at least for the initial LBO), as we have described above, whereas the other two segments are typically club deals. Equally, the average LBO in our dataset has three tranches, whereas the average PF/INFRA deal has about two. These factors would drive the involvement of a larger pool of lenders than infrastructure and project finance deals, even though it is not clear that these deals are per se more complex.

Table 8: Average number of lead arrangers by Member State and loan type (2010-2017)

	LBO	Project Finance	Infrastructure	All loan types
DE	4.4	2.9	2.9	3.9
ES	4.0	3.3	4.8	4.3
FR	3.8	3.8	2.4	3.4
NL	4.5	2.4	3.6	4.1
PL	7.3	1.0	2.6	4.8
UK	4.2	4.1	4.1	4.1
All countries	4.2	3.7	3.7	3.9

Source: Europe Economics (using Thomson Reuters Loan Connector).

The MLAs involved in a deal tend to remain the same across all the tranches in a deal as the syndication process typically occurs at the deal level (this holds in 78 per cent of deals). However, there is a significant minority (22 per cent of deals) where variation of the lead arrangers group happens within the same deal (Table 9). As can be seen in this table, even when the MLA group is not the same across all tranches, the composition of the MLA groups does not tend to vary very much. Banks are taking on risk (credit risk) with each tranche that they participate in. A bank will have different, evolving appetites for revolver, Term Debt etc. that will affect their willingness to bid aggressively to sponsors. Similarly, where a general syndication is intended, different potential MLAs may vary in their expectations around their distributive capacity / capability between tranches. The ability of sponsors / borrowers to differentiate between MLAs in this way is facilitated by the way in which sponsors approach banks (as described further below).

Such variation in MLAs is correlated with deal size (last column of the Table). There is no significant difference in pattern between LBOs and PF/INFRA with respect to this feature. Similarly, there is no clear difference at the Member State level, with the partial exception of Dutch borrowers where the proportion of deals with MLAs varying (at least partly) by tranche increases to 35 per cent.

Table 9: Number of deals with varying lead arrangers across different tranches (2010-2017)

Changes in MLA group	LBO	PF	INFR	Total	Average deal amount
0	586	180	531	1,297	244
1	111	38	128	277	396
2	24	9	24	57	645
3	8	5	16	29	626
4	1	2	6	9	1,345
5		1		1	1,467
6			1	1	1,872

Source: Europe Economics (using Thomson Reuters Loan Connector).

The borrower/sponsor may have a clear idea of the 'relationship banks' that it would like to have on the deal, or it may proceed entirely on the basis of price/terms. A borrower/sponsor's final decision as to which banks to include in the group will be based on margins, fees, hold-levels (if applicable), reputation and track record, (potentially) the ability to provide ancillary services such as swaps, payment services and trustee/custodian services, and the number of banks that the borrower wants to be in the consortium.

Formation of the lead banking group in LBO loans

The formation of the lead banking group in LBO loans is usually a rapid process, particularly if the company that will be the subject of the LBO (i.e. the target company) has been put up for auction by the vendors (which is often the case for those LBOs entering the syndicated loans market). The sponsors to whom the target company has been marketed would need committed funding to finance the LBO ahead of the closure of this auction, and therefore there is time pressure to secure the funding before the end of the auction being run by the M&A advisers to the target's company's owners. The interaction between the sponsor and the lead banking group (i.e. the issuing of RFPs and negotiation of terms) therefore typically occurs during the auction for the target company.

At this point, each sponsor might be contacting multiple banks – with the larger banks generally willing to operate multiple "trees" within origination (and sometimes even syndication) teams such that they are working with multiple sponsors. The rationale for approaching a large number of banks (our lender fieldwork indicates this can be up to 20) is to ensure capacity in the limited time available. In some cases, such as public-to-private transfers (where only one bank may be appointed, and confidentiality is critical) the sponsor may only approach two to three candidate banks to limit the number of lenders who are aware of the deal. Sponsors will seek to maintain competitive tension regardless of the number of banks approached (e.g. by not disclosing the number of candidate banks).[37] As sponsors are often in a competitive situation themselves they have an incentive to ensure a competitive process for raising debt (i.e. if a sponsor does not secure competitive debt terms, then it will likely not win an auction).

Depending on the circumstances of a transaction, banks may have more or less room to propose and negotiate the structure and terms of the loan with the borrower/sponsor. In LBO loans, the borrower/sponsor usually already has a very clear idea of the terms it wants (for example based on past transactions), and LBO loans tend to be more consistent in structure terms and pricing; therefore banks will often receive a 'grid' covering all the terms, including pricing, which they would either complete (if cells are empty) or else accept / propose changes to. This also supports a more time-pressured deal process compared to PF/INFRA loans. Banks would also likely be required to outline features such as their intended hold levels, experience, syndication strategy and views on the way the loan will price in the market as part of their bids.

Sponsors could also seek initial informal views from potential lead banks before issuing an RFP, to assess initial interest. More detailed pre-RFP conversations regarding for example how much could be raised on the market, how the loan would be perceived, acceptable leverage multiples etc. would be less common. These discussions would be under NDA, and the sponsor would then issue an RFP and pricing grids. Our lender fieldwork indicates that these discussions would not guarantee the bank's involvement in the loan (it would still need to bid through the RFP and grid process), and that the borrower/sponsor retains control over which candidate banks are invited to participate The first phase usually entails two to three rounds of 'grid exchange' between the sponsor and each bank (which can last for a few weeks or less), with each round narrowing down terms. During this phase some banks will drop out if they cannot meet or agree to the terms.

[37] Our borrower fieldwork supports this, although does leave room for the direct appointment of MLAs. For example, for the fieldwork question: B6 "Which procedure(s) do you usually follow when the MLA(s) are appointed in this transaction?" In response, 91 per cent of borrowers stated they use a competitive RFP process, and 9 per cent stated that they would directly appoint an MLA without a competitive process (these responses were split evenly across PF/INFRA and LBO loans).

After the initial exchange of grids, the remaining banks would enter a second phase of negotiation with the sponsor to arrive at final, committed bids, which can last between two and three weeks. The sponsors need to commit to funding and they will seek — on a bilateral basis — binding funding commitment letters from all banks left in the process (operating a 'N + x' model with built-in redundancy). Since financing is committed, all terms need to be negotiated at this stage (including the provision for flex, which we describe under the general syndication phase) and credit committee approval obtained. At this stage of the negotiations the borrower/sponsor would also consider which banks to appoint to various fee-paying roles, such as active bookrunner.

Once each bank or lender agrees to the final terms, various documents, which form part of a syndicated loan transaction, are signed to finalise their participation in the loan, such as a commitment letter (i.e. post-credit committee), mandate letter and term sheet. The final syndicated loan agreement is also typically signed at this point containing the loan terms – these may be subject to change during the general syndication round in an underwritten or best efforts transaction (i.e. through flex as described later).Fee letters are also usually distributed at this stage: these would detail any fees payable by the borrower and are usually contained in letters separate to the main loan agreement to ensure confidentiality. These fee letters are sent out by the borrower to the members of the syndicate with fee-paying roles (e.g. the lead arrangers, agents etc.). The loan agreement should refer to the details contained in the fee letters.[38] (We discuss fees further in the Chapter 3 section "Fees").

In some LBO transactions, particular participant lenders (for example an institutional investor who would take a large ticket) with no fee-paying roles may be included in the negotiations at this stage, ahead of the general syndication phase. These would be 'early bird' investors. The rationale for this would be either to allow the investor more time to engage in the transaction (as a preferred investor), or as a means of testing the deal with the investor market at a stage when the terms of the trade are still relatively fluid. Investors would sign an NDA to receive information on the deal. Institutional investors may choose not to be involved if such early engagement prevented or restricted trading opportunities available to those investors. The early-bird investors would be approached either by the borrower/sponsor or advisor, or by one of the lead banks on instruction by the former.

As and when a sponsor wins its auction, its lead banking group would ultimately be responsible for underwriting the senior loan facility, which is commonly structured to incorporate both multiple term loan facilities and a revolving loan facility.[39] The arrangers underwrite the term loan facilities and revolving facilities in order to fund the:

- senior element of the buy-out,
- refinancing of existing debt in the target group, and the
- working capital and capex requirements.

It is only at this stage, i.e. once all the lead banks have been mandated, that they are brought together by the client to discuss the general syndication strategy and agree

[38] Other documents relevant to a syndicated loan are created later in the process, for example the Information Memorandum is usually provided to potential syndicate participants at the beginning of the general syndication phase. We describe this in the relevant section below.
[39] In an LBO, the debt part of the financing package consists of a senior facility (usually provided by banks), a junior facility (riskier and high yield debt provided usually by institutional investors), and often a quasi-equity facility, such as mezzanine debt. See the LMA Guide to Syndicated Loans.

and sign a common set of loan documentation. At this point, as part of the syndication preparation, banks can also finalise with the borrower/sponsor a 'white list' of participants (smaller banks and institutional investors) that will be approached in the general syndication phase (the sponsor's initial take on the white list would be a key part of finalising terms – as an underwriting bank would need to understand how much of the market it can approach in the general syndication phase in order to lay off its risk). We describe the use of white lists in more detail in the section on the general syndication process.

Information sharing and market sounding in LBO loans

As described above, the negotiation of key terms is conducted primarily at this appointment of the lead banking group. In LBO loans this negotiation takes place bilaterally between the borrower/sponsor and the individual banks/lenders. There is seldom scope for banks to discuss the transaction externally at all until such time as the terms have been agreed and the banks mandated. Banks' processes require explicit borrower consent to engage in pre-mandate sounding on the specifics of a transaction.

In preparing their responses to the RFP or grids, our lender fieldwork shows that lenders' decisions on risk, margins and hold amounts are informed by a number of information sources, such as:

- Knowledge of investor sentiment (as well as of precedents for contract terms and covenants), as expressed in the general syndication phase of current and recent internal deal flow, i.e. live primary market deals, as well as the secondary market response to these deals if they are closed. Those banks with greater deal volume should have an advantage here.
- Secondary trading activity in loan markets and bond markets, either through internally held data or via independent data vendors such as Bloomberg and Markit, which collect both venue-traded and OTC data.
- Data such as leverage multiples on comparable loan deals (e.g. comparable industries, loan types, countries, transaction amounts), whether the bank was involved or not. Where the bank was involved, it will have access to detailed information. These data are also accessible through independent data vendors. Dealogic's Loan Analytics and Thomson Reuter's Loan Connector are two commonly used loan databases. The information on transactions contained in these databases includes over one hundred fields on the primary transaction (from pricing data through to descriptions of the borrowers and the banking group, down to detail on covenants). Against this, since it is a private market, these fields may not always be complete. Indeed, as we note in our analysis of pricing and fees, in particular, such economic details are more often omitted. These are on a subscription basis but otherwise available to all market participants willing to pay. These databases also have secondary trading data (such as iQuery in Thomson Reuters, which collects non-executable pricing information from broker-dealers on a daily basis for about 250 more actively traded loan tranches).
- Assessments of current market liquidity, e.g. through assessing public and/or data vendor information on flows into high yield bond funds and CLO formation.

Lenders active in LBO loans consider such data to be much more readily available than in the past, with multiple data vendors competing to provide such transparency.

Our lender fieldwork shows that the syndication desks of banks do not engage in deal-specific market 'soundings' or 'reads' with other potential lead banks or participant lenders related to the details of the transaction to inform decisions made about risk, margins and hold amounts. However, lead banks do maintain relationships with key participants (i.e. particularly institutional investors) relevant to the general syndication

phase and discuss *generic* issues with them (e.g. investors' appetite for loans in certain sectors) to ensure they keep up to date with market appetite. These generic market soundings are important for underwritten and best efforts loans where the lead banks will need to syndicate the loan to further participants, and as such need to be aware of general market appetite. It would also be relevant to a club deal, if there is intent to sell down part of the loan subsequently. The boundary between generic and specific sounding can, however, become somewhat blurred when there are live transactions in the sector that is the subject of the 'generic' discussion or where the sector is somewhat atypical (so that a meaningful understanding of appetite requires additional information-sharing). We note that some papers have suggested a greater use of market soundings than reflected in our lender fieldwork.[40] Indeed, lenders characterised a step change from such specific soundings to current practice as happening several years ago – enabled largely by the growth of the syndicated loans market and of its investor base.

The lender fieldwork highlights that where deal-specific soundings are still made, particularly where liquidity is low and there is uncertainty around how a loan will price in the market, these are conducted under borrower consent and with defined information-sharing parameters. We explore the potential risks associated with market sounding (e.g. around the boundary between generic and specific discussions) and information sharing in Chapter 4.

The flow and timing of information throughout the process of forming the lead banking group is set out below.

- The first step is for the borrower/sponsor to approach candidate banks with an RFP and to sign an NDA which prohibits speaking to anyone else about the deal ahead of the sharing of information. If banks' views are solicited before the issuing of an RFP this is also likely done under NDA.
- In the first phase, when the grid exchange is taking place between banks and the sponsor, banks would be given vendor due diligence (most deals will be competitive process for sponsors, organised by the current owners of the target of the LBO which would provide the due diligence) or other preliminary data about the target from the sponsor.
- After the initial exchange of grids, the remaining banks who are still committed to the transaction (some would have dropped out in the first phase) would enter a second phase of negotiation to arrive at final bids. More information would be available to enable them to make firm bids, for example buyer due diligence (which may have a different perspective to the vendor-commissioned due diligence) and management forecasts from the target. The NDAs would apply throughout this phase as well.

The sharing of specific information related to LBO transactions is governed by NDAs between the borrower/sponsor and the lead banks, such that banks would be contravening contractual agreements with borrower/sponsors if they did engage in specific market soundings (i.e. the process as set out here does not in itself facilitate such information sharing, but there is still the possibility for lenders to do this illegally). This would have implications for competition in terms of increasing the risk of collusion between lenders – we explore the competition implications of this in Chapters 4.

[40] For example Rhodes, T (2009) "Syndicated lending: Practice and Documentation", Euromoney Books and Bretz, Oliver, "Competition law and syndicated loans: identifying the regulatory risks", 2015 http://www.jordanpublishing.co.uk/system/froala_assets/documents/1553/CLJ_article_-_Comp_Law_and_Syndicated_Loans.pdf.

Formation of the lead banking group in PF/INFRA loans

As with LBO loans, PF/INFRA deals may begin with the borrower/sponsor or the advisor to the borrower/sponsor issuing an RFP to selected banks, each of whom would respond individually in order to compete for the opportunity to lend part of the loan. In some cases, invitations may not involve a formal competitive RFP, but rather discussions between each selected bank and the borrower/sponsor or advisor. The number of banks approached varies, although borrower/sponsors tend to approach around double the number they intend to finally appoint, and build latency into the final bids (e.g. they might approach 10 banks with the view to appointing six, and then have these commit to a third of the loan amount).

As noted earlier, clients may hold pre-RFP discussions with selected banks. These are usually informal (either based on publicly available information or else private information subject to NDAs), and used by the client to inform its views on loan structure and terms and (potentially) market appetite before issuing the RFP. Our lender fieldwork indicates these pre-RFP discussions are more common in PF/INFRA loans compared to LBO loans, and can be particularly useful for bespoke loans with little precedent in terms of structure and terms. The process would then usually formalise into an RFP process. The risks associated with the influence of the relationship banks engaging in early informal discussions are explored in Chapter 4.

Competing banks will respond to the RFP or invitation with proposals outlining features such as their hold levels, experience, syndication strategy and views on the way the loan will price in the market. The use of 'grids' is less common in PF/INFRA deals than with LBOs, although these can be used and can range from only a few dimensions proposed by the borrower/sponsor to more prescriptive detailed grids.

The negotiations around pricing and terms would take place bilaterally between the competing banks as outlined in the general process description above. At this stage the borrower/sponsor would also consider whether and which banks to appoint to fee-paying roles, such as a coordinator.

Once each bank or lender agrees to the final terms, a number of documents are signed to finalise their participation in the club, such as a commitment letter (i.e. post-credit committee), mandate letter and term sheet. The final loan terms are also typically signed at this point, and in PF/INFRA (by virtue of being club deals) no further change usually occurs.[41]

It is only at this stage, i.e. once all the lead banks have been mandated, that they generally are brought together by the client in to the club to agree and sign common legal documents.

The process for forming the initial lead banking group described above is definitely the standard process adopted in most instances (particularly in western Europe). However, our lender fieldwork shows that more 'traditional' models are still in use – for example where the borrower/sponsor (whilst still taking the final decision on which lead banks are included in the group and what the final terms are) relies more heavily on a lead bank who would drive the formation of the bank group and the negotiation of terms with those other banks.

[41] If a PF/INFRA loan were to be syndicated further through an underwritten or best efforts distribution method, a 'general syndication' process would apply. As noted however, the majority of PF/INRA deals described to us in our fieldwork are club deals.

If the borrower/sponsor mandates a single bank as a lead arranger (or coordinator), this bank would typically sign an NDA and receive information from the borrower/sponsor, then prepare a term sheet to negotiate with the rest of the candidate banks. The bank might be involved in finding partners for the club, although usually the borrower/sponsor indicates the banks it wants to approach. Usually the lead bank would share all the information it receives from the sponsor with the other club members (although again this would be agreed with sponsor). The lead bank in this instance would be the main interface between the borrower/sponsor and the rest of the club, although the borrower/sponsor would still be very involved and take the final decisions. In such a case, the lead bank will need to understand each potential participating lender's potential interest (e.g. willingness to underwrite/ hold) and at what price. The lenders then communicate between each other. If a lender(s) has a certain price requirement in order to participate at a certain level, which is higher than others, then either (i) the other lenders may be willing to accept an increased participation, (ii) there may be other lenders (not previously involved) who could be invited to participate; or (iii) if the particular lender(s) is 'needed' then the price will have to be set at the highest price acceptable within the group. This would be heavily influenced by the borrower/sponsors' set-up of bidding process, i.e. if they specify that the particular bank wanting the highest price be part of it then the MLA would not be able to replace it. Alternatively, if the consortium is bidding against other consortia or individual banks then normal market dynamics should keep pricing in check (since a high bid will not win the competition). Our lender fieldwork shows that a model where a group of banks is approached in this way is more common in PF/INFRA deals than LBO, and more so in more national, non-west European markets.

Information sharing and market sounding in PF/INFRA loans

Bilateral negotiations between the individual lenders and the borrower/sponsor in a PF/INFRA club deal follow a similar process to those in an LBO deal, whereby information is controlled by NDAs and there is little scope for lenders to legally discuss the transaction externally and share information with other banks until the terms have been agreed with the borrower/sponsor. Where no NDAs are used (i.e. in some informal pre-RFP discussions) the information discussed would be publicly available.

As with LBO loans, lenders in PF/INFRA loans rely in internal deal flow and public information sources to inform their decisions about pricing and terms, in addition to the loan-specific information provided by the borrower/sponsor. However, we note that – based at least on the sources available to us including lender fieldwork and the analysis of Loan Connector data – there are more comparators available in the LBO segment, in that pricing data is more comprehensive than in PF/INFRA, particularly in the secondary market (where LBO loans trade more actively than PF/INFRA loans).[42] All else being equal, this raises the potential for specific market soundings to be more necessary in PF/INFRA loans. A relevant counter-point is that the PF/INFRA segment is largely (but not wholly) a club deal market where the relevant lenders are approached by the borrower/sponsor directly - and there is no underwriting or onward general syndication (but there may be some post-closure downstream distribution). In other words, there is less value (to investors) in participating in a market sounding exercise – but increased value to the bank in having access to either specialist knowledge either as incorporated into particular individuals, internal experts or access to internal deal data. If these are limited, then – absent market sounding – this could represent a

[42] See Chapter 3 for a description of the secondary market for syndicated loans. Essentially, the primary market includes the original loan between the borrower/sponsor and the lead banking group, as well as any further syndication to participant banks and investors. The secondary market consists of the buying and selling of these loans between lead and participant lenders as well as other investors not part of the primary loan.

substantive barrier to entry. We discuss the competition implications of such information sharing in Chapter 4.

As PF/INFRA loans are usually club deals, there will be no further syndication phase and therefore less need for the lead banks to engage in generic market sounding with potential investors in order to assess market appetite.

In rare cases (and more likely in PF/INFRA than LBO according to our lender fieldwork), the borrower/sponsor may request banks to discuss the transaction before the signing of mandates, but this would still be client-driven. Our fieldwork suggests this is more a feature of the past when there was more uncertainty about the availability of funds in the market, but this principle could still hold in the current market with very large and/or bespoke PF/INFRA deals where the borrower/sponsor is more uncertain about how the loan should be priced or, indeed, in some future market state where available funds had significantly shrunk. All lenders were clear that such contact would require explicit consent from their (potential) clients. The discussions and information sharing between lenders at this stage may give rise to competition concerns if it facilitates collusion – we describe these risks in Chapter 4.

If a more traditional model of syndication is used, whereby a lead arranger or coordinator is mandated by the borrower/sponsor to engage with other lead banks to negotiate and agree key loan terms, then the issues of information sharing and cooperation are more pertinent. In such a case, the sharing of information *is* part of the process (rather than lenders acting illegally by breaching client NDAs), and we examine the implications of this in Chapter 4.

The timing of the information flows between the borrower/sponsor and the lead banks builds throughout the RFP process:

- Banks would receive an initial set of information (either along with an RFP or beforehand if the situation involves pre-discussions), which would either be subject to NDA or be wholly public information.
- As banks engage in the RFP process and show commitment to being in the lead banking group, they would receive more detailed information regarding the loan and the underlying project. This might include due diligence conducted by the borrower/sponsor if the loan involves the acquisition of an existing facility. If the underlying project is a new build then other data would be shared such as relevant market research (e.g. traffic forecasts in the building of a road). Other information shared by the borrower/sponsor could include information they have obtained from technical and legal advisors, but potentially also financial, insurance, auditing, tax, market and environmental advisors.
- If banks are brought together in the club before the final terms are agreed, they would share information between themselves and the borrower/sponsor around their desired hold levels, pricing views and views pertaining to other loan terms such as covenants.

Credit ratings

Credit ratings may be sought by the lead banks as a precursor to any general syndication. If the marketing of the loan is to include CLOs, then a credit rating will be required. This will typically be a private rating (i.e. available to only the syndicate participants). The rating will be sought from one of the three major credit rating agencies. Credit ratings agencies would provide ratings for syndicated loans, either for the loan instrument directly, or for the borrower — with the rating of the loan then derived from the rating for the borrower.

The demand for credit ratings is driven largely by institutional investors, e.g. investing via CLOs. Ratings would therefore be sought as a means of marketing the loan to a wide range of investors, and will not be sought for all loans or borrowers (e.g. particularly for club deals where there is no sell-down phase). One of the lead banks would liaise with the ratings agency for the provision of the ratings (this would be a role assigned by the borrower/sponsor). The ratings provided by the agencies may be private, but can also be public. The ratings agency will base its ratings on the information about the loan provided by the syndicate banks requesting the rating, as well as other market information.

Our lender fieldwork confirms that banks and non-bank lenders would undertake their own internal credit rating process, but that some institutional investors may require external ratings.

Generally, one of the MLAs will be tasked with commissioning the credit rating. In our lender fieldwork, this was characterised as one of the tasks that would be undertaken by one of the passive bookrunners.

General syndication phase in LBO (underwritten) loans

The general syndication phase is the marketing and distribution of the loan to other banks and institutional investors. It takes place after the lead banking group has been selected and the loan terms agreed between the lead banking group and the borrower/sponsor. A general syndication phase typically does not take place in a club deal, where the lead banks either hold the full amount of the loan they committed to, or sell parts off onto the market individually (usually on the secondary market).[43] Therefore the majority of this section in the process applies to LBO loans rather than PF/INFRA.

Once the lead banks have been mandated and final loan terms signed, the borrower/sponsor would usually instruct them to get together and agree on a common syndication strategy. This would include agreeing on the total amount that needs to be raised to make up the balance between the underwriters' (or arrangers in the case of a best efforts deal) hold amounts and the total loan amount, and allocating roles such as developing the marketing material, obtaining ratings, and approaching the market of participant banks and non-bank investors. The lead banks can share the active bookrunner role and divide the investor market between them (sometimes strategically based on discussions with the borrower/sponsor, and sometimes simply alphabetically). This is most common in smaller deals with around 2 – 3 lead banks.

Alternatively, in some transactions (larger deals with multiple lead banks) a single bookrunner might have this active role, aka a 'lead left'. The use of a lead left can be beneficial to the borrower/sponsor (or advisor) in that it results in a single story being presented to the market regarding the loan. This is more likely to be important for more speculative loans, or where a deal is struggling, where careful messaging to investors is needed to accurately communicate the details of the loan and to avoid scenarios where mis-communication undermines investor appetite. It may also be more efficient for the sponsor/borrower or advisor to deal with a single active bookrunner, and thus a lead left may hold particular advantages in time-pressured deals. Borrowers/sponsors would appoint a lead left bookrunner based on its track record in distributing debt in similar deals (e.g. country, size or sector), and also on its

[43] That said, there may be a coordinated sell-down where one bank would sell down a centralised amount on behalf of the other banks in the club for a limited time after the loan closure (e.g. 45-60 days), after which banks could choose to sell shares individually on the secondary market if needed. However, this coordinated sell down happens after the loan has closed and is not part of the general syndication phase.

appetite to underwrite and hold debt. A 'lead right' bank may also be appointed to stay up to date with the bookrunning process and step in to fulfil the lead role if the 'lead left' loses confidence in closing the deal or otherwise underperforms.

In either case the sponsor/borrower/advisor is usually closely involved in the decision-making during the general syndication phase.

The initial set of potential general syndicate participants is strongly determined by the borrower/sponsor – the lead banks would put together lists of potential participants which would then be reviewed/changed and signed off by the borrower/sponsor. The banks would make suggestions about certain institutional investors to be included (e.g. those who they know would be particularly interested in a deal, based on their knowledge of the market, thus demonstrating potential to add value to the transaction). The syndication strategy, including selection of members, is usually set out in the mandate letter or term sheet for the transaction. Typically, provision will be made for invitations to be sent to financial institutions or other lenders fulfilling a set of criteria, or on a list previously agreed with the borrower (a 'white list'). White lists are imposed by the borrower/sponsor as a means for them to control which institutions are invited to participate in the general syndication phase. Borrower/sponsors may wish to exclude certain institutions from the loan, in particular institutions which could cause difficulties in the event of a default or restructuring (e.g. "vulture funds") or institutions which may have performed poorly for the borrower/sponsor in the past.

It is naturally important to underwriting banks to understand the size of the white list prior to agreeing final terms, as this will affect their ability to sell-down the loan in the market (i.e. lenders favour as wide a list as possible). Therefore the white lists would be negotiated and agreed with the borrower/sponsor during the first phase of the loan syndication (the formation of the lead banking group, before the final terms are signed). Our lender fieldwork indicates that these are long lists (can include hundreds of institutions) and extend well beyond the number of participants approached, i.e. they are not typically overly restrictive for lenders. In addition to excluding certain investors, borrower/sponsors can also request that specific investors are included in the general syndication. Borrower/sponsors may indeed approach these directly, or leave this to the bookrunners.

The 'white list' approach is the standard approach adopted in Europe (albeit with variation in terms of its length). By contrast, the standard approach in the USA is characterised as being the use of a 'black list', i.e. the sponsor identifies those market participants it does not wish to be involved in the syndication, and allows the lenders to approach anyone else. The latter approach is likely to result in the *potential* consideration of a broader spectrum of the market's participants, i.e. the white list concept is prima facie more narrow (albeit a white list may run to several hundred identified investors or lenders). This continues to be relevant into secondary trading activity, i.e. if the primary loan is traded in the secondary market then an investor on the white list can be presumed to be acceptable – otherwise borrower permission is necessary (albeit this would be subject to a not to be unreasonably withheld proviso). The white list's key purpose is to enable the borrower/sponsor to control which institutions have access to the underlying loan of the borrower/sponsor.

Participants' previous experience with the borrower/sponsor, the industry sector or the geographic area are strong drivers for being put on the white list (i.e. the precondition to being marketed to and to be able to consider joining the syndicate). The white list is initially generated by the borrower/sponsor (particularly the latter). This would be based upon the sponsors' own knowledge, and any marketing to the sponsor by

investors (i.e. an institutional investor could approach a sponsor on a general basis – since they would not be aware of currently private transactions - to state an interest in looking at future transactions). The bookrunners may seek to expand the white list to aid them in laying off risk (as described above). This information would draw upon be provided by the lenders' own past deals and through ongoing generic interactions with investors (i.e. both the banks and sponsors would be engaging with the market on an ongoing basis). Knowledge of the investor base and experience/success in syndicating similar deals is one of the dimensions along which a lead bank would market itself to the borrower/sponsor in the first loan phase, i.e. it would be part of his remit to have sufficient knowledge of the market.

The bookrunners, often in collaboration with the borrower/sponsor, will prepare an information memorandum (IM) describing the terms of the transaction. The IM typically will include an executive summary, investment considerations, a list of terms and conditions, an industry overview, and a financial model, and sometimes the buyer's due diligence. Because loans are not securities, this will be a confidential offering made only to qualified banks and accredited investors, under an NDA. If the issuer (borrower) is speculative grade and seeking capital from non-bank investors, the arranger will often prepare a "public" information version of the IM in agreement with the borrower/sponsor. The main omission relative to the "private" IM would be management forecasts (i.e. it could still be confidential – and certainly the fact of the transaction itself would still be confidential). This is done in order to allow potential investors the opportunity to invest in a company's publicly-traded securities as well as engage in the loan. This version is not necessarily public in the sense that it is readily available to the general public, rather that it does not contain highly sensitive information. This version will be stripped of all confidential material such as management financial projections so that it can be viewed by accounts that operate on the public side of the wall or that want to preserve their ability to buy bonds or stock or other public securities of the particular issuer. Investors that view materially non-public information of a company are disqualified from buying the company's public securities for some period of time.[44]

A 'roadshow' may then be organised to present and discuss the content of the IM, as well as to announce closing fees and establish a timetable for commitments and closing. After the roadshow, the bookrunner(s) make formal invitations to potential participants. Not all participants will be interested in all parts of the transaction, e.g. typically, a revolving credit facility will appeal only to banks, and therefore the marketing usually focuses on the Term Debt (which, as we have noted, has most appeal to institutional investors) rather than on the revolver.[45]

A number of lenders use a secure portal, such as Debt Domain, to manage the information flows to participant bank and non-bank lenders. This ensures that all investors receive the same information at the same time, and provides transparency and an audit trail that this is the case.

The starting point can be a summary one page setting out the key terms for the loan, followed by the more detailed information memorandum, with legal documents towards middle/end of process.

[44] For example, a public version of a loan may be marketed if there was to be a high-yield bond attached to the loan, to enable those investors wishing to trade the bonds to be able to continue to do so.

[45] A bank's willingness to take and hold a meaningful share of the revolver is a necessary requirement in selecting the lead banks in a syndicated loan, and therefore this has already been decided when the roadshow takes place.

General syndication phase for PF/INFRA loans

As set out above PF/INFRA loans are usually club deals. The literature indicates that if a PF/INFRA loan is to be syndicated further, a similar process to other underwritten/best efforts deals would be followed in that the borrower/sponsor would mandate the lead arrangers after the finalisation of the term sheet, giving the MLAs (in the capacity of bookrunners) a legal mandate to syndicate the loan. This time period is rarely shorter than one month and can be as long as one year.[46]

Where there is a general syndication phase, market guides state that the arranging banks and project company representatives may go on an investor roadshow at which they will present the issuer, the project, the management of the project company, the proposed financing and the risk mitigation features, and give the investors the opportunity to ask for more information. At the project company's request, a provisional (private) rating may be provided by one or more rating agencies to facilitate the roadshow phase. Typically, each rating agency would also publish a 'pre-sale report', setting out its rating rationale for the project.[47] Our lender fieldwork indicates that roadshows are less common now due to the increasing proportion of club rather than underwritten deals in PF/INFRA loans.

Negotiation and allocations

The terms of the loan are typically agreed between the borrower and the lead banks and signed before the general syndication phase (in particular, in the case of an LBO involving an auction, the sponsor needs committed funds and terms from the lead banks ahead of the auction close). There is limited scope for investors to individually negotiate terms directly with the arranger banks who approach them to participate in the loan: they can say yes or no to the offered terms – or say yes, if this or that is changed (and this feedback would then be share with the borrower/sponsor). This appears to be in part a feature of current market conditions – in scenarios of low liquidity then participant lenders may have more scope to negotiate key terms (especially large ticket holders).

However, in an underwritten deal's general syndication, if overall demand for the loan proves to be too low (or unexpectedly high), the arrangers can use "market flex" to make loans more attractive to investors (or to the borrowers if the loan is heavily over-subscribed, in which case it is known as 'reverse flex').

A flex works such that the bookrunners feed back to the borrower/sponsor (and to other underwriters) on progress, giving a view as to whether the flex needs to be operated in order to secure the appropriate level of financing. In such a case, the syndication process is re-iterated at the new terms. In the case of under-subscription, if post-flex the syndication is still unsuccessful, there could be additional flex and subsequent syndication rounds. At some point, the arranger could decide not to decrease the price any further. If the deal is underwritten (flex only applies in underwritten deals), this means that the underwriters have to retain a larger share than expected. Sometimes, the underwriters prefer to pull the deal out of the market altogether, issue a bridge loan instead, and defer further syndication attempts.

Market flex allows arrangers to change the pricing of the loan, shift amounts between various tranches of a loan, or even change documentation, provided this is within the boundaries set by the flex clause. All flex provisions are agreed in the initial term sheet signed by the MLAs, for example which elements of the terms can be flexed, ranges for pricing shifts, and criteria for using flex. Typically MLAs must 'pay away'

[46] Prime Bank "Project Finance loan syndication procedures", https://www.primebank.com.bd/downloads/Project%20Finance%20and%20Loan%20Syndication%20Procedures.pdf.

[47] AFME Guide to Infrastructure finance (2015).

some proportion of their fees to the market before they can invoke the flex provisions (cf. reverse flex), and this pain-sharing is also agreed upfront. Narrow flex clauses and fee 'pay aways' are included by the borrower/sponsor as a disincentive to bookrunners to invoke flex unless absolutely necessary. Fee pay aways disincentivise bookrunners from winning a mandate by bidding overly aggressively, only to invoke flex in the general syndication phase. Over-reliance on flex can also be damaging to an underwriters' reputation as it signals a mis-reading of market appetite. Once flex is negotiated into the contract it is 'automatic' (i.e. the bookrunner is free to use it if necessary).

The frequency of use of flex or reverse flex is the result of a dynamic process, as the different actors respond to changes in market sentiment and to feedback from the market on past syndications (with some lag). In the current market, sponsors and borrowers will tend to push hard for borrower-friendly terms, building on past precedent of what they (particularly the sponsors) have achieved previously. Such terms may be agreed with the lenders (albeit potentially with warnings from the bookrunners that such terms may be too much) and which may then be subject to push back from institutional investors in a general syndication.

The nature of flex provisions varies across transactions, but our lender fieldwork indicates that the provision for extensive flex terms is less than it was. Terms have tightened – i.e. bookrunners have less contractual scope to change the pricing in the general syndication phase, and in (relatively rare) cases sponsors push for no flex provisions to be included at all. In addition, the economics have changed such that lenders are less likely to share in gains where loan terms move towards the borrower (i.e. reverse flex), and have increased pay away terms in cases of flex. The negotiation of these terms in parallel with the other terms of the underwritten loan is obviously an important element within the process.

That said, documentation flex provisions were highlighted as a feature of the current market by a number of lenders and investors.[48] In particular, flex can be included around certain documentation terms which the borrower/sponsor removed during the initial negotiations (e.g. limitations on additional indebtedness of the borrower/sponsor) but recognised that doing so may be too aggressive for the market and agreed to allow the arrangers to re-instate the terms during the general syndication phase if necessary. In some PF/INFRA loans flex can be linked to market-moving events (such a change in regulation affecting the viability of renewable energy projects) – however, given that PF/INFRA loans are mostly club deals, flex will only occasionally be relevant.[49]

In a recent paper by Bruche et al.[50], the authors find that, in their sample, loans with a high yield and loans that finance acquisitions or LBOs, are more likely to experience price flex and that the likely direction in which spreads are flexed relates to net inflows into high yield mutual funds and CLOs. These flows occur after the arranger has launched the deal and, hence are not known to the arranger at launch. Net outflows, indicating low aggregate demand, are more likely to be associated with spreads being flexed up. A possible interpretation is that for such more complex loans, the arranger

[48] The majority of lenders in our fieldwork mentioned that the provision for at least some flex is made in LBO contracts, but that the terms of what could be flexed have tightened over time.
[49] In addition, given the longer time-frames of PF/INFRA deals, changes in the market for a loan could be discussed between the lead banks and the borrower/sponsor whilst the loan terms were still being finalised, such that there would be minimal chance of the final terms needing to be flexed.
[50] Max Bruche, Frederic Malherbe, Ralf R Meisenzahl (2017) "Pipeline Risk in Leveraged Loan Syndication" Federal Reserve Board, Working paper 2017-048.

finds it harder to anticipate the true demand for the loan and adjustments occur more frequently.

"Reverse flex" can come into play if demand for the loan is higher than anticipated and the arrangers are able to secure better (pricing) terms for the client. The economics of reverse flex is partly conditional on the market segment. The largest sponsors tend to insist that all the gains go directly to the client, but below this level some degree of gain-sharing (say the book runners taking 25–50 per cent of year one benefits) can still occur.

Subsequent to any flex of terms, the book running bank(s) will recommend an initial allocation among participants. The starting point for this is likely to be pro rata. The final allocation will be signed off by the sponsor, who often will have its own allocation strategy in mind (although sponsors would normally advise the banks of this ahead of time).

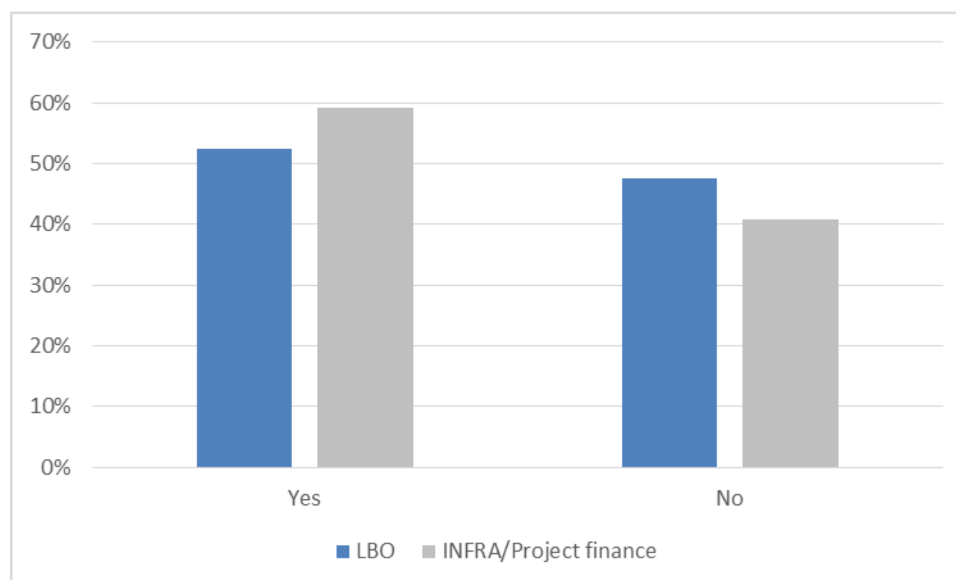
Once the allocation has been finalised, the deal becomes active and the loan is operational, binding the borrower and the syndicate members by the debt contract. The latter sets out the terms and conditions of the loan: the amount, the purpose, the period, the rate of interest plus any fees, the periodicity and the design of repayments and the presence of any security.[51]

Ancillary services in LBO and PF/INFRA segments

There are two main types of ancillary services which can be provided in relation to syndicated loans: those services which can reasonably be split among a number of lenders such as hedging services (e.g. the writing of interest rate or foreign exchange swaps) and those services each typically provided by a single bank, such as cash/collateral management, custodianship and advisory services, as well as credit ratings services.

Our fieldwork with borrowers and lenders showed that it is relatively commonplace for at least one such ancillary service to be incorporated into the loan discussions.

Figure 4: Provision of ancillary services connected to the loan

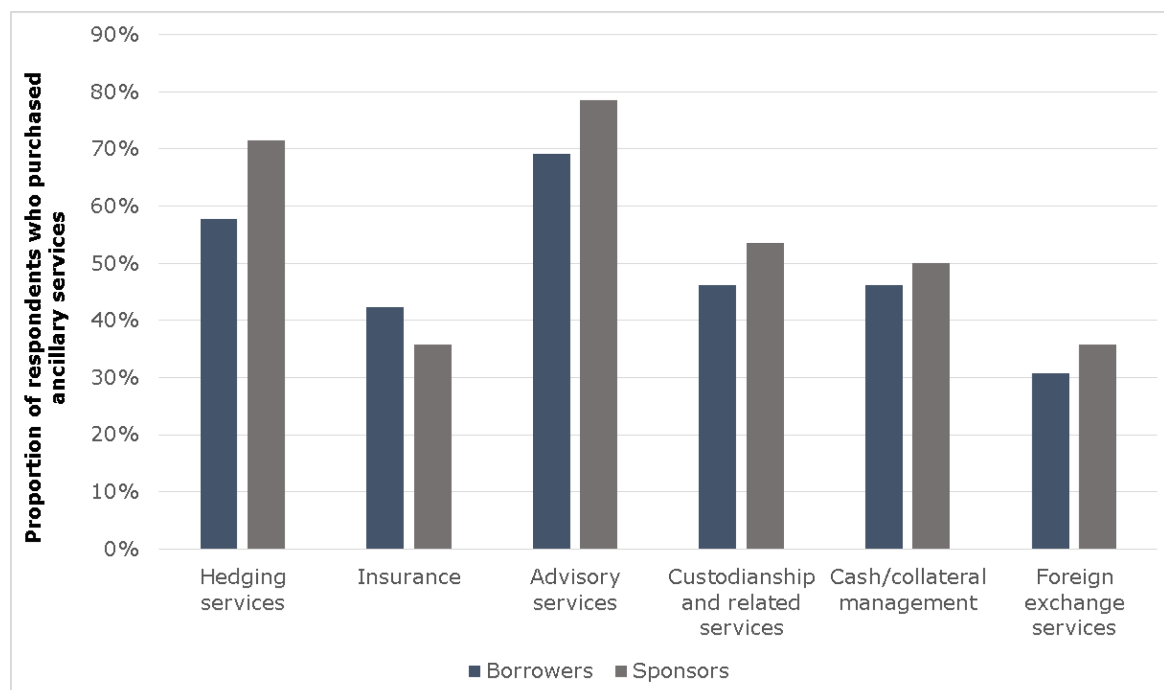


Source: Europe Economics and YouGov fieldwork.

[51] Godlewski, Christophe J. (2007) "What Drives the Arrangement Timetable of Bank Loan Syndication?"

The figure below shows the ancillary services negotiated by borrowers and sponsors as part of the syndicated loan – as can be seen hedging and advisory services are the main two.[52] We have described debt advisory activity earlier in Chapter 2 in the background to the syndicated loan market.

Figure 5: Ancillary services purchased by borrowers and sponsors



Source: Europe Economics and YouGov fieldwork. Question 23B/25S "If you negotiated ancillary services as part of the syndicated loan, which did you agree to purchase?"

Some ancillary services are directly related to the syndicated loan and others are not 'essential' to the loan but can nevertheless be negotiated at the same time as the loan. Below we describe the key ancillary services from this perspective:

- Hedging services: Interest rate or foreign exchange risks are directly related to the loan as they ultimately affect the ability of the borrower to repay. In those cases where these risks are judged material (especially the case with PF/INFRA loans) hedging against these risks can be mandated by lenders in the loan contract.
- Cash management: this is not directly related to the loan, other than in the trivial sense that payments on the loan have to be processed. We note that where a loan is to a new borrower (e.g. an SPV set up especially to manage a new project) then cash management services would be necessary as a pre-condition to completing the loan.
- The same applies to foreign exchange services, custodianship and insurance services: these are not necessarily considered an essential part of a syndicated loan, but borrowers' need for these may arise due to their engagement in the loan.

[52] Our borrower/sponsor sample is not large enough to draw significant inferences of the differences between LBO and PF/INFRA loans, but the data show a greater proportion of borrowers and sponsors in PF/INFRA loans purchased ancillary services in general than in LBO loans, and that hedging services were the most commonly purchased ancillary services in PR/INFRA (75 per cent of those who purchased ancillary services) followed by advisory services (69 per cent); whereas advisory services were most commonly purchased by borrowers and sponsors in LBO loans (79 per cent of LBO sponsors/borrowers who purchased ancillary services) followed by hedging services (64 per cent).

- The loan facility will require the appointment of a facility agent to manage the syndicate. This is directly related to the loan in that it simplifies the administration of the loan for the borrower (which pays the fees) and should also mean that the syndicate members have the same information as each other.
- Borrowers can also agree the sourcing of other services from lenders that are not part of the syndicated loan per se, but are implied by it, namely acting as lead banks on future bond issuance expected to be undertaken to replace a bridging loan that is part of the syndicated loan facility.
- Borrowers can also purchase other services from lenders that are not directly related to the loan, but rather to future business activities, such as to provide future M&A or IPO advisory services.

We describe here the two main services – hedging and cash management, the processes by which they can be engaged, and draw out differences where relevant between LBO and PF/INFRA loans.

Hedging services

The hedging of interest rate or foreign exchange risks may be required as part of the syndicated loan, i.e. mandated in the loan contract. Where hedging services are required, the borrower/sponsor would therefore be obliged to seek a bank(s) approval to write swaps. (They may also wish to take out swaps even if not obliged to do so by the contract terms.) This can, but does not always, involve negotiations with the original syndicate, and borrowers/sponsors can look outside the syndicate. This process can vary along the following main dimensions:

- The timing of when the hedging services are discussed and awarded (e.g. after the primary loan has been concluded or as part of the negotiation of the initial loan terms).
- The banks to whom the hedging services are allocated (e.g. those within the syndicate or not).
- The process under which the services are allocated (via competitive bids from banks or allocated directly by the borrower/sponsor).

Whilst there are no hard and fast trends for how these dimensions apply across loan types, there are some typical differences between LBO and PF/INFRA loans which we draw out below.

LBO loans

The majority of lenders in our fieldwork indicated that interest rate and foreign exchange swaps are mandated less often for LBO loans compared to PF/INFRA loans. The borrower/sponsor may still choose to enter into hedging agreements, but are generally able to resist any contractual obligation to do so. That said, in less usual circumstances hedging may be mandated and therefore the related issues are still relevant to a proportion of LBO loans.

Lenders in our fieldwork indicate that in LBO loans usually the allocation of hedging services is finalised after the loan documentation has been signed, i.e. they do not form part of the initial negotiations for loan itself. The most common process reflected in the borrowers/sponsors fieldwork also involved discussions after the initial loan terms had been agreed.[53] However, there are cases where the provision of ancillary

[53] Fieldwork question: "Did the negotiation with the lead arranger and/or participant institutions include arrangements about provisions of ancillary services related to the loan (e.g. hedging services, insurance, advisory services etc.)?" and "If yes, how".

services are discussed as part of the initial loan negotiations, e.g. in around 20 per cent of LBO cases reflected in the borrower/sponsor fieldwork.

The banks in the lead banking group would generally have the opportunity to bid for the provision of ancillary services (participant lenders, especially non-banks, may not be able or willing to provide hedging services) – in very few cases are such arrangements made completely independently of the syndication group (e.g. only four sponsors and no borrowers indicated this).[54] Whilst this does not mean that the opportunity to bid for such services is *restricted* to the syndicate banks by the borrower/sponsor,[55] in the majority of cases the services are awarded to syndicate banks.

The process of bidding for hedging services can either take place via a formal competitive bid process between the syndicate banks, or through negotiations between the borrower/sponsor and the syndicate banks. In around 40 and 50 per cent of cases, borrowers and sponsors respectively in our fieldwork indicate that lenders compete for such services through a formal competitive process rather than through the loan negotiations.[56] Our lender fieldwork indicates that in many (but not all) banks the teams involved in discussions around ancillary services such as hedging are different to those involved in the loan syndication, and in some cases our fieldwork shows that lenders have a formal separation between these functions. A small number of lenders in our fieldwork indicated that the considerations about ancillary services such as hedging affected their primary decisions about the loan pricing – for the majority these decisions are kept separate.

Borrowers and sponsors also identify very few instances where ancillary services were made a *condition* of the syndicated loan i.e. where a lender includes in its initial bid for the loan the condition that it is allocated some proportion of the ancillary services (only one borrower and two sponsors responding to our fieldwork indicated that this occurred, although they did not specify the type of service involved — i.e. this could apply to hedging and/or other forms of ancillary service, as described below).[57] We explore the potential risks associated with bundling of certain ancillary services and the loan in Chapter 4.

For efficiency purposes, in our lender fieldwork, it was indicated that a single bank could be delegated with the actual execution of the hedging transaction on behalf of the other banks. Borrowers/sponsors may rely on internal expertise in assessing the prices obtained (complemented where available by market prices) by the banks, or they may even engage a hedging broker to handle the transaction (e.g. run an auction). Market risk would be reflected in the price of the swaps which the borrower/sponsor would be able to check on the market via purchasable market data. This is because Interest Rate Swap (IRS) pricing is formula based.[58] In other words,

[54] Fieldwork question "What was the process for deciding ancillary arrangements if this did not entail negotiation with the lead or participant banks?"
55 Out of 89 borrowers/sponsors, 35 (i.e. 39 per cent) generally or wholly made provision for ancillary services independently of the loan process. A further 22 (i.e. another 25 per cent) left negotiation until post-deal but did invite bids from the MLAs.
[56] Fieldwork question: "Did the negotiation with the lead arranger and/or participant institutions include arrangements about provisions of ancillary services related to the loan (e.g. hedging services, insurance, advisory services etc.)?" and "If yes, how". This finding applies across all ancillary services – no breakdown specifically for hedging services is given by borrowers/sponsors.
[57] Fieldwork question: "Did the negotiation with the lead arranger and/or participant institutions include arrangements about provisions of ancillary services related to the loan (e.g. hedging services, insurance, advisory services etc.)?" and "If yes, how".
[58] See for example an introductory primer here: https://insight.factset.com/hubfs/Resources%20Section/White%20Papers/Interest_Rate_Swap_Valuation_WP.pdf?t=1530886131305.

pricing can be benchmarked provided there is access to the relevant financial data and the knowledge to put it together using an appropriate formula. Whilst this may likely be a level of sophistication not universally shared amongst the borrowers and sponsors (even) in the LBO and PF/INFRA segments, there are also dedicated third-party derivative advisory firms, either operating as part of broader debt advisors or an independent basis. Similarly, MiFID2 has created new obligations around transaction reporting, including price data, apply to OTC derivatives that are economically equivalent to those "traded on a trading venue", which ESMA has interpreted as sharing the same reference data details.[59] For Interest Rate Swaps, for example, this would mean: data on reference rate, term, currency, and description of floating and fixed legs (i.e. applicable interest rate). This is expected to capture a substantial part of IRS, particularly 'vanilla' IRS constructed around EURIBOR and LIBOR benchmarks. Some other local benchmarks (e.g. Warsaw IBOR) could fall outside this. As Recital 116 of MiFID2 states, it is expected to "improve the quality of trade transparency information published in the OTC space". However, MiFID2's implementation was only in January 2018 and the industry may take time (and potentially supervisory action) to fully adjust to the new protocols.

PF/INFRA loans

By contrast to LBO loans, it is common in PF/INRA deals for the extent of interest rate hedging on the loan to be specified as part of the negotiation of terms, due to the nature of the projects.

Similar points apply as with LBOs regarding the banks involved in the provision of such services, namely that although non-syndicate banks need not be excluded from the (private) tendering process for the provision of such services, the hedging services end up being allocated to syndicate banks (although this appears to be particularly relevant to PF/INFRA loans – the lead banking group may be best placed to secure the business of writing swaps given their knowledge of the credit risk of the project). Similarly, there are no significant differences in whether such services are allocated by formal competitive bids (52 per cent) or via a negotiation (48 per cent), although our borrower/sponsor fieldwork shows that a competitive process is slightly less likely in PF/INFRA loans than LBO loans (46 per cent versus 54 per cent).

One difference between LBO and PF/INFRA loans is the timing of the discussions around hedging services. Both our lender and borrower/sponsor fieldwork indicate that instances where the discussion of hedging services occurs earlier on in the loan process are more common in PF/INFRA loans compared to LBO loans. For example, our lender fieldwork indicates that in some instances there may be a hedging letter agreed as part of the mandate award stage whereby an agreement to split the hedge between certain banks is made (this aligns with the borrower/sponsor fieldwork which indicated that the tying of ancillary services with the original loan – although only in a few instances in our borrower/sponsor – does happen),[60] even if the final pricing of the derivatives can only take place after the loan has been finalised (i.e. the loan's terms have been agreed). The potential competition issues associated with the bundling and timing of ancillary services are discussed in more detail in Chapter 4.

As hedging services are more common in PF/INFRA loans than LBOs, leading banks (especially if these are commercial banks) might aim to secure ancillary services as a means of maximising the overall returns of the transaction and as part of a long-term strategy of deepening relationships with the borrower - and would seek to use their

[59] ESMA Opinion on TOTV published 22 May 2017.

[60] One borrower and two sponsors (out of 54 in total providing an answer to this question) responding to our fieldwork indicated that lenders make the provision of ancillary services a condition of their initial loan terms. All three were located in Spain (out of 11 borrowers/sponsors answering this question).

experience and relationship with the borrower/sponsor in positioning themselves as the preferred candidate. This would apply to other ancillary services as well. However, our borrower and lender fieldwork indicates that the final decision on ancillary services is at the discretion of the borrower/sponsor, e.g. through negotiations related to the initial loan or through the bidding/negotiating processes after the loan has closed. In Chapter 4 we draw out the risks associated with circumstance where the borrower/sponsor's decision making may be limited in some way.

Cash management services

Other ancillary services such as cash management and advisory/agency services are not split between syndicate banks, but are usually assigned to a particular bank (or a few banks). In the case of cash management services, this is seen as sticky (as systems and processes will vary between banks) and if there is an existing relationship bank that handles this work it is likely to retain this business. Banks might compete for these roles, but some roles (especially cash management) need to be held by a bank local to the borrower and thus the pool of eligible banks may be diminished, and sometimes a bank may already be providing similar services to the borrower or the underlying target corporation. (Indeed, in such cases such a bank may be brought into the syndicate largely on the basis of this relationship to ensure continuity.) There are no significant functional differences in the nature of cash management services across LBO and PF/INFRA loans. With LBO loans it might be that the underlying target already has a relationship with a certain bank which the borrower/sponsor will want to preserve during the loan syndication phase. This is unlikely to be the case with PF/INFRA loans for new builds, but may apply if the borrower is an existing construction company or SPV.

Our lender fieldwork indicates that in general, any anticipated returns from ancillary services are not considered as a factor in loan pricing, i.e. would not compensate for lower loan margins. However, some banks' business models from our fieldwork do not preclude this and there are thus instances where the consideration of ancillary services and the returns to be made would influence decisions about participating in a syndicated loan. Indeed, in most banks the provision of ancillary services is dealt with entirely separately by a group (or groups) other than that involved in the syndicated loan, and as such there may be reduced incentives to consider the returns from such services in the syndication phase. However, as with the areas of hedging services, we explore the risks associated with the bundling of ancillary services e.g. opacity of pricing in Chapter 4.

Post-closure

We touch briefly upon phases that may occur post-closure, once the loan has been fully allocated to lead banks and participant investors.

After the loan has closed – all documentation signed and the loan allocated to all lenders – the facility is administered by the Agent Bank. This bank acts on behalf of all syndicate members (both the leading banks and the participant investors) throughout the life of the loan. The Agent's role is largely administrative – it receives and passes on all borrower information throughout the course of the loan (management report etc.) and is the conduit for all payments and notices under the facility. The post-closure phase is not distinguished across LBO and PF/INFRA segments, and variations would rather stem from the nature of the transaction. Some key variations between LBOs and PF/INFRA exist in relation to the secondary loan market (e.g. the liquidity of the two markets) which we discuss in the section below and in Chapter 3.

After the loan has closed, lenders may choose to engage in the secondary loan market, where loan shares are bought and sold. In time, the loan may also be refinanced, and in the event of any default or distress the loan may be restructured.

Secondary loan market

Secondary market trading here refers to the buying and selling of the primary loan on the secondary market once the loan has been closed.[61] We do not include the buying of ancillary products (such as interest rate or foreign exchange swaps) in this definition – this has been described in the section under ancillary services.

Lenders might have several reasons to sell loans (or parts of loans) in the secondary market. First, they might do so for portfolio management considerations including smoothing risk due to the concentration of particular obligors or industries, or to move on to higher return opportunities. Second, they might do so to change their lending strategy. Banks indeed might become particularly vulnerable to given industries / geographic locations or customers during the business cycle. Third, they might do so to satisfy regulatory requirements. The sale of a loan in a portfolio allows them to use their capital effectively and therefore to engage in a higher level of loan origination activity.[62] In some cases, potential lead banks might signal interest in a particular sponsor or corporate by buying part of a syndicated loan on the secondary market (this is usually accompanied by other discussions with the potential client to indicate that such interest would be welcome).

Equally, certain types of lenders, such as hedge funds, may be more inclined towards rapid trading for short-term profit on the secondary market.[63] Major buyers of syndicated loans in the secondary market are non-bank financial institutions e.g. hedge funds, debt funds using investment vehicles such as CLOs, and other funds.[64] Syndicated loans are an increasingly popular asset class for institutional investors seeking alternative investments and higher returns. Past studies have found that the returns on these loans are only loosely correlated with equity returns.[65]

Another category of participants in the secondary loan market are specialist investors who wish to own part of the debtor company. These may buy a large proportion of the borrower's debt, potentially with a view to acquiring control of the company. Alternatively, the investors may look to influence the borrower's insolvency or restructuring process. The investors may be making an investment on their assessment of the probability that the company will be successfully rescued, the ultimate aim being to profit from any subsequent upside in the value of the business. The investors may also be taking a view that the breakup value or recovery via insolvency will be sufficient to make a profit on its original investment. Our understanding from our fieldwork is that the white lists specified by borrowers/sponsor relating to primary or secondary loan transfers may seek to exclude such specialist investors particularly as the borrower/sponsor may not wish them to have a role in

[61] The LMA Guide to Secondary Loan Market (2016) defines the secondary loan market as follows: "The secondary loan market refers to the sale of loans that occurs after syndication of the original loan has been closed and allocated. It includes sales or trades of syndicated loans made by lenders in the original syndicate and those made by subsequent purchasers.

[62] Gupta, A., Singh, A.K., Zebedee, A.A. (2007) "Liquidity in the Pricing of Syndicated Loans" Journal of Financial Markets, Volume 11, Issue 4, Pages 339–376.

[63] Slaughter and May (2007) "Syndicated Loan Facilities: Non-bank Lenders, and the Influence of Credit Derivatives: Current Issues and Opportunities for Borrowers" on behalf of Association of Corporate Treasurers.

[64] Mutual funds (acting on behalf of retail investors) are common in the US market but not in Europe (there are a few quoted investment vehicles in Europe through which a retail investor can achieve access).

[65] LMA (2016) "Guide to secondary loan market transactions".

any restructuring (e.g. if these investors are likely to favour the break-up of the company).

The secondary market for LBO loans is much more liquid than for PF/INFRA (as described in more detail in Section 3). That said, the common approach among the majority of banks in our fieldwork is to use the secondary market for portfolio management, rather than to engage in continuous trading. The exceptions are large investment banks. PF/INFRA loans tend to be more often held to maturity, and the bespoke nature of such loans (i.e. credit risk etc.) means that finding counterparties willing to take on the exposure can be difficult. Indeed, it is not uncommon for banks needing to sell on part of a PF/INFRA loan to first approach the other lenders in the club before approaching the wider secondary market.

Secondary trading is affected by transfer restrictions specified in the initial term sheet. In some cases (most common in LBO loans), transfers can happen without formal borrower consent so long as these are from within the 'white list' of investors agreed, as described in the previous section. In other cases, borrower consent is required for any transfers (typically 'not to be unreasonably withheld'). These restrictions may limit the efficiency of the secondary market, which we discuss further in Chapter 4.

Types of secondary market trades for LBO and PR/INFRA segments
Our understanding from our fieldwork and market reports (e.g. the LMA's guide to the secondary loan market) is that the process for trading loans on the secondary market is not driven by whether the loan is for an LBO or PF/INFRA purpose, and therefore we describe the process here as applicable to both. There are several mechanisms available for trading loans on the secondary market which differ in the degree to which they transfer the rights and obligations of the existing lender to a third party (i.e. buyer). [66] Starting from the most to least "complete" transfers these are:

- Novation.
- Legal assignment.
- Equitable assignment.
- Sub-participation.

With the first two methods, i.e. novation and legal assignments, the third party enters into a direct contractual relationship with the borrower (i.e. joining the syndicate ex post), while with the other two the third party's involvement in the loan is (to a larger or lesser extent) intermediated by the existing lender.[67]

Given that assignment is the most common method of transfer in several EU Member States (as well as in the US, where the academic literature is concentrated), in the remainder of this chapter we focus on this type of transfer mechanism and, unless stated otherwise, when discussing trade or secondary transactions we mean a transfer of rights by way of assignment.[68]

In general, *assignment* is a transfer of rights but not obligations. It is often accompanied by an indemnity that the new lender will also assume those obligations "as if named as a lender under the facility agreement".[69] As opposed to a transfer by novation, assignment generally does not require obtaining the consent of the borrower

[66] LMA (2016) "Guide to secondary loan market transactions".
[67] Aside from the techniques set out in this section, an additional way of obtaining exposure to the syndicated loan market is through derivatives.
[68] Further details of secondary market transfers are included in Appendix 3.
[69] LMA (2016) "Guide to secondary loan market transactions".

(or other syndicate members).[70] *Legal assignment* is more complete and requires the transfer: to be unconditional, to cover the whole of the existing lender's share of the debt, to be in writing and signed by the existing lender, and to be disclosed in writing to the borrower (and other lenders, if the loan agreement specifies so). If any of those conditions is not satisfied, the transfer is an *equitable assignment*. The main difference between legal assignment and equitable assignment is that the assignee (i.e. the new lender) often cannot bring any action against the borrower or other syndicate members and has to join the assignor (i.e. the existing lender).[71]

Process of trading loans on the secondary market

The process of trading shares of a syndicated loan would generally – regardless of the transfer mechanism – follow the following steps and information flows.[72]

- *Before the trade* both parties would need to be aware of the types of entities to which loans can be transferred or assigned as specified in the original loan agreement (i.e. either through the white lists or other specific references). Once this is determined, the buyer would have to agree to the confidentiality requirements specified in the original loan agreement, after which they would be able to perform due diligence, i.e. examine all the relevant loan documentation and financial information provided by the seller.
- *The trade* usually happens over the phone and constitutes a binding contract. In the oral agreement the parties usually determine: the price paid (par, premium or discount), the exact facility and tranche that will be traded, the amount (entire or part of the tranche), the form of purchase (legal transfer, legal transfer with a fall-back option to funded participation, or funded participation), the treatment of interest payments and fees (any unusual fees such as repayment premiums), trade-specific representations and warranties, and the party responsible for preparing the confirmation of the trade.
- *The confirmation* is a written record of terms previously agreed orally, and therefore it is in principle not subject to further negotiation. The party responsible for its preparation sends it for the other party to review, and in the absence of any objections, sign.
- *Third party consent* might be required (e.g. if the transfer is by way of novation). If borrower consent is required then the seller usually obtains it via the agent rather than by directly contacting the borrower (or other relevant syndicate parties).
- *Transaction documentation* will consist of any documents required to complete the transaction, including transfer certificates, and pricing letters (specifying any transfers of funds between the buyer and the seller, and to the agent).
- *The Settlement date* is directly agreed by the parties, or – in the case of transfer by novation – it is the date specified in the transfer certificate or the date at which the agent signed the transfer certificate, whichever is later. On the settlement date the asset is transferred to the buyer (unless the trade is via a participation) and the settlement amount paid.

[70] There is some inconsistent evidence in the literature as to whether consent is required in the case of assignments:

- S&P (2014) "A Syndicated Loan Primer" says consent is 'typically' required, but that the consent cannot be withheld unless there is a reasonable objection. This is equivalent to what the LMA (2016) guidelines say on novation.
- Thomson Reuters glossary (cited below) states that assignments generally do not require consent.

Our interpretation is that assignments (as we define above) do not require consent. We are of the view that the S&P statement that consent is 'typically' required is the result of their using the terminology slightly differently, namely by grouping novation and assignment together, and collectively referring to them as assignment.

[71] Thomson Reuters, "Assignment", Practical Law Glossary, https://uk.practicallaw.thomsonreuters.com/1-107-6442.

[72] Based on LMA (2016) "Guide to secondary loan market transactions".

- *Post-settlement* there is time for any notices, e.g. notifying the borrower about the assignment.
- *Secured debt* is likely to be a syndicated loan which is part of a multilateral financing structure, which in turn often includes a security trust agreement.[73] There is no need for any amendment in the trust agreement after the trade is complete – the new lender automatically benefits from the security.

The LMA also provides a target timeline specifying when the relevant parties could be expected to complete each of the stages of the trade described above. This is illustrated in the figure below. This illustrates the slowness of such trading compared to transferable securities governed by the CSDR which operate on a T + 2 settlement cycle.

Figure 6: Timeline of secondary market transactions

Timing	Stage
T - x	•Identification of the trade parties •Ensuring confidentiality •Due diligence
T	•The trade
T + 1	•Seller requesting borrower's consent via agent •Seller sending credit documentation to buyer (unless already sent before)
T + 2	•Responsbile party sending the confirmation •Agent requesting borrower's consent
T + 4	•Other party returning the signed confirmation
T + 5	•Responsbile party sending transaction documentation
T + 7	•Borrower providing consent
T + 8 (par) T + 15 (distressed)	•Signing transaction documentation
T + as soon as reasonably practicable	•Settlement date - transfer of assets and settlement payments
T + 10 (par) T + 20 (distressed)	•Delayed settlement compensation starts to accrue
T + 60 (par only)	•Buy-in / sell-out if settlement delivery obligations are not satisfied

Source: Loan Market Association. Note: The LMA does not specify the typical value of x.

Refinancing, restructuring and default

Refinancing

Refinancing is a normal part of the syndicated loan market. Refinancing could be attractive to a borrower/sponsor if the risk appetite in the market has changed significantly (i.e. spreads over Euribor for a particular instrument have narrowed) or if the risks/prospects of the project have changed significantly. This could be where – in an infrastructure project, for example – the project transitions from the construction phase to its operational phase.

[73] A security trust agreement appoints a trustee to hold the security for all lenders for a period of time.

The process for such (voluntary) refinancing will be equivalent to that of the initial, primary syndication process, i.e. there would not be restrictions in place to deal only with existing syndicate members. One point of difference is that, for performing loans, there is much less likelihood of time being a key variable, and so underwritten deals are much less common.

Restructuring and default

A requirement to refinance can also be involuntary. The default rate on sub-investment grade loans is estimated by Moody's to be around 2–3 per cent in Europe.[74] The senior status of the loans can mean that recovery in default can be substantial (e.g. estimated at about two-thirds of par value on a historic basis, globally, by Moody's).

The syndicated loan documentation may contain financial (e.g. around interest cover, maintenance etc.) covenants. A breach of these covenants may represent a default in the loan. The simple failure to pay interest or capital when due would also constitute default events. This would clearly signal that the borrower is in financial difficulties. As such, the parties to the loan would need to determine a solution around re-negotiation of the loan documentation, through to some form of re-structuring (which may be equivalent to a new origination), and even more severe outcomes (i.e. insolvency).

In the event of default (or possibility of default), the typical process is for a separate group within each of the lending banks to take over the management of the loan. This group ("Restructuring", "Special credit" etc.) would either liaise with the origination/relationship team of the bank, or there might be complete separation between the teams. Discussion of solutions between lenders would be instigated by the sponsor/borrower.

Market participants consider it best practice for the sponsor/borrower to engage early with arranger banks to discuss an expected problem, and either give permission for banks to speak to each other, or better give a 'voluntary' presentation by management to the banking group.

A negotiation committee would be set up among some of the lead banks which would lead the negotiations on behalf of the rest of the syndicate – this committee would be arranged by the borrower. From our fieldwork, lenders have differing views on participation in this committee – some consider it a good way to receive information early and have access to the negotiations (particularly if they have large exposure). Others do not consider it necessary and consider all banks to have broadly equal bargaining power as many decisions need to be taken unanimously (e.g. to defer repayment), although sometimes only 75% (of shares in loan) is needed to pass a decision and therefore banks with larger shares would have more power. This will vary – the loan documentation will specify which requests require unanimous consent and what the required majority will be for other requests. Participation in the negotiation committee may restrict lenders from trading as they may be in possession of non-syndicate level information for a time before it is passed to the rest of the syndicate, and some lenders would refuse to join committee for this reason. Negotiations would continue until the necessary majority/unanimous proportions have been reached.

In the event or possibility of a default, where refinancing or restructuring negotiations are being held, it is possible that the lenders would have a degree of market power, as alternative refinancing options would be limited for the borrower (i.e. the market may not be willing to provide the new finance) and the lenders would have an incentive to

[74] Moody's Annual Default Survey, published 2018.

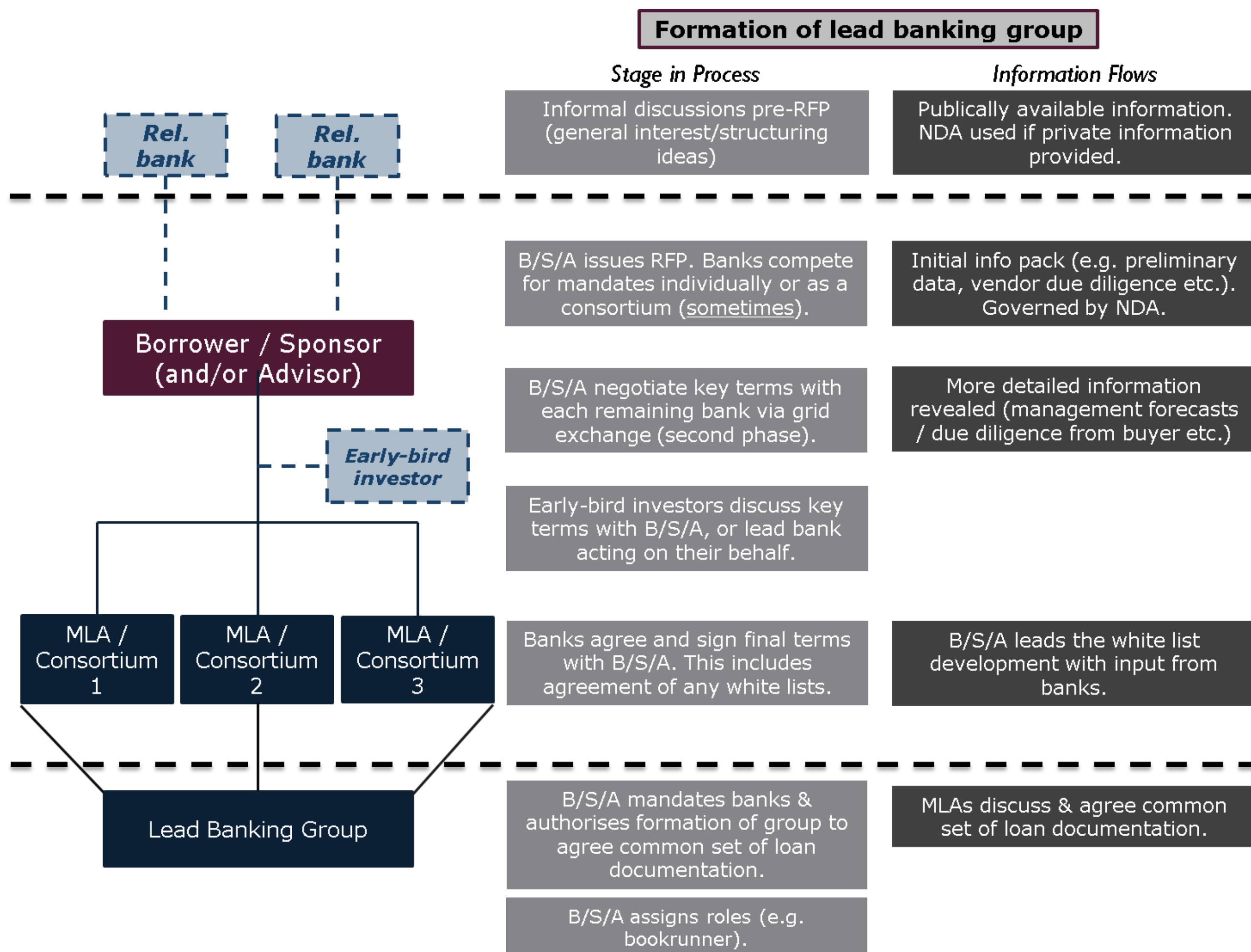
protect their existing investment. The lenders could seek to exploit any such power through bundling in of ancillary services as a condition of refinancing, or, more baldly, through effecting the loan on 'punitive' terms (e.g. pricing excessively). We assess these risks in more detail in Chapter 4.

Banks could decide to sell their shares, which would be an isolated decision (i.e. not discussed with other banks). There is quite a liquid market for distressed debt, e.g. larger banks have specialised trading here. Secondary market sales could be executed by the trading desk, or by the syndicated sales team.

Information exchange in the LBO and PF/INFRA segments

We begin with a series of diagrams that summarise the loan syndicate process for LBO (underwritten/best efforts) and PF/INFRA (club deal) loans, showing the main parties involved and the information flows.

Figure 7: Loan syndication process for LBO (underwritten) loans – formation of the lead banking group



Source: Europe Economics.

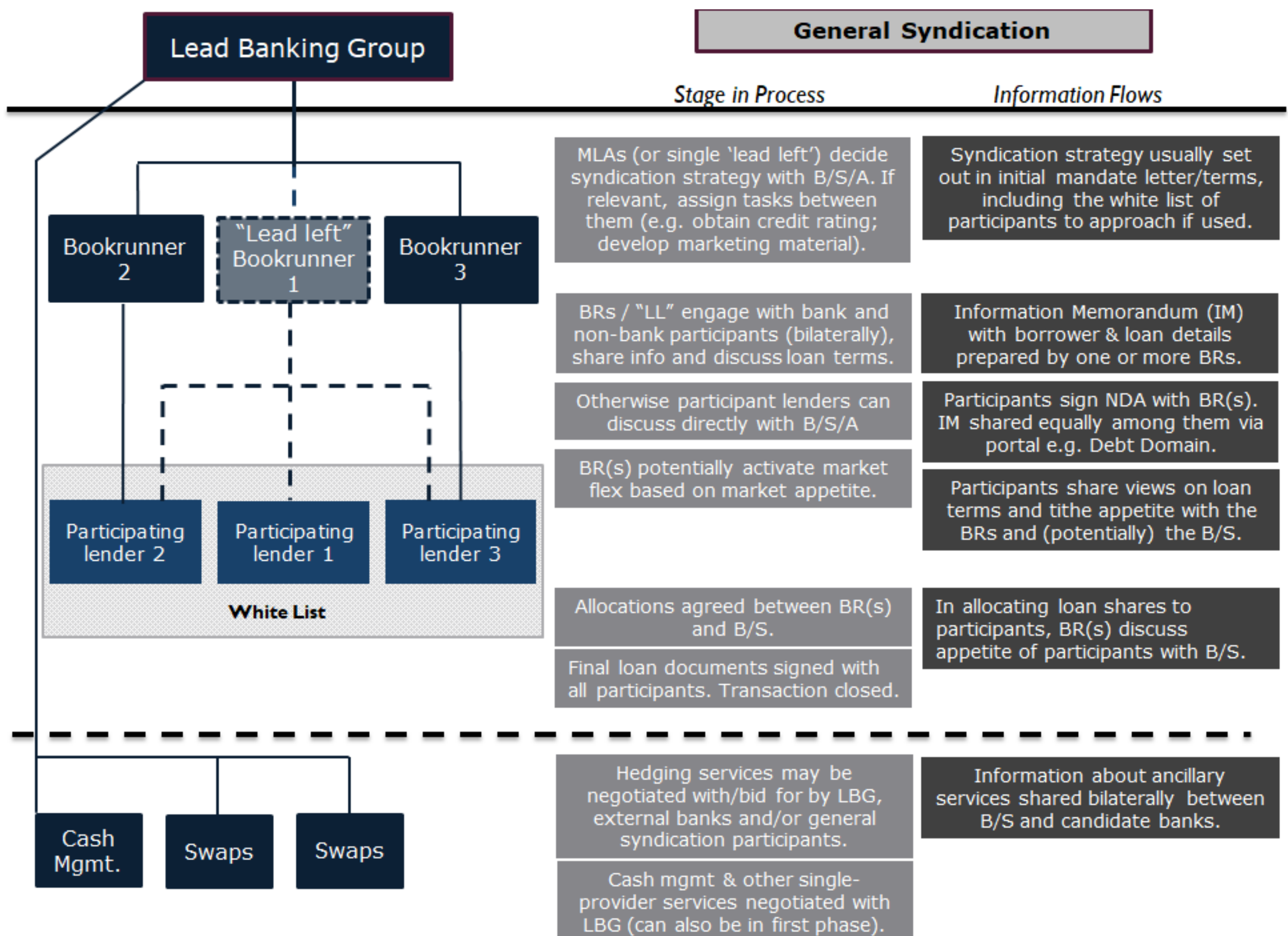
The formation of the lead banking group in the LBO segment involves the borrower/sponsor and/or their advisor, a number of lead banks bidding for various MLA positions – this can be done individually or as a ready-made consortium, and potentially relationship banks providing input before the RFP stage (this happens less often in LBO loans than in PF/INFRA, and the relationship banks would still need to

compete formally in the RFP process). Sometimes a borrower/sponsor may wish to bring a non-bank investor (an 'early bird' investor) into the initial discussions with the lead banking group. Alternatively, a mandated bank could approach the early bird investor pre-marketing (i.e. prior to any general syndication). The diagram above represents only the first of these two possibilities (for clarity).

The process is designed to keep the competing banks separate for as long as possible, with negotiations occurring bilaterally between the borrower/sponsor/advisor and each bank or consortium. Information flows are controlled under NDAs.

Once the lead banking group is formed, the banks are brought together to agree the syndication strategy. The borrower/sponsor also assigns various roles at this stage, including bookrunners who are in charge of the general syndication phase and liaise between the participants and the borrower/sponsor. The figure below illustrates this process.

Figure 8: Loan syndication process for LBO loans – general syndication

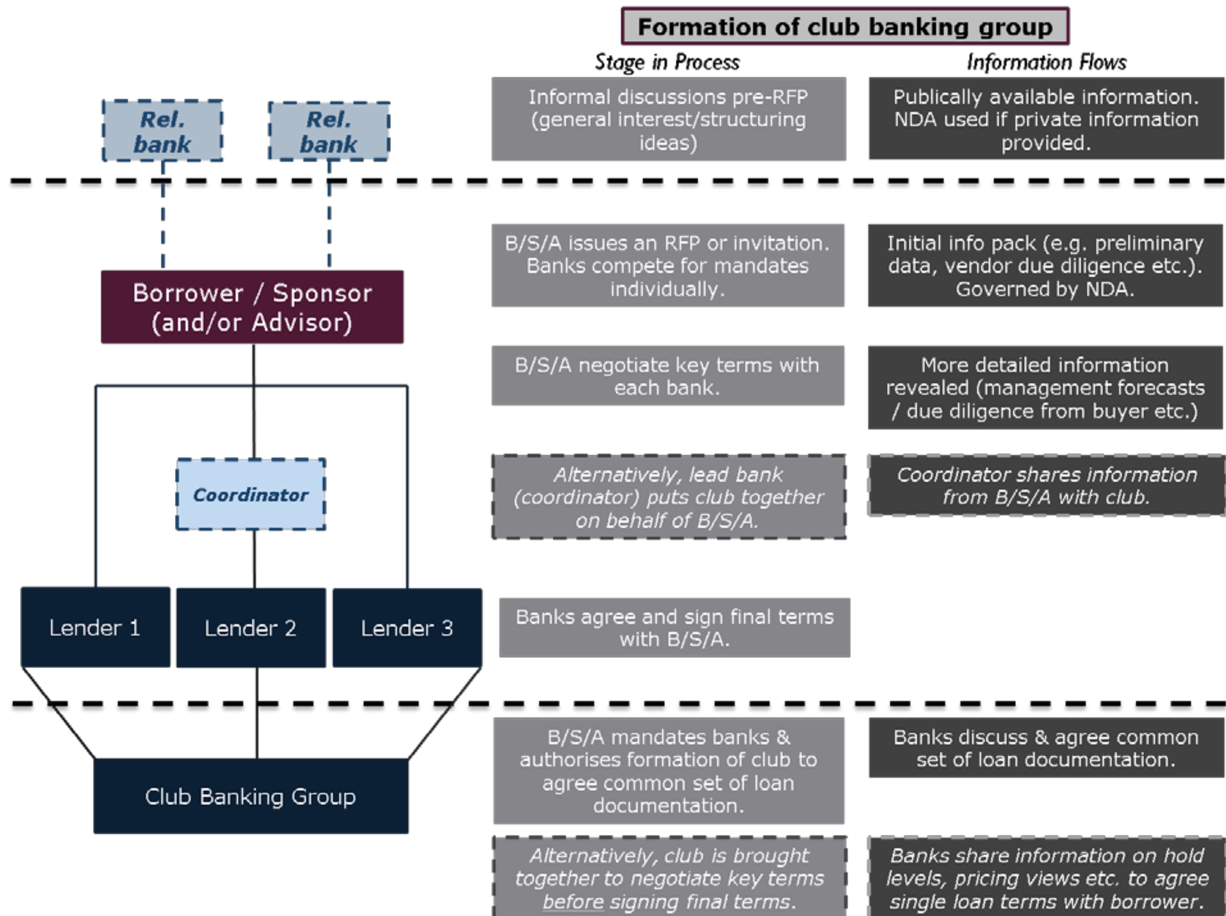


Source: Europe Economics.

The key negotiations at this stage take place between the (potential) participant lenders and the bookrunners, who relay the market response to the borrower/sponsor and the rest of the lead banking group. In some transactions (e.g. very large deals that are potentially more difficult to market) a single 'lead left' bookrunner would be appointed instead of there being multiple bookrunners. Participants to be approached usually form part of a white list imposed by the borrower/sponsor in order to retain control over who can participate in the loan.

At this stage, ancillary services may also be negotiated between the lead banking group and the borrower/sponsor (participant banks may also be involved at this stage but these services are more likely to be awarded to those in the lead group).

Figure 9: Loan syndication process for PF/INFRA (club deal) loans

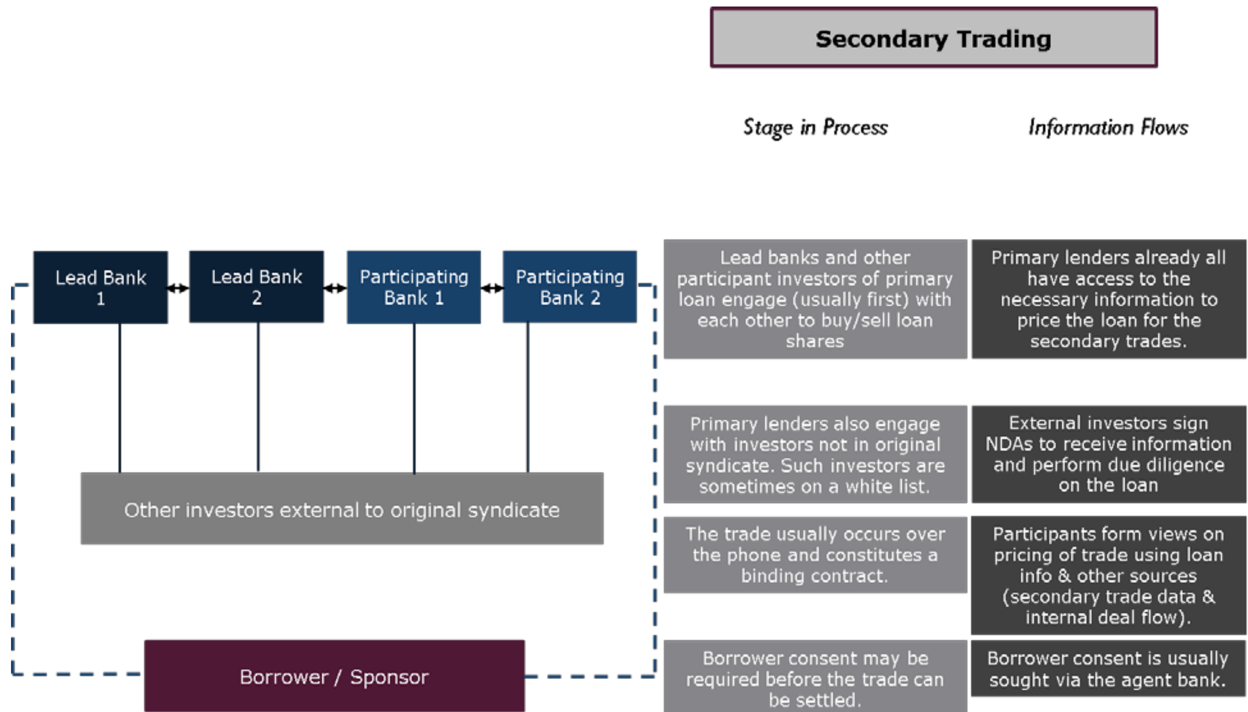


Source: Europe Economics.

The figure above illustrates the process of forming the syndicate in a PF/INFRA loan (i.e. a club deal). The process is largely similar to the formation of the lead banking group in LBO loans, although there is a higher likelihood of relationship banks being involved at the pre-RFP stage. The borrower/sponsor/advisor typically puts the club together and negotiates directly with each lender, although there are cases where a coordinator might be appointed to form the club and negotiate with lenders on behalf of the borrower/sponsor.

The club banks typically agree and sign final terms with the borrower/sponsor before being brought together to agree documentation; however, there are also cases where the club would negotiate terms together and with the borrower/sponsor before signing the final terms. There is no formal general syndication phase to club deals (though the clubs' members may sell down some part of the debt post-close). Any negotiation of ancillary services would be towards the end of the club formation, as illustrated in the general syndication figure for LBOs above.

Figure 10: Post-closure processes for LBO and PF/INFRA loans



Source: Europe Economics.

The figure above illustrates the secondary loan market phase. (For the avoidance of doubt, we treat pre-closure as the primary market, and post-closure as the secondary market in loans). The process is similar for both LBO and PF/INFRA loans, albeit the evidence indicates that secondary activity in LBO debt is substantially more important than in PF/INFRA. Lead banks, participant lenders and non-syndicate lenders can all be involved in the secondary loan market. The borrower/sponsor's white list (if there is one) carries through to the secondary market, such that any non-syndicate (club) investors would either need to be on the white list in order to participate, or the borrower/sponsors consent would need to be given.

Conclusions

In this section we summarise the features of the loan syndication process which may pose risks to competition. The purpose of these conclusions is to highlight issues to be examined more detail in Chapter 4, where our hypotheses of risks are fully developed within our competition framework and then tested against the empirical evidence. The summary points below should therefore not be considered as our developed competition risk hypotheses, but rather an iteration of the points to be addressed further in Chapter 4.

The table below summaries the features of the syndication loan process that may pose risks for competition law or sub-optimal outcomes. We indicate where issues are the same across LBO and PF/INFRA loans, and where they are similar but more pronounced in a certain loan type.

Table 10: Summary of issues to be examined in Competition Framework – LBO and PF/INFRA loan process

Element of process	Feature to be examined under Competition analysis	Applicability to LBO or PF/INFRA loans
Formation of initial banking group		
Appointment of lead banking group	If borrowers/sponsors hold initial discussions with relationship banks before the RFP process this may unduly influence the syndication process in the banks' favour.	Given the bespoke nature of many PF/INFRA loans, the uncertainties around structure and market appetite may be greater and thus initial scoping discussions with relationship banks may be more likely for these loans.
	Appointing the lead banks directly without a competitive (e.g. RFP) process may influence the outcome of the syndication process if these banks propose terms that are uncompetitive. For example, it could make the likelihood of settlement of the loan terms at the 'highest common denominator' amongst the participating banks more likely (because the lenders approached represented insufficient market coverage).	Similar conceptual issues across LBO and PF/INFRA, albeit this looks to be more common in PF/INFRA.
	The risks of information sharing may be influenced by whether banks are invited individually to compete for a position in the lead banking group, or if they compete as ready-made consortia.	Similar issues across LBO and PF/INFRA.
Information issues in the competitive formation of the lead banking group	Where a (bilateral) competitive process is used to appoint banks to the lead banking group and negotiate pricing and other terms, any sharing of information between banks is not an intrinsic/necessary part of the loan syndication process and is governed by NDAs. Borrowers/sponsors use of NDAs to control information sharing between competing lead banks is a key element in retaining competitive tension in this approach to the formation of the lead banking group. The extent to which such NDAs can be enforced will influence the risks associated with [illegal] information sharing.	Similar issues across LBO and PF/INFRA.
Market soundings	The use of deal-specific market soundings (by the syndication desks), where lead banks share details of the loan with potential participants or competitors to gain insight into market appetite and develop their proposals on price and hold levels – with or without borrower consent	Given the more bespoke nature of PF/INFRA loans, the availability to banks of internal / vendor information may be more limited and thus the likelihood of more specific market soundings between potential competitors is greater.

Element of process	Feature to be examined under Competition analysis	Applicability to LBO or PF/INFRA loans
	- raises risks associated with information sharing and possible coordination / collusion between lenders. More generic market soundings by the syndication desks of lead banks are conducted with market participants not involving specific details of the transaction are less risky – and indeed could be pro-efficiency for difficult to price credit – but the line between specific and generic market soundings may become blurred without appropriate policies and safeguards	Generic market sounds as means of remaining up to date with participant market a feature of underwritten loans and thus more relevant to LBO loans than PF/INFRA.
Information issues in a collaborative formation of the lead banking group	Where lead banks are invited by the borrower/sponsor to discuss key terms ahead of the finalisation of the loan terms (for example in situations of high market uncertainty), information sharing becomes an intrinsic part of the syndication process. This may have implications for competition and the outcome for the borrower/sponsor.	More applicable to PF/INFRA loans, although cannot rule out with LBO.
Appointing a single MLA to lead the syndication process	The appointment of a single MLA to lead the formation of the initial banking group (which we describe in the Chapter as a more 'traditional' model of syndication not common to the west Europe markets, but potentially more relevant to other, more national markets) may invest too much power with a single bank and affect intra-syndicate dynamics. This model may also increase the risk of information sharing between banks as the borrower/sponsor is not negotiating bilaterally with each one.	More applicable to PF/INFRA loans, although cannot rule out with LBO.
General syndication		
Information sharing among participants	Unsanctioned information sharing (as information is distributed under NDA) between the participants in the general syndication may facilitate anti-competitive behaviour or invest the syndicate with excessive bargaining power, resulting in the loan terms unduly moving against the borrower/sponsor.	Applicable to underwritten and therefore primarily LBO loans.
Lead left	The use of a single bookrunner ("lead left") to manage the whole general syndication process and be the main point of interaction between the borrower/sponsor and the market may lead to a restriction in the number of eligible bookrunners for future transactions.	Applicable to underwritten and therefore primarily LBO loans.

Element of process	Feature to be examined under Competition analysis	Applicability to LBO or PF/INFRA loans
White lists	The use of white lists to restrict the marketing of the loan in the general syndication phase (and in secondary trading) may unduly limit competition for the loan by participants. Lead banks may be able to exert pressure on the borrower/sponsor to ensure that participants which are favourable to them are included in the white lists, which may facilitate reciprocity and coordination between lenders in future transactions.	Applicable to underwritten and therefore primarily LBO loans.
Provision of ancillary services		
Hedging services	Potential risks around the provision of hedging services include the discussion among banks in order to share out the services between them and/or coordination on pricing, and uncompetitive bundling of the services with the initial loan terms which restricts the choice of borrower/sponsors. The competitive dynamics related to the provision of hedging services will depend on the way in which these are negotiated and awarded, such as: ▪ The timing of when the hedging services are discussed and awarded (e.g. after the primary loan has been concluded or as part of the negotiation of the initial loan terms). ▪ The banks to whom the hedging services are allocated (e.g. those within the syndicate or not). ▪ The process under which the services are allocated (via competitive bids from banks or allocated directly by the borrower/sponsor).	Hedging services more commonly required in PF/INFRA loans, but issues cannot be ruled out with LBO loans.
Cash management	The sticky nature of cash management services may give rise to competition risks if borrowers/sponsors are not able to easily switch providers (however, this stickiness is not a function of the syndicated loan market). The impacts of this would be exacerbated if the provision of such services also gives incumbents an additional advantage in the provision of the syndicated loan.	Similar issues across LBO and PF/INFRA.

Element of process	Feature to be examined under Competition analysis	Applicability to LBO or PF/INFRA loans
Advisory services	The use of an advisor by the borrower/sponsor to assist in the loan syndication, where the advisor is one of the syndicate banks, could give rise to conflicts of interest, undermine the competitive nature of the syndication, and result in sub-optimal outcomes for the borrower/sponsor.	The use of syndicate banks as advisors more likely in PF/INFRA loans, but cannot be ruled out for LBO loans
Post closure		
Borrower/sponsor restrictions on secondary trade transfers	The process of secondary market transfers can be limited by the white list approach, whereby only institutions on the pre-defined list developed for the primary loan would be eligible to participate in secondary market trades. This may lead to inefficiencies if this prevents or holds up trades. Similarly, the need for transfers outside of the white list to be approved by the borrower/sponsor may introduce inefficiencies that may undermine the functioning of the secondary market.	Similar issues across LBO and PF/INFRA, if traded.
Refinancing and restructuring	There is a risk that the existing syndicate may be able to exert bargaining power over the borrower/sponsor in the event of a breach of covenants, i.e. when restructuring negotiations take place the group of leading banks could be in a position of strong bargaining power – against the interests of the borrower - as alternate sources of which may be restricted. This needs to be balanced against the needs of borrower for capital.	Similar issues across LBO and PF/INFRA.

3. The Loan Syndication Market

In this section we provide a description of the syndicated loan market in the EU, focusing on our core sample of Member States and three market segments of interest (i.e. LBO, Project and Infrastructure), by using Thompson Reuters Loan Connector data, covering the period January 2010 to December 2017.[75] We also draw on our literature review and fieldwork with lenders, borrowers and sponsors to develop conclusions and hypotheses for how the features (and evolution) of the market may affect competition.

This section includes the following:

- An overview of the syndicated loan market both globally and in the EU. This covers the syndicated lending market in its entirety. We then focus on the segments of greatest interest to this study, i.e. the LBO segment and the PF/INFRA segment, specifically in the countries of interest.
- We describe the market participants active in these areas from the demand and the supply side, including an analysis of the economic benefits and drawbacks of syndicated lending from both borrowers' and lenders' perspectives; an analysis of the alternatives to syndicated loans; impacts of financial services regulation; and cross-border dimensions.
- We also describe other salient aspects of the market such as loan pricing, fees and covenants. We describe the secondary market for syndicated loans, including the economic benefits of secondary trading and implications for competition.
- The conclusions to this chapter summarise the various hypotheses we will explore in more detail in the framework of competition issues and the associated analysis in Chapter 4. We also summarise our considerations on the product and geographic market for syndicated loans and implications of market trends.

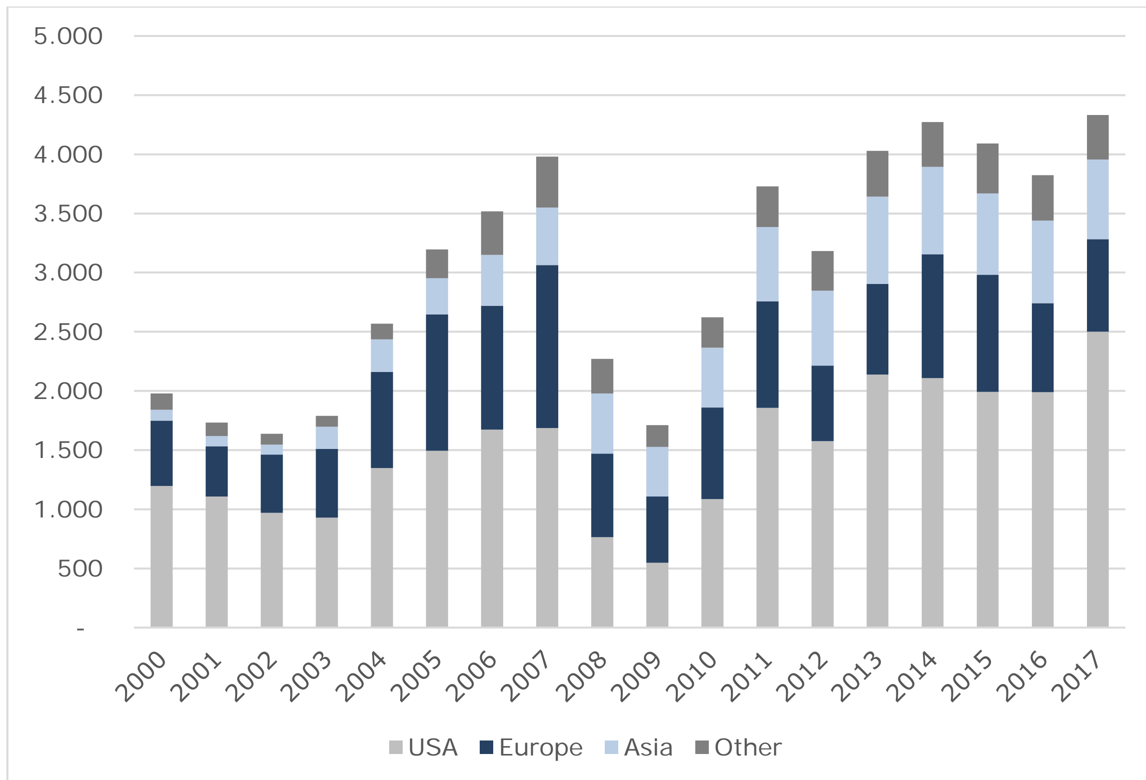
Overview of the global syndicated market

The global syndicated loan market is a major source of debt capital, with borrowers raising over $4 trillion globally in 2017. The graphs below present an overview of the main syndicated loan markets across the world, namely Europe, the United States of America (USA) and Asia. (Many large lenders incorporate Europe into an EMEA-focused region. Given our interest in Europe, we have separated out European borrowers discretely.) These data include all forms of syndicated lending, including corporate loans, etc.

The syndicated lending market in Europe received a major boost from the introduction of the Euro, but was also strongly influenced by the credit bubble building through to the credit and Euro crises of 2008–2010. Indeed, the global impact of the credit crunch is very apparent in these data. The USA market is by far the largest – and its relative significance has in fact grown subsequent to the credit crunch as the European market has only partly reverted to pre-crisis levels.

[75] We describe in Appendix 2 how we defined these segments for the purposes of extracting data from Loan Connector.

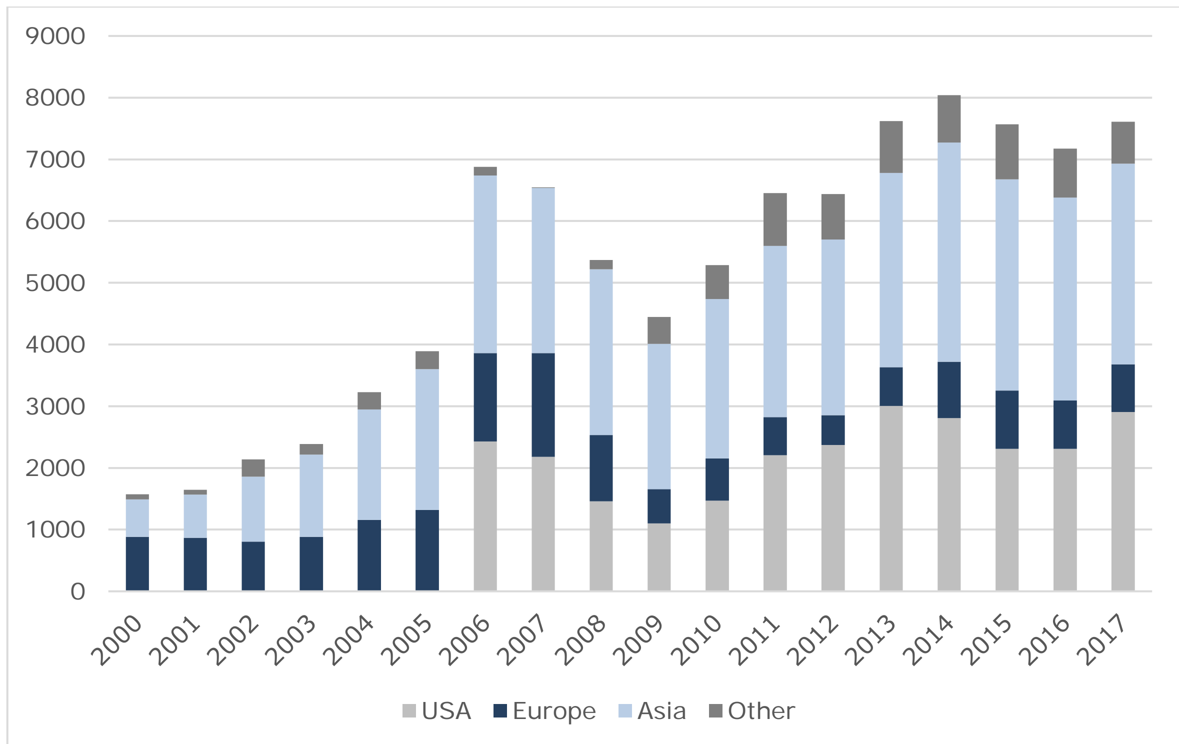
Figure 11: Annual syndicated lending (US$ billion)



Note: Other includes Russia, Middle East and Africa, and the Americas outside of the USA.
Source: Thomson Reuters Loan Connector.

The distribution of transactions is somewhat similar. Again, transaction numbers in Europe have not recovered to pre-crisis levels. (Comparable US transaction data are only available from 2006 onwards.)

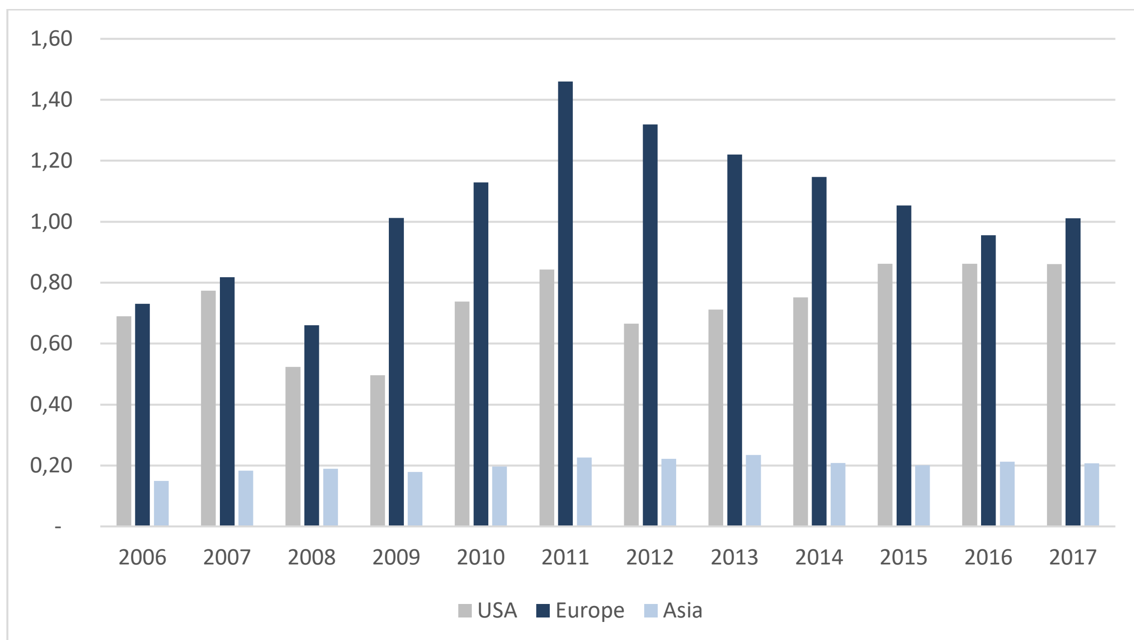
Figure 12: Number of syndicated lending transactions



Note: USA data are only available from 2006 onwards. The number of deals will be underestimated as Loan Connector does not report number of deals for loans that do not easily fall under either Investment Grade or Leveraged according to Thomson Reuters LPC's criteria.
Source: Thomson Reuters Loan Connector.

As implied by these charts, average transaction sizes also vary across these regions – in particular, the average transaction size in the Asia region is significantly below the levels seen in the USA and Europe. On these data, at present, the average transaction value is about $1 billion in Europe and $0.9 billion in the USA.

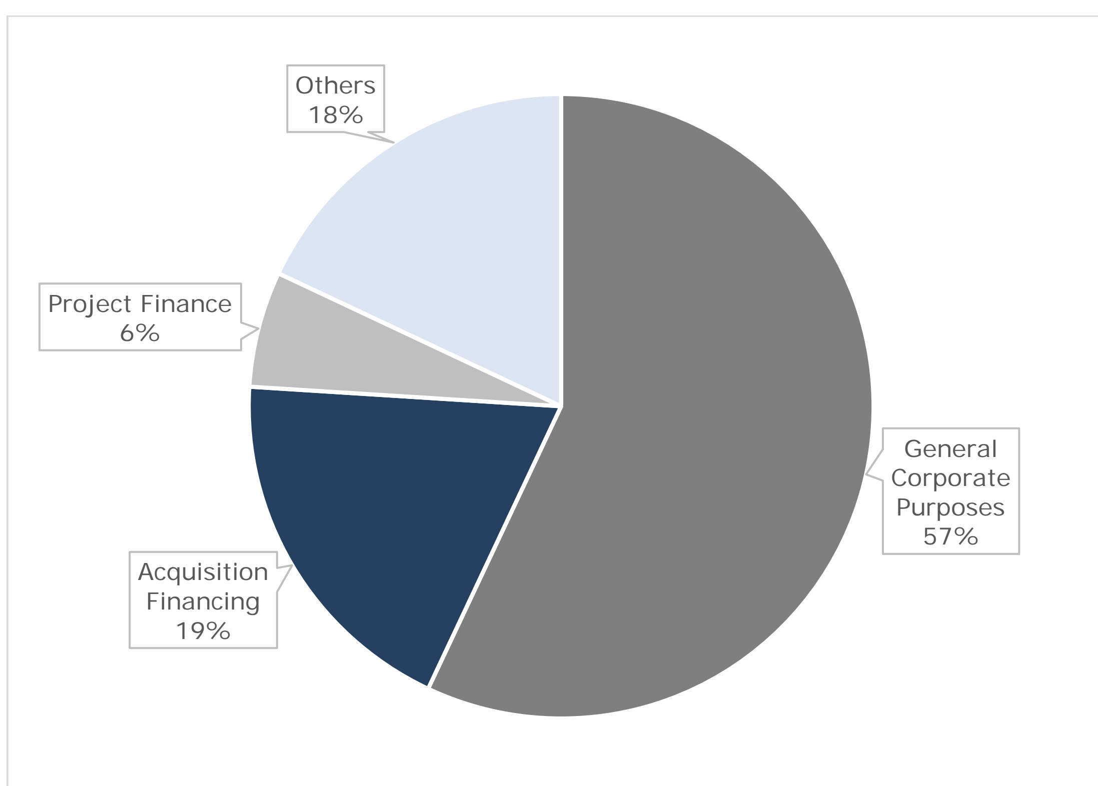
Figure 13: Average deal value of syndicated lending transactions (US$ bn)



Source: Thomson Reuters Loan Connector.

The above has considered the global syndicated loans market. In this study, we are mainly focused upon the LBO, PF and INFRA segments within this market, and within these segments, upon borrowers in France, Germany, the Netherlands, Poland, Spain, and the UK. The chart below approximates the relative scale (within the EMEA region) of these. Project Finance includes both PF and INFRA. The Acquisition Finance share includes – but is not limited to – LBO financing (since corporates also conduct acquisitions).

Figure 14: Distribution of syndicated lending in EMEA in 2017, by purpose of loan



Source: Thomson Reuters Global Syndicated Loans Review 2017.

The syndicated loan market in the LBO, PF and INFRA segments

We now turn specifically to the segments of interest to this study, i.e. LBO, PF and INFRA. Within Europe, across 2010-2017, a total of €670 billion was borrowed across the EU28 in the three segments of interest.

The share of the six countries we focus on in this study (i.e. the UK, Germany, France, Spain, the Netherlands and Poland) is about 74 per cent (€500 billion) of this total of borrowing over the same time period. More than 50 per cent of this borrowing is in LBOs (Table 11). The UK is by far the largest supplying market, with France, Germany and Spain having comparable shares over this time period. LBOs account for the greater share of borrowing in all Member States in our sample, with the exception of Spain where infrastructure has been the main one. The UK also has a relatively higher share of borrowing for infrastructure compared with the other Member States.

Table 11: Total amount borrowed by Member State and loan purpose (2010-2017, €m)

	LBO	Project Finance	Infrastructure	Total (%)	Total (€m)
DE	23%	5%	12%	17%	83,886
ES	10%	12%	23%	15%	73,876
FR	18%	32%	14%	19%	92,958
NL	14%	8%	9%	11%	57,031
PL	3%	0%	2%	2%	9,899
UK	32%	42%	40%	36%	181,379
Total (%)	100%	100%	100%	100%	
Total (€m)	256,499	67,254	175,277		499,030

Source: Europe Economics (using Thomson Reuters Loan Connector).
Note: Loan Connector does not report amounts borrowed for 17 out of the 4,020 tranches.

The evolution of the amounts borrowed from 2010 to the end of 2017 by the purpose of the loan and by Member State is set in detail in Figure 1. A decline in the market was experienced particularly strongly in Spain post-Euro crisis, but is also evident in the Netherlands and Poland. The largest markets – i.e. borrowers located in Germany, France and the UK - exhibit much more consistent deal flow than the others. Poland is a much smaller market than the others, with perhaps only 1-2 transactions "live" at any one time.

By deal number, the most important markets (based on the location of the borrower) over the period 2010-2017 for LBO, PF and INFRA deals have been the UK, France, Spain, Italy, Germany and the Netherlands. This means five of the Member States of interest to this study are among the top six Member States by number of deals, with the other (Poland) being 10th. In 2017, the LBO-related borrowing in these six countries was about €58 billion, whereas PF/INFRA-related borrowing was about €35 billion. It is important to note that the Loan Connector data only record the location of the borrower and not the project itself. This means that some of the deals recorded may apply to projects in other countries within or, indeed, outside of our sample. It is also possible that some projects undertaken in these six sample Member States involved external borrowers and thus do not appear in our dataset, although based on our lender interviews (who reported that the country of the borrower aligned to the country of the project) we do not believe this is likely to be a significant proportion.

Table 12 shows the distribution of deals included amongst the six Member States and by loan purpose, covering the whole period 2010-2017. Most (86 per cent) are split evenly between LBO and Infrastructure, with Project Finance deals being the residual.

Table 12: Total number of deals by Member State and loan type (2010-2017)

	LBO	Project Finance	Infrastructure	Total
DE	150	23	68	241
ES	77	70	228	375
FR	188	50	199	437
NL	76	17	36	129
PL	10	1	22	33
UK	247	78	181	506
Total	748	239	734	1,721

Source: Europe Economics (using Thomson Reuters Loan Connector).

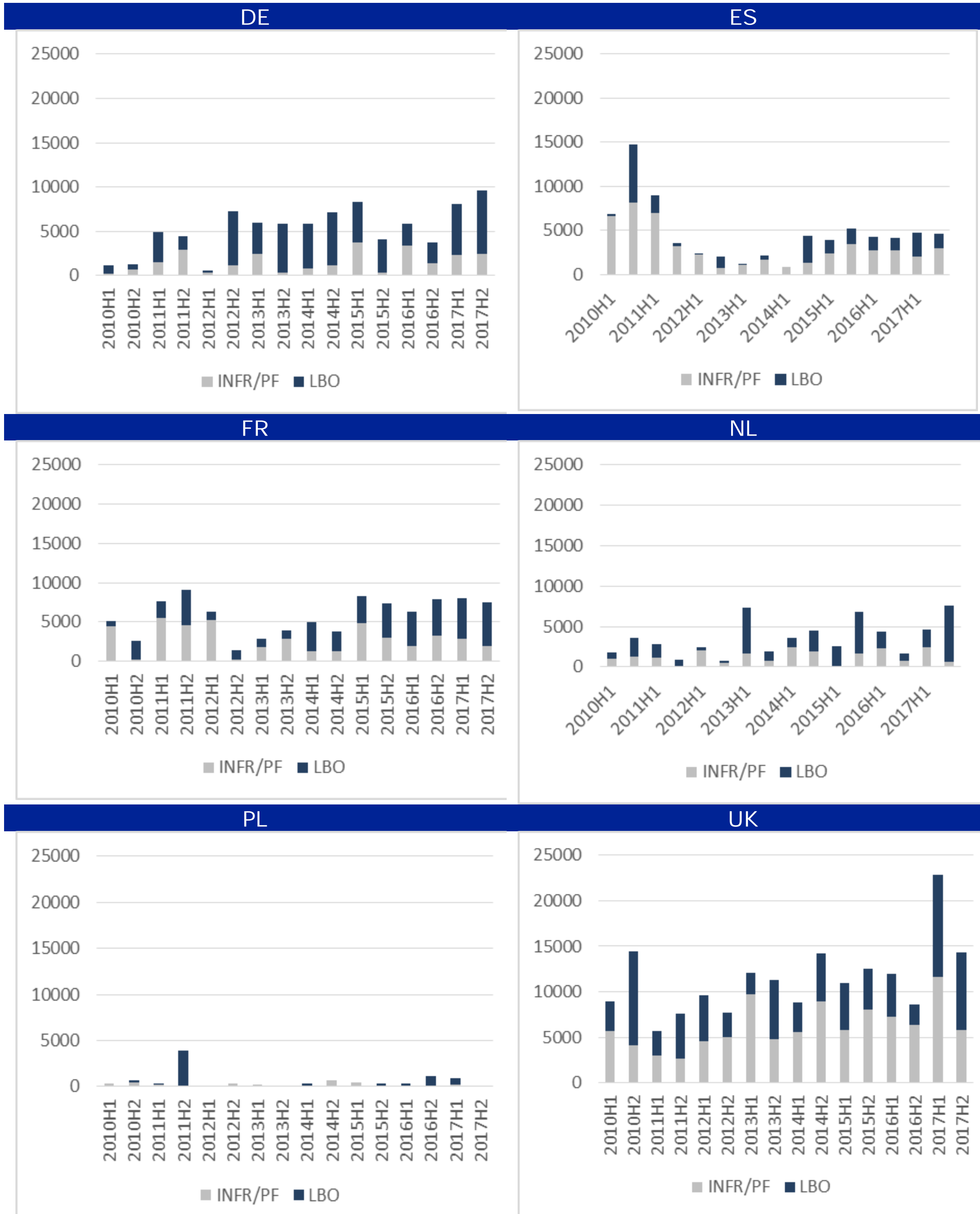
Any given loan syndication can involve multiple 'tranches'. This means that the syndication of a revolving credit facility (one tranche) could differ in process and in syndicate members to a Term Loan (another tranche) on the same deal. The total of 1,721 deals in turn corresponds to over 4,000 tranches.

It is worth noting that the average deal values vary markedly by loan purpose. Again, looking across the entirety of the period 2010-17, the average LBO deal value was about €240 million in the six countries of interest (albeit notably lower than this in France and Germany). By contrast, the average deal in Project Finance (under the definition used here) was almost €1.1 billion, whereas the average Infrastructure deal was less than €0.1 billion.

Evolution of syndicated lending across LBO and INFRA/PF loans

The evolution of the amounts borrowed by the purpose of the loan and by Member State is set out below.

Figure 15: Total value of deals by Member State (biannual, €m)



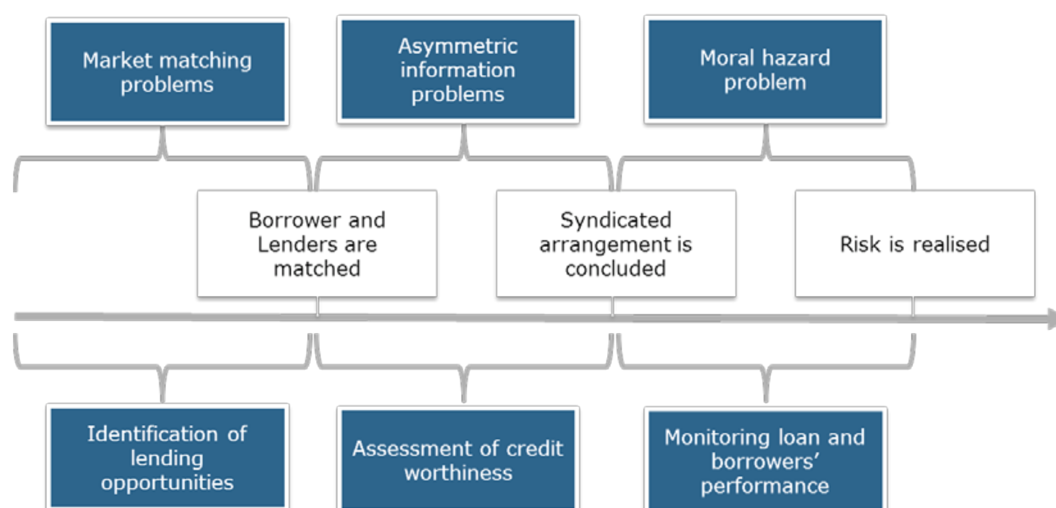
Source: Europe Economics (using Thomson Reuters Loan Connector).

The economic benefits and drawback of syndicated lending

Borrower's perspective

In this section we consider the economic advantages of syndicated lending compared to other forms of lending as part of our consideration of the product market for syndicated loans. We also draw on the literature around the economic benefits and drawbacks of syndicated loans to identify further hypotheses to explore in Chapter 4. The stylised diagram below describes the typical issues arising in a general borrower/lender relationship (the boxes at the top), and how there are typically overcome (the boxes at the bottom).

Figure 16: Typical issues in credit markets



The syndicated loan market addresses the issues around market matching, information asymmetry and moral hazard in a different way relative to both bilateral lending and public debt markets (e.g. the corporate bond market). This creates both benefits and drawbacks for borrowers and lenders, which we discuss below.

Syndicated loans offer an alternative form of debt financing to bilateral lending or corporate bonds. A borrowers' choice of a syndicated loan will be determined by the benefits offered by this form of lending, but also by the availability and suitability of the other two forms. This will depend on several factors, such as borrower characteristics and the characteristics of the loan.

We first discuss the advantages of syndicated loans over bilateral lending and corporate bonds along the three dimensions in the figure above, before describing the potential disadvantages. We draw on our literature review to set out the theoretical analysis before describing insights from our fieldwork.

Market matching. For firms with very large financing needs, obtaining a loan from a single lender may not be possible if individual banks do not have the capacity or the necessary risk appetite. Whilst multiple bilateral loans may solve this capacity problem, they may bring efficiency problems. In comparison, a syndicated loan would provide flexible and efficient funding through access to multiple lenders, but within a single set of terms and conditions, requiring less documentation, time and resources. As a syndicate can consist of lead banks who take on all or a large proportion of the underwriting, it also increases the scope for a broader range of lenders than multiple bilateral loans, and the borrower may benefit from the combined experience of this wider range of lenders.

In terms of market matching, the corporate bond market may provide similar benefits of meeting a large borrowing requirement across a multiple number of investors in a more efficient way than bilateral lending. However, other factors may mean that the corporate bond market is not suitable, such as the costs of raising an IPO, projects that require a degree of confidentiality, and issues such as information asymmetries and moral hazard, as discussed below.

Asymmetric information problems. Information asymmetries can impede investors' assessment of the credit worthiness of a borrower. This may result in borrowers facing higher costs on the bond market compared to private bank lending, as bond investors may require higher returns to compensate for information asymmetries if they did not have access to all relevant information regarding the borrower and the loan purpose. This would be particularly relevant to loans in project finance, infrastructure and LBOs, where public credit ratings of the borrower are less likely to exist for the bond market to access (especially if the borrower is an SPV with no prior credit history). Private lenders (i.e. those involved in syndicated loans) are more likely to be better at assessing the credit worthiness of the borrower and the project than the public bond market. This could also translate to the quality of any credit ratings sought by the lead banks for syndicated loans, as these ratings would be based on this superior private information.

Moral hazard problem. Information asymmetries may be expressed in moral hazard, whereby investors are unable to observe the activities of borrowers. Private lenders can be more efficient and effective monitors. Such monitoring is typically achieved by incorporating restrictive financial and non-financial loan covenants. These are a feature of loan contracts (both bilateral and syndicated, although as we have noted decreasing in prevalence in the LBO segment) but less common in capital market instruments.

Private bank lending may be more beneficial than a public debt market if the borrower requires more flexible contracts, particularly in the event of financial distress. As described earlier, a borrower is more likely to be able to negotiate a solution that does not involve liquidation with a limited number of creditors compared to the bond market. Private bank lending may also be more beneficial if the timing of the loan is critical – i.e. in LBO deals the private equity house typically need certainty of funds ahead of bidding for a target.

However, in this case a syndicated loan may have drawbacks compared to bilateral loans (if that is a viable alternative). There is arguably a more complex relationship between borrower and lenders within a syndicate which could increase decision-making time in crucial moments of distress such as debt restructuring, where a consensus by all (or most) syndicate members would be required for a final decision to be taken. As discussed further in Chapter 4, restructuring in situations of distress may confer a degree of bargaining power on the syndicate, since the borrower may lack options, although this would also be the case with a bilateral loan.

Other benefits and drawbacks of syndicated loans for borrowers compared to alternative sources of lending include:

- Compared to bilateral loans, syndicated loans may present drawbacks to borrowers if they limit the borrower's ability to influence certain aspects of the functioning of the syndicate (such as the negotiation of the final terms and pricing of the loan among the syndicate members). This will depend on the sophistication of the borrower and his role in the formation of the syndicate.

- Syndicated loans introduce different dynamics between lenders and the borrower which could affect loan pricing and other terms. For example, the existence of lead arrangers/underwriters within a syndicate who retain a significant proportion of the loan may reduce the perceived riskiness of the loan to other participant lenders, who would then be willing to lend at a lower price than would otherwise be possible.
- On the other hand, information asymmetries *between lenders* may result in negative pricing impacts for the borrower, particularly where the lead arrangers do not take on a significant amount of the loan or are considered likely to sell it off on the secondary market. The literature indicates that when syndicate-participant banks have information inferiority compared to the lead arrangers in the syndicate, they require higher returns for the increased risk (arising from the asymmetries) – but also that repeated interactions with a borrower can reduce or even eliminate such an inferiority.[76]
- With respect to the moral hazard problem that arises in lending relationships, participant investors /lenders may demand higher prices against ex post opportunistic arranger behaviour. This "diminished monitoring hypothesis" means syndicate-participant lenders cannot rely on the arranger to monitor the borrower post-closure, and would have to perform this role themselves. However, there can be mitigated where the MLAs are reputable,[77] as it has been found that such MLAs suffer (from reduced future lending volume) when reputation suffers (e.g. due to a default).[78] It is important to note here that there is no legal responsibility on MLAs to take ex post responsibility for monitoring (i.e. this falls to all members of the syndicate). The facility agent (which can be part of an arranging bank) has a duty to notify syndicate members in the event of default once this occurs but this role is defined in standard LMA documentation as being "solely mechanical and administrative in nature", i.e. it is not expected that the agent would seek to predict default.
- Compared to bond markets, syndicated loans provide the borrower/sponsor with greater control over loan participants, as white lists can be used to exclude the involvement of certain investors (such as so-called 'vulture funds').

An empirical study for the ECB shows further evidence of where syndicated lending is economically advantageous. The study found that firms in the euro area tend to prefer syndicated loans over corporate bonds when they are larger, more profitable, highly leveraged, with a higher proportion of fixed to total assets, but lower (publicly measurable) growth opportunities.[79] We expand on the characteristics below, which support our discussion of how syndicated loans address the three main issues in credit markets. We note that the ECB's findings are related to corporate loans, but the principles are likely to apply across all lending.

- Firm size — the issuance of corporate bonds entails a significant fixed cost component in terms of issuance costs. Therefore, for relatively small financing needs, it is typically more cost-effective to rely on bilateral bank loans (indeed, there is a practical lower bound below which corporate bond issuance is de facto not available). At the same time, very large firms with large borrowing needs can prefer syndicated loans above corporate bonds. This is driven by the circumstances of the

[76] Gadanecz, Blaise, Kara, Alper and Molyneux, Philip (2014) "Asymmetric Information Among Lending Syndicate Members and the Value of Repeat Lending" Journal of International Financial Markets, Institutions and Money.
[77] Kamstra, Mark, Roberts, Gordon, Shao, Pei (2014) "Does the Secondary Loan Market Reduce Borrowing Costs?" *Review of Finance*, Volume 18, Issue 3, Pages 1139–1181.
78 Gopalan, R., V. Nanda, and V. Yerramilli (2009) "Lead arranger reputation and the loan syndication market".
[79] Altinbas, Yener, Kara, Alper and Marques-Ibanez, David (2009) "Large Debt Financing: Syndicated Loans versus Corporate Bonds" ECB. The study links the choice of debt market to the specific characteristics of firms measured prior to the financing decision.

firm. For instance, issuing corporate bonds can also include substantial costs stemming from information asymmetries (whereby investors who are unable to observe the firm's activities may demand higher returns for the risks generated by such information asymmetry). Firms with complex financing needs and uncertain risk profiles may therefore find it less costly to borrow from the syndicated loan market compared to the corporate bonds market. This information asymmetry issue is relevant to all three areas of interest in this study, i.e. LBOs, project and infrastructure finance.

- Financial leverage — since high financial leverage can be interpreted as a proxy for financial distress, highly levered borrowers are likely to require greater monitoring from lenders. In cases of financial distress, the limited number of parties in bank financing allows for an easier and better-coordinated resolution. Given loan syndication entails a more direct level of monitoring compared to capital market debt, this could explain the findings that firms with higher levels of leverage tend to prefer loan syndication over corporate bonds. Again, all three segments of interest to this study are likely to involve borrowing entities with high leverage (e.g. in an LBO, effectively by definition, and in project/infrastructure finance the borrower may be an SPV, with initially at least, limited assets).
- Growth opportunities — there is evidence that European firms with lower growth opportunities (as measured by the ratio of market-to-book value) tend to prefer syndicated loans over capital market debt. This result can be rationalized by the notion that a high market-to-book value is a publicly visible measure of future expected cash flows which should facilitate firms' access to public capital markets (both debt and equity). In contrast, syndicated loans appear to be a better alternative to bonds when growth prospects can be better assessed through lenders' private information.
- Debt maturity — asymmetric information problems are likely to be exacerbated in the presence of debt with long maturities. This is a possible explanation of why firms that rely on the bond market (where monitoring firm performance is more difficult) tend to carry higher levels of short-term debt, compared to those that rely on syndicated loans.
- Fixed assets — firms with higher levels of fixed assets are more likely to borrow from the syndicated loan market than from the bond market. This could be due to two reasons. First, it is easier to use fixed assets as collateral when borrowing in the syndicated loan market than on the bond market. Second, since fixed assets can be seen as a proxy of liquidation value, the more stringent monitoring of syndicated loans may alleviate the risk of inefficient and premature liquidation of profitable projects.[80]

Lender's perspective

The matching problem in the credit market, as illustrated in the chart at the beginning of this chapter, refers to agents in the market being imperfectly aware of existing economic opportunities. It represents the difficulty of borrowers finding lenders who have an appetite for their level of riskiness, and vice versa. Under some circumstances, in the formation of a syndicated loan the bookrunner acts as the agent in bringing together interested lenders, alleviating the market matching problem. Another way in which the syndicated loan market provides a solution to this market matching problem is by enabling lenders to participate in loans up to their desired

[80] Literature suggests that lenders in public debt (i.e. bond) markets are unable to distinguish, owing to information asymmetry and free-rider problems, between the optimality of liquidating or allowing a project to continue. If such situations are reflected on the debt contracts in the form of harsh covenants, they may, in turn, result in the premature liquidation of profitable projects. See Altinbas et al. (2009).

level of risk and capital, which they would otherwise not have been able to do in a bilateral situation.

Rationale for banks' participation as lead arrangers
Lead banks may have several reasons for participating as a lead arranger in a syndicated loan. It can be a means of avoiding excessive single-name exposure, in compliance with regulatory limits on risk concentration, while maintaining a relationship with the borrower/sponsor. It is also a means of earning fees as part of revenue generation.[81]

In relation to the first point, loan syndications are driven primarily by the lead banks' capital considerations, both in the form of their capital-to-asset ratio and their loan-to-capital ratio.[82] In general, syndication allows banks and other lenders to reduce their exposure to any one borrower and to reduce undesirable concentration. By enabling lenders to serve more borrowers, this provides them with greater geographic and industry diversification. Some of this diversification may be necessary to comply with government regulation.[83]

Lead arranger banks receive high fees for their expertise and efforts, especially in the cases of fully underwritten deals (whilst these types of loans would also entail higher risk, this is likely to be reflected in the pricing).[84] Additionally, commitment fees are imposed on the borrower/sponsor for unused funding and represent a part of lenders' profits. These are associated with the revolver tranches in LBO and PF/INFRA transactions.

Benefits and drawbacks for participant lenders/investors
Syndications and loan sales make it possible for smaller lenders to participate in a loan to a large and/or riskier borrower than otherwise possible on their own, because of legislatively mandated lending limits or internal credit and risk appetites.[85]

Additionally, some participant lenders may not have the size, experience or desire to arrange loans themselves. They would not normally negotiate directly with the borrowing firm, but would have what is defined as an "arm's-length" relationship acting through the arranger.[86] Through syndication, these lenders can gain some expertise and experience in a market where they do not already have exposure.[87]

However, syndicated lending can create an asymmetric information problem between senior and junior syndicate members, whereby the lead arranger(s) has an informational advantage over other syndicate-participants. Prior to the general syndication, the lead banks are likely to know more about the borrower/sponsor than potential participants. In the case of riskier loans, there is a possible hypothesis these lenders may be tempted to retain a lower loan share, syndicating a higher proportion to less informed participants and collecting syndication fees upfront, as well as the opportunity to cross-sell other services to the borrower. One way to mitigate this asymmetrical information problem would be by obtaining a credit rating of the

[81] Gadanecz, Blaise (2004) "The Syndicated Loan Market: Structure, Development and Implications" Publication. Basel: Bank of International Settlements, 2004. Print. BIS Quarterly Review.
[82] Simons (1993) "Why do banks syndicate loans?" *New England Economic Review*.
[83] Simons (1993) "Why do banks syndicate loans?" *New England Economic Review*.
[84] A description of fees and pricing is provided later in this chapter, in the sub-section "Fees".
[85] Simons (1993) "Why do banks syndicate loans?" *New England Economic Review*.
[86] Gadanecz, Blaise, Kara, Alper and Molyneux, Philip (2014) "Asymmetric Information Among Lending Syndicate Members and the Value of Repeat Lending" Journal of International Financial Markets, Institutions and Money.
[87] We examine certain issues around dependency between participant lenders and lead arrangers in the section on general syndication in Chapter 4.

borrower or project.[88] However, whilst credit ratings will be sought in underwritten deals and for certain other loan purposes, credit ratings need not be available for all borrowers or all loan tranches (essentially they are sought when marketing to CLOs and certain institutional investors). Even so, the literature has not found evidence of such opportunistic arranger behaviour. Instead, higher share retention and MLA reputation have been found to mitigate such information asymmetries.[89]

To curb these problems, if an informed lender took on a large proportion of the loan this would provide a credible and positive signal by the informed party to potential participants. When arrangers retain a higher proportion of a syndicated loan, participants view borrowers as less risky and the loans carry lower prices. The empirical literature holds that indeed lead lenders mitigate the adverse selection problem by holding larger proportions of low quality loans with borrowers that require more monitoring.

In the cases when a borrower/sponsor engages in repeated borrowing, participant lenders will not solely rely on information passed on by the arranger but are likely to consider their own information set as well, which they have assembled through repeat interactions with the same borrower.[90] Repeat business is another way of solving asymmetrical information problems. Additionally, since the arranger and participants are repeat players in the loan syndication market, if the lead arranger 'shirks' in its due diligence and monitoring activities, it faces the threat of loss of reputation and future income on part of future syndicate-participants.[91] The credibility of this threat will depend on the nature of the particular loan market. For example, in LBOs, the borrowers may not engage in repeat transactions (although the sponsors of the LBOs — the private equity firms — will do).

The impacts of information asymmetries on competitive dynamics would be influenced by whether the leading banks have particular links with certain junior syndicate members which might enable the latter to take advantage of additional information over other competing syndicate members. The likelihood of leading banks competing as junior members in other deals with the same borrower would also influence competitive dynamics. We explore in more detail in Chapter 4 the issues related to vertical informational asymmetries between lenders.

The regulatory framework of the syndicated lending market

There have been a number of regulatory interventions that have recently come into force (or which are expected to be implemented in the future), which are likely to have an impact on the syndicated loan market. We pay particular attention to the impacts of the Capital Requirements Regulations and Directive IV (CRR and CRD IV), Solvency II, the AIMF Directive and MiFID 2. Our analysis of the impacts draws on available literature and market reports, complemented by our fieldwork among lenders. Details of the regulatory interventions are included in the Appendix 4, and this section presents our conclusions on the key impacts.

[88] The introduction of credit ratings for loans can be understood as a market mechanism that evolved to reduce an adverse selection problem. See Mora, Nada (2013) "Lender Exposure and Effort in the Syndicated Loan Market" *Federal Reserve Bank of Ka*nsas City.

[89] Mora, Nada (2013) "Lender Exposure and Effort in the Syndicated Loan Market" *Federal Reserve Bank of Ka*nsas City.

[90] Baharath, Sreedhar, Dahiya, Sandeep, Saunders, Anthony and Srinivasan, Anand (2009) "Lending Relationships and Loan Contract Terms", RMI.

[91] Gopalan, Radhakrishnan and Nanda, Vikram K. and Yerramilli, Vijay (2007) "Lead Arranger Reputation and the Loan Syndication Market", EFA 2008 Athens Meetings Paper.

CRD IV

The CRD IV and the CRR impose requirements in three areas: capital, leverage and liquidity.

Capital requirements. The capital requirements set by CRD IV are more stringent than those in its predecessor, and the impacts on the syndicated loan market are likely to manifest primarily through the appetite for lending.

- Overall, the amended capital requirements have already had an impact on affected institutions by requiring them to increase the quality and quantity of their existing capital reserves (in turn generating equivalent pressure on returns to equity).[92]
- Increased capital requirements impact the syndicated loan market specifically through their effect on long-term loans. Such corporate loans and long-term asset-based finance businesses (e.g. infrastructure and project finance) have been estimated to increase funding cost by about 10 basis points.[93] This may aid substitution of banks by non-banks in such long-term loans.
- There is an argument that the CRD IV has increased costs claims passed on to borrowers,[94] although any increases in costs would have been justified by the increased financial stability and consumer protection that the regulation sought to bring about.
- The increased regulatory capital charge imposed on financial institutions means that impacted lenders may be increasingly reluctant to take on a fronting role, as this would mean holding more capital to offset the loan asset, as compared to a participating role.

It is worth noting that industry groups, such as the LMA, argued that the CRD IV represents a significant regulatory change for the banking industry which might materially increase the regulatory costs of originating and participating in loan assets and thus the appetite to engage in this activity. On the other hand, empirical and modelling work by the ECB on the impact of higher capital requirements identified some adverse, but relatively limited, impacts on loan supply.[95] The paper states that some distributional impacts would need to be further analysed – in particular in relation to more risky borrowers due to increased risk-based funding costs. [96]

Leverage requirements. The likely impacts on the syndicated loan market include the following:

- The introduction of the leverage ratio could result in due course in a considerable deleveraging of the banking sector, which could decrease banks' appetite for loans in general. Compliance with the leverage ratio requirement could also incentivise banks to take a more junior role in syndicated loans by financing a small part of the loan, in order to keep the requirements for capital low. As a result, in order to compensate for this decreased appetite, particularly for large and high-risk loans, borrowers would — all else being equal — need to pay higher margins. Such an increase has not been observed in the market to date in 2018. This may not disprove the hypothesis since such impacts could be masked by (a) considerable

[92] See LMA (2015) "Regulation and the Loan Market".
[93] Harle et al (2011), "Basel III and European banking: Its impact, how banks might respond, and the challenges of implementation", McKinsey Working Papers on Risk, Number 26.
[94] Bonelli Erede Pappalardo et al. (2014) "Loan documentation in Europe: Recent trends and current issues" http://www.uria.com/documentos/publicaciones/4230/documento/BF001.pdf?id=5398
[95] The ECB's analysis consisted of modelling using established impacts of capital requirements from literature and bank survey data.
[96] ECB (2015) "The impact of the CRR and CRD IV on bank financing: Eurosystem response to the DG FISMA consultation paper". The paper does note that "due caution is required in interpreting the results given the challenge of singling out the effect of the introduction of CRR/CRD IV on banks' loan supplies."

and continued current appetite for loans from non-bank lenders and institutional investors (i.e. these would be substituting for declining bank appetite), and (b) the continuation of central banks' quantitative easing underpinning asset values, and so contributing to (a).

- The prohibition of netting might also increase the cost of borrowing, as without the benefit of netting, borrowers might appear less creditworthy. This could shift the balance of bargaining strength from borrowers to lenders, or encourage borrowers with substantial cash reserves to borrow less.

Liquidity requirements. The potential impacts of the liquidity requirements on the fundamentals of the syndicated loan market include the following.

- The liquidity coverage ratio (LCR) requirements have a significant impact on bank lenders in respect of committed undrawn facilities, since these will be required to be backed with liquid assets. In addition, given that liquid assets tend to be low-yielding, the maintenance of the liquid asset pool itself is likely to result in considerable additional cost. A study by McKinsey estimated a cost increase of 60 basis points for higher liquidity requirements from uncommitted credit lines to financial institutions and uncommitted liquidity lines to both financial institutions and corporates. Banks may not be able to fully pass on these cost increases. (Certainly, no price spike on this scale is observable in early 2018 so far). If they cannot, the higher costs may lead to a reduction in profitability and eventually less capital being allocated to these businesses, i.e. less supply to the syndicated loan market.[97]
- The requirements imposed by the LCR may also lead to changes being made to the documentation of loan facilities in the future. For example, stricter governance may be imposed on borrowers, requiring them to inform lenders of changes to their debt obligations and their activities generally, as well as information undertakings on the part of borrowers to inform lenders of their drawing requirements within the next 30 days could all be introduced. Borrowers who have entered into syndicated loans specifically with the aim of obtaining flexible financing could be put off making or accepting such changes.
- Loans or loan participations are not eligible for inclusion within the liquid asset pool, regardless of the underlying borrower. This may affect banks' decisions to participate in loans.
- The requirement to obtain stable funding for the majority of loan activities under the net stable funding ratio (NSFR) means committed loan facilities with longer tenors, i.e. most syndicated lending for project, infrastructural and LBO lending (at least the senior tranches), are less attractive for banks to provide.[98]

Solvency II

Solvency II is an EU Directive that seeks, amongst other things, to establish new risk-based capital requirements for most insurers and reinsurers. Under Solvency II, affected firms must hold sufficient capital reserves to meet any expected future contractual liabilities, known as "technical provisions".

The likely impacts on the syndicated loan market include the following.

- Insurers and reinsurers may have more freedom to invest in a wider range of syndicated loans, if these were not permitted under the previous legislation. This would increase the supply of eligible investors.

[97] Harle et al (2011), "Basel III and European banking: Its impact, how banks might respond, and the challenges of implementation", McKinsey Working Papers on Risk, Number 26.

[98] Response to European Commission Green Paper: Long-Term Financing of the European Economy by the LMA, 2013.

- In practical terms, debt structures relevant to the syndicated loans market such as long maturity debt, structured finance products, and real estate all carry higher capital charges when compared to other forms of debt. Insurers are allowed to apply their own internal risk model rather than the standardised one and thereby bring about lower capital charges if their assessments indicate a reduced risk. However, not all institutions may wish to follow this approach, as internal risk models first require regulatory approval. This may lower the appetite for syndicated loans.
- Higher-rated instruments are also given better treatment than low or unrated instruments. As a result of the above, interest in loan investment may well increase for loans to higher-rated borrowers, or those that are fully secured and have shorter tenors.
- Solvency II will also impact the syndicated loan market via insurer investment in CLOs, which fall within the definition of a securitisation.[99] The Directive distinguishes between a Type 1 and a Type 2 securitisation with the first type having a lower stress factor and thus requiring lower capital to be held against it. CLOs are unlikely to fall in the first category and thus, investment in CLOs by insurers may fall due to the increased capital requirements.[100]

AIFM Directive

The aim of the Alternative Investment Fund Managers Directive (AIFMD) applies to fund managers of AIFs (AIFM) including hedge funds, private equity funds, retail investment funds, investment companies and real estate funds. The AIFMD was published came into force on 21 July 2011 and had an implementation date of 22 July 2013.

The AIFMD may impact the syndicated loan market in a number of ways.

- The greater due diligence requirements may affect the ability and desire of funds to invest in long duration, less liquid assets such as syndicated loans, thus reducing the size of the market and availability of investors.
- Under the Directive, managers have the duty to act in the best interests of the AIF or the lenders of the AIF and the integrity of the market. AIFMs must act in such a way so as to prevent "undue costs" being charged to the AIF and must also perform any due diligence prior to execution. These could lead to fund managers requiring more streamlined market practices, as settlement delays lead to capital being tied up for periods of time, resulting in AIFMs suffering potential "opportunity costs" by virtue of the fact that they are unable to invest in other assets until settlement. The issue of settlement times is key in the context of the efficiency of the loan syndication market.

MiFID 2

The syndicated loan product is not directly affected by MiFID 2 (as syndicated loans are not financial instruments). Whilst loans themselves may be unaffected, the package impacts lenders generally depending on who they are and what kind of services they provide. An impact directly relevant to syndicated loans market is that structured finance products are now specifically within the scope of MiFID 2, and certain loan-related products (such as CLOs) are also directly affected. Trading in CLOs and other credit securitisations are subject to the transparency and best execution

[99] See LMA Regulation and the Loan Market, 2015.
[100] In general terms, a security will qualify for Type 1 status if it "(i) is investment grade, (ii) is listed in OECD, EEA or other robust markets and (iii) is the most senior tranche of the deal. See NEAM Group (2015), "The European Securitization Solvency II Saga".

regimes, with requirements being tailored to each financial instrument and for different types of trading.

NPL Regulation

The European Commission is also currently seeking to introduce legislative measures to facilitate the reduction of NPLs (i.e. loans where payments are 90+ days overdue) held by European banks (the NPL Regulation). One of the European Commission's objectives is to improve the secondary market's contribution to NPL reduction. For example, the current draft contains provisions that any Member State-level provisions restricting such transfers to non-banks would need to be removed. However, its current draft also contains provisions that would require ex ante disclosure by a bank of all relevant information against a defined disclosure standard for a non-bank to evaluate the credit in question, and ex post reporting of the transfer to the appropriate supervisor. This would not be limited to NPLs, but would also apply to the transfer of performing loans to non-banks. As such, this could essentially end the buyer beware principle (i.e. caveat emptor) in such instances and as such significantly affect the working of the secondary market. Indeed, since some existing non-bank participants in the secondary loan market operate on a 'public side' only basis (i.e. avoiding accessing private information in order not to be prevented from trading any related securities) lenders opined that such mandated disclosure could in fact deter participation (i.e. the opposite of the desired effect). Obviously, the text of the NPL Regulation may change (perhaps significantly) as it is negotiated further but we include reference to it here for completeness.

Conclusions on the impact of the applicable regulatory framework

The existing recently modified regulatory framework implies that the syndicated loan market can be affected in a number of key ways:

- Greater security for borrowers and the wider financial system but increased costs to banks of loans due to more stringent capital requirements. The leverage requirements and liquidity ratios may affect banks' appetite for syndicated loans in general, and PF/INFRA loans in particular (as the capital requirements particularly target long-term loans). The extent to which, if at all, this may reduce lending supply will depend on the relative size of cost increases and their impact on borrowers' demand and banks' overall lending decisions, as well as the availability of other sources of lending (notably non-bank lenders).
- Increased capital requirements may also affect banks' appetite for underwriting loans (where they would be required to hold capital to offset the loan until it is sold down) or club deals (where banks typically hold the majority of the loan) compared to leading in a best-efforts deal or being a non-underwriting participant. Similarly, this could also encourage greater participation in the secondary market whereby lead banks seek to offload loans from their balance sheets after syndication.
- The leverage requirements (particularly the prohibition of netting) would increase the costs to borrowers of borrowing if they appear less credit-worthy. This may affect the balance of power between borrowers and lenders in the favour of the latter, e.g. in a restructuring situation.
- Documentation between lenders and borrowers may become increasingly important e.g. lenders wishing to impose stricter governance on borrowers.
- Overall cost increases stemming from the revamped regulatory framework may be passed onto borrowers, or internalised within banks.
- The activity of institutional investors in the market (notably insurers and reinsurers) might increase as they have more freedom to invest in a wider range of assets. Appetite to invest in infrastructure assets may also increase given the provisions of

Solvency II. Investment behaviour may be negatively impacted by potentially higher capital charges for some loan types as well as investment via CLOs.

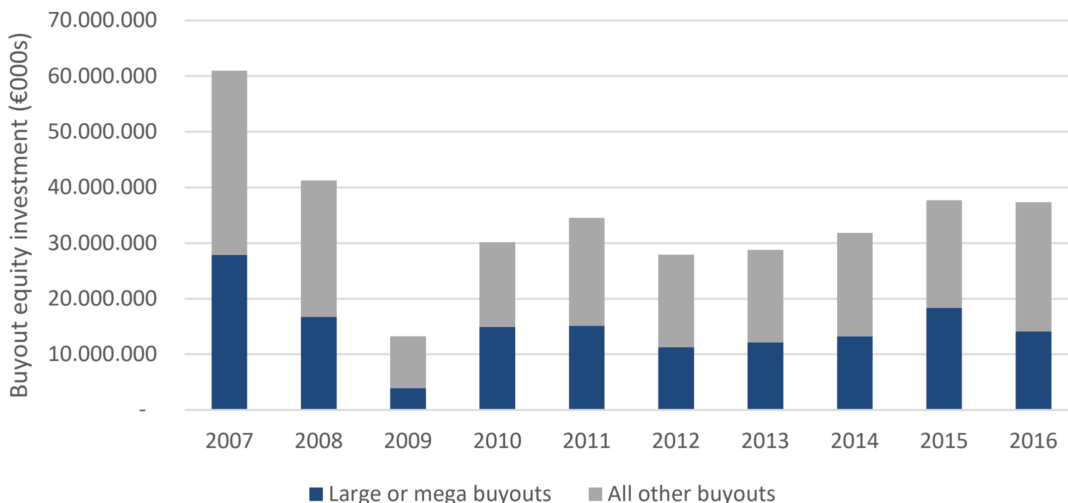
The impacts of these regulatory changes on the loan syndication market depend on how borrowers react to the heightened transparency and how lenders respond to cost increases and change their business models and lending decisions accordingly (considering the full breadth of all regulation and the impacts on many different areas of lenders' businesses). A number of the regulations have only been implemented in 2018 and thus the impacts will take some time to become fully evident.

Our interviews with banks shows that many consider prudential regulation to have had a notable impact on lending costs (particularly for long-dated loans), such that in some markets they are finding it difficult to compete with non-bank lenders. There is no clear evidence of increasing loan prices or fees from our data (i.e. banks being able to pass on costs to borrowers) – banks and other investors will usually decide not to participate in a loan if the economics are not worthwhile. It may be, then, that cost increases are not currently impacting the market in a notable way and that this represents a case of special pleading by the banks.

The demand-side of the syndicated loan market

Data from Invest Europe[101] show that the amount of equity invested in buyout activity fell significantly following the global financial crisis, with the total EU market value falling from over €60 billion in 2007 to just over €13 billion in 2009. It bounced back more sharply in 2010 (to €30 billion), since when increases have been more gradual. The value of "large" (€150-300m) and so-called "mega" (> €300m) buyouts, which are more likely to have a syndicated loan element, have typically accounted for just over 40 per cent of the total buyout market.

Figure 17: Value of equity investment in LBOs in the EU



Source: Invest Europe (2016).

In terms of our sample of Member States, the UK and France have typically had the largest buyout markets (in terms of equity investment[102]), followed by Germany, then

[101] Invest Europe (2016) "Yearbook 2016: Europe and country overview tables"

[102] An LBO will typically include an 'equity' element provided by the private equity house, with the balance of the transaction value coming from debt. These proportions vary from deal-to-deal and over time, but the debt element is likely to be at least as much as the 'equity' contribution.

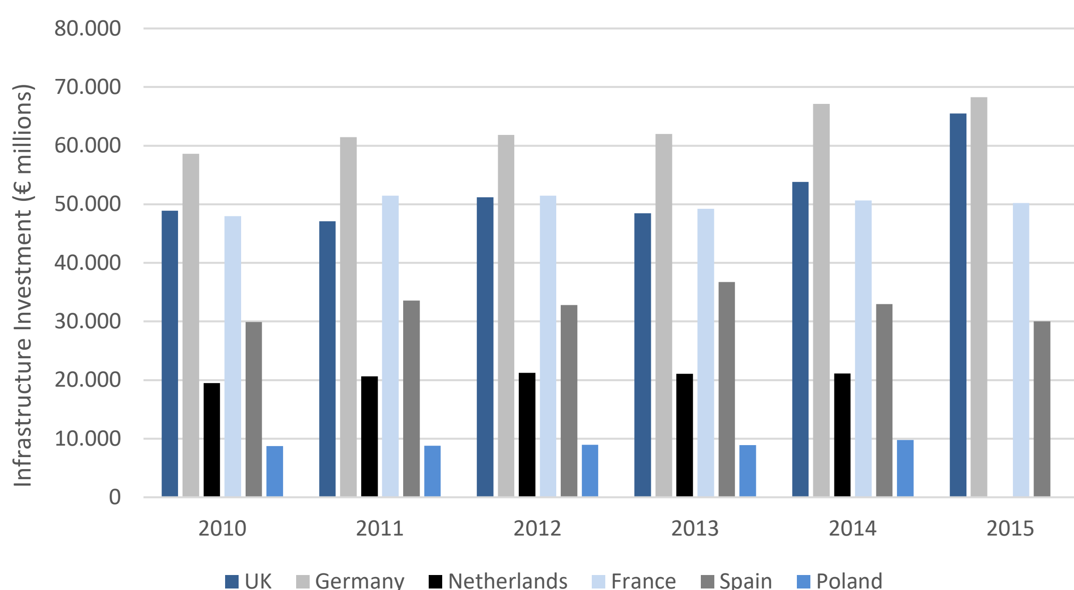
Netherlands and Spain of comparable size, and Poland as the smallest market. The UK was hit hard by the financial crisis with initial LBO volume falling almost 80 per cent (syndicated lending in the LBO segment includes the refinancing of existing transactions as well as new transactions), albeit recovering since. Since then, the Member State which has experienced the strongest recovery is France (268 per cent increase), with the UK showing the weakest recovery (72 per cent).

We have described above the evolution of syndicated lending for LBOs in each of the Member States of interest in the chart on the preceding page. The relative importance of the markets does not fully match that for the location of the private equity sponsors: whilst the UK takes precedence in both, Germany has consistently been more prominent than France in the LBO syndicated lending segment. This implies that French private equity firms are bigger and more active than those based in Germany.

Infrastructure borrowing can be compared to infrastructure investment spending from 2010 to 2015. The European Investment Bank (EIB) in its 2017/18 Investment Report recognises that data on infrastructure investment are 'not available in any ready-to-use' form. As a result, the EIB has developed its own approach to estimation which uses national accounts data on gross fixed capital formation for sectors that are typically considered 'infrastructure sectors'; specifically, education, health, transport and utilities. The figure below displays data for each Member State based on the aggregation of gross fixed capital formation in these four sectors.

The data shows infrastructure investment spending to be fairly stable over this time period. They show that infrastructure investment is highest in Germany, followed by the UK and France. This is an interesting difference to the syndicated lending data, which show greatest activity in the UK. Cross-country comparisons of the infrastructure data should be treated with particular caution however due to some data gaps for specific sectors in specific Member States.

Figure 18: Infrastructure investment spending (€m)



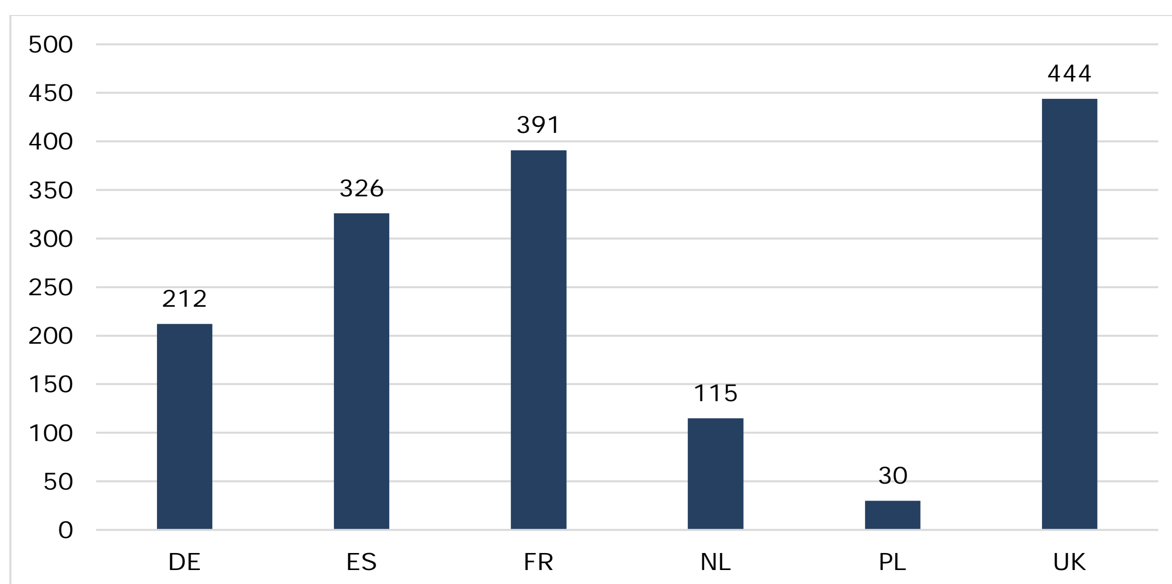
Note: infrastructure investment calculated as the sum of gross fixed capital formation in education, health, transport and utilities. Gross fixed capital formation is calculated by summing the value for relevant NACE codes in each sector, i.e.: Education = "Education"; Health = "human health activities" + "human health and social work activities"; Transportation = "Land transport and transport via pipelines" + "Water transport" + "Air transport";

Source: Europe Economics analysis of Eurostat – Cross-classification of gross fixed capital formation by industry and by asset (flows).

Borrowers in the LBO, PF and INFRA segments

Our dataset includes a total of 1,478 unique borrowers over the entire time span covered by the analysis. The distribution of borrowers across Member States is presented in the chart below, which shows that most of the borrowers are located in the UK, France and Spain. As noted in Chapter 2, as the data reflect the location of the borrower rather than the project, some borrowers may be borrowing for a project in another Member State, and some projects within the sample Member States may not be recorded). However, we consider this eventuality to be low in our sample.

Figure 19: Number of borrowers by Member State (2010-2017)



Source: Europe Economics (using Thomson Reuters Loan Connector).

Borrowers can be further classified based on their organisation type. Most of the borrowers in LBO deals are companies/corporations whereas most of the borrowers in Project Finance and Infrastructure tend to be Infrastructure Special Purpose Vehicles (Table 13). This is fully expected given the nature of these loan types.

Table 13: Number of deals by borrower's organisation type and loan purpose (2010-2017)

Organisation type	LBO	Project Finance	Infrastructure	Total	%
Company/Corporation	567	49	129	745	43%
Project/ Infrastructure SPV, Special-purpose	48	133	371	552	32%
Other	15	8	7	30	2%
Government/Industry Authority	1	7	8	16	1%
Joint-venture	4	1	11	16	1%
Missing	113	41	208	362	
Total	748	239	734	1,721	

Source: Europe Economics (using Thomson Reuters Loan Connector).

Other characteristics of borrower which would be useful to analyse are their size and their credit worthiness. However, Loan Connector data on borrower size is very limited (available for 172 borrowers); likewise credit rating is very limited in scope.

The frequency with which borrowers engage in the market might have an impact on their ability to influence the syndicate process, in particular their experience in appointing MLAs, and their ability to use future appointments as a means of incentivising MLAs to perform well.[103] On the other hand, repeated engagement with the market may increase ties with syndicating banks which may have implications for competitive dynamics. (We describe these hypotheses in more detail, taking account of other factors, and test for them in Chapter 4.) In this respect, our analysis shows that only a small fraction of borrowers engaged in more than one deal over the period 2010-2017, and almost 90 per cent of borrowers across LBO, PF and INFRA segments concluded only one deal (Table 14).

Table 14: Number of borrowers by number of deals and loan purpose (2010-2017)

Deals per borrower	LBO	Project Finance	Infrastructure	Total
1	573	184	596	1,353
2	63	18	51	132
3	15	4	10	29
4		1	2	3
5			1	1

Source: Europe Economics (using Thomson Reuters Loan Connector).

The sectoral distribution of borrowers is highly related to the purpose of the loan. When we consider the deals struck in 2010-17, 68 per cent of Infrastructure deals are listed as within the Utilities sector, with a further 11 per cent categorised as Construction. As noted already, under our definition, there are far fewer Project Finance transactions (albeit, on average, these are larger in value than Infrastructure deals) and these do not exhibit the same concentration in Utilities and Construction. Similarly, LBO deals are spread across many different sectors, reflecting the fact that companies suitable for an LBO can be found across the entire economy. The sector with the most transactions within it, classified by Thomson Reuters as General Manufacturing, accounts for 13 per cent of LBO transactions.

Sponsors in the LBO, PF and INFRA segments

This "recurrence" feature is much more relevant to sponsors, both in the LBO and PF/INFRA segments. As described in Chapter 2, a financial sponsor for an LBO is typically a private equity investment firm that, in addition to bringing capital to a deal, is expected to bring a combination of capital markets expertise, contacts, strategies for operational improvement, and the experience of owning leveraged companies. These features make them more likely to be recurrently engaged. Our lender fieldwork characterised the European LBO market as being more sponsor-dependent than its USA equivalent.

For PF/INFRA, sponsors are usually multinational companies and infrastructure funds, but could also be state-owned firms, and/or governmental bodies that own jointly the SPV and its project financing contractual agreements. In the Thomson Reuters Loan Connector-derived sample, multinational companies and infrastructure funds are identified as sponsors in the PF/INFRA segments. Sponsors contribute equity and

[103] This is discussed in more detail in Chapter 4.

technical expertise. The fieldwork has highlighted how the technical expertise can relate to both engineering and financing (including financial engineering). Debt is, however, the major source of financing. As in the LBO arena, sponsors can be essential actors in any debt-raising, complementing or even substituting for roles allotted to the de jure borrower.

To illustrate this, Table 15 shows the proportion of sponsors by number of deals and loan type: 35 per cent of the 609 sponsors in our sample engage in more than one deal, 7 per cent of which engage in more than 5 deals. The recurrence feature is more marked in the LBO segment than the PF and particularly INFRA segments. In the INFRA segment, 78 per cent of sponsors have engaged in only a single syndicated loan over the period, and only one per cent have engaged in more than five. This compares to sponsors in the LBO segment, only 56 per cent of whom have only engaged in one deal, and 10 per cent of whom have engaged in more than five.

Table 15: Total number of sponsors by number of deals and loan type (2010-2017)

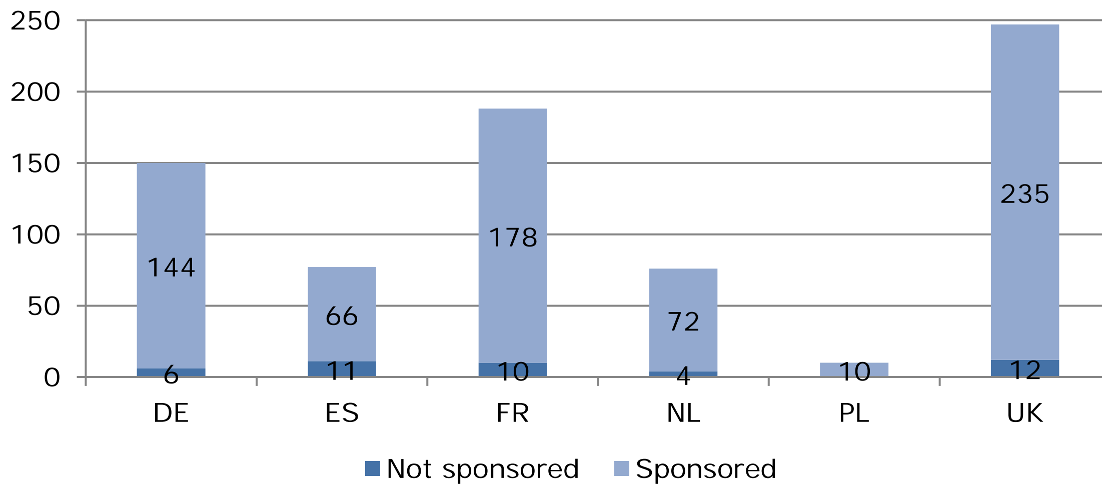
Deals per sponsor	LBO	Project Finance	Infrastructure	Total (number of sponsors)	%
1	56%	62%	78%	413	65%
2	19%	16%	13%	105	17%
3	6%	8%	4%	35	6%
4	3%	4%	3%	21	3%
5	5%	3%	1%	20	3%
>5	10%	8%	1%	40	6%
Total (number of sponsors)	312	76	246	634	

Source: Europe Economics (using Thomson Reuters Loan Connector).

Prevalence of sponsors across LBO, PF and INFRA segments

LBO deals are very likely to be sponsored by a private equity firm, as shown for our sample in Figure 20 below.

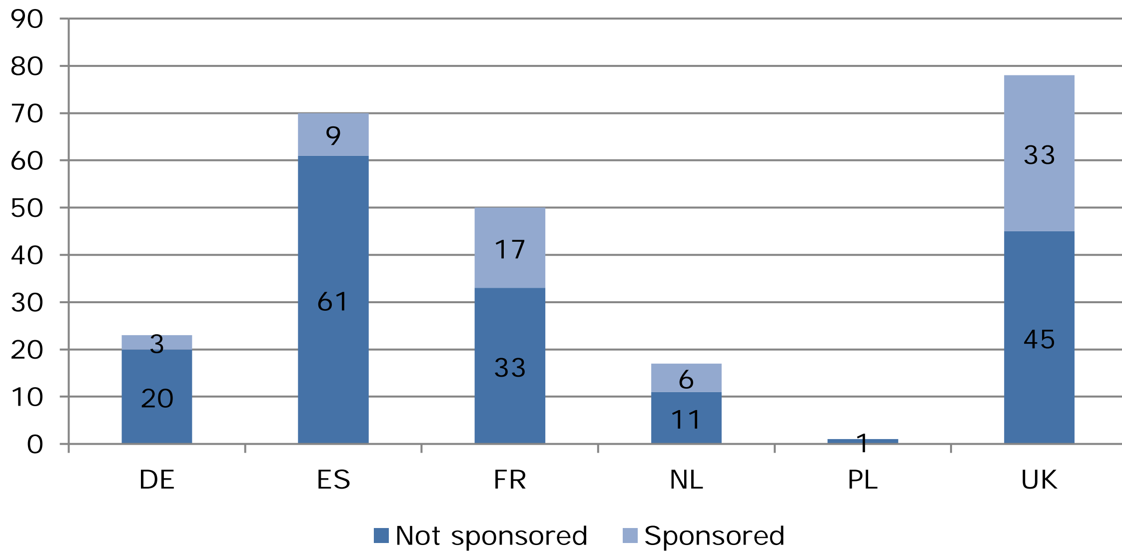
Figure 20: Number of sponsored vs not sponsored LBO deals (2010-2017)



Source: Europe Economics (using Thomson Reuters Loan Connector).

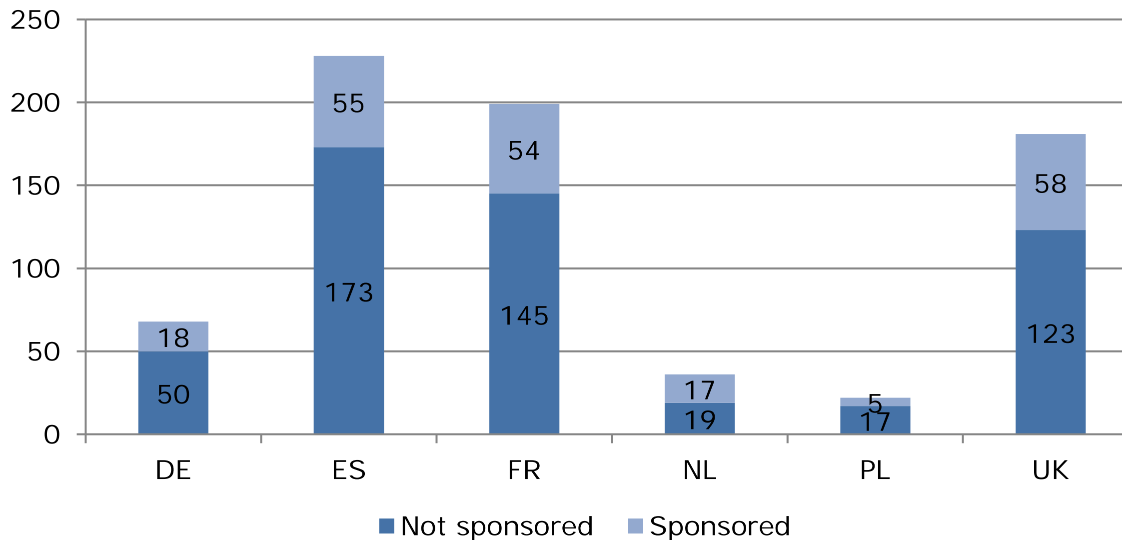
On the contrary, Project Finance and Infrastructure deals tend to rely less on sponsors as shown in the graphs below. Within these loan types, the UK is the country with the largest share of sponsored deals.

Figure 21: Number of sponsored vs not sponsored Project Finance deals (2010-2017)



Source: Europe Economics (using Thomson Reuters Loan Connector).

Figure 22: Number of sponsored vs not sponsored Infrastructure deals (2010-2017)



Source: Europe Economics (using Thomson Reuters Loan Connector).

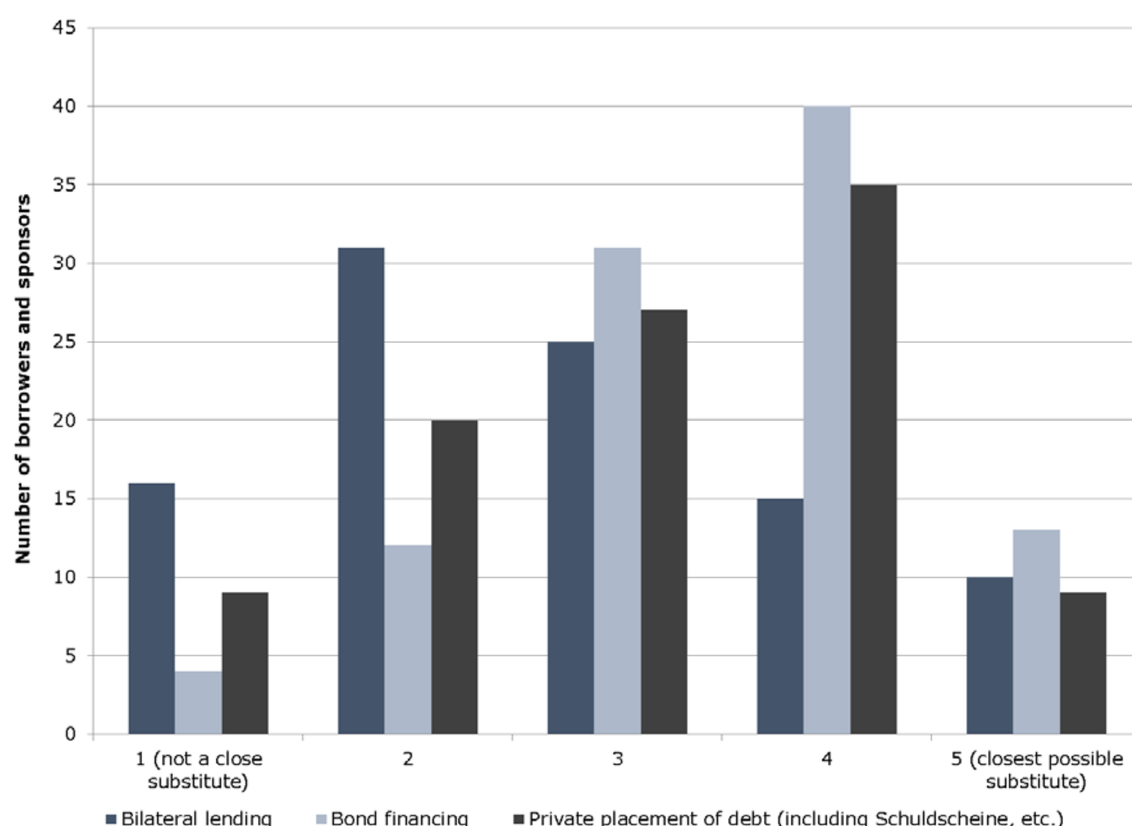
This implies that the issues related to repeat engagement in the syndicated loan market are more relevant in the LBO segment than the PF/INFRA segment. We discuss these issue in detail in the competition framework and analysis in Chapter 4.

Syndicated loans and its alternatives

The availability of other sources of lending will increase the choice borrowers/sponsors have and limit their reliance on syndicated loans. This would be particularly beneficial in markets where syndicated lending is more at risk of competition concerns, for example where the pool of potential MLAs is small or where certain banks have a stronger market position.

The main substitutes for syndicated lending are bilateral loans, corporate bonds and private debt placement. In general borrowers and sponsors consider there to be alternative funding options readily available for their organisation. Of bilateral loans, bonds and private placements, bonds were considered to be the closest substitute by the most respondents, followed by private placement and then bilateral loans – this is shown below.

Figure 23: Benefits of syndicated loans over alternative debt



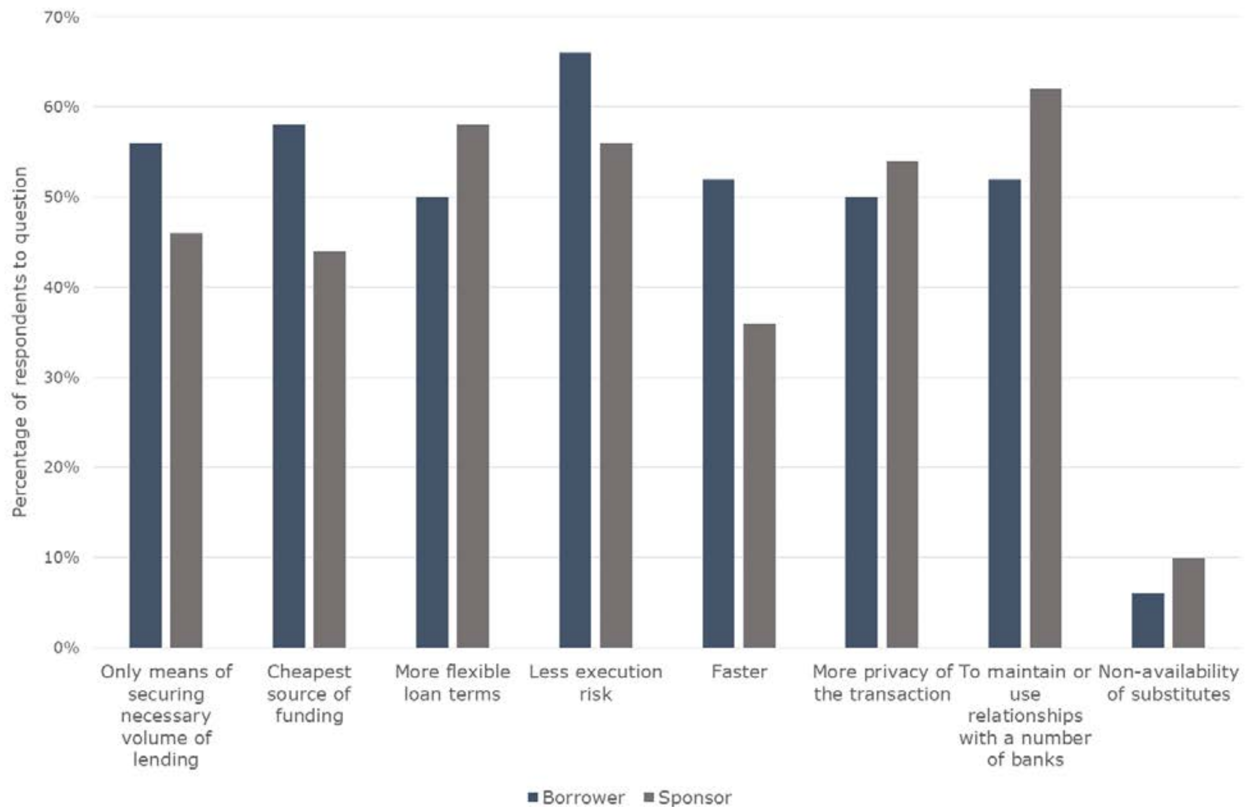
Source: Europe Economics/YouGov survey of borrowers and sponsors. Question: "Where you do use syndicated loans, how close a substitute for syndicated lending are each of the following usually (1 being not a close substitute to 5 being the closest possible).

In PF/INFRA, the closest identifiable substitute was not clearly identified amongst the respondents to the YouGov survey. By contrast, bonds and private placement were comfortably ahead of bilateral loans as the closest identifiable substitutes in the LBO segment.

The advantages of syndicated loans as perceived by borrowers and sponsors differ slightly, conditional upon which form of finance is perceived as the closest substitute. The main advantage cited by those considering a bilateral loan as the closest substitute (and ranked the closeness at either 4 or 5 on the scale in the figure above) considered the price of syndicated loans to be its major advantage. Those considering corporate bonds and private placement as the closest substitute cited reduced transactional risk as its main advantage.

Our fieldwork confirms the benefits to borrowers and sponsors of syndicated loans. Syndicated loans are preferred over alternative lending options for a number of reasons principally because they are seen as less risky than other forms of lending, more flexible and cheaper. This can be seen in Figure 24 below, which shows the reasons borrowers and sponsors have for choosing syndicated loans over alternatives.

Figure 24: Benefits of syndicated loans over alternative debt



Source: Europe Economics/YouGov survey of borrowers and sponsors. Question: "Compared with the closest substitute, what were the reasons for choosing to take out a syndicated loan?"

The benefit perceived by the most sponsors was to maintain or make use of relationships with a number of banks, whereas the key benefit perceived by borrowers was the lower risks associated with syndicated loans. A small proportion of respondents – 10 per cent of sponsors and six per cent of borrowers – said that they chose a syndicated loan as there were no substitutes for that loan.

Borrowers and sponsors connected to LBOs generally had similar views to those connected to PF/INFRA transactions. However, it is worth noting that reduced transaction risk was particularly important in LBOs. This is intuitive in that we have noted already that underwritten loans are used here to provide the private equity sponsors with financing certainty, which in turn is required of the sponsors by the vendors of the target company. In PF/INFRA, the flexibility of the loan terms was the most cited factor.

The consideration of substitutes is complicated by the fact that debt can be acquired by borrowers on a mixed basis, i.e. in a combination of loans and High-Yield bonds (or even sometimes private placement financing). In the LBO segment the syndicated loan can be part of a funding package that (ultimately) also includes High-yield (HY) bonds (as opposed to investment grade corporate bonds). When HY bonds are part of such a package, then bridging facilities would be established (since the timeline for raising the HY bonds is generally too slow to meet the wider transaction's deadlines). Similarly, projects and infrastructure have a set of substitutable and complementary modes of financing, specifically project-related bonds (which are issued on a syndicated, book-building basis) and private placement.

However, these different types of debt would not be sourced simultaneously. Instead, a package based upon the syndicated lending may be acquired by a borrower/sponsor, but with this incorporating some element of bridge finance. In this way, the borrower/sponsor obtains the financing package at the point in time necessary (such as to but the target in an LBO). The bridging loan would then be replaced at some point subsequently by a bond issue.

One point arising here is whether and on what basis the arranger of the bridging loan would be privileged in terms of involvement with such a bond issue. This is an area investigated by the UK's FCA in its work on corporate and investment banking. In its subsequent policy statement,[104] the FCA determined that "right of first refusal" clauses (i.e. a contractual right to be given the opportunity to enter into a business transaction with a company before anyone else can), the client subject to the right is prevented from accepting offers from third parties should be banned but that "right to match" clauses are acceptable (please see the analysis of FCA's market study is at Appendix 5g).

However, the FCA explicitly excluded bridging loans from its ban on such clauses, identifying clear benefits to the borrower. Specifically, the FCA concluded that banks would not be likely to provide such bridging finance on equivalent (or conceivably not provide it at all) without being able to exercise subsequent control of any future 'take-out' of the bridging loan by being mandated with the bond issue (or whatever the subsequent longer-term financing was determined to be). On the other hand, the FCA was not convinced of client benefits in other areas, e.g. debt or equity issuance not connected to taking out a bridging loan, or the provision of M&A services. The FCA's ban applies to regulated firms operating in the UK (irrespective of the client's location.) We discuss this further in Chapter 4.

Our fieldwork (please see Figure 23 and Figure 24 above) shows that there are generally potential substitutes for syndicated loans (e.g. almost no borrowers said there were no close substitutes, and around half said that bond financing or debt private placement were fairly close substitutes). Syndicated loans are used because of their added value including the ability to attract a sufficient volume of lending, more flexible loan terms, less risk (a particular benefit for borrowers versus sponsors), greater privacy and the benefits of maintaining relationships with lenders.[105]

The availability of other sources of lending will increase the choice borrowers/sponsors have and limit their reliance on syndicated loans, although this will depend on the additional benefits provided by syndicated loans over and above other lending forms as well as the existence of a sufficient number of competing lenders to those involved with the syndicated loan. The availability of alternatives would be particularly beneficial in markets where syndicated lending is more at risk of competition concerns, for example where the pool of eligible banks is small and where banks may enjoy a strong position (have market power).

Bargaining power of borrowers and sponsors

The 'bargaining power' of borrowers and sponsors is a key factor influencing the competitive dynamics of syndicated lending. Bargaining power refers to the ability of borrowers and sponsors to dictate terms and to react to potentially anti-competitive behaviour of lenders. This is influenced by the availability of alternative lending options, the expertise of the borrower/sponsors, and current market conditions.

[104] FCA PS17-13 "Investment and corporate banking: prohibition of restrictive contractual clauses", https://www.fca.org.uk/publication/policy/ps17-13.pdf.

[105] Fieldwork question: "Compared with the closest substitute in the previous question, what are the reasons generally for choosing to take out a syndicated loan?"

The sponsors in the LBO and PF/INFRA syndicated loan market are generally considered to be sophisticated in terms of raising finance, i.e. they have sufficient expertise to weigh the pros and cons of different financing options. Private equity firms acting as sponsors in both LBO and PF/INFRA segments may have in-house, specialist debt finance expertise (at least for larger private equity firms with dedicated in-house Debt Financing Teams) and/or can complement in-house knowledge through access external debt advisors. This has also enabled them to more readily construct club deals (particularly prominent in PF/INFRA, and where may not be a role for MLA(s), or at least the MLAs' role will be reduced). Such sponsors are assessing debt financing on each LBO that they progress (i.e. they have relevant experience). There may be other sponsors with less past experience (e.g. less well established private equity firms or ones with insufficient scale to justify resources dedicated to raising debt), who would consequently be more dependent upon either advisors and/or the MLAs. The latter instance would represent a heightened risk of an adverse outcome.

The borrowers generally have less experience than the sponsors, at least in the LBO space (since they are not raising syndicated loans on a near-continuous basis). However, the target companies subject to LBOs where syndicated lending is applicable are not SMEs – i.e. they should be expected to have finance professionals with some expertise in raising and managing financing, even if not necessarily experience with syndicated lending. This contributes to the strong influence exerted by sponsors in the process.

Indeed, the sponsors will seek to control much of the debt origination/syndication process, from the selection of the initial group of lead banks to be approached, to negotiating terms with those banks and even having the final decision on further participant members. However, this 'control' is not total. In particular:

- In the initial approaches, sponsors/borrowers use a competitive process whereby several banks are approached independently, followed by bilateral negotiation. However, the use of such a process is not total, and where it is not used the MLAs approached would exercise greater influence (and if only one MLA is approached, this influence could be substantial).
- Even when an RFP style process is used, one feature that could be problematic in terms of the exercise of borrower/sponsor control is the use of market soundings. Market soundings can be efficient, particularly if a particular credit is not mainstream as it would enable better judgements to be made on pricing and any eventual marketing. Lenders emphasised that internal policies meant that any deal-specific soundings would require client consent, and that this would need to be demonstrable to compliance teams. However, lenders also conduct generic soundings, raising a potential boundary issue as to what is generic and what is specific. There is also the question of who is approached: an approach to an institutional investor who lacks the capacity to act as an MLA is relatively unproblematic whereas an approach to another MLA would have the potential to be highly problematic even when the sounding was generic.
- Where a general syndication takes place (e.g. in an underwritten deal), it is the bookrunners that deal directly with the potential participating lenders. Whilst the sponsors can aim to control who is approached (through the white list), and seek feedback from the process (either from the bookrunner, but also indirectly from firms on the white list), the MLAs again exercise relatively greater influence here. The MLAs will also seek to add potential participants to the white list, albeit subject to borrower/sponsor approval.
- The borrowers/sponsors will also have curtailed bargaining power where a borrower is in financial difficulties and faces default. The options available to a borrower may be very limited in such an instance.

Another aspect of this is that the main substitutes for syndicated lending - bilateral loans, corporate bonds and private debt placement – can involve the same firms. Banks (particularly leading investment banks) will be involved in each of these. However, this is not exclusively so. For example, there are corporate finance boutiques that can arrange bond issuance or private debt placement as an alternative to a bank. Similarly, bilateral loans can also be made by debt funds. However, the extent of the importance of non-bank actors here should not be overstated since in the (current) market such bilateral lending from debt funds is only towards the lower end of the syndicated lending spectrum. Likewise, banks dominate book-running in bonds, particularly at larger ticket sizes.

The obvious thoughts that flow from this are whether this critical role for banks could influence pricing or fee levels. On fees, as we describe in the relevant section below, these can be substantial. Whilst the involvement of non-bank actors should add market discipline, at least where there are such participants, in other cases the competitive determination of fees is driven by the process (i.e. in the RFP setting, all economic terms – including fees and loan pricing – would be subject to that process). In terms of pricing, an important, further distinction can be made between bilateral loans and the other sources of debt in that all the others have some degree of direct non-bank input in the price formation process. In the syndicated loans area, this could be through the secondary market or, indeed, in the primary issuance phase as part of a general syndication. We have observed that there are no significant short-term deviations from par in the secondary market in syndicated loans (see page 139 below). This suggests that syndicated loan pricing, at least in the LBO segment where general syndication and secondary trading are more common, should be in line with "market" pricing. However, as we have noted elsewhere, the PF/INFRA segment is more club-orientated, has reduced (but not non-existent) institutional investor involvement and less post-close trading activity than the LBO segment. The possibility of any pricing impact would depend on what the substitutes are, and the transparency of pricing in those markets — but more largely on the extent to which other participants (including other banks) are willing and able to compete, and the capacity of the borrowing entity (and its sponsors, where applicable). This can only be assessed on a case-by-case basis.

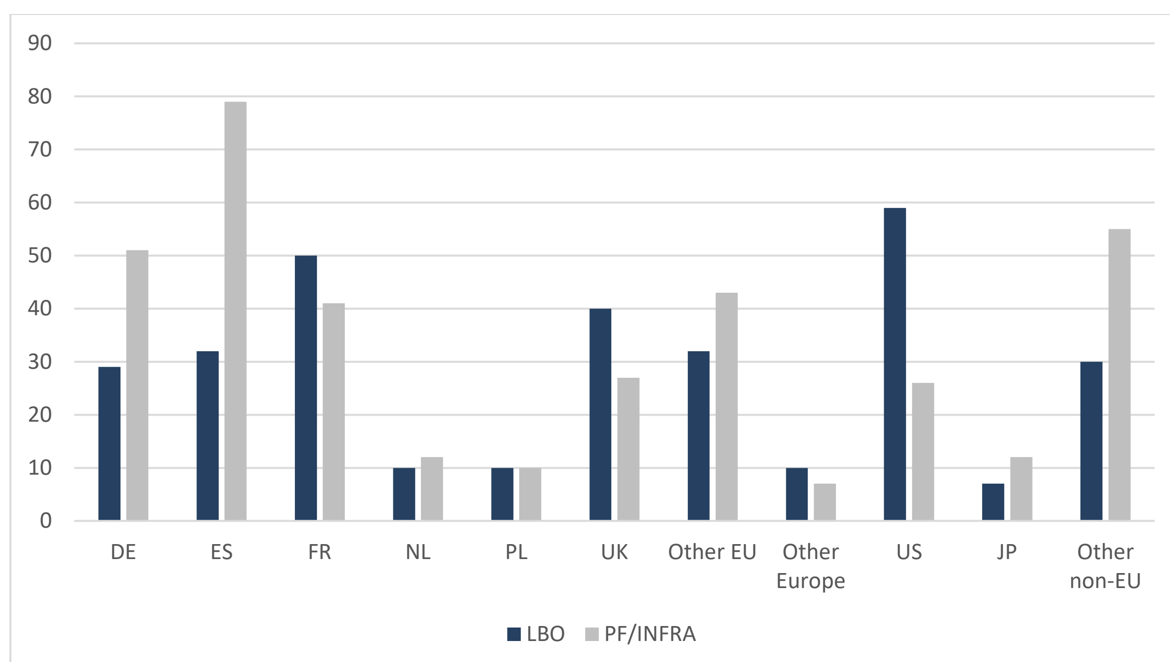
The supply side of the syndicated loan market

This section gives an overview of the supply side of the syndicated loan market, such as the total number of lenders by Member States, the number of leading lenders, their relation to the geographic origin of the borrower (i.e. domestic or cross-border) as well as the type of lenders (i.e. banks, non-banks). Our sample includes a total of about 540 lenders. The chart below shows their distribution across parent countries.[106]

Most of these are banking institutions (70 per cent) while the remaining 30 per cent are other non-bank financial institutions.[107] However, this should not be taken as a full description of non-bank involvement: the data available on Thomson Reuters Loan Connector/Deal Scan does not capture all participants, especially those lenders/investors that engage solely at the general syndication stage.

[106] Operating country is distinct from parent country. So for example a German subsidiary in the UK would have UK as its operating country and Germany as its parent country.
[107] A few notes apply to this table. First, Loan Connector does not report lender operating country and institution type for each lender individually but rather combines in alphabetic order all lender operating countries and institution types in a single cell for each tranche. We therefore carried out an exercise to link each lender to its operating country and institution type. Second, consolidation has been carried out to rename lenders uniformly if they were named differently but in fact referred to the same entity. Third, we have consolidated subsidiaries, i.e. this shows "unique" entities.

Figure 25: Total number of lenders by parent location and loan purpose (2010-2017)



Source: Europe Economics (using Thomson Reuters Loan Connector).

As can be seen from the above, lenders from different countries can have different focus: whereas more lenders with parents based in Germany, Spain and Japan have a greater appetite for PF/INFRA, the opposite holds for lenders from France, the UK and the USA. The large number of non-EU lenders involved in loans syndicated in the EU can be interpreted as a signal of the internationalisation of this market, i.e. the syndicate is likely to engage with lenders that operate in a country which is different from the borrower's country. We discuss this further in the below in terms of both the LBO and PF/INFRA segments.

Lenders in the LBO segment

The involvement of lenders in the LBO syndicated loan segment can be described in a number of ways. In particular, it is possible to distinguish between those lenders listed by Loan Connector as being involved in a transaction, i.e. participants, and those identified as having a more prominent role (i.e. identified by Loan Connector as being an MLA). As noted already, title inflation can mean that the label MLA could signify a lender actually taking an important role in the process (acting as bookrunner or coordinator, say), or providing more of its balance sheet (i.e. lending more), or for some other reason. Therefore, we constructed league tables showing the market share of the top lenders in each Member State for 2010-2017, incorporating all lenders identified as participants in a deal or tranche.[108]

This analysis does not identify any of the markets as being very highly concentrated. It is worth noting, even so, that France is less fragmented than the other markets. Calculating the Herfindahl-Hirschman Index (HHI) for each of these markets confirms this. Based upon the market shares of the top 20 participants, these range from 267-

[108] We replicated the approach followed by Loan Connector as to allocate the amount borrowed to each lender. When available, we applied the loan share of each identified lender to the total amount borrowed. When the loan share was not available, a pro rata amount was awarded to each lead arrangers involved in a syndicate.

316 for all countries save France (where the HHI score is just above 500). HHI scores in these ranges, i.e. below 1000, are generally taken as indicative of non-concentrated markets. We discuss the possibility of collective bargaining power at the end of this chapter.

Table 16: Leading participants by market share in the LBO segment (based on loan value, 2010-2017)

	DE	ES	FR	NL	PL	UK
Lender ranked 1	7%	7%	11%	8%	7%	8%
Lender ranked 2	6%	7%	10%	7%	5%	7%
Lender ranked 3	6%	6%	10%	6%	5%	5%
Lender ranked 4	5%	5%	9%	6%	5%	5%
Lender ranked 5	5%	5%	5%	5%	4%	4%
Lender ranked 6	4%	4%	4%	5%	4%	3%
Lender ranked 7	4%	4%	3%	4%	4%	3%
Lender ranked 8	3%	4%	3%	4%	4%	3%
Lender ranked 9	3%	4%	3%	4%	4%	3%
Lender ranked 10	3%	4%	3%	3%	4%	3%
Lender ranked 11	3%	3%	3%	2%	3%	3%
Lender ranked 12	3%	3%	2%	2%	3%	2%

Source: Europe Economics (using Thomson Reuters Loan Connector data).

There is evidence of some degree of "home bias" in that the top ranked lenders tend to be lenders with a parent in that country. Such "domestic" lenders are highlighted in pale blue in the table above. This effect is particularly deep in France in the LBO segment (where over 40 per cent of the estimated total loan value is accounted for by such local banks). Local clearing banks may be able to lever existing relationships (e.g. in terms of already providing cash management services to the borrowers) to take leading roles in transactions. Momentum (i.e. local banks have the relevant experience) may also be a factor. As we have noted already, the Loan Connector data do not pick up all investors in loans – the above analysis may be best understood as what has been underwritten, not - necessarily - what is retained by these lenders. In the literature, there are indications that borrowers tend to borrow in their natural home market and hence bank portfolios display significant home "bias."[109]

The extent of this effect should not be over-stated however. The LBO segment has a number of leading banks active in all or nearly all of the six markets. If we consider the top 20 banks in the LBO segment in each Member State, we find that no less than twelve banks feature in at least five of the country-specific Top 20s. Each of these twelve banks is a G-SIB (i.e. Globally Systemic Important Bank). All twelve of these G-SIBs are in the Top 20 in Germany – whereas only 8 feature in Poland's top 20. This offers some (weak) support to the idea that internationalisation of the LBO market is stronger in west Europe than in Europe as a whole.

This means that there is considerable homogeneity between the different league tables (Top 20) – but (a) positioning of these G-SIBs in a given country's league table is at least partly influenced by whether the bank is based in that country, and (b) the identity of the other banks in the Top 20 is influenced by the country the borrower is

[109] Mark Carey and Greg Nini, (2007) "Is the Corporate Loan Market Globally Integrated? A Pricing Puzzle" Journal of Finance, 62, (6), 2969-3007.

in (being a mix of "local" banks and other G-SIBs that are simply less consistently prominent in the LBO market).

Over 300 lenders were involved in at least one LBO transaction in at least one country during the course of 2010-2017. This is a low threshold to signal active engagement in the market. If we – as a rule of thumb – assume that an active lender would be involved in a deal at least every other month then 46 lenders pass this test – and 34 were involved in at least 96 deals (i.e. one per month) across all six Member States in this time period. If we double the threshold again, there are still 13 lenders that were sufficiently active to pass this test. This is simply to reinforce the point that there are a non-trivial number of lenders that have the necessary skills and wherewithal to participate in the LBO segment. This was reinforced in our fieldwork where the vast majority of lenders had a leveraged team specialised in originating and executing such transactions (somewhat fewer had a dedicated PF/INFRA team).

These more active lenders pursue a variety of strategies. As we have noted above, some are very active across all of the countries of interest. But there are also lenders that are highly active, but with a very clear country focus.

There is also some degree of segmentation by size. We divided deals into three broad bands: those with total debt below €250m, those between €250m–€1bn and those above €1bn. If we consider those 34 lenders that were involved in at least 96 deals across all six countries in 2010-17, then eleven of these were most prominent in the €1 billion band, i.e. they were primarily focused on larger transactions. These eleven overlap significantly (but not perfectly) with the twelve G-SIBs mentioned above. Such large banks should have the skills necessary to execute the process well but also have access to broader banking knowledge (provided that they can effectively manage any ensuing conflicts of interest and properly harness such knowledge to better assess credit risks). There are also lenders focused on such larger deals, but which do not appear to be volume players (at least in Europe), nor are they G-SIBs.

Other lenders are active across all size bands relatively evenly. This latter group also includes several of the G-SIBs. These are lenders particularly focused on the volume, or flow, of deals.

A further dimension is the capacity to underwrite high-yield bonds within debt structures. In the larger banks that we interviewed, it was most often the case that such capacity sat in the same originating teams as for syndicated lending. This reflects a degree of convergence between these products.

Lenders in the PF/INFRA segments

As with the LBO market, we conducted a similar analysis of the leading lenders in the PF/INFRA segment. We combine these here (indeed, lenders tend to operate PF/INFRA activity out of the same units). Most countries – the exceptions are France and the UK – are less fragmented/more concentrated than the LBO segment. More lenders (almost 370) are recorded at least once in a PF/INFRA deal in Loan Connector, with about 150 appearing in both the LBO and PF/INFRA segments.

Table 17: Leading participants by market share in the PF/INFRA segment (based on loan value, 2010-2017)

	DE	ES	FR	NL	PL	UK
Lender ranked 1	17%	13%	12%	13%	23%	6%
Lender ranked 2	11%	10%	10%	14%	14%	6%
Lender ranked 3	6%	10%	8%	8%	9%	5%

Lender ranked 4	5%	6%	5%	8%	8%	5%
Lender ranked 5	4%	4%	2%	4%	4%	4%
Lender ranked 6	3%	4%	4%	3%	4%	3%
Lender ranked 7	3%	3%	2%	2%	3%	3%
Lender ranked 8	3%	2%	4%	3%	3%	3%
Lender ranked 9	3%	2%	2%	2%	3%	3%
Lender ranked 10	3%	2%	3%	3%	2%	3%
Lender ranked 11	3%	2%	3%	3%	2%	2%
Lender ranked 12	3%	2%	5%	2%	2%	2%

Source: Europe Economics (using Thomson Reuters Loan Connector data).

As with the LBO segment we calculated the HHI for each of these markets based upon the market shares of the top 20 participants. The results were higher for all markets, except the UK. These were in the range from 465-582 for all countries save Poland (where the HHI score is just below 1000). HHI scores in these ranges are generally taken as being prima facie indicative of non-concentrated markets, with Poland's market being on the cusp. As noted above, we discuss the possibility of collective bargaining power at the end of this chapter.

The evidence of some degree of "home bias" is more apparent in PF/INFRA than in the LBO segment. Now "domestic" lenders (highlighted in pale blue in the table above) have over 40 per cent of the estimated total loan value in Germany, Spain, France and Poland. There are also banks operating across all of these countries – however, this is less pronounced than with the LBO segment. The number of leading banks appearing in the Top 20 in all (or at least five) of the markets is eight rather than the twelve seen in the LBO segment. Again each of these is a G-SIB (together with the European Investment Bank). Such large banks should have the skills necessary to execute the process well but also have access to broader banking knowledge (provided that they can effectively manage any ensuing conflicts of interest and properly harness such knowledge to better assess credit risks). This may be both more important and more challenging than in LBOs. In was clear in the fieldwork both that PF/INFRA often has dedicated bank professionals working on such deals – but also that there are many specialisms within PF/INFRA, i.e. knowledge of the credit risks in building a windfarm may not transfer well (if at all) to an understanding of the credit risks in a pipeline.

We explored any segmentation by size amongst lenders. The results were broadly comparable with the LBO segment, which we have described above, except that there were more lenders mostly focused on larger transactions (i.e. above €1 billion). This is not particularly surprising given the typical deal sizes relative to LBOs (as described earlier in this chapter).

There are four banks that are consistently in the league tables for all (or nearly all) countries for both the LBO and PF/INFRA segments. Three of these are based in France.

Lenders' business models

We draw on our lender fieldwork to describe lenders' approaches to syndicated loan organisation and client relationships. There are a few key differences according to whether lenders are engaging in LBO or PF/INFRA loans, which we describe below, but overall lenders' business models reflect individual firms' preferences rather than loan segments (for example two different lenders both engaged in PF loans may have very different approaches).

Organisation
The approach to deal origination and execution varies across lenders according to their business models (although overall they follow a similar process as described in Chapter 2). Many MLAs seek to manage borrower/sponsor *relationships* locally (i.e. in the various geographic markets where the lender is active), but manage the deal *execution and syndication* centrally. In contrast, some international banks may organise around product rather than geographic markets, e.g. with a project finance team covering all deals in PF/INFRA across the relevant geographic markets. These local/product business lines would be responsible for originating a loan and developing the credit risk assessment.

This local / product-specific presence is often considered critical to origination (i.e. interacting with the borrower and assessing the merits of the loan for the bank) and credit risk assessment, but matters less to the syndication process per se (i.e. selling the loan down in the wider investment market, where the important factor is where the investor base is, rather than where the loan is based). For this reason many banks have a more centralised syndications team which is involved when a loan is to be syndicated (and would likely also be consulted on loan pricing even if not). These syndications teams tend not to have a balance sheet and their role is to support the syndication process in terms of advising on pricing, underwriting (taking into account market appetite and the ability of the bank to sell down), and terms and documentation to negotiate with the borrower/sponsor, and executing the deal in the market (which would include managing the general syndication phase – sometimes along with a sales or distribution team). These teams tend to be based in regional hubs, close to the main investor base and (potentially) large sponsors. Some very large international banks might have syndication teams across multiple cities to respond to local deal teams.

In some cases, the syndication expertise will typically be integrated with a broader team responsible for origination, structuring and securing access to capital markets for loans within the same institution. In the case of LBO loans, where national markets are less relevant and the main drivers are the location of the sponsors and investors, many origination and syndication teams are based in London regardless of the overall geographic scope of the bank. For PF/INFRA loans, on the other hand, local or product-specific presence is considered to be more valuable by many (although not all) lenders in our fieldwork (the syndication function would still likely be centralised). This could explain in part the greater degree of "home bias" shown in Table 16 and Table 17 for PR/INFRA loans compared to LBO loans.

Sign off for syndicated loans generally happens centrally (various committees would review submissions from the origination and syndications teams); this may depend on the size and risk of the loan, with some decisions being taken regionally and others at the central/global level in the bank. Non-EU banks may have some delegated authority to sign off deals in the relevant EU hubs, with deals over a certain threshold signed off in the bank's headquarters.

Approaches to client relationships
Some banks tend to take an 'originate to distribute' approach to syndicated loans, accessing underwriting (and other lead arranger) fees and distributing a large proportion of the loan away in the general syndication phase (some parts of the loan would still be held, in particular the revolver element and possibly part of the Term A loan). This approach relies particularly on experienced syndication and distribution teams to ensure the sell-down of the loan, and is generally adopted in LBO loans (PF/INFRA loans generally being club deals where the lenders are more likely to hold

their allocations). There is no clear trend in the banks adopting this approach – non-EU investment banks are more likely to originate to distribute but there are still those with a take a hold approach. Similar variation exists with other large EU banks in our sample, although the majority appear to favour a take and hold approach. Smaller banks with MLA roles in smaller markets also tend to take and hold.

This approach may be driven in part by the importance of the banks' commercial operations, with investment banks likely to be more focused on deal flow and underwriting fees and commercial banks interested in using loans as an entry point to providing other banking services. Indeed, those lenders in our fieldwork with a strong local presence tended to favour take and hold approaches (which may encourage participation in the PF/INFRA market).

That said, building relationships with borrowers and sponsors is important to banks across the board, regardless of the ability to provide additional commercial banking services or the approach to holding or distributing loan shares. Banks maintain relationships with borrowers and sponsors actively through local teams and their more centralised syndications teams (the latter usually focussing on sponsors), and through repeat business (reputation). For some banks cultivating relationships with sponsors may influence their lending strategies. For example, in LBO loans it is common for banks to work with more than one sponsor bidding for the asset (through the use of trees) as this maximises the chances of being attached to a winning bid and securing the deal. However, some banks prefer to focus exclusively on one sponsor in a particular transaction and build a relationship with them. The relationships between lenders and borrower/sponsors is explored further in Chapter 4 where we set out and test competition hypotheses.

Deal flow is important for determining pricing and loan precedents, but not essential. A strategy that is overly focused on deal flow may incentivise a bookrunner to activate market flex when a deal is going badly (bearing the loss of fees but also potentially resulting in a worse deal for the borrower/sponsor) sooner than if it was focused on embedding its relationship with the client.

Having strong relationships with borrowers and sponsors is advantageous to lenders in terms of ensuring they are among the initial banks approached to bid for a role in the syndicate, and providing the possibility to influence the loan structure through 'early bird' discussions with the borrower. In some cases a relationship bank might be appointed directly as a lead arranger and bookrunner without a competitive process (e.g. in cases where the underlying transaction is highly confidential and need to be executed quickly). We explore potential competition concerns related to the appointment of a lead arranger without a competitive process in the analysis of competition hypotheses in Chapter 4.

Cross-border dimensions of syndicated loans

Overall then, the west European market is largely an international one. Banks with a different country of origin to the borrower are active in the syndicated loan market. Such non-domestic or foreign bank underwriting and arranging of syndicated loans is found throughout the European markets, in small countries as well as the largest countries with the most sophisticated domestic financial systems.[110] In the analysis of lenders above, we noted that the majority of lead banks are active across all (or mostly all) these geographies in at least LBO and likely both LBO and PF/INFRA loans, and either have local offices and teams based in these countries or access borrowers

[110] Houston, Joel, Itzkowita, Jennifer and Naranjo, Andy (2007) "Borrowing beyond Borders: The Geography and Pricing of Syndicated Bank Loans", University of Florida.

and sponsors from a central hub. In this section we draw on our literature review to analyse the cross-border dimensions of syndicated loans, which are summarised at the end of this chapter along with our data analysis (e.g. around lenders' geographic presence in Table 16 and Table 17) and lender fieldwork results in the lender business model section).

Foreign banks[111] might initially have less local, market or firm specific information than their domestic counterparts and may also overcome cultural and bureaucratic barriers in the host country. Yet cross-border lending is widespread in Europe and around the world. Given the costs imposed by these barriers, the empirical literature provides some specific reasons why foreign bank entry takes place.[112] A key benefit of cross-border lending arises from its effects on risk diversification – when a domestic bank invests abroad, it becomes less exposed to domestic shocks. Another reason is that foreign banks – initially at least - tend to follow their customers abroad when they enter foreign markets. When the foreign bank serves existing customers from their home country, customer-related informational and cultural barriers are essentially not present, although country/market-specific informational barriers may still exist.[113] Third, foreign banks might have technological (expertise) advantages over domestic banks and thus operate more efficiently. Foreign bank entry would occur when these technological advantages outweigh the informational disadvantages.[114]

Syndication offers syndicate lenders the possibility to benefit from the each other's' knowledge of the borrower and expertise in lending to a given market; by contrast, bilateral lending requires costly market research and relationship-building. Syndicated lending enables foreign banks to come together with domestic banks and therefore may provide greater opportunities for these foreign banks compared to bilateral lending.[115] Additionally, banks with lower levels of capital in lender countries favour syndicated loans over other kinds of cross-border loans. Borrower country characteristics such as level of development, economic size, and capital account openness, play a lesser role for syndicated lending compared to bilateral lending, suggesting a diversification motive for syndications.[116]

Borrower country risk characteristics that are generally relevant in a bank's decision to extend cross-border loans should reflect external and domestic vulnerabilities, and may include solvency, liquidity, and financial openness. Since syndicated loans allow banks to diversify risks by lending to a wide range of borrowers (i.e. by lending a potentially smaller amount to a greater number of borrowers than would have been possible bilaterally), including riskier ones, individual borrower risk profile is likely to be less relevant for syndicated loans compared to bilateral lending.[117]

Another potential explanation for the presence of foreign lenders in the syndicated loan market is underdevelopment of the domestic credit supply. For example, a recent

[111] The Bank of International Settlements' definition of foreign banks is: "bank whose controlling parent is located in a country other than that where the borrower resides, i.e. bank whose controlling parent is a non-resident financial institution."

[112] R. Haselmann, P. Wachtel (2011) "Foreign banks in syndicated loan markets". *Journal of Banking & Finance* 35 (2011) 2679–2689.

[113] Buch and Golder (2001) "Foreign vs. domestic banks in Germany: Do they differ?" *Kredit and Kapital* 19-53.

[114] R. Haselmann, P. Wachtel (2011) "Foreign banks in syndicated loan markets" *Journal of Banking & Finance* 35 (2011) 2679–2689.

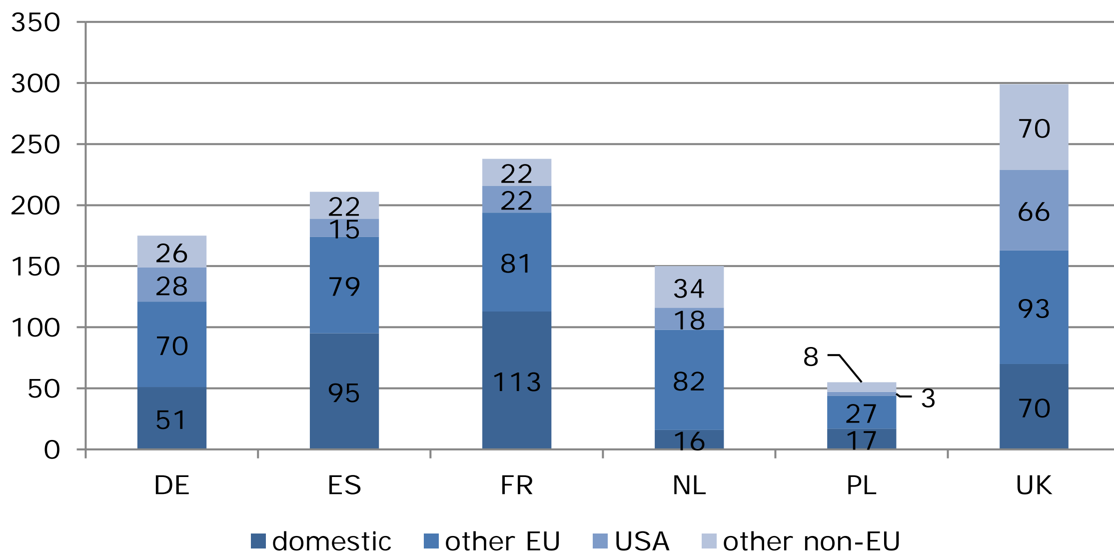
[115] As part of our further data analysis, we will explore the frequency with which foreign and domestic banks join together on the same deal.

[116] Cerutti, Eugenio, Hale, Galina and Minoiu, Camelia (2015) "Financial Crises and the Composition of Cross-border Lending", IMF.

[117] Cerutti, Eugenio, Hale, Galina and Minoiu, Camelia (2015) "Financial Crises and the Composition of Cross-border Lending", IMF.

analysis[118] of the motivation for cross-border activity in the European syndicated market has found that, after controlling for loan and borrower characteristics, loan spreads are larger in large countries, and particularly for foreign banks. In contrast, in smaller and less developed markets spreads are lower and so is the difference between the spreads charged by foreign and domestic banks. This suggests that whilst cross-border activity in large markets is motivated primarily by risk appetite and larger loan spreads, in smaller market syndications by foreign banks serve may fill in for the absence of domestic borrowing opportunities.

Figure 26: Number of lenders by borrower's country across sample (2010-2017)

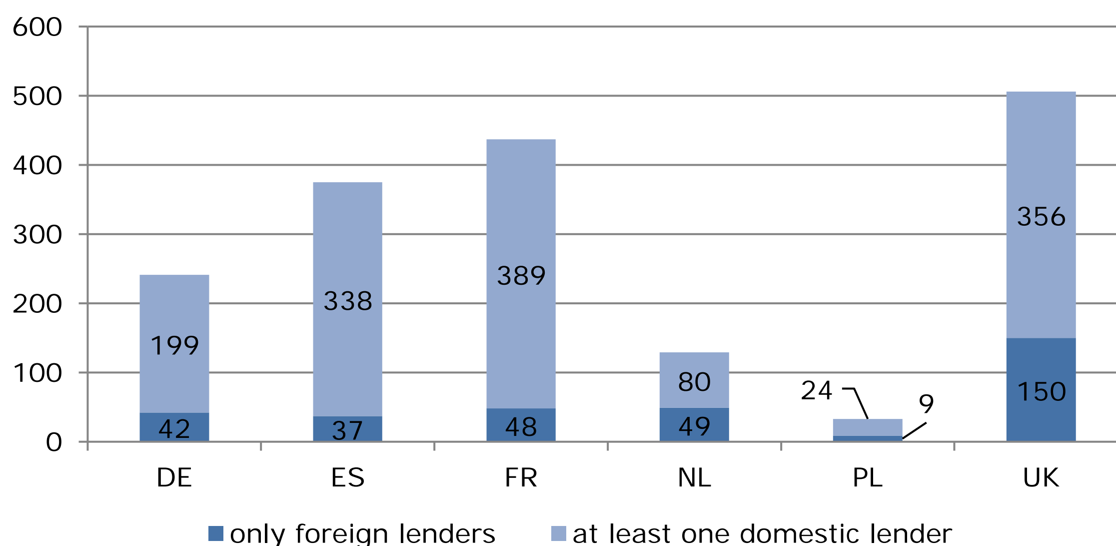


Source: Europe Economics (using Thomson Reuters Loan Connector).

Figure 27 below shows the number of deals involving *only* foreign lenders or *at least one* domestic lender. The graph shows that most of the deals involve at least one domestic lender, however some variation is visible across countries. Whereas almost 90 per cent of deals in Spain and France have at least one domestic lender, this percentage decreases to 82 for Germany, to around 70 for Poland and the UK and to 60 for the Netherlands.

[118] R. Haselmann, P. Wachtel (2011) "Foreign banks in syndicated loan markets" *Journal of Banking & Finance* 35 (2011) 2679–2689.

Figure 27: Number of deals by Member State and lender operating country (2010-2017)



Source: Europe Economics (using Thomson Reuters Loan Connector).

An important potential benefit of cross-border lending for the banking system as a whole, is due to the interaction of competition and stability. Foreign entry in the domestic market will tend to increase competition in the domestic banking market. This effect will be particularly pronounced if the domestic market was previously highly concentrated or if domestic banks were operating inefficiently (as is often the case in developing countries).[119] If foreign banks are more efficient (for example, foreign banks that enter developing markets may have more advanced risk management systems), then competitive forces may push domestic banks to becoming more efficient as well, further enhancing stability.

On the other hand, foreign capital can be more mobile than domestic capital. Following a negative event that reduces the attractiveness of investment in the domestic economy, foreign banks may decide to rapidly exit the market. Domestic banks, on the other hand, cannot divert their capital as quickly outside their country. It should be kept in mind that foreign banks are less likely to exit the market if they have established their presence in the form of a subsidiary, possibly due to the presence of significant fixed costs.[120]

The availability of cross-border supply has not diminished the importance of local banks, as can be seen above. In terms of loan amount and the number of deals local banks (by parent) rank highly in the league tables in all Member States in our sample. In our lender fieldwork, banks were divided as to the merits of having a local presence to either help secure origination or else better assess a potential client's credit risk. These preferences do not appear to be driven by segment focus (i.e. LBO versus PF/INFRA).

[119] Allen, Franklin; Beck, Thorsten; Carletti, Elena; Lane, Philip; Schoenmaker, Dirk and Wagner, Wolf (2011) "Cross-Border Banking in Europe: Implications for Financial Stability and Macroeconomic Policies", CEPR.

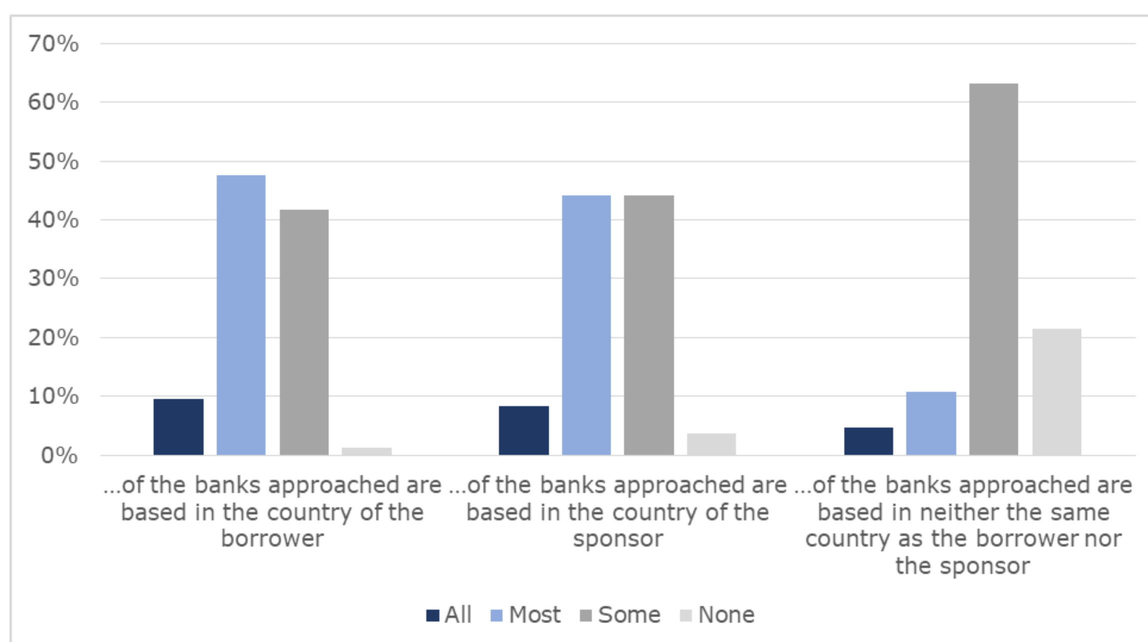
[120] Allen, Franklin; Beck, Thorsten; Carletti, Elena; Lane, Philip; Schoenmaker, Dirk and Wagner, Wolf (2011) "Cross-Border Banking in Europe: Implications for Financial Stability and Macroeconomic Policies", CEPR.

In Poland, there are evidently fewer lenders active in the syndicated loans market (at least for the segments that we have examined). This is largely a function of the significantly smaller deal pool in Poland (as can be seen from Figure 26 and Figure 27 above). In addition, provision of a competitively priced zloty loan is seen as requiring access to local currency deposits (to avoid hedging costs).[121]

Some lenders (notably in Poland) focus predominantly on deals with a domestic link – e.g. either a local borrower/sponsor, or a foreign borrower involved in a local project or buyout. (This is driven in some part by the capacity to lend in currencies other than zloty, which may be uncompetitive for some banks.) A further explanation offered by lenders in our fieldwork for the dominance of local banks relates to the point that some of the ancillary services (such as cash management) to syndicated loans are best provided by a local clearing bank, and where such a local bank is already providing the borrower with such services, then this may drive its inclusion in the syndicate.

These findings are broadly mirrored in the survey of borrowers and sponsors. The fieldwork show some or most lenders approached to act as MLAs were local to the borrower and/or sponsor in the majority of cases. This could also include foreign banks with local operations – indeed, UK borrowers and sponsors were the most likely to go exclusively or mostly approach locally-based lenders to act as an MLA on the loan, which we interpret as being reflective of the importance of London in this market.

Figure 28: Proportion of banks approached to act as MLA from same country as borrower and/or sponsor



Source: YouGov survey results, sponsors and borrowers combined, N=84.

Obviously, there is a difference between approaching a bank and appointing one (meaning that the former group could be notably more diverse than the latter). However, the clear capacity of sponsors and borrowers to approach non-local banks should provide some element of market discipline.

121 We also note that ninety per cent of loans with Polish borrowers (where the disclosure is made) use the WIBOR benchmark, rather than LIBOR or EURIBOR. Again, this limits cross-border appeal.

The key question is whether the “home bias” is a signal of competition being undermined by restricting the pool of potential MLAs. We consider this unlikely, at least in the west European markets covered by this study, where non-local banks can be readily accessed. In Poland, on the other hand, the low deal frequency and use of a non-mainstream currency, may make the pool of potential MLAs relatively small. This appears to be more of a concern in the PF/INFRA segment.

It could still be possible for local banks, though, to establish a degree of market power in connection with services ancillary to loan where the service is (a) to be provided by a local lender, and (b) the provision of the service is restricted to amongst the MLA pool. On the other hand, any desire to bring in a local clearing bank into the syndicate (i.e. without including it in the competitive RFP process to act as MLA) to provide commercial cash management services is unlikely to affect the competitive dynamics of the loan itself (although where these services are awarded to an ‘incumbent’ local bank without a competitive process, then this could of course lead to sub-optimal results).

Participation in the market and barriers to entry

The size of the eligible lending pool has an influence on competition in two main ways, by affecting the likelihood of collusive outcomes and the likelihood of an abuse of market power. We note that this analysis is at the loan segment / country level, rather than any case-by-case level and as such our assessment is limited to whether the market features and the various processes within loan syndication are more or less *conducive* to competition problems, rather than establishing specific cases of competition law violation.

The number of lenders approached will depend on the loan process. The most pro-competitive process involves borrowers/sponsors (and potentially their advisers) creating competitive tension amongst lead banks by negotiate terms individually with each lender, with little or no interaction between lenders pre-mandate. Subject to the number of participants capable of bidding being reasonably large (or, at least, not small) this feature will make any coordinated bidding difficult.

We have seen above that several hundred lenders are recorded on Loan Connector as having participated in at least one LBO or PF/INFRA transaction in 2010-17. However the number of these capable of acting as an MLA is clearly significantly smaller. This varies between markets, by segment (as we have noted previously, PF/INFRA loans are perceived as more idiosyncratic than LBO debt) and by transaction size.

Beginning with the LBO segment, in larger transactions (above €250m), the lender fieldwork indicated that banks expected the potential competition for a mandate in the western European markets of interest here to be from a pool of 10–12 international banks (being universal or investment banks) and a small number of regional players (with the latter likely to be, but not necessarily, local to the borrower).[122] Lenders expect to compete for lead roles (i.e. a place in the initial lending group) on a number of dimensions including price and other terms, experience in similar deals and knowledge of the investor market (especially important in bidding for bookrunner roles). This does not mean that sponsors/borrowers need to approach all of these. In less large transactions, fewer of the international banks would be relevant, but more local or regional banks would have the necessary capabilities. In Poland, for number of potential MLAs will be fewer, with estimates of the number being as low as 6–8.

[122] Loan Connector, of course, only shows who was selected as an MLA, not who was approached.

PF/INFRA is somewhat different, at least in terms of the composition of players. At least some of the international investment banks active in LBOs have limited or wholly curtailed coverage of this segment. This decision was described as being down to both low returns coupled to low velocity of money (i.e. a bank could be locked into a deal for long-term) and the absence of underwriting opportunities (since it is largely a 'club market'). This is why the number of banks awarded multiple MLA mandates across several markets in both LBO and PF/INFRA is relatively small, at just four. On the other hand, to the extent that it is fairly characterised as a club market, provision of balance sheet is more important than demonstrating distribution expertise. It is also the case that banks (e.g. Japanese ones) that have very limited presence in the LBO segment are highly active as MLAs in PF/INFRA. Altogether this means that the number of capable MLAs is at least as large as in the LBO space. However, a point emphasised in the lender fieldwork is that the PF/INFRA segment is more heterogeneous, with the result that in at least some parts of it, MLA choice (e.g. toll roads) would again be more restricted.[123] As before, the Polish market was described by lenders as having fewer MLAs than elsewhere with the skills and appetite in the PF/INFRA segment. The consensus view of those with one was that it fewer than in the LBO segment, i.e. suggesting six or fewer.

We also note that, if the same lenders are repeated on multiple transactions with a sponsor/borrower and if the pool of lenders is small (e.g. because of the nature of the credit risk is likely to restrict who the potential MLAs could be), this might enable lenders to converge their terms and prices over time even without explicit cooperation.

Reputation, including previous interactions with the sponsor/borrower, involvement in successful syndications and willingness to underwrite or lend significant tickets, also matters. Some aspects of reputation are institutional (i.e. associated with the lender itself), whilst others are individual (i.e. the skills and expertise to make an effective cash flow-based lending assessment, or to gauge market appetite well).

This suggests that three main barriers to entry to acting as an MLA in the syndicated loan market would relate to having the *right people* in place at lenders with the *reputation to deliver* and *access to the necessary information*. Lenders with recent experience of building market position (e.g. growing from regular participant to regular MLA over the course of several years) did not consider the ability to hire expert individuals represented an insurmountable entry barrier. We are not in a position to comment on how individuals in the market could lead such a transformation (clearly, this is a different proposition to 'simply' being able to execute a syndication effectively).

Deal flow is widely (but not exclusively) viewed by lenders as an important factor contributing to banks' development of their offers, e.g. building and sustaining relationships with sponsors, assessing appropriate price levels and other terms. This, combined with the importance of past experience and reputation, as well as high existing liquidity, could also imply that new entrants would face a slow take-up. MLAs considered the availability of other sources of information (such as publicly available

[123] Toll roads were identified as such an area in the lender and investor fieldwork. It is difficult to draw robust conclusions from the PF/INFRA dataset without identifying false positives because the majority of sub-divisions identified within Loan Connector have only a few transactions within them – i.e. those MLAs on those deals actually done would appear to dominate MLA choices. It can be observed that as the number of transactions in a given PF/INFRA segment increases, so the shares of the leading MLAs in that segment decrease. Segments with more than 15 transactions (across the eight years in our sample period) do not exhibit signs of concentration amongst MLAs. (Interestingly, toll roads also fall into this pattern – this segment has enough transactions such that it does not appear to exhibit concentration amongst the MLAs active in it).

deal data from a mix of databases) to be much improved from the position pre-crisis and generally to be sufficient to assess comparable transactions adequately. On the other hand, since the syndicated lending space remains a private market, there are various critical elements of information that do not always get released (specifically – and most critically – pricing information, at least based upon the availability of this in Loan Connector).

Outside of MLAs, the number of potential participating lenders is large (i.e. several hundred banks and institutional investors have participated). Markets where non-bank involvement is more limited across the board would have a smaller pool of lenders with this feature is evident in Poland which is a very bank dominated market, the involvement of institutional investors is currently very limited.

Conclusions around the remainder of Europe

Given that we were tasked with considering borrowers in six countries, we need to be careful in not over-extrapolating the results to elsewhere in Europe. We repeat that we are basing our analysis on activities in the countries of interest, within a set time period (largely speaking, post-crisis). However, in conjunction with views expressed in the lender fieldwork, we are able to make some tentative observations. First, that there is some degree of geographic segmentation between western Europe and the remainder of the EU, with the former more likely to have more lenders and more institutional investors following those markets. This could mean that Poland is a good proxy for non-west European countries more generally.

Second, we note that lenders do not have a common view on whether a local presence is significant or not. Those lenders considering this to be relatively unimportant are potentially less constrained in geographic coverage than those that do. The latter group are likely to focus upon local markets and large markets (where scale could justify the investment). Such an effect, if material, could mean that smaller markets (whether or not in western Europe) could be less well-served than the large markets covered by this study.

Subject to the same conditions as with the LBO segment, we are able to also make tentative observations about PF/INFRA outside of the six countries of interest to this study. First, there is some degree of geographic segmentation between western Europe and the remainder of the EU, with the former more likely to have more lenders. Again, this may mean that Poland is a good proxy for other non-west European countries, or other non-Eurozone countries (i.e. Scandinavian ones) – but this is in the context of more localised participation generally in PF/INFRA relative to the LBO space.

Non-bank institutional investors

Non-bank, institutional investors such as insurers (particularly life insurers that have long duration liabilities and wish to match long-duration assets against these), pension funds, family offices and sovereign wealth funds have been a significant feature of the LBO segment for some time. This can be through direct participation in a loan or indirectly through an investment vehicle, such as a Collateralized Loan Obligation (CLO). Whereas as pre-crisis such participation was generally through CLOs, it is now much more mixed according to the investors interviewed. Whilst such investors' involvement in the PF/INFRA arena lags behind, it has been increasing in the past few years such that the latter can no longer simply be characterised as a "bank market".

As noted, non-bank investors have various ways of accessing the market. Direct participation has normally been at the general syndication stage, but some investors

have developed dedicated teams, such that earlier participation in a transaction is achievable (e.g. the debt structure of an INFRA deal might be designed such that a long-dated, Term B tranche can be marketed directly at institutional investors such as insurers).

Over and above this, investors can participate via a mix of investment vehicles. The main forms are:

- Collateralized Loan Obligations (CLOs). These are portfolios of loans that are sub-investment grade or towards the bottom of the investment grade spectrum that are securitised and held in closed-ended funds. They are constructed and managed by dedicated managers. It is typical for such vehicles to incorporate fund-level leverage (i.e. the fund borrows in order to increase its firepower in the market, with current multiples being around 9x). Whilst such an approach can raise returns, it also magnifies losses and so can expose the CLO to significant loss if any loans in the portfolio default. The CLOs were severely affected by the financial crisis, but began a recovery in about 2013. However, these have not fully recovered their former prominence in the LBO segment where pre-crisis they may have accounted for 75–80 per cent of institutional monies, this is estimated to now be closer to 35-40 per cent. Given the increased diversity of investors, and the greater use of direct participation, it does not appear likely that CLOs will fully recover their old prominence in at least the short- to medium-term.
- Credit funds. These provide debt finance either through participation in a syndicate or through bilateral lending. These funds may well be leveraged, albeit at modest levels compare to a CLO. Credit funds are often managed by alternative asset fund managers (including private equity firms).
- Separately Managed Accounts. These are where a specialist third-party manager is tasked by an institutional investor with managing a pool of capital. These are typically unleveraged (i.e. the manager is able to invest the capital provided by the institutional investor to the account and no more).

Benefits to institutional investors of participating in the syndicated loan market

The European syndicated loan market is important not just to borrowers, but also to institutional investors. (Of course, this is recursive: the willingness of investors to contribute to the supply of capital impacts upon the terms upon which deals are struck, affecting demand).

Investing in a syndicated loan has a mix of economic benefits and drawbacks.

- First, as an asset class, syndicated loans share many features originally designed for bilateral bank lending. The most important of these is their location in the borrower's capital structure. As senior secured instruments, loans would be first to get repaid by a borrower. Similarly, in the event of default, loans enjoy a first lien claim over substantially all of the assets of that borrower.
- Second, it is essentially a floating rate market rather than a fixed rate market (as with bonds). (Borrowers may convert a floating rate instrument into a quasi-fixed rate one by executing interest rate swaps, etc. – however, unless these swaps are executed with the investor, the latter would still own a floating rate asset). As such, syndicated loans provide investors with protection from rising interest rates. It follows that the supply of capital to this market will tend to increase in periods of rising rate expectations (such as now).
- Third, a feature of syndicated loans that can be attractive to lenders relative to bonds is the (potential) availability of a covenant package. Project Finance and infrastructure loans tend to have strong covenant packages. In contrast however, in the leveraged market, the current tendency is for very limited covenant packages

("covenant lite", or cov-lite). This appeals to private equity sponsors as it provides them with additional flexibility in handling the companies in their investment portfolios. In particular, cov-lite can facilitate earlier repayment of the sponsor's investment or even payment of dividends to the sponsor. This is seen by participants as being very much driven by current market conditions, i.e. as and when the cycle turns, more traditional covenant packages will return to the leveraged market as well.
- Fourth, syndicated loans tend to be long-life assets, ranging from 5-8 years (LBOs) to up to 25-30 years (new build infrastructure). For those institutional investors with long-dated liabilities — such as life insurers and pension funds (or at least, asset managers investing on the behalf of these entities) — this match can be particularly attractive.

The increasing supply of non-bank lenders

Non-bank, institutional investors are increasingly interested in long-term financing in areas such as infrastructure and other large-scale projects, as well as leveraged assets (where their interest is longer-established). Attracted by the higher returns on offer, institutional investors have taken advantage of the financing opportunities in Europe as banks have pulled back to meet stringent capital requirements imposed by regulators, following the global financial crisis. In 2016, institutional investors accounted for nearly two-thirds of total primary loan issuance in Europe, a share that has steadily increased since the end of the financial crisis.[124] The share of non-bank investors in the European syndicated loan market is below the level of that in the US market, but this is essentially due to the presence of retail investors that are absent in the EU. Indeed, an analysis by M&G (2017, using S&P IQ data) indicates that institutional investors have larger-scale participation in Europe than in the USA, notwithstanding institutional investor participation in the US predating that of Europe.

This increasing participation by non-bank, institutional investors is confirmed by our fieldwork.[125] Non-bank lenders are particularly active in LBO loans, and tend to prefer PF/INFRA loans for projects that are in the operational phase, typically avoiding construction risk and the staggered draw-down phases (e.g. preferring the early utilisation of funds). Historically they have also targeted higher returns associated with leveraged loans. However, some investors have become comfortable with construction risk and there has been some softening in expectations on yield (i.e. moving nearer to banks) such that non-bank participation across all types of PF/INFRA loans is increasing too.

This increase in participation in PF/INFRA can also be explained by institutional investors' current strong appetite for long-dated loans (e.g. 20–30 years), as indicated in our lender fieldwork. Banking regulations (e.g. capital requirements and Basel III, discussed earlier in this chapter) have decreased banks' willingness to participate in long term loans and institutional investors are an increasing source of liquidity here. Indeed, our fieldwork shows that banks (in particular MLAs/active bookrunners) welcome the participation of institutional investors as this facilitates the general syndication phase by increasing the pool of investors to whom underwriters can sell down their loan shares

There is also a consensus in the academic and industry literature from the US and the EU that non-bank investors have contributed to increased liquidity in the secondary

[124] M&G Institutional (2017) "*Comparing the investment cases for European and US leveraged loans*", March 2017.
[125] Data from Loan Connector does not include a comprehensive picture of the participation of non-bank, institutional investors participating via the general syndication phase.

market.[126] Our fieldwork evidence indicates that non-bank investors (especially certain debt funds) actively trade here.

The increasing participation of non-bank, institutional lenders may well displace some banks in the general syndication phases of syndicated loans, and potentially also displace non-lead banks in the initial banking group (particularly in non-underwritten deals). For example, there is evidence from our fieldwork of loans in our sample Member States being structured to include whole tranches that are marketed directly to non-bank lenders. This may increase over time as non-bank investors become increasingly comfortable with PF/INFRA loans.

However, banks' role in syndicated lending is still critical, in particular for underwriting and arranging loans and taking on the revolving credit facility, even if (with LBO loans) banks do not retain the majority of the loan.[127] Increasing participation by non-bank lenders is therefore unlikely to significantly alter market dynamics within these core lending groups (increasing non-bank interest is as much complementary as substitutive). Banks participating in our fieldwork in general welcomed the increased participation of non-bank institutional lenders and as such do not see them as a threat to their lead roles in syndicated lending, although some banks did note increasing competition for loan shares from non-bank lenders.

That said, our lender fieldwork shows that key non-bank institutional investors have sufficient interaction with borrowers/sponsors which is likely to affect syndicate dynamics. For example, they might be approached directly by a sponsor/borrower, in addition to the bookrunner, during the general syndication phase, which can add to the borrower/sponsor's ability to monitor the behaviour of bookrunners leading the general syndication phase (i.e. by hearing directly from investors how the bookrunner is leading the general syndication and whether he is making every effort to sell down the loan at a good price). The impacts of non-bank lenders on the syndicated loan market dynamics will depend on the relationships between them and the lead bank lenders – if the two are vertically integrated in any way (i.e. lending banks have ownership in a non-bank lender) or there is a special dependent relationship between the two this would reduce the pro-competitive dynamic of non-bank involvement. We explore this hypothesis further in Chapter 4.

It is important to note that non-bank participation is not across the board. For example, in our sample Poland is still very much a bank-dominated market and there is very little non-bank participation. Respondents to our lender fieldwork suggested that institutional investors (i.e. insurers, pension funds) in Poland are limited by regulation with regard to what they can invest in – in particular complex and less liquid structures – and that changes to their regulation may be needed to facilitate their investment in syndicated loans The same may be true of other smaller markets across the EU28. In more national, bespoke markets where there is not a large pool of eligible banks and limited alternative lenders (as may be the case outside the west European market) any loss of lending appetite among banks resulting from regulation or changing market conditions could reduce the overall supply and lead to a reduction in executed lending volume or an increase in borrowing costs.

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[126] See for example Gupta, Singh and Zabedee – US (2008); Kamstra, Roberts and Shao - US (2013), Godlewski – EU (2015) and LMA "Guide to Secondary Loan Market Transactions" - EU (2016).
[127] The IMF identifies as much as 15-20 per cent of very high leverage debt in 2017 in the USA as originating with a non-bank as lead agent. This phenomenon does not appear to have crossed the Atlantic as yet.

Non-banks lenders and asymmetric information

A hypothesis associated with non-bank investors' attitude to pricing relates to asymmetric information. If non-bank investors are not likely to have pre-existing relationships with borrowers/sponsors they could be relatively less informed compared to bank investors. Therefore, to compensate the less informed institutional investors engaging in costly information production, loans with non-bank participation should have higher spreads than bank loans ceteris paribus (the "asymmetric information hypothesis").

Analysis of spreads on US loans with institutional investor participation against deals without such participation reveals that the difference in spreads between institutional and bank loans was larger in the earlier years when institutional loans first came into existence, but gradually decreased subsequently. The paper's authors establish the causal relationship between the informational disadvantage of institutional lenders and the premium on institutional loan spreads, supporting the argument for decreasing asymmetrical information over time. However, these higher spreads may simply be justified by risk factors, as non-bank investors will participate in risker loans. Indeed, the overwhelming majority of disintermediated loans were leveraged loans in the study of the US market through to 2006. Thus, risk factors alone may justify a higher spread on institutional loans (the "selection effect hypothesis").[128]

We explore the hypothesis around information asymmetry between lead banks and non-bank lenders in detail in Chapter 4.

Non-bank lenders' impact on pricing

Non-bank lenders include pension fund and insurers, as well as alternative asset managers of CLOs (such as hedge funds and also credit funds managed by private equity general partners). These asset managers usually target a higher rate of return than other institutional investors and banks. As a result, they may be more inclined to participate in higher-risk, complex transactions that would provide them with higher returns. Investment in syndicated loans may also be through funds that are themselves leveraged, such that the alternative investment fund manager still aims to achieve a higher return on its 'equity' in the fund.

Empirical evidence from the US market shows that loans involving institutional investors tend to be with riskier borrowers. For example, an average borrower from a non-bank lender was found to have a lower market-to-book ratio, a higher leverage ratio, and a higher default probability than an average bank borrower in the US market (using data from the mid-1990s to 2006).[129] Borrowers that approach institutional lenders are also found to be willing to pay higher spreads at loan origination.[130] It has been argued that because non-bank lenders can be willing to lend at times and situations when banks are not (for example very long-dated loans), where they are the 'marginal lender' necessary to complete a syndicate, then this will influence pricing.

This may be the case in the EU markets examined for this study – specific tranches within a loan can be structured such that they are marketed directly to institutional investors, potentially at a higher price than other tranches. Our fieldwork showed this is more likely to occur in PF/INFRA loans, where bank demand for long-dated loans is

[128] Nandy, Debarshi K. and Shao, Pei (2010) "Institutional Investment in Syndicated Loans". Proceedings. 394-409.

[129] Nandy, Debarshi K. and Shao, Pei (2010) "Institutional Investment in Syndicated Loans". Proceedings. 394-409, using data from the mid-1990s to 2006.

[130] Lim, Minton, Weisback (2012) "*Syndicated Loan Spreads and the Composition of the Syndicate*", NBER Working Paper No. 18356.

reduced and where institutional investors have become more active in the past few years.

However, the impacts on pricing of non-bank lenders would need to be considered along with the overall demand for the loan. Presumably such structures are adopted in order to attract non-bank demand in the face of insufficient bank demand, and therefore they are necessary to complete the funding, i.e. if a borrower requires a given sum, then it is for the borrower to determine whether the overall debt package required to provide that sum makes sense. The argument also does not account for causation – institutional investors may be focused on higher returns, but this likely dictates the types of loans they participate in, rather than resulting in them pushing up the price of all loans they are active in.

The role of the state actors

Based on our research, public sector actors are not involved in the LBO segment (we are excluding those lending banks temporarily under national government ownership or control as a result of remedial action taken post-financial crisis).

The PF/INFRA side is different. Their role in PF/INFRA could be as borrowers /sponsors (e.g. in the context of a public-private partnership, or PPP) and also potentially as lenders.

Infrastructure projects can also be developed and owned by public-private partnerships. As such, their financing may reflect either explicit or implicit guarantees from public authorities. This could decrease the credit risk to lenders either directly (the debt is guaranteed) or because the project's revenues are partly or wholly derived from government. Such reduced risk could allow the SPV to obtain funding at lower pricing than would otherwise be the case.

The central or local government, if it is involved, may contractually provide a number of undertakings to the Project Company, Sponsors, or Lenders which may include credit support in respect of the Procurer's payment obligations (real or contingent) under a concession agreement. If there is some governmental involvement, the choice of the lead arranger (and the other lenders) may even involve some level of scrutiny from the relevant public authorities. It is unclear whether this means it is more likely to involve competitive bidding in the selection of the MLA.

PPP debt, with its reduced risk (e.g. due to stable, even potentially guaranteed income) and longer maturities, was seen by several participants in our fieldwork as making it more attractive to institutional investors. In this sense, public actors (acting as sponsors) can be seen as contributing towards encouraging such investors to respond positively to a partial gap in the market created by the withdrawal of some banks from longer-term PF/INFRA financing.

There are also public sector lenders in the PF/INFRA space. Syndicated lending has also opened the gate for participation of multilateral development banks, state or European Union-sponsored structural funds into eligible loans. One such fund with particular importance is the EIB-operated European Fund for Strategic Investments (EFSI). The EFSI's link with the syndicated market is most tangible in the scope of infrastructure project financing. The EIB is likely to use EFSI funds to provide guarantees and loans via a financial intermediaries, who would then participate or lead a syndicate.[131]

The EIB does not itself act as a sponsor. It is a significant actor in the PF/INFRA segments, often able to provide finance in larger ticket-sizes than commercial banks.

[131] See http://www.eib.org/efsi/what-is-efsi/ for more information.

In our lender fieldwork (who, obviously, may be partial), it was noted that deals can be re-structured to accommodate EIB involvement, e.g. developing a tranche that is specific to the EIB. This can then mean that the deal is effectively re-structured around EIB involvement. If the deal was commercially financeable (i.e. the EIB's involvement is substituting for debt that could have been provided by commercial banks, rather than complementing this) then the borrower/sponsor would need to assess carefully the trade-offs involved. In our lender fieldwork, no bank claimed that the EIB was depressing prices through its involvement.

This EFSI program may have an effect on the incentives of borrowers and lenders in the sectors which it targets, specifically in SME and infrastructure lending. The Fund's activities may service a demand that existed but has not been adequately addressed until now. According to a document published by the EIB, new potential borrowers may include:

- Cities or regions with lower credit rating;
- Municipal or regional companies (e.g. utilities, transport companies, private social housing companies) with limited recourse to public sector guarantees;
- Companies or structures owned by associations of municipalities;
- Investment funds with an enhanced risk appetite (e.g. long tenor, long-term investment strategy, focus on very specific sectors such as brownfield decontamination and redevelopment);
- Financial intermediaries with lower credit rating, including those selected to implement financial instruments using European Structural and Investment Funds (ESIF);
- National/Regional Promotional Banks or commercial banks through risk-sharing structures; and
- Investment platforms.

Borrowers that would have benefited from the efficiency and lower borrowing costs, but do not have the financial standing in order to access the syndicated loan market, are likely to benefit from the Fund's activities. By providing guarantees and securitisation, the Fund effectively allows borrowers, such as high-risk, but socially beneficial projects to have access to syndicated (and bilateral) lending. This would be particularly true for those Member States where sovereign guarantee schemes are few and underdeveloped. The EFSI would provide a complementary financial instrument to syndicated lending. That said, it is not possible to conclude from the data available to us (or rather not available) whether the presence of a public sector actor actually does lead to lower borrowing costs for a given credit risk nor whether it has other effects on the commercial aspects of a transaction (e.g. resulting in increased fees due to higher expected bidding costs, etc.).

Apart from addressing the demand for certain types of loans, the Fund may impact the supply side of lending. While the EFSI is unlikely to divert funds from the few large banks, smaller national-level banks and lenders, who have been deemed partner financial intermediaries are likely to become more active in the lending process, either on a bilateral basis or as members in the syndicate, as the EFSI guarantee effectively serves as collateral. The idea is that smaller banks that have to follow strict regulatory rules would be willing to give loans more readily.[132]

[132] European Investment Bank (2016) "The role of EFSI in financing urban and regional projects: Factsheet".

EIB funding under EFSI is not considered to be state aid.[133] However, the EIB does look at the overall funding of a project to check whether there is state aid from one of the other co-financiers. In particular, according to a joint statement by the EC and the EIB, state aid rules apply for programmes managed and implemented by the EIB Group on behalf of, or together with, a Member State, funded by resources from national budgets, or by resources from the Union budget which flow through national budgets, or by a combination of those resources.

The main motivation for such involvement would be to resolve a market failure, i.e. providing capital to (narrowly) sub-marginal borrowers (i.e. those borrowers that could not afford debt priced according to their risk). In current market conditions, there is a risk that such actors will displace lending that could have come from commercial lenders.

Loan pricing per segment

Syndicated lending is essentially a floating rate market. This is a point of difference to the bond market, which is a fixed rate product. (A floating rate syndicated loan can of course be converted into a fixed rate loan through, for example, the use of interest rate swaps.)

As a floating rate market, typically the pricing mechanism of a syndicated loan is expressed in terms of a spread over a benchmark rate, e.g. the London Inter Bank Offered Rate, LIBOR (in this way it resembles the pricing of conventional bilateral loans in the corporate market). Table 18 shows that the majority of tranches with pricing information have Euribor (Euro Inter Bank Offered Rate) as benchmark rate whereas the price of the second largest group of tranches is benchmarked against LIBOR. Only 2 per cent express price in terms of a spread over the Warsaw Interbank Offer Rate.[134]

Table 18: Number of tranches by pricing mechanism (2010-2017)

Base rate	Number of tranches	% of total tranches with this disclosure
Euribor	1,069	63%
LIBOR	601	35%
Warsaw Interbank Offer Rate	29	2%
Fixed Rate	10	1%
Total	1,709	100%

Source: Europe Economics (using Thomson Reuters Loan Connector).

It is worth noting that Euribor, for example, is currently negative. For example, the three month Euribor rate has been negative since 2015, and currently sits around -0.3 per cent. It is understood, however, that the LMA's standard clauses around having a zero floor for Euribor and Libor has been fairly widely adopted.

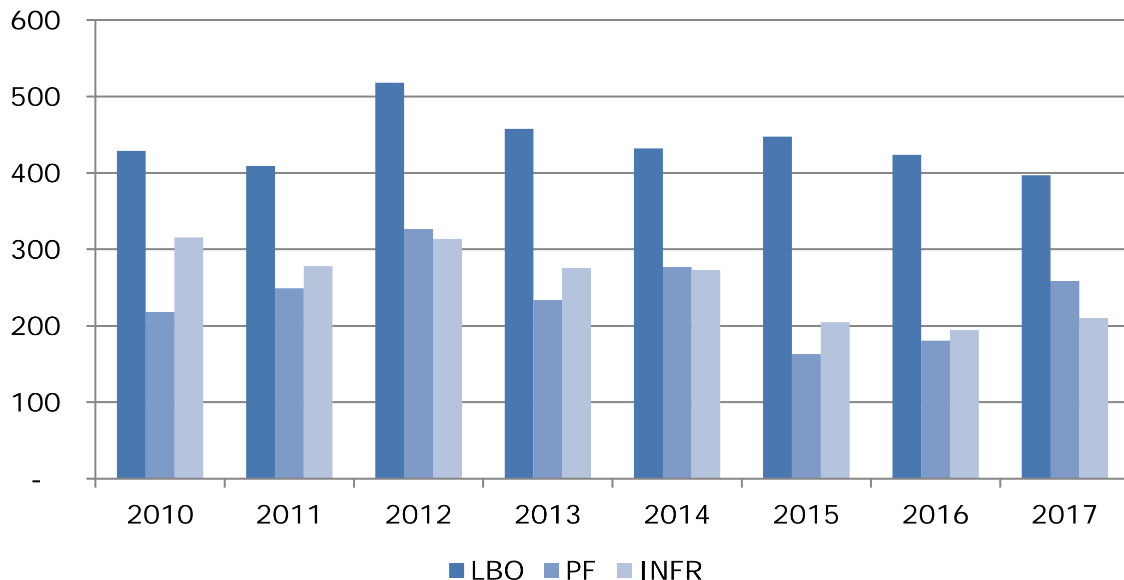
LBO loans are systematically more expensive than Infrastructure and Project Finance loans. LBO margins tend to remain within the 400-500 bps band whereas a larger

[133] European Commission (2016) "European Structural and Investment Funds and European Fund for Strategic Investments: Complementarities".

[134] Syndicated lending in Europe remains a private market. In consequence, Loan Connector is not able to provide pricing data for all loan tranches as it can be kept confidential by market participants. Pricing information (i.e. on a loan's applicable interest rates) available for 41 per cent of the tranches in our sample, ranging from 57 per cent for LBOs to 29 per cent and 22 per cent for Project Finance and Infrastructure loans respectively. That these data are not comprehensive needs to be borne in mind in the analysis below.

price variation over time is identifiable for Project Finance and Infrastructure. This pattern holds in each Member State.

Figure 29: Average margin by loan type over time (bps)



Source: Europe Economics (using Thomson Reuters Loan Connector).

Similarly, the benchmarks in the market, for example, the LPC Top 40 (focused on the leveraged market), shows a similar downward trend starting around the end February/early March 2016 to the new issuance chart above. Relatively benign macroeconomic conditions and significant supply of capital are putting pressure on spreads/yields.

Figure 30: Average yield on LPC Top 40 Leveraged EMEA (bps, 2010-2017)

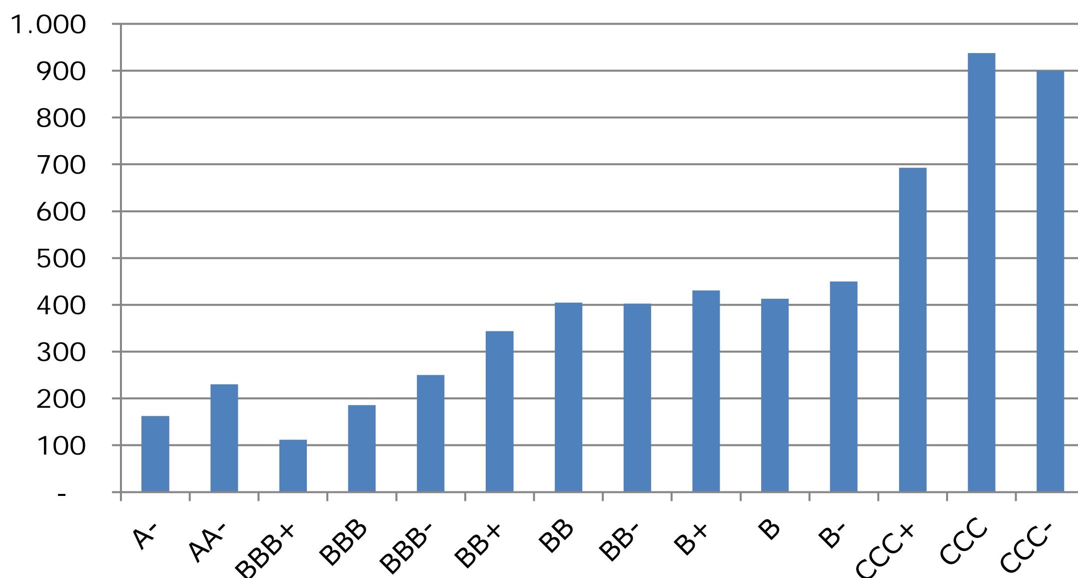
Source: Thomson Reuters Loan Connector.

There are two main ways in which we can consider pricing using the data from Loan Connector. First, we can consider how pricing is linked to the rating category of the

tranche, i.e. since we would indeed expect higher prices to be associated with riskier loans. Given the nature of the market it is unsurprising that the Loan Connector data on tranche ratings are very restricted (ratings information is provided only for 296 tranches, 95 per cent of which are LBO tranches). Over two-thirds of these ratings are B+/B (S&P classification), i.e. towards the bottom of the investment grade spectrum, just above junk.

We nevertheless explored the extent to which a higher price is an indicator of risker loans. Figure 31 shows indeed that the lower the credit rating the higher the price of the tranche on average. It is possible that the variation in pricing of loans between countries noted above could simply be a function of different risk profiles of the tranches syndicated.

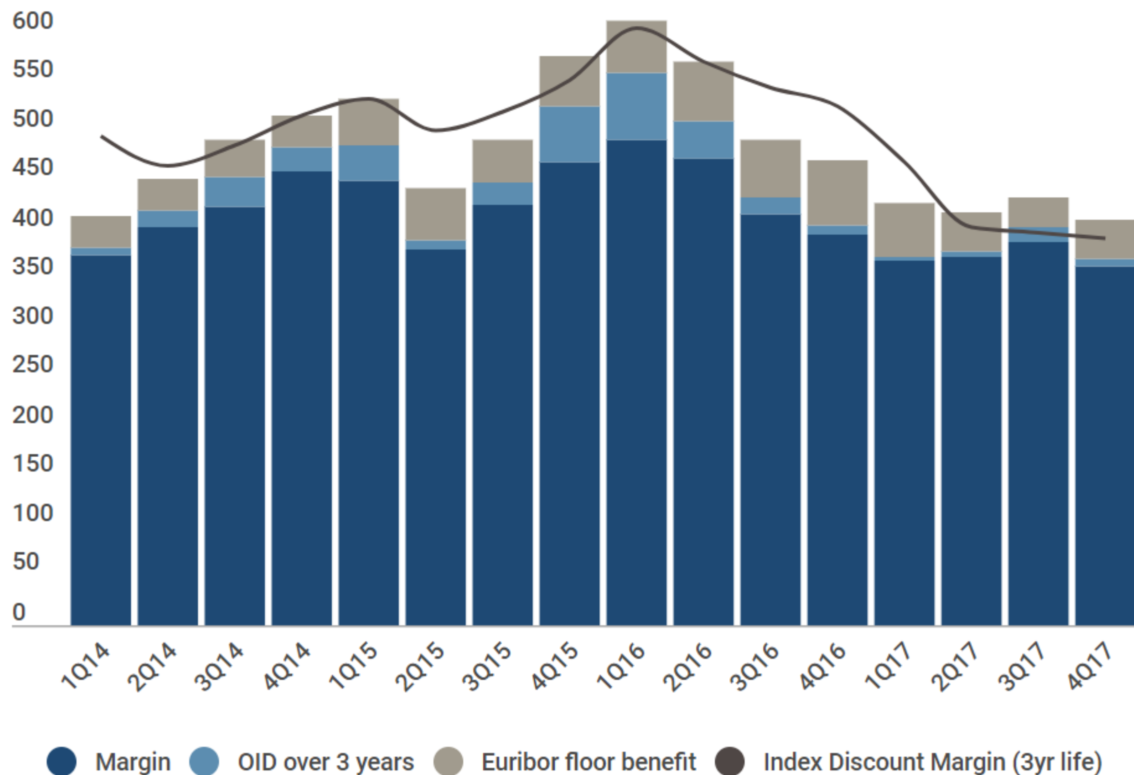
Figure 31: Relationship between tranche rating and average spread (bps, 2010-2017)



Source: Europe Economics (using Thomson Reuters Loan Connector)
Note: Rating categories correspond to the S&P classification.

Second, we can consider the pricing of different types of loan facility (e.g. considering the prices of all tranches identified as 'Term B' debt. This is cruder than looking at credit ratings, but does significantly increase the size of the available data set. The recent experience in Europe has been that loans have generated a significant premium relative to index, albeit this has been declining in the past few years.

Figure 32: Spread of Term B New Issuance relative to Index

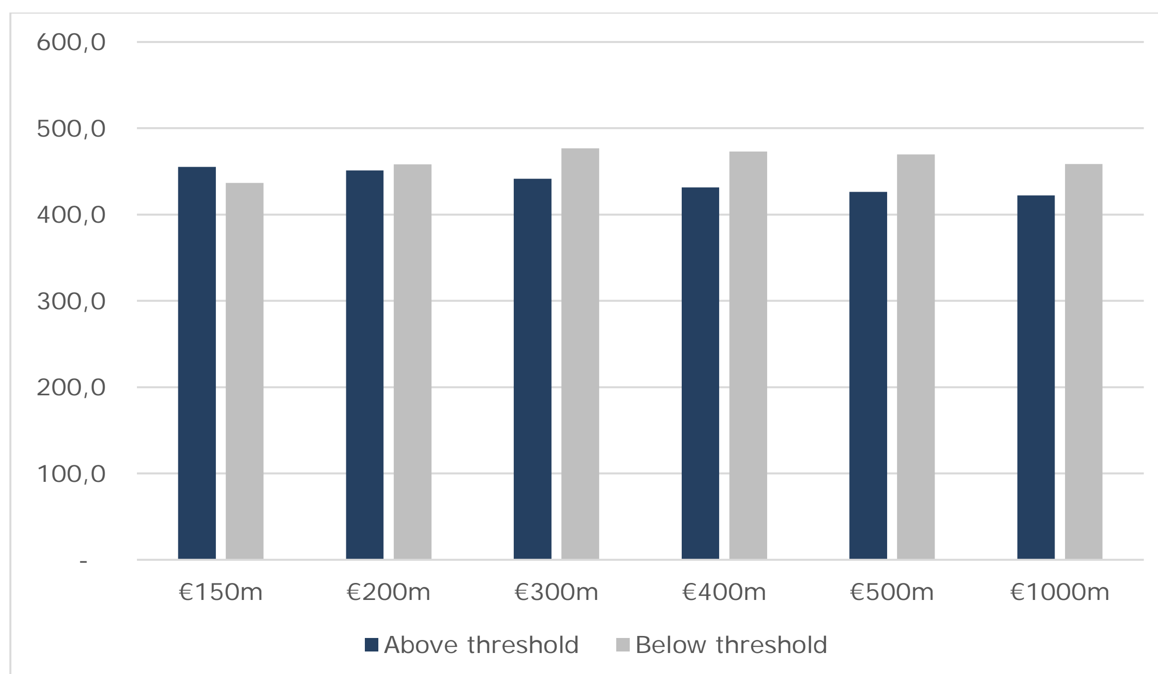


Note: OID is the Original Issuer Discount.
Source: Muzinich & Co.

This access to a larger dataset allows us to examine the influence of factors – in particular deal size – on spreads. The most data on spreads available to us relate to Euribor-benchmark Term B Loans, where we have spread data on over 250 loan tranches. We note that whilst Term B loans are a recognisable product in the market, they are not a commodity, i.e. there are many idiosyncratic features that are not captured here. As can be seen below, larger deals tend towards lower spreads (the chart below looks across the entirety of 2010-17 – but this effect also holds for shorter timeframes, say the most recent 2-3 years).

There are two main potential, non-mutually exclusive explanations for this. First, there may be qualitative differences between large and small loans, e.g. larger deals are consistent with larger borrowers, which correlates with superior prospects, i.e. lower credit risk. Second, larger deals are more likely to have secondary markets made for them by broker-dealers, i.e. there should be some reduction in liquidity risk at work. The phenomenon described here is consistent with both these, and with any risk reduction being – at least in part – passed on to borrowers through standard competitive dynamics.

Figure 33: Euribor Term B spreads on LBO Loans, by deal size, 2010-17



Source: Europe Economics (using Thomson Reuters Loan Connector).

Fees

Market participants are not under an obligation to publish fees in what remains a private market. Therefore, as with pricing data, Loan Connector does not provide comprehensive pricing data for loan tranches.[135] Given the paucity of this data, we are cautious here not to overly rely upon it in case it suffers from selection bias, or equivalent issues. Similarly, in our fieldwork, we found that many participants were reluctant to share such information. In addition, because of the different tasks involved in the formation and management of a syndicated loan (e.g. identifying potential members, determining commitment shares, negotiating the contractual terms, monitoring loan performance, managing many transfers between syndicate members and the borrowers, etc.), and the different types of loan facility provided, the typologies of fees in a syndicate can be quite complex.

However, the data from both sources are broadly complementary and we have used both these sources in the description below. Therefore, we are able to provide an approximate picture of both issuance fees and the cost of ancillary services such as cash management and hedging. We do so in two illustrative cases, one for an LBO, the other for a PF/INFRA transaction.

Fees in LBOs

We take as our first example an LBO. One key determinant of fees will be whether or not underwriting is provided. Underwriting fees remunerate the banks for the additional risk for committing to provide (in aggregate across all the underwriters) the full value of the loan (such fees can also be seen as a way of remunerating a lender for providing what would otherwise be unremunerated services).

[135] According to the product specialists at Thomson Reuters, this is due to the confidential nature of pricing and fee data which is not always provided by banks. Looking across the entirety of the sample, 2010-17, there are 357 data points for what Loan Connector terms upfront fees and about 200 on commitment/cancellation fees.

As we have noted above, LBOs are frequently underwritten. This is to provide certainty as to financing in a constrained timeline. Therefore our illustrative LBO example incorporates underwriting. Based on those lenders willing to provide a gauge, such underwriting fees can vary from 150–175 basis points (i.e. 1.50-1.75 per cent on the underwritten amount), but this range will increase to 175-200 bps where there are cross-border dimensions or other complications. Underwriting fees would vary conditional upon the role taken, e.g. an active bookrunner would likely get more of the total underwriting fees than a passive one. The apportionment of such fees is obviously a key element within the negotiations between the borrower/sponsor and the banks pre-mandate.

Table 19: Transaction costs in underwritten LBO

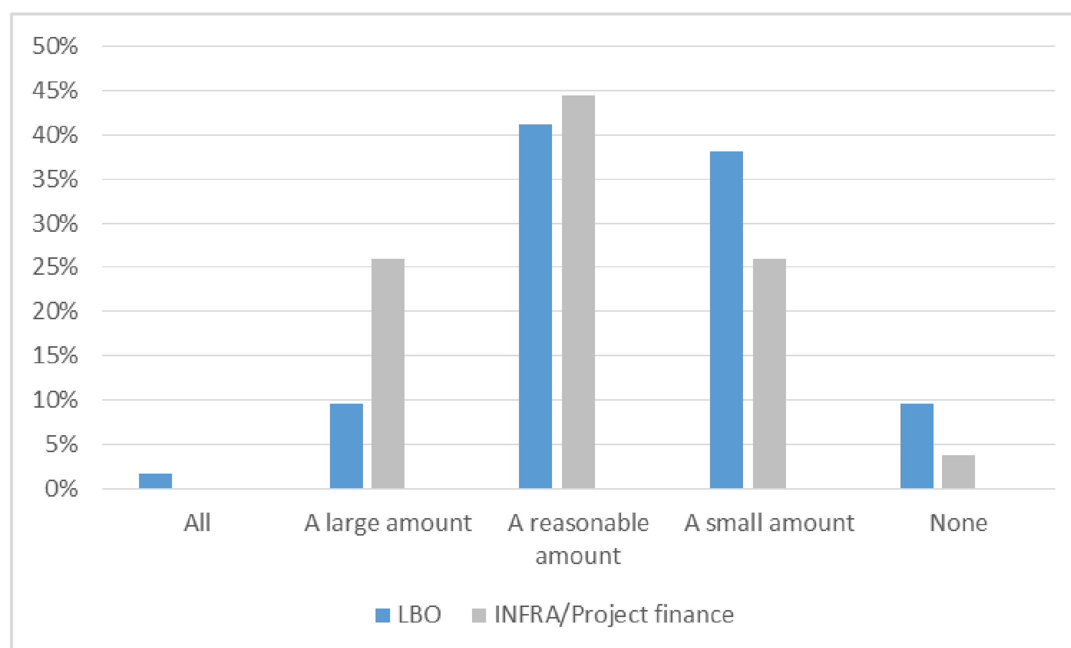
			€m	€m
Loan value			500	500
	bps			
Underwriting fees	175	200	8.75	10
Participation fees	50	100	2.5	5
Total one-off fees			11.25	15

Participation fees can also be payable upfront. Participation fees are more generally known in the market as the OID (Original Issue Discount). These can vary depending on ticket size, typically ranging from 0.25-1.00 per cent flat (although the data are limited in scope, the Loan Connector data on participation fees are in line with this, with a median around 100 bps, and the average of those OIDs reported being 99.0).[136] These would be paid directly to the participants by the borrower (i.e. the issuer). In the event of Reverse Flex, the OIDs can be reduced or eliminated such that the borrower retains the full benefit of the reverse flex (at least in larger ticket sizes). In smaller transactions, underwriters may be able to retain some fraction of the benefit.

The one-off fees payable to MLAs generally incorporate an element of contingency (i.e. where the full amount is payable only upon meeting set conditions for success) in order to provide additional incentive for MLA performance (and potentially to provide a degree of protection should the transaction bot complete for any reason). An element of contingency obviously provides economic justification for higher fees than otherwise (provided there is some risk of the success conditions not being met).

[136] For the avoidance of any doubt, this symmetry is of course not a coincidence. The participation fees and OID are either both reported or neither is, with the participation fee being the difference between par value and the stated OID price.

Figure 34: Share of contingent elements within fees payable to MLAs



Source: YouGov borrower and sponsor survey, N=90.

Agency fees are paid annually to the Facility Agent. These vary dependent on the complexity of the deal, the number of drawdowns anticipated, expected secondary market trading volume, etc. The range in an LBO could be €50,000–€200,000. The lender fieldwork characterised this activity as (a) generally functionally separate from origination/ syndication activity, and (b) being essentially administrative in nature.

Table 20: Annual costs in an LBO

			€m	€m
Facility agent fees (annual cost)			0.05	0.2
Cash management (annual cost, 3-5 year contract)			0.05	0.075
			0.1	0.275

Cash management is generally provided independently from the syndicated loan. The charging structure will vary according to local practice, with some variation of an annual fee supplemented by transaction volume fees if transactions exceed a defined amount.

On an ongoing basis, there could also an annual facility or commitment fee on undrawn facilities (e.g. if a capex facility of up to €100m was in place, but undrawn). These are not included in the table above. Such fees compensate lenders (along with the margin) for providing capital (even when not drawn down). The loan documentation can also contain cancellation fees (although this is not common — other than on sub-ordinated tranches – such as mezzanine debt - as one of the advantages of a syndicated loan relative to a bond is the absence of significant early repayment fees). Loan Connector's data on both commitment and cancellation fees is limited in scope, but about 100 bps appear typical.

The lender fieldwork indicated that the LBO market has moved away from contractual hedging requirements. The CFO of the LBO issuer may of course still decide to hedge

part of their exposure anyway, but this would be subject to a discrete competitive process. There may be independent derivatives boutiques or a financing team within the sponsors which can create an organised auction to establish the terms and to ensure that the price is correctly set.

Fees in PF/INFRA

Since these are a club deal, no underwriting fees would be payable. However, there could be a role for advisers to the borrower/sponsor (this would also apply in the case of an LBO, but we have omitted these from the above for simplicity and because our fieldwork indicates that private equity sponsors are more likely to have in-house expertise to fulfil at least some functions that could otherwise be delegated to an adviser). This could be about £0.5-£1m on a transaction such as this. (There would also be legal costs to cover, but these are not shown).

Participation fees – where payable - are at similar levels to those in an LBO, at around 1 per cent, payable on the full allocation made, but could be lower (0.8 per cent) in less complex transactions (i.e. with fewer tranches, or lacking cross-border complications).

Table 21: Transaction costs in club PF/INFRA

			€m	€m
Loan value			500	500
	bps			
Participation fees	80	100	4	5
Advisory fees			0.75	1
Total one-off fees			4.75	6

We understand that agency fees would tend to be in the €100,000–€250,000 range here. There are a diminishing number of banks interested in undertaking this role in PF/INFRA due to the tenor of the transactions (i.e. up to 20 years) and the complexity of the role (e.g. due to a growing number of conditions precedent that have to be complied with). There are third party providers who can undertake this role.

Cash management is generally provided independently from the financing / syndication activity. The charging structure will vary according to local practice, but likely with some variation of an annual fee supplemented by transaction volume fees if transactions exceed a defined amount. The estimate below draws on the lender fieldwork.

Table 22: Annual costs in PF/INFRA

			€m	€m
Facility agent fees (annual cost)			0.05	0.2
Cash management (annual cost, 3-5 year contract)			0.05	0.075
Total annual fees			0.1	0.275

Again, commitment fees could also be payable, as with LBOs.

In PF/INFRA deals there is likely to be a requirement for contractual hedging of some defined part of the exposure. Given the complexity of the transactions the natural providers will be the arranging banks who understand the security package and

project risks best. However the project finance sponsors can create bidding pressure from a group of potential derivatives providers or run auctions through independent derivative boutiques.

Our lender fieldwork indicated that banks' interest in writing very long-dated swaps as these can be constrained because these are an inefficient use of regulatory capital. Instead:

- Combining cap and floor interest rate derivatives into a self-funding collar. For example, this was the standard practice in the Spanish project finance loans subject to the recent CNMC review (please see summary at Appendix 5f).
- Alternatively, the debt structure may introduce a fixed rate component to achieve the same overall goal as hedging (i.e. to reduce the scale of exposure to floating interest rates). This could mean substitution by tranches of mini bonds or fixed rate private placements distributed to institutional investors for bridge loans introduced as part of the syndication.

One further aspect of the fees picture, which relates equally to both LBOs and PF/INFRA, is that the borrower pays for the banks' lawyers. This has resulted in sponsors and borrowers choosing the lawyers used. This feature may mean that institutional investors push back harder on documentation than the banks, potentially resulting in some degree of document flex. We discuss this feature further, in our discussion of flex at Chapter 4.

Covenants

As we have identified in the previous chapter, access to a covenant package is a traditional differentiator between syndicated lending and corporate bonds (excluding, to a degree, high-yield bonds). Whilst access to such a strong covenant package remains the norm in the PF/INFRA segments, such protections have been watered down in the LBO segment over the past few years. 'Covenant-lite' (Cov-lite) loans are a particular kind of syndicated loan facility, which lack some of the traditional protective covenants (or erode the headroom around a covenant) and place fewer restrictions on the borrower's future behaviour (e.g. around taking on new debt, paying dividends). There are also 'cov-loose' loans that are essentially an intermediate grouping.

Indeed, such borrower-friendly "cov-lite" loans have become increasingly common in European LBO debt markets. In 2014 10 per cent of European LBO loans were cov-lite but that had increased to 70 per cent in 2017. Such cov-lite loans are increasingly common as deal size increases.[137] It is worth noting that the high-yield bond market (which is also accessed by private equity sponsors to fund transactions) – and, indeed, may be originated out of the same leveraged finance teams within lenders – have also seen deterioration in covenant quality, albeit from a more cov-lite starting point.[138] This may also partly represent a structural shift due to convergence in investors' minds between syndicated debt and high-yield bonds.[139]

The US market has a longer history of cov-lite loans. The incidence of such cov-lite loans has represented 70–80 per cent of leveraged loans in the USA since 2014, i.e. the European market has converged with the USA.[140]

[137] See for example, https://www.debtexplained.com/explore/insights/covenant-erosion-continues/
[138] For example, "Tensions over junk bond covenants start to boil over", Financial Times, 14 February 2018.
[139] For example, "CLO demand weakens lender protections", Financial Times, 18 June 2018.
[140] See Moody's analysis of loan covenant quality (USA only).

Secondary market for syndicated loans

In Chapter 2 we provided a brief description of the process of trading syndicated loans on the secondary market. We now discuss secondary trading for syndicated loans in more detail, covering the market as a whole including a factual description of the market and its evolution, the rationale for its existence, the types of trades, the types of players active in the market, and the types of loans more likely to be traded. We also draw out distinctions between LBO and P/INFRA loans.

Secondary market overview

Once a syndicated loan has been closed in the primary market, it can be traded in the secondary market, subject to any restrictions included in the primary documentation (e.g. borrower permission may be required). These loans, as with other private financial instruments, are traded solely on an over-the-counter (OTC) basis or via bilateral negotiation.

Initially, i.e. up to the mid-90s, loans in Europe were traded predominantly among a small number of US investment banks, specialist debt traders and so-called 'vulture funds'.[141] However, subsequently a wider range of players has entered the market, including most notably other banks, hedge funds, mutual funds and other funds such as CDOs (Collateralized Debt Obligations) and CLOs. Other institutional investors that have also started (albeit to a lesser extent) trading loans on the secondary market are pension funds and insurance companies.[142] The increased heterogeneity in the types of market players active in the secondary market also reflects an increased heterogeneity in the market players in the primary market.

Evolution of the market

There was a clear and rapid growth in the secondary loan market from the early 1990s up to the global financial crisis. In the USA, for example, the volume of loans traded increased from $8 billion (approx. €6.5 billion) in 1991 to $176 billion (approx. €142 billion) in 2005,[143] which is equivalent to an annual compound growth rate of around 25 per cent in that period. Similarly, data for the EMEA region show a sharp increase in trading volumes from €32 billion in 2002 to €157 billion in 2007.[144] Both the EMEA and US markets their experienced their sharpest growth (by quite some way) between 2005 and 2007.

Trading volumes fell back sharply however following the financial crisis. In the EMEA region, trading volumes more than halved from 2007 (at €157 billion) to 2008 (at €73 billion) and have remained at a lower level than pre-crisis since. The volume traded in 2016 (€54 billion) is still less than that traded back in 2005 (€61 billion), as shown in Figure 35 below. The US saw more moderate declines (in percentage terms) following the global financial crisis and has witnessed significant growth since 2012, with 2016 trading volumes more than three times their 2005 level.[145] As such, the US market has pulled further ahead of the EMEA market in more recent years. Indeed – looking

[141] LMA (2016) "Guide to secondary loan market transactions". A 'vulture fund' is a hedge fund or private equity fund that invests in distressed securities (debt considered to be very weak or in default).

[142] Gupta et al. (2008) "Liquidity in the pricing of syndicated loans", *Journal of Financial Markets* 11 (2008) 339-376.

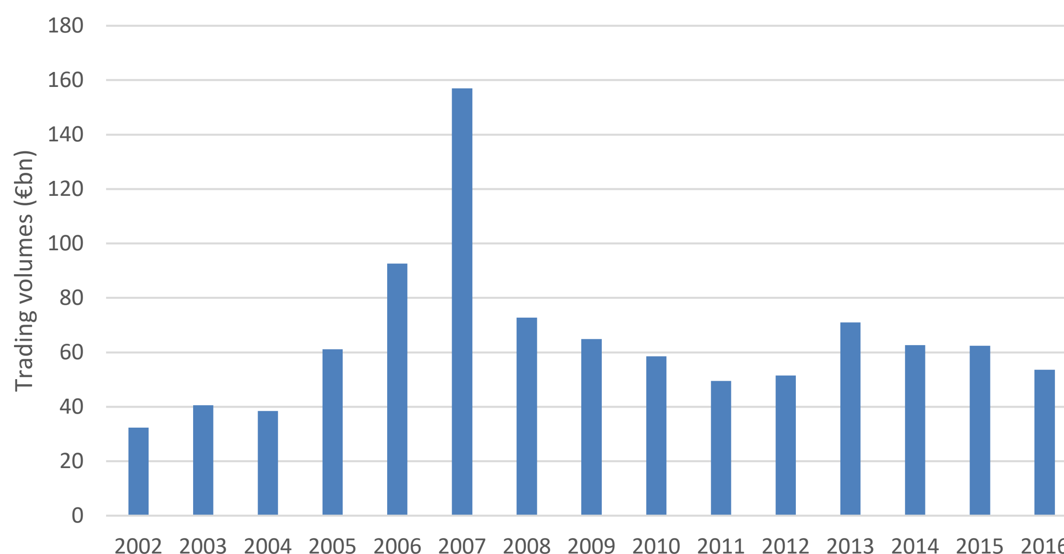
[143] Santos & Nigro (2009) "Is the secondary loan market valuable to borrowers?" *The Quarterly Review of Economics and Finance* 49 (2009) 1410-1428.

[144] All EMEA and Member State data referred to in this section is taken from Thomson Reuters Loan Connector data tool, in particular its Market Monitor and Deal Scan Search tools. The Deal Scan Search application allows one to search, by a number of different criteria, the syndicated loan market, including data on the borrower, lender, deal, tranche, credit rating, secondary pricing if relevant, spreads and fees etc. Market Monitor provides aggregate data, e.g. on trading volumes, for the syndicated loan market.

[145] International Comparative Legal Guides (2017) "Loan Syndication and Trading: An Overview of the Syndicated Loan Market".

across all loan types — secondary market trading in the USA is approximately 3–4 times greater relative to issuance volumes than it is in EMEA.[146] A return to the level of secondary trading in EMEA last seen in 2007 would match what is seen in the USA, all else being equal. In our fieldwork, those banks with transatlantic operations characterised the US market as being broader, with less focus on LBO debt than still is the case in Europe. This may mean that the difference in the level of trading may be less in the LBO segment than in the syndicated loan market as a whole.

Figure 35: Annual secondary trading volumes in €billion for EMEA (all loan types)



Source: Thomson Reuters Loan Connector. Analysis by segment not available.

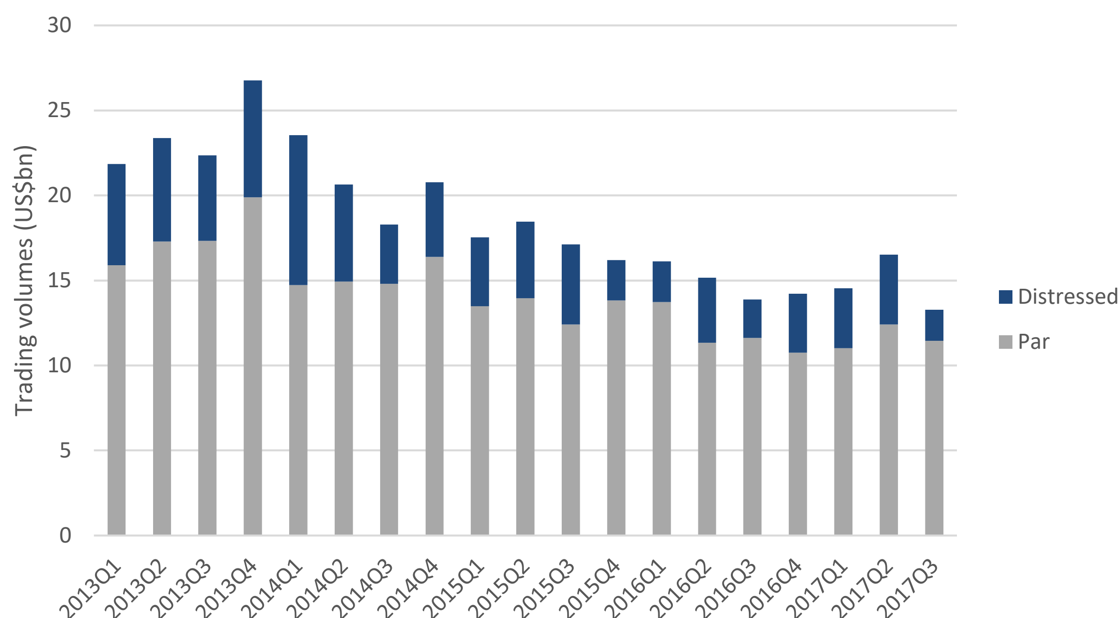
Trading in the secondary loan market can be both in "par" loans and in distressed debt. This is a long-standing trend in the USA can be seen in Gupta et al. (2008).[147]

The EMEA data show that the share of distressed loans to par loans in Europe was just under 14 per cent of secondary market trades in the most recent quarter (Q4 2017). (This has declined from close to 25 per cent in 2013-14, which is unsurprising given the broad recovery in the EU economy). In the same time period, in the larger and more liquid US market, distressed loans have only constituted around 4 per cent of secondary market trades (the economic recovery in the USA has longer roots than that in the EU as a whole).

Distressed debt is inherently higher risk, but also has potentially higher rewards for investors in it. An increase in non-bank investor appetite for participation in non-distressed (i.e. par) debt in the EU would of course see some convergence towards the US position. A more active secondary market could, in turn, allow increased recycling of capital to the primary market. However, particularly in PF/INFRA, the investors at the primary stage (whether take and hold banks or institutional investors seeking long-term assets) are long-term ones, i.e. there may be a dearth of ready sellers.

[146] Thomson Reuters only provide aggregated secondary trading data on EMEA, not the EU.
[147] For US evidence see Gupta et al. (2008) "Liquidity in the pricing of syndicated loans", *Journal of Financial Markets* 11 (2008) 339-376.

Figure 36: Secondary market trading volumes by par and distressed loans, across all loan types in EMEA



Source: Thomson Reuters Loan Connector.

Trading of LBO versus PF/INFRA loans

Based on data from our sample of Member States (DE, ES, FR, NL, PL and UK) for the period 2010 to 2017, just over 10 per cent of primary syndicated loan issuance has secondary market trading data. Loan Connector (specifically iQuery) concentrates on the more liquid loans, providing daily (non-executable) pricing in these – in other words, there will be a greater proportion of loans that may see some secondary market activity. This set of more liquid (less illiquid) is dominated by LBO loans – of the total 241 tranches listed in iQuery, 224 were LBOs. This means that any benefits due to secondary trading (discussed later in this chapter) would be experienced differentially in these market segments.

Table 23: Number of tranches with secondary market data by purpose of loan, across 6 Member State sample

Loan type	Number with secondary market data	% of primary market
LBO	224	10.3%
PF	6	0.3%
INFR	11	0.5%
Total	**241**	**11.1%**

Source: Europe Economics (using Thomson Reuters Loan Connector).

There is less variation in the extent of trading data across the different Member States, being more common in Germany, the Netherlands and the UK.

Table 24: Number of LBO tranches traded in secondary market by Member State

Member State	Number of LBO tranches traded in secondary market	% of LBO primary market
DE	52	12.4%
ES	16	7.4%
FR	49	8.2%
NL	36	14.6%
PL	2	5.7%
UK	69	10.4%

Source: Europe Economics (using Thomson Reuters Loan Connector).

The data also show that those tranches with secondary market data are typically larger, on average (at €316 million), than those without (€111 million).

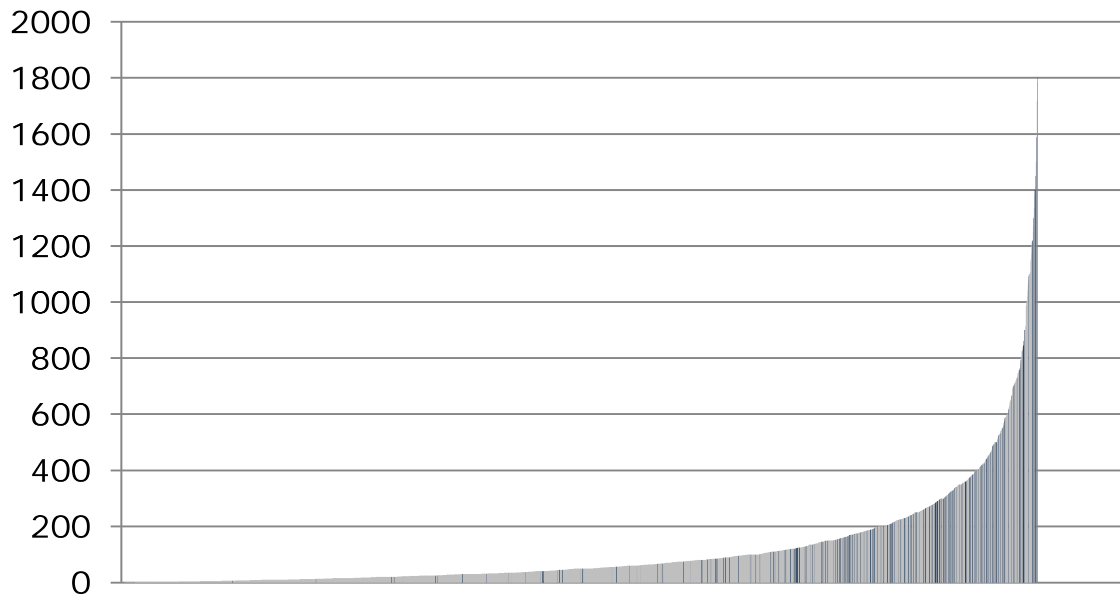
Table 25: Average value of tranches with secondary market trading data

	Secondary market data		No secondary market data	
	Average value (€ million)	Number of tranches	Average value (€ million)	Number of tranches
LBO	300.71	217	100.60	1,901
PF	669.52	6	124.48	508
INFR	426.92	11	119.71	1,425
All sample	**316.10**	**234**	**110.87**	**3,834**

Source: Europe Economics (using Thomson Reuters Loan Connector).

The obvious inference is that markets are much more likely to be made in larger loans, i.e. deals valued at €250 million or more. Indeed, this is further corroborated by the chart below, which depicts the full spectrum of deals, from the lowest value deals on the left hand side to the highest value deals on the right hand side. Deals with secondary market data are denoted in blue, while those without are denoted in grey. The chart demonstrates that high value deals are more likely to have secondary markets than low value deals — though the cut-off is do occur even in relatively small tranches.

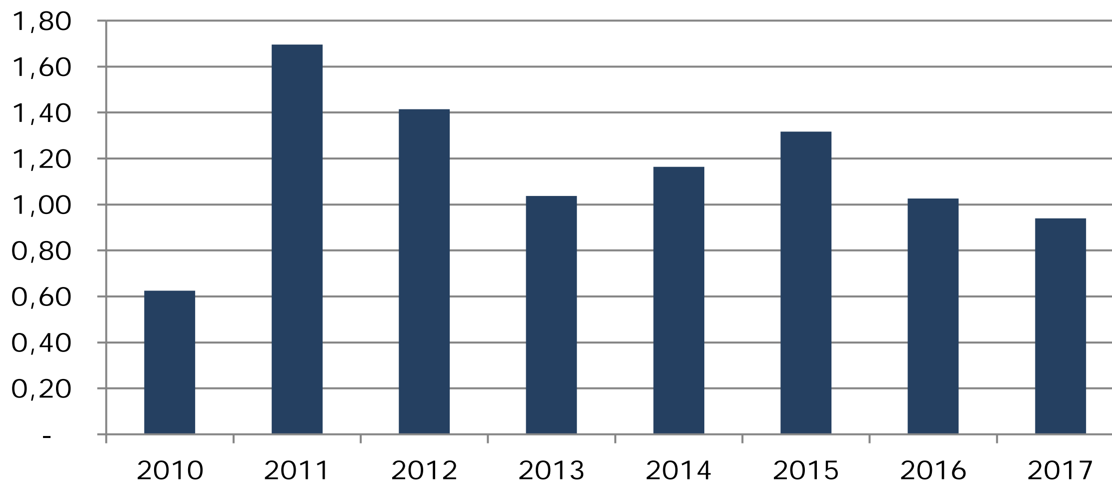
Figure 37: Spectrum of deal values and whether secondary market is made or not



Source: Europe Economics (using Thomson Reuters Loan Connector).

The average bid-ask spread, across all loan types and member states in our sample, is shown in the figure below. It shows bid-ask spreads rose sharply in 2011, but have generally been in decline since. There does not appear to be a clear correlation between average bid-ask spreads and the trading volumes shown below.

Figure 38: Bid-ask spreads



Source: Europe Economics (using Thomson Reuters Loan Connector iQuery).

Given these spreads, it is not surprising that the majority of secondary market activity is in more speculative grade loan tranches – the low margin on AAA investment grade loans would make trading economically unattractive since the trading spread is 25-50 basis points. Indeed, all of the LBO tranches listed on iQuery are speculative (normally BBB) grade.[148]

[148] Non-investment (speculative) grade defined as Ba1 or lower on Moody's scale, and BB+ and lower on S&P scale.

Participants in secondary market trading

The main motivation for banks to participate in trading loans is to more actively manage loan portfolios, whether for regulatory reasons (i.e. managing risk-weighted assets) or to reduce/diversify risks (e.g. to free up additional capacity to lend more to a client or sector).[149] The banks originating loans are not exclusively sellers (obviously they are selling more than they buy) - in the lender fieldwork it was noted that banks might buy debt in order to signal intent to the borrower, i.e. trying to build a commercial relationship, which should be pro-competitive in the absence of a past relationship. The (net) buyers are institutional investors and funds managing their money (e.g. CLOs), although of course these can and do further 'churn' loans to other investors or banks as the value proposition evolves. We do not see a specific competition issue arising from this market feature, beyond the point about post-close coordination by the MLAs described above.

The larger investment banks will also have more active secondary trading desks, i.e. buying and selling loans. Lenders indicated that the scale of such operations had not recovered to pre-crisis levels, with a large desk having a portfolio of perhaps €200–250 million at any one time.[150] As we have noted in Chapter 3, this contributes towards lower market volumes (one measure of liquidity). The academic consensus is that the benefits of trading transparency (whether pre- or post-trade), i.e. where a market is 'lit', are heavily influenced by the liquidity of the instrument being traded – with there being a significant risk that lit trading will significantly disturb trading in less liquid markets (such as even the syndicated LBO loans market), and so would likely be counter-productive from the perspective of increasing efficiency.

Economic benefits of trading on the secondary market

There are various economic benefits to lenders in trading syndicated loans on the secondary market. In very general terms, the seller (lender) could sell the loan to crystallise a gain and raise capital; to diversify and manage its exposure to risk; to satisfy regulatory capital requirements; or to crystallise a loss. Being able to sell loans on the secondary market also reduces financial frictions for lenders, and can increase balance sheet liquidity.[151]

Our lender fieldwork confirms the rationale behind engagement in the secondary loan market, namely to make room on their balance sheet, or to sell positions in markets they are no longer active in. They also engage in the secondary market to buy loans from (new) borrowers they wish to signal an interest to. Some lenders (banks and non-banks) may also engage more actively in secondary trading (i.e. making markets in more liquid loans, holding a trading portfolio), but this is largely restricted to investment banks and the largest universal banks (and not all those).

Some non-bank investors – such as CLO managers – may be more active in the secondary market than the primary phase, looking to buy and sell on a value basis. In an effort to cater to the demands of CLOs, deals (particularly LBOs) can be structured in a way to aid "primary assignments", which are pre-arranged loan purchases on the origination date and at the primary market price, but which are otherwise similar to

[149] If the sale is executed through its own trading desk, there will also be a trading commissions. However, in our lender fieldwork, the lenders made clear that the secondary trading desks were separate to the origination and syndication teams, i.e. to the extent that the latter should be treated in the same way as a third party.

[150] The banks adopt a mix of strategies for such trading desks. These could be sited within or wholly separate to the syndicated lending unit, and could be set up to operate either on private or public information (if functionally separate, the latter is more likely).

[151] See Gupta et al. (2008) "Liquidity in the pricing of syndicated loans", *Journal of Financial Markets* 11 (2008) 339-376 and referenced papers by Stein (1998), Kashyyap and Stein (2000), Holmstrom and Tirole (2000), Diamond and Rajan (2006)

secondary market transactions.[152] Mark-to-market discipline for institutional investors (e.g. as a result of Solvency II) means that funds often need to sell quickly when there is a downgrade.

The buyer, on the other hand, may view the secondary loan trade as a way to establish a relationship with a specific borrower or to achieve exposure to certain sectors or countries where their market position would not allow them to participate in primary loan origination; to make a profit; or to obtain rights over a proportion of the borrower's asset in case the latter defaults.[153]

Another demand-side factor which could drive growth in the secondary loan market (and the demand for speculative loans in particular) is that syndicated loans are senior, typically secured instruments. All of this implies – everything else being equal – higher recovery rates given default than a bond. Moreover, the fact that syndicated loans are generally floating instruments implies less risk regarding future inflation or interest rates, which could be particularly important for long-duration investments. Finally, the returns on these loans can be fairly uncorrelated with equity returns – Gupta et al. (2008) reports that in the period 1992-2002 the correlation of returns between loans and the S&P 500 was 0.12.[154] This can make them an attractive investment for investors, for whom the high yields they could achieve on distressed loans justify the cost associated with a relatively complex trading process and other limitations of trading in a private market. On the other hand, investors who are seeking to de-risk, and thus who would be more willing to buy investment-grade loans rather than distressed loans, might find the trading costs outweigh the returns (at least in the current interest rate environment).

On the other hand, one challenge in secondary trading is that loans are private – the documentation around the loan contains commercially sensitive information about the borrower and thus is subject to strict confidentiality agreements. An implication of this is that only the sellers have access to all the relevant information. Since other market participants (i.e. those not party to the syndicate) may not be privy to all the relevant information, even after the due diligence conducted pre-trade, it has been argued that an announcement of a loan sale on the secondary market would be perceived as a negative signal of the likelihood of the borrower defaulting on payment.[155] More recently, studies have shown that the first secondary market trade transaction of a loan has a *positive* stock price effect.[156] This does not necessarily mean that the disadvantages of secondary loan trading have disappeared, but that the benefits have been recognised more widely and could (in certain circumstances or in certain aspects) outweigh the costs.

There is agreement in the literature – albeit based on US market data - that the secondary market "unambiguously lowers borrowing costs". Kamstra et al. estimate at 16 basis points for leveraged loans. This observed benefit is the net effect of two countervailing effects. The reduced liquidity risk to lenders from access to the secondary market is a gain that, in a competitive market, should flow back to borrowers.

[152] Benmelech, Efraim & Dlugosz, Jennifer & Ivashina, Victoria (2009) "What lies beneath: An inside look at corporate CLOs collateral".
[153] See LMA (2016) "Guide to secondary loan market transactions", and Gupta et al. (2008), "Liquidity in the pricing of syndicated loans", *Journal of Financial Markets* 11 (2008) 339-376.
[154] Gupta et al. (2008) "Liquidity in the pricing of syndicated loans", *Journal of Financial Markets* 11 (2008) 339-376.
[155] Gande, A. and Saunders, A. (2012) "Are Banks Still Special when there is a Secondary Market for Loans?" Journal of Finance 67, 1649–1684.
[156] See Gupta et al. (2008) "Liquidity in the pricing of syndicated loans", *Journal of Financial Markets* 11 (2008) 339-376.

However, there are also potential risks associated with MLAs accessing the secondary market (e.g. in the originate-to-distribute model). Some academics have argued that an MLA selling a loan in the secondary market undermines the ex post monitoring role of MLAs. One of the key roles of lenders is to monitor the borrowers with whom they enter into agreements to ensure that the likelihood of loan repayment does not deteriorate. The argument is that an accessible secondary market could lower lenders' incentives to thoroughly screen and monitor borrowers as they would be able to sell any loans in case of increasing risk of default.[157] However MLAs do not have a contractual role to other lenders in the syndicate post-closure. Equally, the role of a facility agent does not encompass monitoring credit quality other than in an administrative way, i.e. passing information onto the syndicate in general. In other words, it is the responsibility of the individual owners of the syndicated loan to monitor credit quality (although some may choose to rely on credit ratings, where available, or professional asset managers, i.e. those managing CLOs or managed accounts). As such, we find this argument unconvincing, and we have noted already that the institutional investors buying loans are sophisticated (indeed, since it is a 'buyer beware' market, this is imperative). The importance of reputation in the syndicated loans market also appears to play a role here in limiting any misbehaviour by MLAs – for example, Gopalan et al. (2009) have shown that low quality screening by a lead arranger adversely affect its subsequent lending activity, consistent with a loss of reputation.

Bushman et al. (2009) found no difference in credit performance between traded and untraded loans involving reputable (experienced) MLAs – but did find some evidence of worse performance by traded loans originated from less reputable MLAs.[158] Equally, Santos and Nigro (2009) examine the difference between the borrowing costs to a borrower on an initial loan and the cost of the loans originated after that first loan was sold in the secondary market. The analysis shows that borrowers holding more liquid loans are able to borrow at lower interest rates afterwards. This is interpreted as evidence that the benefits associated with the higher liquidity outweigh the risks associated with reducing the incentives lenders have for monitoring the borrower. Gupta et al. (2008) find that loans which are expected to be more actively traded in the secondary market have – everything else being equal – lower spreads than loans expected to be more illiquid. His estimates varied from an 88-128 basis points impact compared to otherwise equivalent loans.[159] Kamstra et al. (2014) argues that the benefits achieved by the borrower are stronger for leveraged loans (i.e. such as in the LBO segment) than for investment grade loans, for which the existence of the secondary market drives the cost of borrowing up rather than down. This implies the reduced liquidity risk should be priced into the loan in the primary market – assuming that the market is sufficiently competitive for these gains to be passed on in the form of lower prices.

We undertook an analysis to test this finding in the EU market. The question we addressed is whether being traded on the secondary market has an impact on the pricing of the primary loan. (This analysis assumes that it is known at the time the

[157] Gupta et al. (2008), "Liquidity in the pricing of syndicated loans" *Journal of Financial Markets* 11 (2008) 339-376.

[158] Bushman, R and Wittenberg-Moerman, R (2009) "Does secondary loan market trading destroy lenders' incentives?"

[159] The approach taken in Kamstra et al. (2014) is different – contrary to the approach in Gupta et al. (2008), it seeks to distinguish between liquidity and the probability of being resold. The former is proxied by the resale constraints – the stronger than constraints the lower the liquidity. The probability of being resold, on the other hand, is interpreted as a proxy for the incentives lenders have to monitor the borrowers. As such, the theoretical prediction would be that as those incentives decline (i.e. as the probability of resale increases) spreads are increasing.

primary loan's price is being finalised that there would subsequently be a secondary market in it (and, unless there are contractual restrictions, this is a reasonable expectation for at least larger LBO loans).

We used Thomson Reuters Loan Connector data to compare the primary pricing of loans traded on the secondary market with the primary pricing of similar loans that have not been traded on the secondary market. In undertaking this analysis we controlled for certain loan characteristics. Ideally, this would have included controlling for the credit ratings of the tranches. However, only a small proportion of tranches have credit ratings in the Loan Connector dataset (mostly BB or BBB, i.e. the typical credit quality to the characterisation of most non-distressed LBO debt). This has therefore limited the use of credit rating as a control variable.

Given the data limitations, we were able to investigate the following control variables: type of loan (e.g. Term B loans in LBO deals); country; and benchmark (Euribor v Libor).[160] We analysed the pricing data on a quarter-by-quarter basis – again, a more granular analysis (e.g. month-by-month) is not possible given the limited amount of data. The lack of data availability stems from the less liquid secondary market in the EU compared to the USA, with the EU market experiencing a more difficult recovery post-crisis than the USA one.

Based on the empirical literature, we would expect to see lower pricing at issuance on the traded loan sample. However, our analysis does not find any significant evidence of differences between the primary pricing of those tranches with market makers and those without.

Conceptually, it can also be seen that at the time of pricing a loan, its likelihood of being traded would only be imperfectly known. Our analysis in Chapter 2 suggested that larger loans were more likely to be traded, and would also access lower spreads. For comparison, then, we also analysed issuance pricing on tranches in deals above and below a deal size of €400m. This makes the difference much more marked – however, attribution between the size of the loan and access to secondary trading is not possible given the high correlation between the two, and, in particular, the small datasets available to us here. In both cases, we have limited the comparison to the 2013 to 2016 period as prior to 2013, the data are increasingly scarce to make meaningful comparisons even on this simplistic basis. The results are shown below.

[160] Controlling for borrower characteristics beyond the details of the loan (such as size and ratings) is also not feasible as these data are not incorporated into Loan Connector. Academic papers that have included these controls have always used external databases.

Table 26: Comparison of average spread for tranches with market makers and those without (Euribor-benchmark, Term B, LBO)

Date	Count of market made tranches (with pricing data)	Count of non-market made tranches (with pricing data)	Average spread for market made tranches	Average spread for non-market made tranches	Which is greater?
Q1-2013	1	10	400	613	Non-MM
Q2-2013	1	3	400	475	Non-MM
Q3-2013	2	13	375	454	Non-MM
Q4-2013	3	3	413	458	Non-MM
Q1-2014	2	2	463	425	MM
Q2-2014	2	6	438	413	MM
Q3-2014	8	13	331	417	Non-MM
Q4-2014	3	2	483	550	Non-MM
Q1-2015	5	1	498	425	MM
Q2-2015	6	2	433	513	Non-MM
Q3-2015	8	7	434	457	Non-MM
Q4-2015	7	5	439	390	MM
Q1-2016	8	6	491	475	MM
Q2-2016	9	6	494	463	MM
Q3-2016	6	2	504	475	MM
Q4-2016	1	1	425	425	Non-MM
Q1-2017	6	0	396		
Q2-2017	8	2	369	363	MM
Q3-2017	10	0	393		
Q4-2017	5	3	475	350	MM
Total	**101**	**87**	**433**	**460**	

Note. ST denotes secondary traded tranches; Non-ST denotes non-secondary traded tranches.

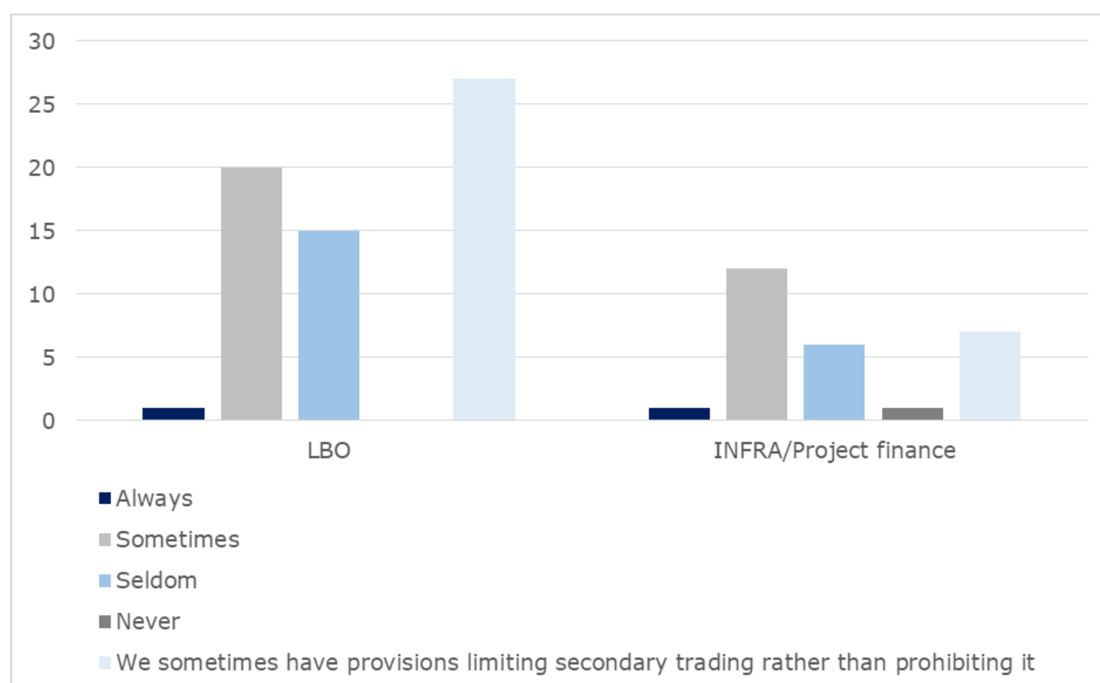
Table 27: Comparison of average margin for tranches on deals above and below €400m (Euribor-benchmark, Term B, LBO)

Date	Count of deals >=€400m (with pricing data)	Count of deals <€400m (with pricing data)	Average spreads for >=€400m	Average spreads for <€400m	Which is greater?
Q1-2013	5	6	460	704	Below 400
Q2-2013	3	1	442	500	Below 400
Q3-2013	8	7	409	482	Below 400
Q4-2013	3	3	417	454	Below 400
Q1-2014	3	1	450	425	Over 400
Q2-2014	6	2	413	438	Below 400
Q3-2014	19	2	379	438	Below 400
Q4-2014	2	3	500	517	Below 400
Q1-2015	2	4	425	516	Below 400
Q2-2015	4	4	431	475	Below 400
Q3-2015	7	8	429	459	Below 400
Q4-2015	5	7	370	454	Below 400
Q1-2016	11	3	475	517	Below 400
Q2-2016	9	6	478	488	Below 400
Q3-2016	3	5	483	505	Below 400
Q4-2016	1	1	425	425	Below 400
Q1-2017	3	3	400	392	Over 400
Q2-2017	7	3	364	375	Below 400
Q3-2017	5	5	380	405	Below 400
Q4-2017	4	4	444	413	Over 400
Total	**110**	**78**	**422**	**479**	

Restrictions on trading

It is evident from the fieldwork with sponsors and borrowers that restrictions can be imposed on secondary trading. These can involve prohibitions, but can also involve restraints on who the loan can be sold to (the default LMA clause references consent not to be unreasonably withheld by the borrower but the use of this is not, of course, mandatory). The evidence from the fieldwork suggests that the adoption of such clauses are at least regularly considered by sponsors and borrowers.

Figure 39: Use by borrowers/sponsors of clauses prohibiting or restricting secondary trading activity in LBO and PF/INFRA segments



Source: YouGov survey of sponsors/borrowers, N= 90. Respondents provided the response that best fitted their current practice.

The motivations cited by borrowers and sponsors for putting in place some form of restriction can be ranked by frequency:

- The most frequently cited response (two-thirds of those putting some restriction in place) was that a sale of their debt could imply a more burdensome re-negotiation process in case of default, as more (new) parties would need to agree to any change in the loan agreement (this would depend on the structure of the secondary market transaction).
- The second most common reason was that it could complicate loan payment procedures (cited by about half).
- Also referenced by about half were concerns about the leakage of confidential information outside of already known parties. The concern here is not necessarily (or even particularly) limited to the loan itself, but rather about the overall transaction (i.e. the INFRA project or LBO itself).
- Fourth (referenced by about one-third) was that there were some lenders that the borrower did not wish to borrow from, e.g. such as distressed debt funds, or debt funds owned by rival private equity houses.[161]

[161] Our fieldwork shows that the majority of borrowers and sponsors have contract provisions either preventing or limiting secondary trading. Interestingly, sponsors are more likely to have provisions

As a result, a borrower may place restrictions on the ability of a syndicate to enter into secondary transactions. Where secondary trading is permitted, any such transfer restrictions put in place by borrowers/sponsors would be a potential source of inefficiency in the secondary market. These constraints could include restrictions on transfer to those investors not on the 'white lists' used in any general syndication (the inefficiency being that the borrower's consent would be required before a secondary trade could be settled).

For an MLA, particularly one focused on an originate-to-distribute strategy, (or any member of the original syndicate) such restrictions are generally unattractive. That they are in place in transactions implies that borrowers/sponsors are considering the trade-off between the negative consequences outlined above (i.e. complicating any potential default, etc.) against any saving on the price of the loan. Those borrowers/sponsors using RFP-style processes (i.e. 93 per cent in the YouGov fieldwork) could make this an explicit feature of that process. Those mandating an MLA directly would find this more challenging. The use of white lists can be contrasted with the USA where such transfer restrictions are less common, and where shorter 'black lists' are used instead (i.e. stating which institutions could not be sold to, but otherwise with the presumption that the sale to anyone else is acceptable).

Although the default LMA clauses state that consent is 'not to be reasonably withheld', this process can delay the settlement process and is seen as inefficient by a number of market participants. We discuss this further in the sub-section on back office inefficiencies towards the end of this chapter.

Impact of secondary market activity on information transparency in the primary market

As we have noted already, the secondary market for syndicated loans exists predominantly for LBO loans, with the secondary market for PF/INFRA loans being virtually non-existent in terms of Thomson Reuters iQuery data. In general, PF/INFRA transactions are club deals where the lenders indicated in our fieldwork that they expected to hold the majority of loan shares. The difficulties in pricing PF/INFRA loans on the secondary market also contributes to lower activity, i.e. the need for investors to be familiar with the project and associated risks. Potential secondary market investors may need to sign an NDA to receive information that will enable them to quote a price. Lenders indicated to us that these loans are typically more likely to be traded once the project is out of the construction phase and into the operational phase.

Market participants can access a range of publicly available data on secondary trade pricing, for example from Thomson Reuters, Bloomberg and others. Licence costs can be €10–€30,000 per annum per seat. However, the low liquidity in the EU market means that such data are widespread.

It is not simply lenders that can access such data: so can borrowers, sponsors and debt advisors. However, whilst information transparency afforded by the secondary market may increase the ability of borrowers/sponsors to assess competitive pricing levels in the primary market and so enhance competitive dynamics, they do not rely solely on such data (and, indeed, would not be able to in PF/INFRA loans).

The transparency of the market in terms of who the competitors are and what terms the competitors are ultimately proposing and receiving for the loans, could be an important factor in determining the scope for anti-competitive behaviour. Loans are

preventing such trading than borrowers. Q32S and Q30B: "Do the loan agreements include any provisions preventing secondary trading of the loan?"

private contracts and unlike bond issues, pricing features can be kept confidential. Yet the unique characteristics of the syndicated loan market, especially where there is a secondary market for leveraged loans (even if that remains relatively illiquid), render it more transparent than the bilateral loan market. Data vendors such as Thomson Reuters Loan Connector publish data on syndicated loan deals with the goal to aid investors in both primary and secondary markets (where one exists in a particular loan). In addition, a significant portion of the infrastructure market consists of public-private partnerships and public procurement is likely to rely on transparent funding, again facilitating loan pricing data availability. Such additional transparency allows market players to compare pricing and loan structure. This would also allow borrowers and sponsors to better understand the market and to uncover what a competitive pricing should look like. This could exert pressure on an MLA to keep the pricing in line with market standards.

Secondary market activity and pricing in the primary market

Were the loan market to be competitive some of these benefits should be reflected in a lower loan spread at the time of origination, at least where secondary trading of the loan was anticipated or was reasonably expected. One hypothesis here is that if lenders misprice a primary loan (due, potentially, to a lack of competition), we would expect the loan to be traded above par in the secondary market. On the other hand, the absence of significant price discounting (i.e. selling below par) at initial sale indicates that the market does not interpret the act of selling a loan as evidence of enhanced moral hazard or adverse selection problems.[162]

We have investigated the secondary loan pricing just after launch (specifically at 1, 2, 3 and 6 months after launch) to see whether there is any peak in pricing. The analysis is based on data from Thomson Reuters Loan Connector tool, specifically the iQuery database. The iQuery database provides daily average ask and bid data for loan tranches that are traded in the secondary market. We have undertaken our analysis using the mid-price between bid and ask prices.

We find no evidence of loans being systematically traded above par in the secondary market for which we have data. Table 28 below shows the proportion of loans being traded above and below par, the median mid-price and lower (Q1) and upper (Q3) quartile mid-price. The data do not show a systematically higher proportion of trades being above par (as can be seen by comparing Columns 2 and 3). It can also be seen that the median trade price is very close to par.

The upper and lower quartile data shown in Table 28, along with the frequency distribution of secondary loan pricing presented in Figure 40, show that the pricing of secondary loans is concentrated around the median (which itself is close to par). This is captured by a positive kurtosis value for the distribution, which indicates that the data are more concentrated around the mean than in a normal distribution (i.e. the tails of the distribution are ‘light’). The data also indicate a slight negative skew, indicating a longer tail of pricing below the median price than above.

Table 28: Statistics on pricing of secondary loans

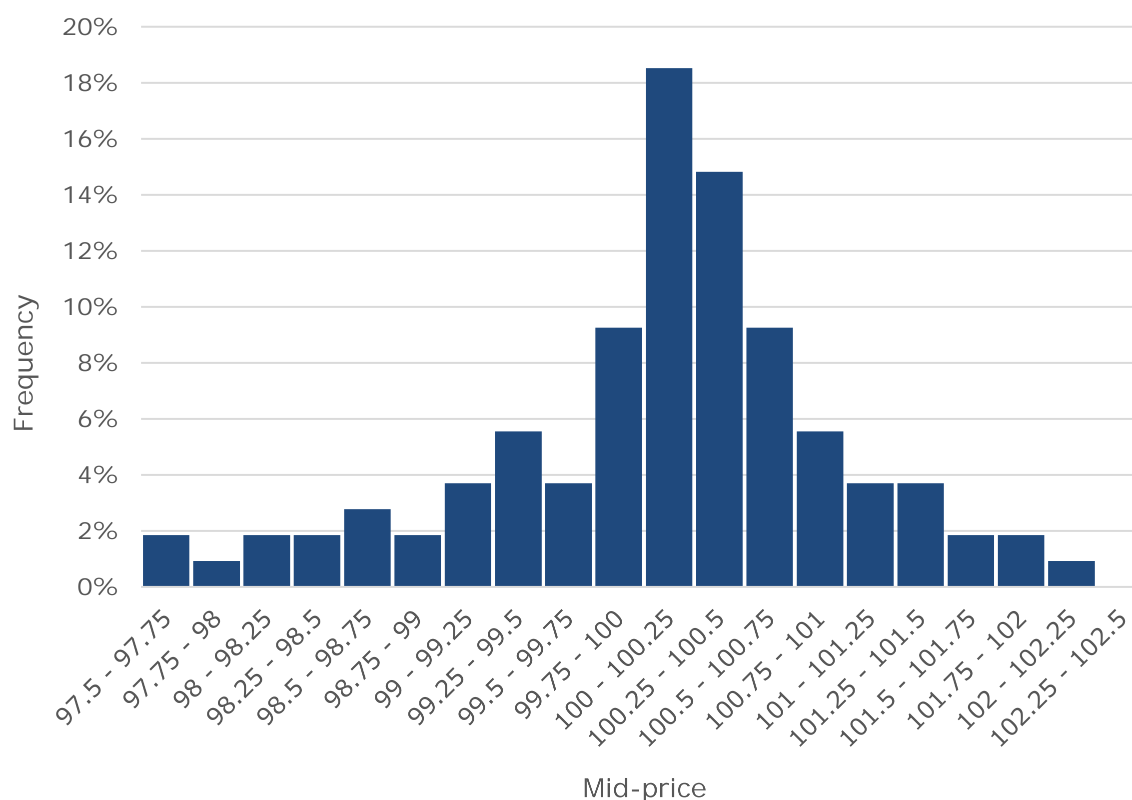
Mid-price after…	Proportion of trades below par	Proportion of trades above par	Median	Q1	Q3
1 month	0.41	0.55	100.08	99.25	100.5
2 months	0.48	0.47	100	99.13	100.5

[162] Bushman, R and Wittenberg-Moerman, R (2009) “Does secondary loan market trading destroy lenders’ incentives?”

3 months	0.44	0.53	100.06	99	100.54
6 months	0.5	0.48	99.98	99	100.44

Source: Europe Economics analysis of Loan Connector data.

Figure 40: Distribution of secondary loan pricing one month after deal date



Source: Europe Economics analysis of Loan Connector data.

NB. We only present data for the range of mid-prices 97.5 to 102.5. A small number of data points lie outside this range.

Overall, we find no evidence of loans being systematically traded above par in the secondary market for the tranches for which there are data (i.e. the more actively traded loans). Instead, the pricing in these loans on the secondary market appears to be strongly concentrated around par.

More broadly, we do not have evidence to indicate that trading in the secondary market in Europe is inefficient (we do discuss the presence of back office inefficiencies below). However, the scale of the secondary market remains significantly below that in the USA (by a factor 3–4 across all types). Whilst institutional investors have become more active in the primary market, secondary market activity remains relatively muted and has certainly not recovered to pre-crisis levels. The US secondary market has been shown to have beneficial impacts on the US primary market. Whilst we note that the data are limited, such beneficial impacts are less clearly apparent in Europe.

Back office inefficiencies in the primary and secondary markets

An issue cited repeatedly in the fieldwork was the slowness of back office processes. This could increase transaction costs, resulting in sub-optimal economic outcomes.

Whilst this is a source of inefficiency, the impact on the market should not be overdone — i.e. it has not prevented the development of institutional investor appetite for syndicated loan assets. The inefficiencies identified to us are:

'Know your client' (KYC) requirements which banks need to adhere to participate in loans with other counterparties, which involve banks collecting a range of documentation from all loan participants. Depending on the size of the syndicate this can be very onerous for lead banks, particularly where debt funds are involved (a participating debt fund manager might manage many different funds such that across the whole loan ultimately investors could – in extremis - number in the hundreds, with the banks having to process KYC requirements for all investors).

Equally, lengthy KYC requirements can add to long settlement windows (although other factors contribute here e.g. borrower/sponsor approval for some loan transfers and the manual nature of many settlement systems). For example, settlement can take up to 20 days, or even longer. Long settlement windows can be a risk factor, for example they potentially could lead to gaming if views on the credit evolve significantly during the window. They also hold up the start secondary market trading by delaying transfers and thus increase transaction costs.

A central repository for all KYC documentation may help here, whereby each investor only needs to upload its documentation once for all banks to access. A key barrier here is the differences across countries and banks regarding the implementation of KYC requirements[163] which impede the sharing of a common set of KYC documents, and which would require significant industry and potentially regulatory initiative to overcome.

Another issue raised (not directly related to KYC) was the transparency around the settlement process. Funds can get queued between the investors and the agent banks, meaning that if the agent bank has little visibility of where the funds are and when they are likely to arrive, its treasury may need to make up the difference in order to provide the client with the funds on time if money from investors has not yet arrived.

Market participants pointed to the greater settlement efficiency of the US market as a sign that current inefficiency is largely market-driven rather than technological (although direct comparisons are difficult given the larger size and liquidity of the US market, and the fact of its single jurisdiction).

Secondary market settlement is also considered inefficient – d borrower/sponsor restrictions on loan transfers (e.g. requiring that consent is sought) slow down the process and can also introduce settlement risk (i.e. where a lender might be unsure if a counterparty will be approved). A borrowers/sponsors are not directly involved in the secondary market they have limited incentive to explore ways of reducing this friction. The manual settlement systems and the process of KYC also contribute to settlement time.

In summary, back office inefficiencies in the primary and secondary loan markets – driven by KYC requirements, loan transfer restrictions and a more general lack of sophistication in the systems used – increase transaction costs and can even create settlement risk. Whilst these inefficiencies (in particular those relating to KYC requirements) are exacerbated in syndicated loans involving multiple institutional

[163] The implementation of these requirements can be different and even small differences can be a barrier to a shared system. An example given in our fieldwork was the need for 'wet' as opposed to electronic signatures in some countries.

investors, they are not sufficient to deter banks' involving these investors in loans – indeed, the benefits of the liquidity provided by a strong pool of investors (i.e. enabling a lead bank to successfully syndicate a loan) far outweigh the associated costs. Nevertheless, overcoming these inefficiencies would contribute to a better functioning primary and secondary market. Given the current lack of consistency across the industry in terms of KYC processes it is possible that a more coordinated approach at the EU-level will be required to address these inefficiencies. We discuss this in more detail in Chapter 4.

Conclusions

We have been tasked with researching two segments within the syndicated lending space, i.e. LBOs and PF/INFRA. We end this chapter by bringing together our analysis of competition dynamics in these segments.

Nature of LBO and PF/INFRA segments

Both LBOs and PF/INFRA projects have significant needs for debt financing. The main substitutes for syndicated lending are bilateral loans, corporate bonds and private debt placement. Borrowers and sponsors considered such alternative funding options to generally be readily available, albeit with differing attributes (e.g. floating rate loans versus fixed rate bonds). These are all forms of debt finance but they are not perfect substitutes for each other. This means that a borrower/sponsor can still differentiate between these different products, and have meaningful preferences between them. The dynamic between borrowers/sponsors on one hand and the lenders on the other would determine how much borrowers/sponsors would need to pay to secure their preferred form of funding.

Another aspect of this is that the main substitutes for syndicated lending - bilateral loans, corporate bonds and private debt placement – can all involve a critical role for the same banks. We discussed earlier in this chapter how the involvement of non-bank actors and the adoption of competitive processes (i.e. in the RFP setting, all economic terms – including fees and loan pricing – would be subject to that process) should add market discipline. There are no current signs of upward pricing pressure in the segments of the syndicated loan market of interest to this study. Indeed, the margin on debt has generally been falling over the past few years and our fieldwork indicated that overall loan costs (including fees) are under pressure from borrowers and, especially, sponsors. These trends may be a function of recent/current strong investor appetite for – in particular – LBO debt.

Our analysis of the market shares of individual lenders does not identify any of the markets as being very highly concentrated, with the HHI for each of the national markets in both the LBO and PF/INFRA segments confirming this. This finding is particularly strong in the LBO space. In the PF/INFRA segment the HHI scores were higher but only in Poland (where the HHI score is just below 1000). It is worth noting that the PF/INFRA segment is more heterogeneous than the LBO one, in that there are credit risks (say related to a particular type of infrastructure construction, such as specific forms of renewable energy) where knowledge could be less well distributed than the HHI-based analysis might suggest.

There is also segmentation between lenders by deal size. Taking LBOs as an example, amongst the most active lenders (there are 34 lenders averaging at least one LBO per month), about one-third was most prominent in the €1+ billion deal size band, i.e. they were primarily focused on larger transactions with this group overlapping significantly (but not perfectly) with G-SIBs – but other were active across all size bands relatively evenly. Again, some of this latter group are G-SIBs. These are lenders particularly focused on the volume, or flow, of deals. There are four banks that are

consistently in the league tables for all (or nearly all) countries for both the LBO and PF/INFRA segments. Three of these are based in France.

On the other hand, there is evidence of "home bias" in that the top ranked lenders tend to be lenders with a parent in that country. This is not experienced evenly, being more prominent in PF/INFRA than in LBOs. We consider it unlikely that this "home bias" is a signal of competition being undermined by restricting the pool of potential MLAs, at least in the west European markets covered by this study, where non-local banks can be readily accessed. In Poland, on the other hand, the low deal frequency and use of a non-mainstream currency (relative to the £ and €), may make the pool of potential MLAs relatively small. This appears to be more of a concern in the PF/INFRA segment. Obviously, there is a difference between approaching a bank and appointing one. However, the clear capacity of sponsors and borrowers to approach non-local banks (since otherwise these could not be appointed) should provide some element of market discipline.

Evidence of competition among lenders

We described in Chapter 2 how a very high proportion (93 per cent) of borrowers and sponsors have adopted RFP-style process. The selection of such a competitive form of process should enable the achievement of competitive outcomes in those cases by giving the banks the incentive to reveal their best prices.

The other main rider here would be whether sufficient banks were invited to participate in the competition (i.e. the *ability* of the borrower, the transaction's sponsor and their advisers (if any), to identify banks with the appropriate skills and capacity to provide the relevant services, and to adequately judge the offers received, and also the *availability* of such banks).

Availability of banks/ MLAs

The availability of MLAs is a key consideration in assessing the possibility of MLAs having excess bargaining power over borrowers/sponsors, i.e. where the pool of available MLAs is restricted, borrowers/sponsors may have less choice and competition may operate less effectively. Our research shows that borrowers and sponsors are generally considered to have sufficient sophistication either to assess and negotiate the price and terms of the loan in-house or else to appoint advisers to assist them in that. In terms of the availability of lenders, the number of lenders participating in both LBO and PF/INFRA segments is large. However, far from all of these would have the wherewithal to compete effectively for any given MLA mandate. We have described in Chapter 3 how in the LBO segment there are at least 12–15 credible MLAs in the west European markets of interest here but that in Poland, there are fewer, with estimates of the number being as low as 6–8. PF/INFRA is somewhat different, at least in terms of the composition of players. On the other hand, to the extent that it is fairly characterised as a club market, provision of balance sheet is more important than demonstrating distribution expertise meaning that banks (e.g. Japanese ones) that have very limited presence in the LBO segment are highly active as MLAs in PF/INFRA. Altogether we consider that the number of capable MLAs is at least as large as in the LBO space. However, a point emphasised in the lender fieldwork is that the PF/INFRA segment is more heterogeneous, with the result that in at least some parts of it the choice of MLA (e.g. toll roads) could be more restricted. As with LBOs, the Polish market generally has less choice.

Although the study has been focused on six Member States, we are able to make some tentative observations about the LBO and PF/INFRA segments outside of these countries. There is some degree of differentiation between western Europe and the rest of the EU, with the former likelier to have more lenders. This may mean that Poland is a good proxy for at least other non-west European countries.

Another aspect of the availability of lenders is the capacity of lenders to transition from participation to acting as MLAs. Reputation of the lead bank is regarded as an important mechanism in the literature,[164] and more generally previous interactions with the sponsor/borrower, involvement in successful syndications and the demonstrable willingness to underwrite or lend significant tickets also matter in terms of MLA appointment. This may mean entry into the 'MLA market' is more difficult for lesser known institutions.

Some aspects of reputation are institutional (i.e. associated with the lender itself), whilst others are individual (i.e. the skills and expertise to make an effective cash flow-based lending assessment, or to gauge market appetite well). Therefore, the three main barriers to entry to an institution acting as an MLA in the syndicated loan market relate to having the right people with the relevant skills, the reputation to deliver on providing loan finance, and access to the necessary information. Lenders with recent experience of building market position did not consider the ability to hire expert individuals represented an insurmountable entry barrier. We are not in a position to comment on how individuals in the market could lead such a transformation (clearly, this is a different proposition to 'simply' being able to execute a syndication effectively). Deal flow is widely (but not exclusively) viewed by lenders as an important factor contributing to banks' development of their offers, e.g. building and sustaining relationships with sponsors, assessing appropriate price levels and other terms. This, combined with the importance of past experience and reputation, as well as high existing liquidity, could also imply that new entrants would face a slow take-up. MLAs considered the availability of other sources of information (such as publicly available deal data from a mix of databases) to be much improved from the position pre-crisis and generally to be sufficient to assess comparable transactions adequately. On the other hand, since the syndicated lending space remains a private market, there are various critical elements of information that do not always get released (specifically – and most critically – pricing information, at least based upon the availability of this in Loan Connector).

Market features that could facilitate collusion

It is also the case that any collusion by lenders ahead of submitting bids in an RFP process would obviously invalidate the anticipated competitive outcomes. Collusion arises from dynamic interactions amongst the competitor firms. In the case at hand, repeated interactions between the banks competing to be the MLA, would be an important factor in maintaining any potential collusion. Coordination is easier, the smaller the number of parties involved, in particular when coordination is only based on a tacit common understanding of the market.[165] For example, identifying a "focal point", in terms of loan margins, underwriter and arranger fees charged and market shares, would be easier in a market consisting of a few symmetrical market players. For each firm the long-term benefit of maintaining collusion is reduced, precisely because it gets a smaller share of the collusive profit.

We have described earlier in Chapter 3 how sponsors/borrowers seek to control the debt origination/syndication process, but also note certain areas where the control would be reduced. Some of these could facilitate collusive outcomes, in particular:

- The use of market soundings by MLAs. This would be particularly problematic where the sounding crossed the boundary between generic sounding and deal specific-sounding and where the sounding was with an MLA (or even an entity connected to an MLA). The main safeguard here is that lenders emphasised that internal policies

[164] See for example Dennis and Mullineaux, 2000, and Sufi, 2007.
[165] Arnaboldi, Francesca and Casu, Barbara (2011) "Corporate Governance in European Banking" Working Paper.

meant that any deal-specific soundings would require client consent, and that this would need to be demonstrable to compliance teams. In its strongest form, such consent should be specific as to who is contacted.

- The provision of ancillary services where this provision is restricted to the syndicate, or some sub-set of it, e.g. an obligation – or strong expectation – that purchase would be from the MLAs, especially if not all MLAs were able or willing to provide or quote for that service.
- When general syndication takes place (e.g. in an underwritten deal), since it is the bookrunners that deal directly with the potential participating lenders there is scope for this to underpin tacit reciprocity in the market. We note, however, that there are several safeguards that can help to counter any such attempts (i.e. borrower/sponsor-driven white lists, direct feedback loops between investors and sponsors, regular feedback from the bookrunners and approval by borrowers/sponsors of final syndicate member allocations).
- The borrowers/sponsors will also have curtailed bargaining power where a borrower is in financial difficulties and faces default. The options available to a borrower may be very limited in such an instance.

We also note that, if the same lenders are repeated on multiple transactions with a sponsor/borrower if the pool of lenders is small (e.g. in some parts of PF/INFRA), this might enable lenders to converge their terms and prices over time even without explicit cooperation.

Overall, then, there are particular market features that have greater cause for prima facie concern. We also consider those markets (specifically Poland amongst the countries we have considered) with fewer potential MLAs should be monitored most closely. This could also apply to other countries within the EU where borrowing is not in the £ or € and to smaller markets more generally (particularly those less well connected to the main locus of the syndication market in Europe, i.e. the City in London).

Involvement of state actors

Based on our research, public sector actors are not involved in the LBO segment (we are excluding those lending banks temporarily under national government ownership or control as a result of remedial action taken post-financial crisis).

The PF/INFRA side is different. Role in PF/INFRA could be as borrowers /sponsors (e.g. in the context of a public-private partnership, or PPP) and also potentially as lenders. The proportion of PF/INFRA borrowers within the Loan Connector dataset is, however, rather low — at just 2 per cent of the total. Such public sector sponsors are not discretely identifiable.

PPP debt, with its reduced risk (e.g. due to stable, even potentially guaranteed income) and longer maturities, was seen by several participants in our fieldwork as making it more attractive to institutional investors. In this sense, public actors (acting as sponsors) can be seen as contributing towards encouraging such investors to respond positively to a partial gap in the market created by the withdrawal of some banks from longer-term PF/INFRA financing. There are also public sector lenders in the PF/INFRA space. The main motivation for such involvement would be to resolve a market failure, i.e. providing capital to (narrowly) sub-marginal borrowers (i.e. those borrowers that could not afford debt priced according to their risk). We note that, especially in current market conditions, there is a risk that such actors will displace lending that could have come from commercial lenders.

Secondary market

The European secondary loan market is notably smaller than that in the USA. The USA's secondary market has been shown to have beneficial impacts on the US primary market. Whilst we do not have evidence to indicate that trading in the European secondary market is inefficient and, whilst noting that the data are very limited, such beneficial impacts on the primary market are less clearly apparent in Europe.

Back office inefficiencies

Back office inefficiencies in the primary and secondary loan markets – driven by KYC requirements, loan transfer restrictions and a more general lack of sophistication in the systems used – increase transaction costs and can even (in extremis) create settlement risk. Whilst these inefficiencies are exacerbated in syndicated loans involving multiple institutional investors (e.g. a debt fund manager investing through multiple debt funds, each of which would require KYC checks), they are not sufficient to deter banks' involving these investors in loans – indeed, the benefits of the liquidity provided by a strong pool of investors (i.e. enabling a lead bank to successfully syndicate a loan) far outweigh the associated costs. Nevertheless, overcoming these inefficiencies would contribute to a better functioning primary and secondary market. Given the current lack of consistency across the industry in terms of KYC processes it is possible that a more coordinated approach at the EU-level will be required to address these inefficiencies.

Further issues to be covered in analysis of competition at Chapter 4

We now turn to those features of loan syndication that may pose competitive risks (either in terms of breaches in competition law or else those market features that could result in inefficient outcomes). The purpose of these conclusions is to highlight issues to be examined more detail in Chapter 4, building on those already identified in the conclusions to the preceding chapter, where our hypotheses of risks are more fully developed within our competition framework and then tested against the empirical evidence. It follows then that the summary points below should therefore not be considered as our developed competition risk hypotheses, but rather an iteration of the points to be addressed further in Chapter 4. The table below summaries the features of the syndication loan process that may pose risks for competition law or sub-optimal outcomes. We indicate where issues are the same across LBO and PF/INFRA loans, and where they are similar but more pronounced in a certain loan type.

Table 29: Summary of issues to be examined in Competition Framework – LBO and PF/INFRA loan markets

Element of process	Feature to be examined under Competition analysis	Applicability to LBO or PF/INFRA loans
Formation of initial banking group		
Appointment of advisers	The borrower/sponsor has to assess its own capacity (i.e. knowledge and resources) to act independently in the process, or whether it needs to engage advisers for part or all of the process. Where there is a lack of separation between the advisers and the potential MLAs, there is clearly scope for conflicts of interest that, without adequate management, could result in sub-optimal outcomes.	Advisors located within banks that also act as MLAs is more a feature of the PF/INFRA space than the LBO segment.
Appointment of lead banking group	Frequency with which borrowers / sponsors engage in the market might have an impact on their ability to influence the syndicate process, in particular their experience in appointing MLAs, and their ability to use future appointments as a means of incentivising MLAs to perform well.	The main drivers of repeat interactions are the sponsors, particularly present in LBOs. By implication, there is greater scope for sponsors/ borrowers who are not highly sophisticated in PF/INFRA segment.
Appointment of lead banking group	Appointing the lead banks directly without a competitive (e.g. RFP) process may influence the outcome of the syndication process if these banks propose terms that are uncompetitive.	Similar issues across LBO and PF/INFRA.
Appointing a single MLA to lead the syndication process	The appointment of a single MLA to lead the formation of the initial banking group (which we describe in the Chapter as a more 'traditional' model of syndication not common to the west Europe markets, but potentially more relevant to other, more national markets) may invest too much power with a single bank and affect intra-syndicate dynamics. This model may also increase the risk of information sharing between banks as the borrower/sponsor is not negotiating bilaterally with each one.	More applicable to PF/INFRA loans, although cannot rule out with LBO.
Availability of (independent) price information to market participants	Whilst MLAs and other market participants have a variety of sources of information on the prices of comparable loans from data vendors, those MLAs with a greater flow of transactions may have access to more (and/or better quality) data, providing an informational advantage.	Public pricing information is available in both segments, but the relatively low levels of secondary trading activity in PF/INFRA coupled with the apparent greater diversity in PF/INFRA may increase the risks in that segment. The availability of price information in public databases may limit (or make more costly) the process of assessing the market rate for a given credit risk – creating a barrier to entry for lenders seeking to build a mandate as an MLA

Element of process	Feature to be examined under Competition analysis	Applicability to LBO or PF/INFRA loans
General syndication		
Information exchange between MLAs and others	Information asymmetries between the MLAs and the potential investors in the loan (and reduced visibility on process for sponsors). Misaligned incentives could result in sub-optimal outcomes for borrower (i.e. affecting the terms of the loan).	Applicable to both segments, but given greater use of underwriting in LBO, and more developed secondary market there, any potential risk is greater there.
Non-bank investors	Potential vertical integration between sponsors, banks and non-bank investors participating in syndicated loans, and its potential to impact competitive pricing of loans.	Non-bank investors are more present in LBO segment.
Flex	The borrower pays all costs, including for the banks' lawyers. This has resulted in sponsors and borrowers choosing the lawyers used. This feature may limit negotiating power of banks in terms of finalising documentation, and also potentially resulting in some degree of document flex. This could mean that loan documentation standards are weaker than optimal.	Applies to both segments, albeit scope for document flex is limited to underwritten transactions.
Provision of ancillary services		
Provision of ancillary services directly related to the loan	MLAs can seek to make the award of connected services, such as hedging, one of the conditions attached to the provision of the loan. Potential risks around the provision of hedging services include the discussion among banks in order to share out the services between them and/or coordination on pricing, and uncompetitive bundling of the services with the initial loan terms which restricts the choice of borrower/sponsors. This would be highest risk should only some sub-set of MLAs have the capability of delivering the service (this could facilitate tacit collusion between these MLAs). Ancillary services directly related to a loan include hedging services and agency services (e.g. acting as facility agent).	There is slightly greater use of such ancillary services in the PF/INFRA segment.
Provision of ancillary services not directly related to the loan	MLAs can seek to make the award of future services one of the conditions attached to the provision of the loan. Such future services can range from leading any bond issuance undertaken to replace a bridging loan, to providing future M&A or IPO advisory services.	Bridging finance is likely equally applicable. There may be greater scope for services such as M&A or IPO advisory in the LBO segment.
Post closure		

Element of process	Feature to be examined under Competition analysis	Applicability to LBO or PF/INFRA loans
Secondary trading	Restrictions on transfers may limit liquidity in the secondary market, resulting in sub-optimal economic outcomes. The slowness of settlement processes could increase transaction costs, with equivalent consequences.	Secondary activity is greater in the LBO segment than in PF/INFRA.
Refinancing and restructuring	Restructuring in situations of distress may confer a degree of bargaining power on the syndicate, since the borrower may lack options. This would not be any more the case than with a bilateral loan.	Similar issues across LBO and PF/INFRA.

4. Analysis of Competition Issues

Introduction

This chapter sets out our analysis of the economic and competition dynamics of the syndicated loan market. The aim of this analysis is to identify features of the loan syndication process and wider market dynamics that pose risks in terms of competition law in particular, and to the competitive functioning of the market more broadly.

The starting point for this analysis is the development of a **theoretical framework** for how competition law might be contravened and how sub-optimal market outcomes might arise in the loan syndication market. This framework describes the key risks at each stage of the syndication process along with potential safeguards that could be put in place to mitigate these risks. Given the absence of direct case law relating to the syndicated loan market, this framework draws on "first principles" of competition law.

Once these have been identified we consider the extent to which such concerns may become more or less significant across different types of syndication and under different market dynamics. In this framework we consider a broader interpretation of competition concerns – such as competitive dynamics and relationships – than simply potential infringements of competition law.

The competition analysis framework, including the risks and safeguards, is then tested using the evidence presented in Chapters 2 and 3 on the background to the market, as well as further evidence gathered from the lender and borrower/sponsor fieldwork.

We note that the analysis of competition law issues in relation to Articles 101 and 102 is based on our own judgement, and that the European Commission has not taken a position on what is falling within/outside the scope of these Articles as regards syndicated lending.

The chapter structure first sets out an **overview framework** for the legal and competition analysis, describing the basis for the legal assessment of the compatibility of syndicated loans with Articles 101 and 102, and setting out other considerations for assessing competition. The purpose of this overview is to identify the types of competition concerns that the general nature of the loan syndication process itself may create, and to establish broad criteria along which to evaluate these concerns; this overview does not contain specific references to the evidence, which is brought out in the sections relating to each specific stage of the loan process.

It then focuses in more detail on **each main stage** of the syndicated loan process, considering the extent to which the general concerns set out in the overview may become more or less significant across different stages of the syndication process and under different market dynamics. This picks up and assesses in more detail the features highlighted in Chapters 2 and 3 as being potential risks (see Table 10 and Table 29). For each stage, the chapter sets out:

- The specific framework for legal and broader economic analysis for that stage, including the main risks and potential safeguards.
- The evidence describing the likelihood and magnitude of the identified risks, and for how/whether the suggested safeguards are implemented in practice.

Where there is sufficient difference between the syndication processes between LBO and PF/INFRA loans, we draw out separately the evidence associated with the risks and safeguards.

Overview framework for legal and competition analysis

Multi-bank lending, including the provision of syndicated loans, by its nature involves a group of banks (and other lenders) who are otherwise actual or potential competitors coming together on commonly agreed terms for the purposes of providing joint funding to a borrower for a particular transaction. Syndicated lending necessarily involves co-operation between the lenders and agreement between the lenders and the borrower on elements such as the required amount of capacity, a single price, a unified term sheet and the allocation of the proportion of the loan between the various lenders. Furthermore, to facilitate this co-operation, the competing lenders may need to exchange certain information for the purposes of arranging the financing for the borrower. What exchange is legitimate and necessary will depend on the stage of the transaction and the way in which the process has been designed by the borrower/its advisors – we discuss this where relevant in the stage-by-stage description below.

There are a number of potential competition concerns that this may give rise to which we consider in this framework. We begin this framework by examining the compatibility of syndicated loans with Article 101 and Article 102 of the Treaty on the Functioning of the European Union (TFEU) (drawing on the Horizontal Guidelines of Article 101 and 102[166]).

Compatibility with Article 101

Article 101 (1) TFEU prohibits agreements and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition. Article 101(3) provides for an exemption from the application of Article 101(1) if the pro-competitive benefits (in terms of improvements in production, distribution, technical or economic progress) of the agreement or concerted practice outweigh the restrictive effects provided that (i) those benefits are shared with consumers (ii) the restrictions do not go beyond what it indispensable to achieve the pro-competitive benefits (they are indispensable) and (iii) does not result in the possible elimination of competition.

Agreements or concerted practices which are anti-competitive by <u>object</u> are those that are considered by their very nature to have the potential to restrict competition without having to examine whether there is an actual restrictive effect on competition (see paragraph 24 of the Guidelines on the applicability of Article 101 TFEU to horizontal co-operation agreements) (the "Horizontal Guidelines").

Whilst there are various categories of agreements and practices that have been considered anti-competitive by object, each agreement must be examined in its context, in terms of the objectives it seeks to attain, and the legal and economic context in which it operates (See para 25 of the Horizontal Guidelines).

Some of the key aspects that are common to syndicated lending, such as in some cases an agreement between lenders to jointly provide a service at a single price, are arrangements which, in other contexts, have been examined as potential restrictions of competition by object. However, given the context of syndicated lending, to the extent that any potentially restrictive agreement or practice is inherent to the provision of the syndicated lending (as opposed to being extraneous to but facilitated by the syndicated loan process) then an effects-based analysis of such agreements or practices is likely to be much more appropriate. Such restrictions are also sometimes considered to fall outside Article 101 (1) altogether on the basis that they are directly

[166] European Commission (2011) "Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements" (2011/C 11/01). We draw mainly on the general information sharing guidelines, and also on the Agreements for Commercialisation guidelines.

related to and necessary for the proper functioning of the provision of the financing pursuant to the loan syndication agreement.

It is also relevant to the overall context and to any determination as to whether an agreement or practice which is part of the provision of syndicated lending has an anti-competitive object or effect, to recall that lenders are generally co-operating in line with the instructions or clear mandate of a borrower to discuss the loan and share information and in a borrower's interests to secure funding. Such instruction from the borrower/sponsor, the transparency and/or consent demonstrates a lack of anti-competitive purpose and the absence of anti-competitive intent, which whilst not determinative as to whether an agreement is anti-competitive by object, is a highly relevant factor in the assessment.

This is to be contrasted with potentially restrictive agreements or concerted practices that either might be *facilitated* by the syndicated lending process or which may occur in the context of the provision of a syndicated lending, but which fall outside the borrowers' instructions or mandate or which are otherwise not inherent to or otherwise a necessary element of the syndicated lending. Such "spillover" practices, depending on their nature, may well be anti-competitive by object (we develop these in more detail in the subsequent stage-specific sections of this chapter).

In considering whether the provision of any particular syndicated loan or the process by which the syndicate is formed has the effect of restricting competition, a key consideration is whether the lenders could have competed individually. As set out in the Horizontal Guidelines (paragraph 30) "co-operation between competitors that, on the basis of objective factors, would not be able to independently carry out the project or activity covered by the co-operation….will normally not give rise to restrictive effects on competition within the meaning of Article 101(1)."

In the case of syndicated lending it is not the case that prospective lenders cannot compete at all – they can and do compete for various different roles. Further, the borrower sets a process for the formation of the initial lending group that will typically ensure competitive tension is maintained. Rather, in syndicated lending, whilst different banks will compete for different roles, ultimately no one bank could provide the required capacity on its own and thus the provision of a multi-bank loan with a unified price on unified terms, based on the selection of banks through a process mandated by a borrower is unlikely to have an anti-competitive effect, in so far as the lenders have not engaged in potentially restrictive practices which are extraneous to that process.

If nonetheless, in any situation it is concluded that the provision of the syndicated loan has the effect of restricting or distorting competition, then such restrictive effects may be compatible with the Treaty in so far as the lenders can establish that the conditions of Article 101(3) are satisfied.

Elements that are inherent to the loan process set up by the borrower, such as the setting of a single price, single term sheet etc. in line with the instructions and mandate of the borrower are thus either outside Article 101(1) or, which is more likely, may benefit from Article 101(3).

Compatibility with Article 102

Article 102 prohibits the abuse of a dominant position. Such a dominant position can be enjoyed and abused by one or a group of undertakings (so called "collective dominance"). Dominance is defined as *¨[A] position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on*

the relevant market by giving it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers" [United Brands v Commission].

In order to establish a collective dominant position, the economic entities must be: *"united by such economic links that, by virtue of that fact, together they hold a dominant position vis-à-vis the other operators on the same market."* [Italian Flat Glass]. A position of dominance must be established in respect of a particular relevant market, both product and geographic. Accordingly, before a finding of dominance can be made it is necessary to define precisely the relevant market on which that dominance operates. If dominance can be established, then certain unilateral acts may be considered to abuse its dominant position through either exploiting that position or excluding competition.

There are potentially certain circumstances where a group of lending banks might together have market power in that they jointly have the power to behave to an appreciable extent independently of their competitors and the borrower. This may be in circumstances, for example, where a borrower is in financial difficulties and faces an event of default. In this scenario, given the relationship between the lending banks under the loan agreement there are likely to be sufficient economic links to result in an alignment of their behaviour in relation to the approach to the borrower. Furthermore, it may be the case that the relevant market should be defined very narrowly – market definition consists in identifying the effective alternative sources of supply for the borrower and, in this situation, the options available to a borrower may be very limited as other lenders may be unwilling to refinance and furthermore the existing lenders are likely to have substantial rights to protect their investment.

If the lending banks were to together impose certain conditions on refinancing which were not objectively justified (e.g. to protect their investment or reflect a higher degree of risk in any refinancing), for example tying the purchase of other services to the refinancing and imposing excessive prices as a condition to the lending, then it cannot be excluded that such actions could raise competition law concerns.

Summary of key risks

Based on this assessment of Article 101 and 102 and drawing on wider competition analysis, we summarise the key risks that we will examine further in the specific context of the loan syndication process:

- Horizontal information sharing – for example this may lead to the disclosure of strategic information (such as strategic market practices to be adopted) which may serve to coordinate the pricing policies of the lenders, thereby facilitating a collusive outcome on the market in terms of price in particular, but also quantity and quality.
- Agreements between banks to collude, for example to share markets or customers, limit supply or to rig bidding processes.
- Agreements in relation to ancillary services such as allocating the share of supply and fixing prices.
- Vertical market power held by individual MLAs and/or the lenders may lead to sub-optimal loan terms.
- Syndication may confer market power or dominance to a syndicate in certain (exceptional) circumstances, which may lead to sub-optimal outcomes and may increase the negative impacts of collusive behaviour (for example if lenders agree to increase loan prices on refinancing where the borrower has limited alternatives).
- Misaligned incentives between lenders within a syndicate, and between lenders and borrowers, may give rise to more general sub-optimal outcomes.

In the following sections, we develop for each stage of the loan syndication process a more detailed framework of legal and competition analysis, drawing out whether, and in what circumstances, behaviours are likely to be compatible or not with competition law; what the risks to competitive outcomes are (i.e. expanding on the list above); and what safeguards might be implemented to reduce these risks.

Criteria for analysing the evidence on potential issues

The extent to which information sharing and any potential market power would be able to restrict competition through facilitating collusion and abuse of dominance depends on a number of market characteristics and the nature of the information exchanged. In the following sections we discuss any mitigating market features and analyse the evidence relating to the existence of these. These might include:

- The level of concentration in the market – a concentrated market where the cooperating parties have a wide market coverage is more likely to facilitate collusive outcomes.
- Equally, any market features that would facilitate sustainable, tacit collusion amongst market participants through collective bargaining power.
- The availability of substitutes for the borrower and their sophistication – this will affect their ability to switch lenders and their bargaining power *vis-a-vis* the syndicate and/or MLAs.
- The extent of market transparency – a transparent market (and/or if the information exchange will increase that transparency) is more conducive to collusive outcomes.
- The complexity of the products – complex, non-homogenous products with a large range of prices contribute to a less conducive market for collusive activity.
- The frequency of interaction and information exchange – more frequent information exchanges are more conducive to anti-competitive impacts as they facilitate a better common understanding of the market.
- The nature of the information shared, i.e. data that reduces strategic uncertainty will be more risky (such as pricing).
- The likelihood of the individual lenders being able to compete without the formation of a syndicate. The Horizontal Guidelines in relation to Commercialisation Agreements state that a "commercialisation agreement is normally not likely to give rise to competition concerns if it is objectively necessary to allow one party to enter a market it could not have entered individually or with a more limited number of parties than are effectively taking part in the co-operation, for example, because of the costs involved. A specific application of this principle would be consortia arrangements that allow the companies involved to participate in projects that they would not be able to undertake individually. As the parties to the consortia arrangement are therefore not potential competitors for implementing the project, there is no restriction of competition within the meaning of Article 101(1)."

For cooperative agreements that do have the potential to limit competition, Article 101(3) provides further assessment criteria (we consider these as relevant evaluation criteria here even though it has not been established that information sharing in loan syndication restricts competition).[167] These would be relevant in assessing whether

[167] Article 101(1) first establishes whether co-operation has the potential to limit competition; only once this is established does the assessment under Article 101(3) become relevant – whether the co-operation has pro-competitive benefits which outweigh the competitive restrictions. As our study assesses at a broad level whether there is the potential for competition concerns across the markets as a whole we draw on both elements under Article 101(1) and 101(3), even though in practice for an individual case the assessment under Article 101(3) would only be undertaken if it had been established that the co-operation has the potential to limit competition.

the information sharing in loan syndication could result in the competition problems above.

- Whether the cooperative agreement (or the nature of information exchange) is efficiency enhancing. The Guidelines note that the efficiency gains must not be savings which result only from the elimination of costs that are inherently part of competition, but must result from the integration of economic activities. In this context, some cooperation and information sharing is necessary to (a) ascertain the willingness of lenders to form a syndicate and provide the loan and (b) to agree to a final term sheet and price. Without this, the ability of banks to form syndicates would be severely limited (not to say impossible) which would require borrowers to pursue less efficient loan options (more costly; lower volumes) or may deny them access altogether.
- Indispensability of the information shared. Information sharing that goes beyond that which is strictly necessary to form a syndicate and agree terms would constitute as potentially risky to collusive behaviour. Considerations here would include what limits the borrower puts on discussions between banks before syndication; what information is shared during/within a syndicate, and at which points.
- Pass-on to clients. Efficiency gains obtained by indispensable restrictions on competitive behaviour must be passed onto consumers (in this case borrowers). The lower the market power of the syndicate the greater the likelihood these gains would be passed on.

In addition to market features, as mentioned above there may be various safeguards that could be put in place that could mitigate the risks to competition, which we also draw out in the specific stage assessments below.

Stage-by-stage analysis of competition issues

We now turn to the detailed analysis of the competition issues relating to each element of the syndicated loan process. The nature of competition risk varies depending on the stage of the syndication process. We analyse in turn:

- The formation of the lead banking group, consisting of (a) a competitive bidding process between individual banks; (b) a competitive bidding process between ready-made consortia; (c) the direct appointment of a single/relationship bank.
- Post-mandate to loan agreement.
- General syndication phase, including the bargaining power of the syndicate, the selection of participants, information asymmetry and the role of a lead left bookrunner.
- General syndication phase focusing on market flex.
- Ancillary services.
- The use of debt advisors.
- The secondary loan market.
- Default and refinancing.
- Back office processes.

Competitive bidding process – individual banks

Our description of the syndication process distinguishes between scenarios with appointment by means of a competitive bidding process, and those where roles are appointed directly by the borrower without a formal bidding process. We begin with the analysis of a competitive bidding process.

Framework for competition analysis

In the case where a competitive RFP process is followed, lenders would compete for the mandate of MLA or other role under the terms of the RFP issued by the borrower/sponsor. The key competition risk at this stage is related to information sharing – information exchange (even if unilateral) between actual or potential competitors *may* result in a concerted practice which restricts competition where it facilitates alignment of their competitive behaviour (see paragraph 65 Horizontal Guidelines).

Information exchange could occur on two levels: between potential lead banks and the wider market of potential loan participants, and between potentially competing banks.

In the first case, at the pre-RFQ stage (i.e. on an ongoing basis) banks' syndication desks might gather general market intelligence in order to understand potential appetite for participation in potential lending opportunities. However, in gathering general market intelligence potential competing banks must be careful not to exchange specific, detailed information about other banks' future behaviour which could influence their competitive behaviour – for example detailed information about the banks' respective lending capacity to particular segments could be used to coordinate their responses to particular future bids (e.g. whether to bid or not in an upcoming RFQ, or how much to bid for).

In addition, in submitting their responses to a specific RFP the lead banks might engage in 'market sounding', i.e. solicit informal feedback from potential market participants on their appetite for the deal and the price at which they are willing to invest (provided this is not prohibited by the borrower). These discussions may have efficiency enhancing qualities, as they would reveal the extent of the underwriting risk for the potential lead banks.

Secondly, in cases where the borrower/sponsor's process does not require that lead banks remain separate during the bidding phase (for example for loans where pricing and appetite are uncertain), there may be a legitimate reason for a bank to gain an understanding of other lenders' appetite for the transaction – for example whether / how much and at what price level the other potential lenders would be interested in participating. Potentially competing banks might exchange information such as views on their appetite for the loan, views on pricing and views on loan term and structure.

However, it is at this pre-bid stage that any exchange of information has the greatest risk of impacting the competitive outcome of the bidding process by potentially removing uncertainty between competitors. The market soundings or inter-bank information exchanges could become a conduit for pricing information that may influence the banks' individual responses to the borrower's RFP, which could compromise the outcome of a superficially competitive auction process. Whilst every exchange must be examined in its specific context, exchange of such strategic intentions with other potential MLAs (in particular) on future conduct are especially likely to lead to an anti-competitive collusive outcome (see paragraphs 72-73 of the Horizontal Guidelines).

One important consideration here is the role of the origination and syndication functions, and the degree of separation between them (e.g. in terms of whether or not there are different individuals or teams conducting each activity). If there is a syndication team within the bank responsible for gathering general market intelligence on lenders' appetite for loans, then the risk of information sharing is reduced if there is an enforceable separation — in terms of the flow of information — from the origination team (i.e. the function responsible for negotiating the price and other loan terms with the borrower and other lead banks). If the origination team receives no deal-specific information about appetite about individual lenders (some of which may

be competing to act as MLAs), then the risks of that team coordinating its responses to the loan terms with other lenders in a manner not sanctioned by the borrower are reduced.

Whether information exchanges will have a restrictive effect on competition and/or whether it can be considered indispensable under Article 101(3) requires a case by case assessment, but various factors such as the availability of relevant information either publicly or through the lenders' own prior experience on previous recent transactions in the same or similar segments, and the number of potential lenders /appetite for lending to the segment, are likely to be relevant to the analysis. For example, if sufficient information to enable banks to perform their role as arrangers/underwriters is already available to them, then information exchanges would not be justified. On the other hand, if it is the case that based on the knowledge (or lack thereof) available to the banks, in the absence of some information exchange banks would be less likely to respond to the RFQ or would have to respond on less competitively attractive terms than might otherwise be the case given the difficulties of accurately pricing the risk, then it is potentially the case that the information exchange either does not have an anti-competitive effect or that it satisfies the conditions for exemption under Article 101(3).

Whether or not this is the case will also depend on an analysis of precisely what information is strictly required in this situation, for example will a general indication of interest in a segment within a range be sufficient as compared to a highly specific indication of exact interest at a price. Furthermore, could the necessary insights be provided by potential investors who, whilst they may participate in the wider syndication, will not be competing for a role as an MLA or underwriting. These are all relevant questions on a case by case basis.

A key factor in assessing the compatibility of information exchanges with competition law is whether or not these are sanctioned by the borrower/sponsor. Where such information exchange takes place with the express (and freely given) consent of the borrower, whilst not ultimately being totally determinative as to the anti-competitive effect, is good prima-facie evidence that the exchange is not anti-competitive by object and may further indicate that the exchange was considered and accepted by everyone as necessary in the circumstances. However, there are potential safeguards that could be imposed by the borrower/sponsor to reduce the risks of this information sharing (which we describe below).

If, on the other hand, the process set up by the borrower is designed to prevent the interaction between banks and the exchange of information (for example by keeping bank separate and through the use of NDAs at different stages of the process), then there would be a higher risk of such unsanctioned information exchanges being anti-competitive (as well as being in breach of contractual law).

The information exchange scenario outlined above is to be contrasted with information exchange pre-bid which may amount to a concerted practice and which is not potentially justified by circumstances such as those indicated, or is expressly prohibited by the borrower/sponsor. Lenders could undermine the competitive process by sharing information with one another during the bid process to align their offerings,[168] engaging in cover pricing,[169] encouraging bidders to drop out in return for

[168] For example, the case of RBS, which revealed its confidential and commercially sensitive loan pricing information to Barclays in order to restrict competition between the two banks. See https://www.gov.uk/cma-cases/loan-products-to-professional-service-firms-investigation-into-anti-competitive-practices.

compensation, promising each other tranches in the syndication process in exchange for dropping out of the origination, limiting capacity, or even by agreeing to take turns to bid for specific contracts. The same is true for any 'consolation prizes' for those banks that are not chosen for the banking group. All these actions would clearly be beyond what is necessary to the syndication process and such information exchange could well be considered as having the object of restricting competition.

Initial banking group formation through to mandate
Similar issues exist in the stage after the bids have been received and before the individual banks have been mandated. At this next stage of the transaction the borrower will evaluate the respective responses to the RFQs and select the preferred banks based on their bids. At this stage of the process banks may decline to participate (and others may then be invited to participate) based on the borrowers' invitation.

Until the initial bank group is formed and the mandate is granted, the banks are still competing independently for a role/participation in the provision of the loan. Banks may not yet have decided whether they are willing to participate, based on the borrower's invitation. Information exchange between the banks about the terms of their respective RFQs post bid but pre-mandate could thus still undermine the competitive bidding process and accordingly are likely to fall within Article 101(1) and outside Article 101(3).[170] Such information exchange may be considered a restriction of competition by object – if done without the consent or knowledge of the borrower then this could be further indicative of an anti-competitive intent (which whilst not determinative as to whether a practice is anti-competitive by object is likely to be relevant context in such circumstances).

For example, discussions or agreements directly between the banks at this stage (under an individual RFQ response scenario) concerning their respective willingness to participate or adjust the amount they are willing to lend could potentially lead to agreements or concerted practices to fix prices or restrict supply to the borrower. If a bank or banks are not willing to commit at a certain price but others are willing to increase their hold levels or other banks are willing to participate and can potentially be invited to join, then agreements or practices that undermine this would likely be agreements that have the object of restricting competition.

In some cases, the borrower/sponsor may appoint a single lead arranger bank to set up the initial banking group and negotiate the loan terms with the other banks, instead of this being controlled bilaterally by the borrower/sponsor. In this case, the borrower/sponsor would mandate that the banks share information in order to reach a common loan price and terms. The interaction with the banks should be strictly within the parameters set by the borrower. There is a risk that information shared between the lead bank and other banks involved in setting the terms of the loan could lead to the loan terms moving against the borrower.

Potential safeguards
There are a number of potential safeguards that could be adopted which could reduce the abovementioned risks to competition at the bidding stage. Safeguards could be undertaken by the borrower/sponsor or the lenders.

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[169] Cover pricing was the main form of collusion discovered in the construction industry in 2009 — the OFT concluded that between 2000 and 2006 around one hundred construction firms colluded in almost 200 tenders. See https://www.gov.uk/cma-cases/construction-industry-in-england-bid-rigging.
[170] We note that the European Commission has not taken a position on the application of Article 101(1) or 101(3) with regard to syndicated lending.

- *A degree of separation between syndication and origination functions*. In the case of ongoing market intelligence gathering by syndication desks (prior to any RFQs), introducing a degree of separation from the origination desks (those responsible for bidding for the loan and deciding on price, structure and hold levels) could reduce the risk that information obtained by the syndication desk regarding other lenders' appetite is unduly passed onto the origination team and facilitates coordinated bidding in any way. This would mean that the syndication desks provide only consolidated, anonymised views of market appetite for a given borrower/sponsor to the origination desks, such that the latter is not privy to information relating to specific lenders. This would serve the purpose of ascertaining information to assist in assessing underwriting risk etc., whilst avoiding the sharing of specific information. In principle, the greater the degree of separation the better. This may be difficult to achieve in practice, at least in smaller lending institutions where syndication and origination functions could be combined into the same team, and we cannot provide definite views on the degree to which separation should occur across all institutions. However, at the very least, the same *individuals* should not be involved in syndication and origination functions if the latter involves any market sounding.
- *Competition law guidance or training for banks about information exchange issues*. Tailored training and guidance could be put in place for both origination and syndication functions within banks. The value of the information separation between the syndication and origination desks may not always be understood by banks, i.e. that the primary role of the syndication desk should be simply to decide how to lay off the risk of a loan onto the market, not to help the origination desk in winning a bid for a role in a loan. Clarity on these roles, and on the risks involved in information sharing, could be valuable in raising compliance among banks.
- *The structure of the bidding process*. Borrower/sponsors may be able to structure the bidding process so as to keep lenders separate for as long as possible and reduce the need or potential for any information sharing. This could be achieved not revealing the identities of the lenders invited to respond to the RFP, and by engaging in bilateral negotiations with each lender during the bidding process and only bringing the banks together once final loan terms have been signed and the opportunity for banks to collude in order to move the loan terms against the borrower/sponsor is very limited. Borrower/sponsors could also bring banks together for some discussions, and separate them when negotiating other areas. All communication with other prospective banks should only be at the express consent of the borrower. These separations would need to be enforced by NDAs preventing the exchange of any information. NDAs can be difficult to enforce in practice – sanctions could include the expulsion of the offending bank from the process. Nevertheless NDAs signify the intent to protect the bidding process set up by the borrower, and any breach thereof would be a breach in a contractual obligation and a determined effort on the part of the bank to circumvent the borrower's wishes (i.e. and therefore not excusable as being part of the syndication process).
- *Setting clear parameters for information exchange*. In some cases, given the nature of the financing some insight into market appetite is needed before banks can respond to an RFP. In these circumstances (with the borrower/sponsor's clear consent to any interaction a pre-condition), safeguards could be for the borrower/sponsor to identify the potential investors/lenders that could be approached for the purposes of gauging market appetite, which could further specify those likely to act as participants but who would not be bidding to be part of the lead banking group. The borrower/sponsor could also identify what information is strictly necessary for the purposes of banks being able to form a view on the loan and to submit a bid, and specify that no other information is shared. As mentioned above, where possible such communication should be done by the syndication desk

only, with a consolidated view provided to the origination desk. For example, communications about hold-levels, approval levels and the like would generally be problematic, and so the borrower can seek to mitigate this risk by specifically prohibiting such contacts (although enforcement may be difficult in practice).

- *The implications for investors of information exchange*. Non-bank investors e.g. those investing on behalf of institutional investors who are also involved in trading instruments will face laws (in particular Market Abuse Regulations) about limits on trading activity if in possession of private information relating to a specific listed company. These investors should therefore have in place the necessary compliance structures to avoid receiving and trading on information received from lead banks during any deal-specific discussions.
- *Borrower/sponsor sophistication*. The experience and skills of borrowers/sponsors in coordinating syndicated loans will also mitigate – to some extent – attempts by lenders to collude on pricing and terms. If the borrower/sponsor already has in mind a target price and structure for a loan, he may be able to detect coordinated behaviour among lenders and effectively discipline lenders by removing them from the bidding process and excluding them from future financing opportunities.

The nature of the market may influence the effectiveness of the safeguards. For example, in markets where the number of eligible lead banks is limited it may be more difficult to ensure that they are not aware of the identity of the competing bidders, or to enforce a prohibition on interaction and information sharing. This could be the case in smaller geographic markets (as described in Chapter 3, geographic markets appear to be split between a large west Europe market and smaller, national markets such as Poland) or in product markets where the esoteric nature of the underlying transaction is such that only a few banks have the experience to participate in a syndicated loan, for example in very large or very bespoke PF/INFRA loans.

Evidence and analysis

Evidence for competition law risk or risk of sub-optimal outcomes in LBO segment

We now turn to the evidence relating to the formation of the lead banking group in the LBO segment to analyse the likelihood of the above-mentioned risks being present, and whether and how the safeguards discussed are in place.

Pre-RFP market intelligence

As shown in Chapter 2, our lender fieldwork indicates that lenders commonly engage in the continuous gathering of generic market intelligence from potential investors in order to remain up to date with market appetite and potential candidates for syndicated loans. Lenders argued that no deal-specific information is discussed during this process, and that information sharing is governed by internal compliance rules. This engagement also happens between the lead banks and potential investors, as opposed to between the lead banks themselves. Deal-specific market sounding was characterised as atypical, and lenders were clear that any deal-specific sounding would require explicit borrower/sponsor consent. In its strongest form, such consent should be specific as to who is contacted. Some banks were cautious in defining the boundary between generic and deal sounding, e.g. one stating that if a retail sector transaction was under consideration, and conversation around appetite for retail in general would be dropped from generic soundings. For the most active market participants, with many contemporaneous transactions, that level of restriction may not be possible.

Even so, borrowers/sponsors have concerns about the sounding process: either worried that market soundings could lead to some information or privacy leaks (seven per cent) or potentially enable the lead arranger to gain market information which he

may use to inflate the terms of the loan (29 per cent).[171] Around 16 per cent of borrowers/sponsors in the LBO segment stated that they either do not allow market sounding at all or place restrictions on the information that can be shared, and a further 22 per cent did not allow it pre-mandate. One further aspect of this would be where a lender is vertically integrated with a sponsor (e.g. a bank also has a private equity investment arm). Where the sponsors themselves are in a competitive bidding process, this would require additional protocols safeguarding against unwarranted information sharing.

One important safeguard identified is the degree of separation between the syndication and origination desks, such that any investor-specific information is not passed onto origination individuals. Our fieldwork indicates that such functional separation between syndication and origination is not always a feature of lenders' business models, and thus the risk remains. Many lenders, in particular the larger ones, have separate syndication and origination teams, with some syndication teams being based in central hubs with the origination teams based more locally across regions and countries. However, there does not appear to be a fully functional separation between these (i.e. they are part of the same overall unit within the bank), and in some cases the syndication and origination teams will be structured along product/geographic lines rather than function, such that for a particular product or geography the same team would cover both origination and syndication. Therefore whilst there is no evidence from our fieldwork that detailed information sharing takes place, the absence of specific functional separation safeguards means that this is still a risk.

Information to prepare bids

A feature that influences the need to information sharing is the ability of banks to use existing information sources to formulate their bids for a loan. In the LBO market there is a sufficient amount of information available to lenders so that specific market reads are not necessary when forming their responses to an RFP – indeed all lenders in our fieldwork indicate that they do not engage in specific market reads. As set out in Chapter 2, the information available includes prior deal flow of comparable deals with information on pricing and loan structure, as well as information available to purchase from data vendors. The risk of specific information sharing through market reads is therefore low.

Bidding process

Our fieldwork shows that the bidding processes set up by borrowers and sponsors in the LBO segment are competitive processes in which the borrower/sponsor negotiates bilaterally with each individual bank (usually through the use of a terms grid). There is no opportunity for the lenders to come together to discuss terms collectively until they have been mandated and each has signed a commitment letter with the borrower/sponsor. Therefore sharing strategic information such as pricing and loan structure is not facilitated in any way by the process pre-mandate, i.e. the process does not (and obviously should not) itself give the lenders an opportunity to align their bids in a coordinated way. The majority of lenders in our fieldwork indicated that they do not know who the other bidding banks are. However, this is not the case across the board – lenders have told us that in some cases it is possible to speculate who the competing lenders by the ways in which the loan terms evolve throughout the negotiations. Equally, the borrower/sponsor fieldwork shows a different picture,

[171] Fieldwork question S14 / B12 "Which of the following, if any, best represent(s) your attitude to the MLAs engaging in market sounding activities?

whereby 55 per cent of those in the LBO segment responding to the questions stated they do allow lenders to know who the participating banks are.[172]

The key safeguard here is the use of NDAs to ensure that lenders do not reveal to each other that they are participating in an RFP, and to ensure that they do not interact and exchange any information here. There can be issues in enforcing NDAs, for example identifying who the offending banks are or claiming potential damages. Therefore although the process set up by the borrower/sponsor in LBO loans reduces the risk of anti-competitive information sharing, the risk remains that this may happen.

A further mitigating factor is the sophistication of the borrower/sponsor in terms of their ability to control the syndication process and set the terms for the pricing and structure of the loan. Our fieldwork shows that borrowers and sponsors in this segment are sophisticated and even have in-house debt financing teams experienced in pricing loans in the LBO market – this is particularly the case as LBOs are dominated by sponsors who would be private equity houses responsible for undertaking many syndicated loans. Third-party debt advisers can also be used (to provide resources in terms of managing the process or specialist knowledge, e.g. on derivatives) even when the sponsor has its debt financing specialists. We elaborate on borrower/sponsor bargaining power in later sections.

A single MLA/coordinator setting up the syndicate
The likelihood of a single MLA being appointed by the borrower/sponsor to set up the syndicate and negotiate the key loan terms with the rest of the lead banks is low, based on the processes adopted by borrowers and sponsors in the LBO segment. Our lender fieldwork indicates that borrowers/sponsors control the formation of the lead banking group, keeping the individual banks separate until each has agreed the key terms with the borrower/sponsor and signed the initial loan agreement. This separation is again governed by NDAs and therefore the same potential risks related to breaches of NDAs would apply as discussed above.

Evidence for competition law risk or risk of sub-optimal outcomes in PF/INFRA segment

Pre-RFP market intelligence
As PF/INFRA loans are usually club deals (our lender fieldwork indicates that the majority of these loans are club deals, and among borrowers club deals are more common than best-efforts or underwritten deals for PF/INFRA loans[173]), there is less need for these lenders to engage in generic market intelligence with potential investors in order to inform underwriting risk (although the same issues would remain as with the LBO segment if the loan was to be underwritten).

As with the LBO segment, the borrower/sponsor fieldwork also shows that information market soundings take place. Around 20 per cent of borrowers/sponsors in the PF/INFRA segment responding to this question do not allow market sounding at all or place restrictions on what can be shared, and a further 12 per cent do not allow it pre-mandate, but do allow if post-mandate. A further 24 per cent allow it to ensure the success of the syndication. Concerns were raised by some respondents in that market soundings could lead to some information or privacy leaks (12 per cent) or potentially

[172] Fieldwork question S12 / B10 "Do candidate MLAs typically know the identity of the other MLA candidates?" to which 38 per cent responded "Yes, the process of appointment sometimes requires this" and 16 per cent responded "Yes, this is a standard part of our process".
[173] Of the borrowers engaging in PF/INFRA deals, 10 reported using club deals and 8 reported using best efforts (2) or underwritten (6).

enable the lead arranger to gain market information which he may use to inflate the terms of the loan (31 per cent).[174]

Our lender fieldwork indicates that the same issues apply when banks are involved in PF/INFRA deals as with LBO deals, in that there are not always formal processes for separating the functions of the syndications and originations teams. The absence of this safeguard is not in itself evidence of anti-competitive information sharing, but there would be such a risk where origination and syndication functions are not separated and not subject to enforceable (and enforced) protocols around deal-specific information sharing with the origination team.

Information to prepare bids
Our lender fieldwork indicates that banks do not engage in any interaction during the bidding phase when competing for a role in a club in order to inform their views about the price of the loan and the amount they may need to hold. However, given the more bespoke nature of PF/INFRA loans the availability of information to assist in banks forming their views is likely to be lower. For example, lenders indicate that for certain types of loans (very large, bespoke or infrequent types of projects) there would be fewer comparable transactions either from internal deal flow or available from data vendors. Whilst the economic performance of a project could be estimated, we understand that banks' credit committees require further evidence to assess the credit risk of a loan, in particular comparator transactions.

Therefore there could be a heightened risk that the safeguards set in place by the borrower/sponsors are undermined in PF/INFRA loans, and a greater risk that interaction and information sharing does take place between lenders in the bidding stage.

Bidding process
Our lender fieldwork indicates that PF/INFRA club deals are put together in a similar way to LBO loans, whereby the borrower/sponsor invites banks and negotiates with them individually before agreeing the loans terms and inviting the club to get together to discuss documentation. NDAs would be used to protect the process. In these cases the bidding process and use of NDAs provides a safeguard, although as mentioned the risk that these safeguards are undermined could be higher in PF/INFRA segment due to a lack of available information in forming bids.

A single MLA/coordinator setting up the syndicate
Our lender fieldwork indicates that, whilst it is not common, there may be times in PF/INFRA deals when a borrower/sponsor will use a single MLA or coordinator to set up the syndicate and play the role of the borrower/sponsor in negotiating terms with the other lead banks. This might be for transactions which need to take place quickly and bilateral negotiations between the borrower/sponsor and banks would require too much time.

Whilst the lender fieldwork indicates that borrowers/sponsors retain control of this process, there remains the possibility that information sharing may occur such that the negotiations of the syndicate could be coordinated and the price and terms of the loan move against the borrower. This remains a risk area.

[174] Fieldwork question S14 / B12 "Which of the following, if any, best represent(s) your attitude to the MLAs engaging in market sounding activities (this refers to the informal scouting of interest - both pre and post-appointment of the MLAs - in participation in the loan from other market participants"?

Competitive bidding process - consortia

Framework for competition analysis

Where a group of banks come together to submit a joint bid in response to an RFP at the request of a borrower then, provided that the bank group operates within the instructions of the borrower, it is likely that the any information exchange between the banks for the purposes of putting together that proposal and the ultimate agreement that the banks reach as to the terms of that bid, will either fall outside Article 101(1) altogether or satisfy the conditions of Article 101(3). [175] [176]

Such an agreement /information exchange would certainly not appear to have the purpose or objective of restricting competition and, taking into account the overall context of the arrangement, would not be anti-competitive by object. Arguably, it should therefore fall outside Article 101(1) altogether. For the purposes of bidding for the particular loan the lenders must co-operate (in order to meet the borrower's request) rather than competing independently and to the extent that the information exchanged and the agreement reached is inherent to that joint bid then it is directly related and necessary to the joint bidding. Alternatively, such a joint bid may benefit from an exemption under Article 101(3).

To the extent that discussions or agreements go beyond what is required for the purposes of submitting the joint bid then, depending on their nature, such discussions may breach Article 101(1) and indeed may be anti-competitive by object. A borrower can appoint (perhaps informally) a lead bank to bring the consortium together (this would be akin to a club deal, with an MLA). (This might be, for example, where an existing club/consortium exists from previous funding rounds). The lead bank will need to understand each potential participating lender's potential interest (e.g. willingness to underwrite/ hold) and at what price. The lenders will need to communicate this between each other and ultimately agree. We can usefully illustrate this with a worked example. A borrower wants £500m and – of five banks approached – four offer £100m at 165 bps and one offers £100m at 195 bps. The borrower's options are as follows: (a) the borrower can accept a reduced volume of credit (i.e. £400m) from the four banks at 165 bps, (b) the borrower can seek £500m from those four (albeit likely at a margin higher than 165 bps), i.e. the other lenders are willing to accept an increased participation, (c) those four banks approach a sixth bank (not involved in an alternative bid), or (d) if the borrower insists on the participation of the original high-bidding bank (i.e. particular lender(s) is needed for the purposes of the joint bid), then the price would shift to 195 bps because the other banks would not be able to replace it.

As such, discussions or agreements between the lenders that might undermine or distort this process, such as agreements not to invite other lenders to participate, or not to increase their participation (where acting independently they could and would have done so) are likely to have an anti-competitive effect and could in fact be anti-competitive by object.

The risk of a consortium engaging in uncompetitive coordination in order to increase the price of the bid would be influenced by the nature of the bidding process. If the consortium submits its bid as part of a competition with other bids, then the

[175] We note that (as throughout this report) assessments of the application of Articles 101 and 102 are based on our own judgement and that the European Commission has not taken a position on this with regard to syndicated lending.

[176] Whilst the submission of bids by competing consortia is not part of the typical loan syndication process, it is a possible alternative.

borrower/sponsor would assess their 'higher priced' bid against other bids (in the same way that it would do so with individual banks' bids). Increases in price above the competitive level would therefore be detectable, and consortia should therefore have an incentive to be competitive.

However, if the banks coming together in a consortium have market power and the consortium is able to engage in practices that inflate the price through information sharing and co-ordination, this may raise competition law concerns. The extent to which a consortium could be considered to enjoy market power would need to be assessed on a case-by-case basis.

Potential safeguards

The following safeguards could be applied to reduce the risks of anti-competitive information sharing or coordination and sub-optimal outcomes.

- *Clear parameters for the consortium.* The borrower/sponsor should ensure that there are clear instructions to the consortium as to what they should agree jointly and what information they can share. This would control the extent of the cooperation needed to submit a joint bid. Any variation in these parameters (e.g. if it becomes clear that this is needed to submit a full bid) should be at the consent of the borrower/sponsor.
- *Limits on the interaction between banks.* The borrower/sponsor may split the consortium at any point during the bidding process, for example asking the banks to bid jointly on expertise and syndication strategy, but separately on price. The banks would need to abide by these instructions and cease any communication. The instructions around information sharing and interaction would be supported by NDAs.
- *Impacts of borrower/sponsor instructions.* The borrower/sponsor should consider carefully the impacts of imposing certain criteria on the consortium (such as the need to include certain banks) which may give rise to sub-optimal outcomes.
- *Bidding process.* If consortia are invited to submit bids that compete with other consortia (instead of bidding as the only consortium) then there is scope for the borrower/sponsor to compare bids and maintain competitive pressure.
- *The regulatory regime.* In the case where a borrower/sponsor sets up a process that leads to sub-optimal outcomes, for example by setting parameters that limits the number of competitive bids it will achieve, or limits the competitive tension, the regulatory regime could place some responsibility on the banks responding to the RFP to highlight to the borrower/sponsor that the process may not be in its interests.
- *Tailored competition law training and guidance.* Training could be provided to banks as well as borrowers/sponsors regarding the risks of consortium bidding and the processes to follow in terms of information sharing.

Evidence and analysis

Evidence for competition law risk or risk of sub-optimal outcomes in LBO and PF/INFRA segments

Our fieldwork shows just under half the borrowers reported they can issue an RFP for funding from consortia as well as individual banks.[177] This indicates that such bids are a feature of the market.

[177] Fieldwork question: B6 "Which procedure(s) do you usually follow when the MLA(s) are appointed in this transaction?" to which 40 per cent of borrowers said they issue a competitive RFP for funding from individual banks and 49 per cent they use an RFP for funding from individual banks and consortia.

The main safeguard is that borrowers almost always use a competitive RFP process when appointing the lead banking group (whether this is soliciting bids from individual banks or consortia). Indeed, in the YouGov survey, no borrowers reported directly appointing a consortium without a competitive RFP process.

Appointment of single/relationship bank

Framework for competition analysis

As an alternative to a competitive bidding process for appointing the MLA or lead banking group, the borrower/sponsor can directly appoint a lender or a number of lenders to act as MLA or coordinator who then arrange the loan lead banking group or club.

In this scenario the appointed MLA(s) or the coordinator in a club deal is likely to be a relationship bank, i.e. a lender who has already worked with the borrower (or is currently providing other services) and thus has insight of the borrower's risk profile and financing needs. The literature shows that the existence of lending relationships are strongly associated with an increased probability of winning future debt underwriting business from the same customer.[178] Such an established relationship could generate a number of benefits by resolving asymmetric information issues between the main lender and borrower.[179] Other benefits could include easing the sharing of sensitive information,[180] the ability to monitor collateral,[181] and the ability to smooth out loan pricing over multiple loans,[182] and may translate into lower interest rates on the funding.[183]

In the absence of a competitive bidding process when a lead bank is directly appointed, the information exchange issues which are most sensitive in a pre-bid stage are not present in these arrangements, as the lead bank is selected and appointed on an individual basis by the borrower without the need to compete with other banks.

Risks of subverting the competitive price level

However, the use of relationship banks rather than a competitive process, can create concerns for the effectiveness of competition and may risk sub-optimal outcomes for the borrower, in particular, around the inherent re-negotiability of loans and potential monopoly power of the lender.[184] We consider this issue to be one of general regulation rather than competition law, as the borrower has mandated the appointment of the relationship bank. Dahiya (2003) finds that the cost of borrowing from a relationship lender is lower compared to borrowing from a non-relationship lender. However, the relationship bank could still have some element of "hold-up" power that could enable it to use its position to offer a price which could appear to be more competitive than that of other banks, but is still above a competitive level. This is because as the lender acquires private information over the course of relationship, it

[178] Sreedhar Bharath; Sandeep Dahiya; Anthony Saunders and Anand Srinivasan, (2007) "So what do I get? The bank's view of lending relationships" Journal of Financial Economics, 85, (2), 368-419

[179] See e.g. Diamond, Douglas W. (1984) "Financial Intermediation and Delegated Monitoring" The Review of Economic Studies, vol. 51, no. 3, 1984, pp. 393–414; and Bhattacharya, Sudip, and Anjan Thakor (1993) "Contemporary banking theory" Journal of Financial Intermediation 4, 328-357.

[180] Bhattacharya and Chiesa (1995) "Proprietary Information, Financial Intermediation, and Research Incentives" Journal of Financial Intermediation, 4, (4), 328-357.

[181] Rajan, Raghuram & Winton, Andrew (1995) "Covenants and Collateral as Incentives to Monitor" Journal of Finance.

[182] Berlin, Mitchell and Loretta Mester (1998) "Deposits and Relationship Lending" Working Paper, Federal Reserve Bank of Philadelphia.

[183] Sreedhar Bharath; Sandeep Dahiya; Anthony Saunders and Anand Srinivasan, (2007), "So what do I get? The bank's view of lending relationships", Journal of Financial Economics, 85, (2), 368-419

[184] See e.g. Rajan, Raghu (1992) "Insiders and outsiders: The relationship between relationship and arms-length debt" Journal of Finance 47, 1367-1400.

can use this information to extract monopoly rents from the borrower. To the extent these "lock-in" effects dominate the benefits of relationship, such a relationship would be associated with higher costs of future services that the lender provides.[185]

Risks of influencing the syndication process
Relationship banks may also be able to unduly influence the syndication process in their favour. For example, other banks may wish to participate in the syndicate in order to gain access to the borrower, provide future ancillary banking services and potentially challenge the position of the relationship bank. The existing relationship bank may resist these challenges by influencing the formation of the syndicate to exclude these challenger banks.

The ability of the relationship bank to leverage off its relationship will depend in part on the nature of the market. In smaller geographic markets where the number of relationship banks available to take on the role of MLA or coordinator might be relatively low, the borrower would have limited choice or bargaining power, and likelihood of repeat lending from the relationship bank and further information lock-in would be increased.

In addition, our research with stakeholders shows that the use of relationship banks is likely to be linked to the 'life-cycle' of the borrower. For example, as borrowers engage more in the market and become more sophisticated, they may move away from relying on local relationship banks and include an increasing number of international banks in the syndicate. Some borrowers however, may not be able to move out of the local market – such as those in bespoke product or geographic markets which rely on the expertise of local banks, or those what engage very rarely with the syndicated loans market.

Potential safeguards
The key issue here is that the process set in place by the borrower (by selecting a single relationship bank without a competitive process) may result in a sub-optimal outcome. This is not directly relevant to competition law but nevertheless is an important economic risk (i.e. the relationship bank may not have market power but may still be able to exert undue influence on the borrower/sponsor).

The extent to which the risks of appointing a relationship bank may arise in practice could be reduced by a number of safeguards:

- *The role of reputation.* The extent to which the MLA is likely to compete based on its reputation (i.e. for appointment by the borrower on other syndicated transactions). A relationship bank that prevented other lenders from joining the syndicate and ended up with an unsuccessful syndication may lose out on future opportunities with the borrower/sponsor. This would depend on the sophistication and monitoring power of the borrower/sponsor, the frequency of loan transactions, and the availability of other relationship banks.
- *The control retained by the borrower/sponsor*. A mitigating factor would be the sophistication of the borrower/sponsor in driving the syndication process and the extent to which they relied on the advice or influence of the relationship bank. For example, if the borrower/sponsor had control over which banks were appointed to the lead banking group or club, then the ability of the relationship bank to exclude challenger banks would be very limited.
- Similarly, the ability of the borrower/sponsor to monitor the MLA's interaction with participant investors would undermine undue influence or the risks of the

[185] Hasan, Iftekhar & Ramirez, Gabriel & Zhang, Gaiyan (2012) "Lock-In Effects in Relationship Lending: Evidence from Dip Loans" SSRN Electronic Journal 10.2139/ssrn.1785686.

relationship bank manipulating loan terms, i.e. of borrowers/sponsors are engaged with other lenders (both in the lead banking group and participant investors)

- *The ability of the borrower to replace the MLA in case of underperformance*. This would enhance the disincentives on the MLA to underperform. This would depend on the size of the potential market – in some cases there may be a number of potential MLAs ready to take over, and in some cases the borrower may face time and supply constraints such that a replacement would not be feasible. It would also depend on the sophistication and monitoring power of the borrower/sponsor.

Evidence and analysis

Evidence for competition law risk or risk of sub-optimal outcomes in LBO segment

The extent of single MLAs and the importance of relationship banks
Our borrower fieldwork shows that the use of single MLAs in LBO transactions is not uncommon – just under 30 per cent of borrowers and sponsors in our fieldwork report usually appointing just one MLA.[186] However, such MLAs are very rarely appointed without a competitive process,[187] and so the risks associated with a directly appointed single MLA are unlikely to be extensive in this market (although cannot be ruled out).

Relationships between banks and borrowers/sponsors are clearly important. The majority of sponsors indicated that an existing relationship was important when selecting MLAs – around 45 per cent of sponsor engaged in LBO deals said they tend to approach the same lead bank(s) because their established relationship guarantees the most efficient loan.[188] In addition, 50 per cent of borrowers and sponsors said that all or most of the MLAs approached had a pre-existing relationship with the borrower, and 74 per cent said that the MLAs had a pre-existing relationship with the sponsor.[189] Out of all the sponsors engaging in LBO deals, 94 per cent that the existence of a relationship with the MLAs was either very or quite important when selecting MLAs.[190]

The main advantages of appointing relationship banks are considered by these sponsors to be more competitive pricing on both the loan (70 per cent of sponsors) and on ancillary services (58 per cent), and a better response in the case of refinancing or default (60 per cent). This suggests that the appointment of relationship lenders is likely to be efficiency enhancing.

Repeat interactions and 'lock-in'
Our dataset shows that it is relatively rare for borrowers to engage in multiple syndicated loans in the LBO segments, at least within an eight year window. Table 13 in Chapter 3 shows that of the 651 borrowers in LBO loans, 88 per cent had only engaged in one deal in the period, with 10 per cent and two per cent participating in two and three deals respectively. (The target companies that are the subject of an LBO may be resold as another LBO, but within our dataset this is not the norm.) Whilst their relationships with lenders are still important (e.g. from other services),

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[186] Fieldwork question S11/B9 "Thinking about your MLA appointments, which of the following usually applies?

[187] In response to the question: "Which procedure(s) do you usually follow when the MLA(s) are appointed in this transaction?" Only six percent of borrowers/sponsors typically appoint MLAs without a competitive process.

[188] Fieldwork question S4 "How would you describe your experience in selecting banks (e.g. lead arrangers) to lead syndicated loans?"

[189] Fieldwork question S10 / B8 "Thinking about the banks approached to act as MLA, please say whether all, most, some or none are..."

[190] Fieldwork question S41 "When selecting lead arrangers, how important is the existence of an existing relationship?"

the risk of borrower 'lock in' discussed in the literature is low (as this relies in repeat loan transactions with the same borrower).

Repeat transactions between lenders and sponsors are more common – Table 15 in Chapter 3 shows that only 56 per cent of sponsors in LBO deals had undertaken only one deal, with 19 per cent having undertaken two deals and 10 per cent over five deals. However, this is also not likely to lead to an information 'lock in' effect as the underlying borrower would change from transaction to transaction and there would be no chance for a relationship lender to gain increasing information on a particular borrower, for example on its risk profile.

Safeguards related to the sophistication and control of borrowers/sponsors
The ability of borrowers and sponsors in the LBO segment to control the syndication process and the behaviour of the MLAs is likely to be high given their sophistication and experience (this particularly applies to sponsors – i.e. private equity houses - who are commonly in control of LBO loan transactions). Private equity houses have their own expertise in setting up funding transactions (e.g. internal debt finance teams). They are also often competing themselves for a target in the case of an LBO and therefore have an even greater incentive to ensure competitive loan terms. Private equity houses are also a source of future funding opportunities and as such the reputational incentives on MLAs to perform well should be high.

Our lender fieldwork shows that LBO transactions are controlled by borrowers and sponsors and that these have a direct say in the appointing of the syndicate banks, both lead banks and participants. This applies in terms of participants (i.e. the white list specified by the borrower/sponsor up front) and in terms of the loan shares allocated to participants - lead banks would usually suggest allocations but the final decision is taken by the borrower/ sponsor. This is supported by our lender fieldwork and all the borrower/sponsor fieldwork – of the borrower/sponsors in the LBO segment, 94 per cent said that either the borrower/sponsor (32 per cent) or borrower/sponsor together with MLA (62 per cent) had a role in determining the participating institutions for the syndicate. Six per cent said that the MLAs usually have the decision.[191] Therefore, in any circumstances in which a single MLA *is* appointed it is unlikely to be able to influence the selection of the syndicate in its favour.

The ability of borrower/sponsors to monitor and sanction MLAs
Our borrower/sponsor fieldwork shows that the ability of the borrower/sponsor to ensure that MLAs perform well during a transaction is less clear (although this applies to all MLAs and not just those that are appointed singly). Replacing MLAs that are not performing well does appear to be difficult – 45 per cent of LBO borrowers and sponsors reported being dissatisfied with an MLA, and this included 29 per cent who found it either too costly or contractually difficult to replace them, and seven per cent did not have a suitable replacement.[192] The fieldwork did not explore the reasons for this dissatisfaction, which could include inability to successfully syndicate the loan, or other sub-optimal behaviour. Borrowers/sponsors have some control over the performance of MLAs through fees, which are contingent (to some extent) on the successful conclusion of the loan.[193]

[191] Fieldwork question S19 / B17 "Who has ultimate say on which institutions join the syndicate?"
[192] Fieldwork question S14 / B12 "Have you ever been dissatisfied with the performance of an appointed MLA during the formation of the syndicate? What actions did you take?"
[193] Fieldwork question S33 / B31: "How much, if any, of the MLA's fees are contingent on successful conclusion of the loan?" 93 per cent of borrowers/sponsors said fees were contingent to some extent, but only 16 per cent said "All" or "A large amount".

The evidence in the LBO segment of the safeguards that could mitigate the risks of a single relationship bank having undue influence on the loan process or terms is mixed – borrower and sponsors in this segment retain control of the process and can exercise reputational pressure on the performance of MLAs, although practically disciplining them for underperformance during a loan is less widespread. The likelihood of having a single MLA in charge of the syndication process in LBOs is however low. We conclude that this is a lower-risk area in LBO loans.

Evidence for competition law risk or risk of sub-optimal outcomes in PF/INFRA segment

The extent of single MLAs and the importance of relationship banks

Our borrower fieldwork shows that the use of single MLAs in PF/INFRA transactions is less common than in LBOs, with only 11 per cent of borrowers and sponsors in our fieldwork report usually appointing just one MLA (compared to just under 30 per cent in LBO).[194] As with the LBO segment, such MLAs are very rarely appointed without a competitive process,[195] and therefore the risks associated with a directly appointed single MLA are unlikely to be extensive in this market (although cannot be ruled out).

Relationships between banks and borrowers/sponsors are also important in the PF/INFRA segment – around 30 per cent of sponsors engaged in PF/INFRA deals said they tend to approach the same lead bank(s) because their established relationship guarantees the most efficient loan.[196] In addition, 50 per cent of borrowers and sponsors said that all or most of the MLAs approached had a pre-existing relationship with the borrower, and 74 per cent said that the MLAs had a pre-existing relationship with the sponsor.[197] Out of all the sponsors engaging in PF/INFRA deals, 94 per cent that the existence of a relationship with the MLAs was either very or quite important when selecting MLAs.[198]

As with LBOs, the main advantages of appointing relationship banks are considered by these sponsors to be more competitive pricing on both the loan and on ancillary services, and a better response in the case of refinancing or default. This suggests that the appointment of relationship lenders is likely to be efficiency enhancing.

Repeat interactions and 'lock-in'

Our dataset shows that it is relatively rare for borrowers to engage in multiple syndicated loans in the LBO segments, at least within an eight year window. Table 13 in Chapter 3 shows that of the 870 borrowers in PF/INFRA loans, 90 per cent had only engaged in one deal in the period, with eight per cent and two per cent participating in two and three deals respectively. Therefore as with the LBO segment the risk of borrower 'lock in' discussed in the literature is low (as this relies in repeat loan transactions with the same borrower).

Repeat transactions between lenders and sponsors are more common, but not as much as for LBO segment. Table 15 in Chapter 3 shows that only 74 per cent of

[194] Fieldwork question S11/B9 "Thinking about your MLA appointments, which of the following usually applies?

[195] In response to the question: "Which procedure(s) do you usually follow when the MLA(s) are appointed in this transaction?" Only six percent of borrowers/sponsors typically appoint MLAs without a competitive process.

[196] Fieldwork question S4 "How would you describe your experience in selecting banks (e.g. lead arrangers) to lead syndicated loans?"

[197] Fieldwork question S10 / B8 "Thinking about the banks approached to act as MLA, please say whether all, most, some or none are..."

[198] Fieldwork question S41 "When selecting lead arrangers, how important is the existence of an existing relationship?"

sponsors in PF/INFRA deals had undertaken only one deal, with 14 per cent having undertaken two deals and only two per cent over five deals. Repeat transactions with sponsors are not likely to lead to an information 'lock in' effect as the underlying borrower would change from transaction to transaction and there would be no chance for a relationship lender to gain increasing information on a particular borrower, for example on its risk profile.

Safeguards related to the sophistication and control of borrowers/sponsors
The ability of borrowers and sponsors in the PF/INFRA segment to control the syndication process and the behaviour of the MLAs likely to be more variable than in the LBO segment, as these market participants are likely to be a more heterogonous group in terms of skills and experience than the private equity houses that dominate the LBO segment. This is evident in the very large proportion only engaging in a single syndicated loan transaction as shown in our data, and in the wide range of potential institutions including corporates, state-owned borrowers, construction companies etc.

Our lender fieldwork shows that PF/INFRA transactions are nevertheless controlled by borrowers and sponsors and that these have a direct say in the appointing of the syndicate banks, both lead banks and participants. This applies in terms of participants (i.e. the white list specified by the borrower/sponsor up front) and in terms of the loan shares allocated to participants - lead banks would usually suggest allocations but the final decision is taken by the borrower/ sponsor. This is supported by the borrower/sponsor fieldwork – of the borrower/sponsors in the PF/INFRA segment, 74 per cent said that either the borrower/sponsor (26 per cent) or borrower/sponsor together with MLA (48 per cent) had a role in determining the participating institutions for the syndicate. A greater proportion than the LBO segment however reported the MLAs as usually having the final say on participants (26 per cent compared to six per cent).[199] In any circumstances in which a single MLA *is* appointed it could be relatively more able to influence the selection of the syndicate in its favour, but this risk remains low in our view given the rarity with which a single MLA is appointed in the PF/INFRA segment.

The ability of borrower/sponsors to monitor and sanction MLAs
Our borrower/sponsor fieldwork shows that the ability of the borrower/sponsor to ensure that MLAs perform well during a transaction is less clear (although this applies to all MLAs and not just those that are appointed singly). Replacing MLAs that are not performing well does appear to be difficult, and a greater proportion of respondents in the PF/INFRA reported being dissatisfied with an MLA (60 per cent of respondents to the question compared to 45 per cent in the LBO segment). This included 24 per cent found it either too costly or contractually difficult to replace them, and 16 per cent did not have a suitable replacement.[200] Interestingly, a far greater proportion of PF/INFRA respondents said that the other MLAs and/or loan participants ensured the MLA performed adequately in the end (20 per cent compared to five per cent in LBO segment). The fieldwork did not explore the reasons for this dissatisfaction, which could include inability to successfully syndicate the loan, or other sub-optimal behaviour. Borrowers/sponsors have some control over the performance of MLAs through fees, which are contingent (to some extent) on the successful conclusion of the loan.[201]

[199] Fieldwork question S19 / B17 "Who has ultimate say on which institutions join the syndicate?"
[200] Fieldwork question S14 / B12 "Have you ever been dissatisfied with the performance of an appointed MLA during the formation of the syndicate? What actions did you take?"
[201] Fieldwork question S33 / B31: "How much, if any, of the MLA's fees are contingent on successful conclusion of the loan?" 93 per cent of borrowers/sponsors said fees were contingent to some extent, but only 16 per cent said "All" or "A large amount".

The evidence in the PF/INFRA segment of the safeguards that could mitigate the risks of a single relationship bank having undue influence on the loan process or terms is again mixed – borrower and sponsors in this segment retain control of the process and can exercise reputational pressure on the performance of MLAs, although practically disciplining them for underperformance during a loan is less widespread. The likelihood of having a single MLA in charge of the syndication process is lower in PF/INFRA than in LBOs. We conclude that this is a lower-risk area in PF/INFRA loans.

Post-mandate to loan agreement

Framework for competition analysis

At this stage the borrower has instructed the banks in the lead banking group to agree a single term sheet /loan agreement for providing the financing. That may include some element of underwriting (in which case, there would be a back-to-back general syndication of the loan). At this stage the lenders need to come together to agree all the terms of the loan (i.e. a single unified price on unified terms for a specified amount) and they do so with the express mandate of the borrower.

Accordingly joint meetings and discussions between the banks for the purposes of agreeing those terms are an essential element of the loan syndication process and provided that the banks are operating within the terms of the mandate granted by the borrower and their actions are designed to achieve that aim, then the loan agreement itself and the discussion and exchanges of information between them which are related to achieving that aim may fall outside Article 101(1) or alternatively benefit from an exemption under Article 101(3).

At this stage of the process banks may still be able to drop out of the syndicate (e.g. if they do not agree with all the unified terms being discussed), which may raise the risk of the loan terms moving against the borrower if, for example, certain banks require a higher price to remain in the syndicate and there are no other banks to take their place. This is not a competition risk per se, but rather a risk of a sub-optimal outcome for the borrower/sponsor which may be driven by the structure of the deal (e.g. if the borrower/sponsor stipulates that a certain lender must be part of the lending group and therefore needs to agree to a price that restructures the transaction or converges at the highest common denominator to ensure that all banks can participate).[202]

Information exchange at this stage may merit a slightly different approach to that pre-mandate. At the pre-mandate stage where the bids are still independent, information exchange between the lenders without the consent or knowledge of the borrower/sponsor would not be justified. However at this stage, where the banks have been put together and where the MLA(s) (and banks with other lead roles) have a mandate to secure the loan, a unilateral flow of information from one bank to other banks concerning its requirements for continued participation would need to be viewed against this changed context and accordingly may fall outside Article 101(1) or benefit from an exemption under Article 101(3), provided that the communication is no more than is required in the circumstances. In this situation (akin to the situation outlined in a consortium bid) banks must be careful not to go beyond what is required under the borrower's mandate and reach any agreement or engage in any concerted practice to (artificially) raise the price or to restrict supply. Any such agreement is likely to be viewed as anti-competitive by object.

A related risk at the post-mandate stage (or indeed any stage where the banks are brought together by the borrower) would be that repeat interactions among lenders on

[202] By 'highest common denominator' we refer to the highest price (say for a particular tranche within the loan) or most stringent documentation terms (e.g. nature of covenants around use of free cash flow by the borrower) required by a bank to remain in the syndicate.

transactions may lead to *inadvertent* information sharing, in that lenders might observe each other's behaviour or strategies and use this knowledge to align their bids in *future* transactions.

Potential safeguards

The necessity of bringing the banks together at this stage suggests that the key safeguards are those that govern the type of information that can be legitimately shared. These include:

- *The process for forming the lead banking group.* The information required to be shared during the post-mandate phase will depend on the process undertaken in setting up the initial banking group pre-mandate. If the borrower/sponsor negotiated the key terms of the loan (hold levels, pricing, covenants) with each lead bank bilaterally and signed a commitment letter and initial term sheet with each before bringing them together at the post-mandate stage, then there would be no scope for the banks to agree to fix the pricing and move against the borrower.
- *The involvement of the borrower/sponsor in post-mandate discussions.* All discussions between the banks at this stage should be in line with the mandate, and the outcomes of discussions between the banking group should be communicated to the borrower/sponsor to avoid the risk of anti-competitive information sharing. The involvement of the borrower/sponsor at this stage in controlling the process would be key.
- *Adoption of appropriate strategies by borrowers/sponsors.* One concern highlighted above is that a bank could drop out of the syndicate during the post-mandate discussions of terms and increase the risk that the loan terms move against the borrower. The lenders would have seen due diligence materials at this stage and have the necessary internal approvals around the credit decision (this is part of the final offer made pre-mandate). This should make the risk of such an event low, but this can be further mitigated by the borrower/ sponsor employing strategies that factor in redundancy into the process – e.g. by requesting a commitment by each of say five banks to underwrite one-third of a loan (which would build in N+2 redundancy, in that two lenders could be lost without affecting the transaction's viability or causing a re-opening of negotiations.
- *The frequency of interactions.* In relation to the risks of strategic information being inadvertently shared between the lead banking group members, this could be governed in part by the nature of the process (i.e. by ensuring that there is no need for banks to discuss pricing or hold levels at this stage). The frequency with which the lead banks work together on transactions in the same market will also influence their ability to use any strategic information in an anti-competitive way, e.g. coordinating offers or limiting supply in the future – the more frequent this interaction the more sustainable collusive behaviour would be, as it is easier for participants to monitor the behaviour of each other and to deter deviations from the coordinated agreements.

Evidence and analysis

Evidence for competition law risk or risk of sub-optimal outcomes in LBO and PF/INFRA segments

The process of forming the lead banking group and borrower/sponsor control

The key safeguard influencing the sharing of information and the potential for collusive behaviour among the lead banks as they are brought together in the post-mandate stage is the process used to form the lead banking group and agree terms. In both LBO and PF/INFRA segments, the usual process is for borrower/sponsors to negotiate bilaterally with the lead banks and to control the process such that the key terms are agreed with each bank before the group is put together. Our lender fieldwork shows

that the joint discussions post-mandate are limited to agreeing the loan documentation and syndication strategy.

However, our lender fieldwork does show that in some cases the borrower/sponsor will bring the banks together to discuss the loan terms ahead of signing the final agreement (a few cases like this were provided in the PF/INFRA segment in our lender fieldwork. There does not appear to be any systematic reason for this, rather it is based on the preference of the borrower/sponsor). This could be more likely where the loan is sufficiently bespoke for there to be few benchmarks or precedents such that the borrower/sponsor must discuss and agree the terms with multiple banks rather than bilaterally.

Adoption of appropriate strategies by borrowers/sponsors
Our fieldwork indicates that the adoption of such strategies (i.e. building in a degree of redundancy into the process in case of lenders dropping out) was a normal ambition amongst borrowers/sponsors. In such cases where the agreements between lenders and the borrower/sponsor have already occurred pre-mandate, then the pricing and participation levels will be reasonably well set – this is typically the case in LBO loans and is also common in PF/INFRA loans (as shown in the process description, for example the grid approach adopted by borrower/sponsors). However, if such strategies are not adopted then terms may move against the borrower/sponsor during the post-mandate phase. However, the borrower/sponsor still retains bargaining power through (a) creating some redundancy by approaching many banks and (b) the ability to restructure the loan if the terms move unfavourably.

Our fieldwork shows that in the majority of cases borrowers/sponsors negotiate a common price with the syndicate and are not obliged to agree to a price at the highest common denominator – only four sponsors and no borrowers stated that they set the price at the highest common denominator amongst all propositions to secure the necessary volume.[203] This shows that there is the possibility that the structure of the loan means that the sponsor must agree to a price that is high enough to satisfy all lenders in the syndicate.

Risks from repeated interactions between lenders
There are a number of factors that influence the risk of lenders working together on multiple transactions. First, the larger the number of lenders eligible to bid for a loan, the less chance there is of the same lenders making up the whole lending group on multiple transactions to enable collusive behaviour. As described in Chapter 3, the data show that in the LBO segment there are a large number of eligible lenders to fulfil this role – over 300 lenders were involved in at least one LBO transaction in at least one country during the course of 2010-2017, with around 46 'highly active' lenders being involved in a deal every other month. A similar result is obtained for PF/INFRA, where around 370 lenders had participated in a syndicated loan. This shows that there is a large pool of lenders such that having (all) the same lenders on a deal is unlikely.

That said, there is a smaller set of lead banks that dominate the league tables *across* the six sample Member States in our study. Around 12 in the LBO segment and eight in the PF/INFRA segment are in the top 20 banks across the sample, (although their positioning in each Member State's league table depends on whether the bank is a local bank). Therefore it is highly likely that these banks meet each other on a number of loan transactions across the Member States, although the syndicates would be made up of other banks too (e.g. local banks and other less prominent international banks) such that the likelihood of repeated 'closed' interactions would be very low.

[203] Fieldwork question S28/B26 "How is the final price of the loan typically negotiated per tranche?"

The potential exception would be in markets with a relatively small pool of eligible lenders, such as PF/INFRA in a non-Euro/£ market – such as Poland in our sample, or other smaller, national markets across the EU. The fieldwork shows that the process of MLA appointment adopted by borrowers/sponsors could involve either sometimes or regularly sharing the identities of those banks approached with the other MLAs (this was most commonly cited in Poland, although small sample sizes prevent us from drawing and statistically significant conclusions).[204]

We have considered data on the composition of the MLA groups across Member States to further explore the issue of multiple interactions. The figure below shows that there are a number of examples of MLAs appearing on the same deals together multiple times. The highest number of deals where two of the same banks are present is in Spain (89), representing 60 per cent of the deals that the first bank has undertaken. High results are also seen in the Netherlands and (at least for the most common pairing) in Poland. This shows that banks can work together on multiple deals, although the presence of other banks on each deal will also be a factor.

Figure 41: Deals with the same two banks, 2010 - 2017

Spain

Banks in same deal	Number of deals together	% of Bank 1 deals	% of Bank 2 deals
A + B	89	60%	49%
B + C	64	36%	61%
D + B	59	61%	33%

France

Banks in same deal	Number of deals together	% of Bank 1 deals	% of Bank 2 deals
A + B	50	45%	40%
C + B	45	30%	36%
B + D	43	34%	50%

UK

Banks in same deal	Number of deals together	% of Bank 1 deals	% of Bank 2 deals
A + B	45	36%	39%
B + C	40	34%	35%
A + C	39	31%	34%

Netherlands

Banks in same deal	Number of deals together	% of Bank 1 deals	% of Bank 2 deals
A + B	25	76%	56%
B + C	22	49%	73%
A + C	20	61%	67%

Germany

Banks in same deal	Number of deals together	% of Bank 1 deals	% of Bank 2 deals
A + B	17	43%	27%
C + B	17	38%	27%
C + D	15	33%	44%

Poland

Banks in same deal	Number of deals together	% of Bank 1 deals	% of Bank 2 deals
A + B	6	60%	60%
C + B	3	27%	30%
C + A	1	9%	10%

Source: Thomson Reuters Loan Connector database analysis.

There may be a number of reasons for repeat interactions between the same banks across deals. The role of local clearing banks is one, whereby most deals in a Member State would include at least one of the local banks in order to secure cash management services. Repeat interactions are likely to be more common in the PF/INFRA markets, which as we have seen in previous chapters remain relatively more bank-dominated (in the absence of non-bank investors) and where our fieldwork

[204] Just under 60 per cent of respondents in Poland said that the appointment process sometimes required this, compared to 45 per cent of respondents in the UK, and under 30 per cent in other Member States. The proportions incorporating this disclosure into their standard process was much lower, not exceeding 20 per cent. In general, sponsors were less likely to disclose such identities than borrowers.

suggests specific expertise may be in more limited supply in certain project areas (e.g. a different set of banks might participate in renewable energy projects than in civil construction). Certain banks may also work more frequently with similar sponsors/advisors (e.g. if the latter approach the same banks over time if they know they are likely to agree to similar terms and facilitate a more efficient process).

The data do not show whether such multiple interactions are 'engineered' by MLAs in order to facilitate collusive agreements. However, the fact that they occur presents the risk of tacit collusion between lead banks through observed behaviour and strategy. As discussed the large number of eligible banks able to participate in deals reduces the risk that the same banks are the only ones present in a deal and this reduces the risks of tacit collusion, but there may be circumstances where this risk is more pronounced (i.e. in smaller markets with a stable, limited pool of eligible banks).

General syndication phase

Framework for competition analysis

In this section we consider competition issues in the appointment of further syndicate participants in the general syndication phase, and in the negotiations between syndicate members. These issues are relevant to underwritten and best effort deals where there is a general syndication phase (as opposed to club deals) and therefore the LBO segment is most relevant here.

The issues relating to market flex, which is a feature of the general syndication phase, are dealt with separately in the following section given the complexity of this topic.

Bargaining power of the syndicate

In an underwritten syndicated loan the intention of the lenders is to, at least in part, lay off their exposure through inviting a wider group of lenders to participate in the loan (in contrast to club lending where the lending is multi-bank but the initial group of banks intend to retain the loan themselves). Other investors, including both banks and other non-bank lenders will be invited to participate on the terms agreed between the initial bank group.

In so far as the banks are operating within the borrower/sponsor's mandate, then provided that such terms have been determined in line with a competitive process which has not been undermined by any actions of the banks, and the differing lenders are not connected to each other, then the process of inviting other investors to participate on the basis of the agreed terms should fall outside Article 101(1) altogether or alternatively benefit from exemption under Article 101(3) on the basis that it is inherent to securing the financing.

It has been noted in some market commentaries that the syndicate as a whole during the general syndication phase may use its bargaining power as the single (joint) provider of the loan to coordinate negotiations and move against the borrower/sponsor when agreeing final terms. This will depend on the process used to develop and agree loan terms – i.e. if this is done between the lead banking group and the borrower/sponsor *before* the general syndication phase, then there will be little scope for the wider syndicate to influence the loan terms beyond what is permitted in the flex provisions (flex is discussed later). It will also depend on the scope for the wider syndicate members to interact with each other – if their participation is limited to bilateral discussions with the bookrunners about their participation in the loan, then the ability of the syndicate to coordinate its response to the loan terms will be limited.

The selection of participant lenders

If MLAs are able to influence the selection of other banks into a syndicate, this could facilitate collusive behaviour by enabling reciprocity. Reciprocity is a practice whereby lenders make agreements between themselves in return for future business. This could include agreements to artificially limit the supply for a loan in return for a certain share in a future loan, or agreements for one bank to award loan shares to another in return for the latter awarding the former loan shares in the future. The FCA's investment banking market study considered reciprocal arrangements whereby a bank issuing its own financing might award mandates to another bank in part based on return business.[205] Reciprocity may cause competition concerns by facilitating collusive behaviour (such as agreements to limit supply) or by aiding foreclosure by restricting the ability of other lenders to compete in the market.

Reciprocity is only possible if lenders are able to influence the selection of other banks into a syndicate (e.g. through influencing the composition of the white lists drawn up by borrowers/sponsors) – this will depend on the process adopted by the borrower/sponsor for selecting the lead banking group and wider syndicate participants. For example if the borrower/sponsor retains control over which participants are included in the general syndication then the certainty that lenders will have of being able to provide reciprocal loan shares to each other in future transactions will be undermined.

Further, the impacts of reciprocal behaviour will also depend on the nature of the syndicated loan process and wider market. For example, in the case of agreements to limit supply in return for future loan shares, the ability of the colluding lenders to influence the price and loan terms would be limited by the presence of other lenders willing to provide lending capacity at a market price. If the loan terms are agreed between the lead banking group *before* the general syndication phase, then an MLA's influence over the selection of general syndicate members would have a limited impact on the loan terms.

The ability of other lenders to compete for loan shares would also affect the outcomes of reciprocal behaviour. In the case of potential foreclosure, the FCA found that although reciprocal behaviour was identified between banks issuing their own financing, there was no evidence that this practice excluded other banks from competing for and winning such mandates, and thus the risks of foreclosure were not considered to be sufficient to warrant further analysis or the proposal of remedies.

Information asymmetries between the MLAs and participant investors

Syndicated lending can create an asymmetric information problem between senior and junior syndicate members if the MLAs have an informational advantage over the syndicate participants (e.g. by having access to better information about the borrower and loan risks prior to the general syndication phase). MLAs could exploit this advantage for economic gains by not sharing all the relevant information about the loan and borrower with the participants during the general syndication phase, for example to present a risky loan in a more favourable light in an attempt to sell down loan shares more successfully (e.g. more quickly for the borrower, with no need to invoke market flex and pay away underwriting fees) and justify its underwriting and bookrunning fees. MLAs might also exploit information asymmetries by retaining a lower share of the risky loan and selling down a larger share to less informed participants.

An extension of this risk may arise if an MLA had any links with certain participant investors (e.g. reciprocal agreements or some form of common ownership), such that

[205] See the UK Case Law summarised in Appendix 5g for further commentary on this.

these participants also had an informational advantage over competing syndicate members.

The level of information asymmetry will depend on how the information on the loan and borrower is shared between the MLAs and the syndicate participants. If borrowers/sponsors have oversight of what information is shared with participants during the general syndication phase and agree that what is shared is sufficient to enable accurate market appetite and pricing, then this will reduce the risk of MLAs exploiting any informational advantages they may have.

In addition, the degree to which the participant investors rely on the information shared by the MLAs will also affect the outcome – if they undertake their own due diligence, ask for more information where they perceive gaps and/or are in contact with the borrower/sponsor then this reduces the risk of the MLAs manipulating the information flow.

The transparency with which information is shared between the MLAs and participant investors is also relevant. Mechanisms to ensure that all participants receive the same information at the same time (such as electronic information portals) will reduce the risk that some participants are better informed than others.

Use of 'lead left' bookrunner
As described in Chapter 2, a single 'lead left' active bookrunner can be appointed from the lead banking group to lead the general syndication process and engage with the market. Whilst the use of a lead left by borrowers/sponsors can be efficiency enhancing, it may lead in time to the restriction in the number of eligible bookrunners for future transactions, and thus raise the risk of sub-optimal loan outcomes (i.e. raise the risk of a situation in which a small number lead left bookrunners could abuse a position of excess bargaining power).

This is due to the fact that the ability to be an effective active bookrunner depends on a bank's experience in distributing similar loans, its knowledge of and relationship with the investor market, its understanding of market appetite and how to communicate and potentially flex a deal to ensure its success. If there is a trend towards appointing sole lead left bookrunners, this could ultimately reduce the pool of eligible active bookrunners to a few very large banks, with other MLAs increasingly losing bookrunning experience.

Although the use of single 'lead lefts' is borrower/sponsor (and advisor) driven, it may eventually undermine competition in the market for active bookrunners and leave the borrower/sponsors with less choice of eligible banks to fulfil this role.

Potential safeguards
The following safeguards could be applied to reduce the risks of anti-competitive information sharing or coordination and sub-optimal outcomes.

- *Process and timing for agreeing loan terms.* If loan terms are agreed among the lead banking group *before* the general syndication phase, then the risk that the general syndicate uses bargaining power to move against the borrower is reduced. Further, the separation of participant lenders would further reduce the risks of coordinated behaviour.
- *Exercise of control over ultimate participation in the syndicate.* If the MLAs do not have a strong influence over which lenders are included in the general participation phase then their ability to engage in reciprocal agreements is limited.

- *Ability of other participants to compete for / participate in the loan.* The risk of foreclosure raised by reciprocal arrangements is reduced if these agreements do not prevent other lenders from competing for or participating in syndicated loans.
- *Control over information-sharing with participants.* If borrowers/sponsors have oversight of the information shared with participant investors this will reduce the risks of MLAs manipulating this information flow. Similarly, mechanisms to ensure that participants receive the same information at the same time will reduce risks of information asymmetry between participant investors. Vertical separation (e.g. through compliance practices) between MLAs and participant investors with whom they have links (e.g. through common ownership) will also serve to mitigate this risk.
- *Use of alternative single bookrunners.* If borrowers/sponsors do not use the same small number of banks to act as sole lead lefts then the number of eligible banks will be more sustainable.
- *Ability of banks to gain bookrunner experience.* If banks are able to gain bookrunner experience and enter the lead left market then the risk of a restriction in supply is reduced.

Evidence and analysis

Evidence for competition law risk or risk of sub-optimal outcomes in LBO and PF/INFRA segments

Bargaining power of the syndicate

The key safeguards identified against the general syndicate acting jointly and using its bargaining power to move against the borrower/sponsor are upheld to a large extent in practice. First, our fieldwork with participant lenders shows that these engage in the syndication process once the loan terms have been negotiated and agreed between the lead banking group and the borrower/sponsor. Whilst the participants advise the bookrunners of their appetite for the loan and can push back on terms/pricing they don't agree with, they do not negotiate terms with the bookrunners together with other participants – indeed participant lenders stressed the existence of NDAs as a pre-condition to them receiving information about the loan. (Bookrunners gather information from individual participants and only if there is a sufficient shortfall in appetite might the bookrunners then invoke flex provisions, discussing these with the borrower/sponsor and other MLAs rather than with the participants. The rules governing flex provisions are set in the initial loan terms and not open to negotiation at the general syndicate phase.)

Our borrower fieldwork does show some scope for the negotiation of terms during the general syndication phase – 13 borrowers (26 per cent) said that loan terms can be re-negotiated during the general syndication phase, compared to 74 per cent who said that the loan terms were finalised before general syndication.[206] This revision of terms may refer to market flex, but it is possible that some broader negotiation does take place during the general syndication phase.

Second, our fieldwork shows that participant investors do not interact with each other to discuss the loan terms and thus the scope for them to coordinate their actions is not facilitated by the loan process. Bookrunners engage bilaterally with participant investors, and the large number of such investors in the market also restricts the opportunities for coordination.

[206] Fieldwork question B18 "the final syndicate is formed. What is the typical process for negotiating the terms of the loan (fees, margin, covenants, adverse situations) where there is a main group of banks involved and further participant lenders?"

The evidence suggests that while the risk of the general syndicate coordinating their behaviour to move against the borrower cannot be eliminated – as some negotiation of terms during this phase is possible – the likelihood of this risk is low given the large number of investor participants and the way in which these engage with the bookrunners during the general syndication phase.

The selection of participant lenders

The evidence from our fieldwork indicates that MLAs do have some influence in selecting the participant lenders as part of the general syndication phase. Whilst the evidence presented in Chapter 2 on the loan process shows that the scope for MLAs to influence the selection of other MLAs is very limited (this process being led by the borrower/sponsor),[207] MLAs do have some scope in deciding which banks join the wider syndicate. Our borrower/sponsor fieldwork shows that 18 per cent of borrowers and 10 per cent of sponsors said that the MLAs have the ultimate say on which institutions join the general syndicate (compared with 82 and 90 per cent respectively who said that either the borrower/sponsor alone has the decision or the borrower/sponsor decides together with the MLAs).[208] Therefore there is at least the possibility that MLAs might engage in reciprocal agreements when including lenders in the general syndicate. This is exacerbated by the fact that, although the final loan allocations are generally overseen by the borrower/sponsor there is no exact 'science' to allocating loan shares across participants, such that it would be possible for a bookrunner to favour certain participants (subject to the sign off by other MLAs and the borrower/sponsor).

The risk that lenders could use reciprocal arrangements to influence the loan terms is low but still present, based on the fact that these terms are most often, but not always, agreed between the lead banking group and the borrower/sponsor before the general syndication phase (as shown in the process described in Chapter 2 and supported by our lender fieldwork). However, our fieldwork shows that around 26 per cent of borrowers say that loan terms can be re-negotiated during the general syndication phase (74 per cent said that the loan terms were finalised before general syndication).[209] Whilst this may refer to market flex provisions (which are difficult to manipulate as discussed in the following section), in cases where terms are negotiated with the lead banking group *and* the wider syndicate (and not just among the lead banking group), then there is scope for the MLAs to influence the selection of participant banks with a view to sustaining coordinated agreements or facilitating reciprocity. Given the extent to which terms are agreed before general syndication we do not consider this risk to be significant.

The use of white lists by borrowers/sponsors is a way for them to control which lenders can be approached to participate in the loan. Our lender fieldwork shows that these lists are long (often with hundreds of potential investors) and do not restrict the ability of the bookrunners to find suitable investors to participate in the loan. This shows that there are a large number of potential lenders who are approached and who could participate in the loan, such that the risks of potential foreclosure resulting from any reciprocity are low. Our interviews indicated that other the recent past sponsors

[207] Our fieldwork shows that borrowers and sponsors appoint the MLAs themselves, either directly or through a competitive process – see question S8/B6. The possibility remains that relationship banks who are advising borrowers/sponsors may influence the selection of other MLAs – this is discussed earlier in this chapter.

[208] Fieldwork question S19 / B17 "Who has ultimate say on which institutions join the syndicate?"

[209] Fieldwork question B18 "the final syndicate is formed. What is the typical process for negotiating the terms of the loan (fees, margin, covenants, adverse situations) where there is a main group of banks involved and further participant lenders?"

had become more relaxed about the inclusion on white lists of non-bank investors vertically integrated with other sponsors.

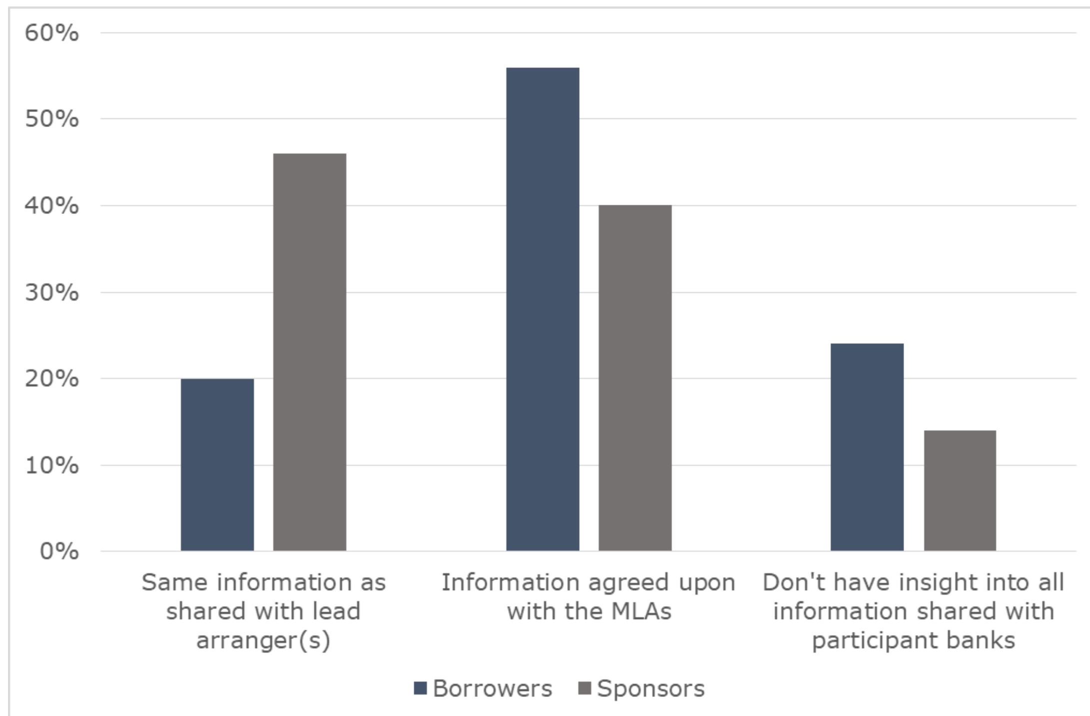
Information asymmetries

The first safeguard reducing the risk of information asymmetry is the oversight that borrowers/sponsors have regarding the information shared with participant investors by the MLAs and bookrunners. Our lender fieldwork shows that the sell-down phase is commenced by the MLAs producing an information memorandum collectively with the borrower/sponsor setting out all the terms of the transaction, and containing information about borrower creditworthiness, investment considerations, a list of terms and conditions, an industry overview, and a financial model.[210] Throughout the process of engaging with participants, more information is released as investors demonstrate continuing interest in the loan.

Our fieldwork shows that borrowers and especially sponsors retain close control over the flow of information to potential participants in the loan, as shown in the figure below. This information is mostly either the same as that shared with the MLAs, or it is agreed with the MLAs. This oversight is not across the board however – 24 per cent of borrowers and 14 per cent of sponsors do not have insight into all the information that is shared with participant investors. However, the extent to which this may lead to participant investors not receiving sufficient information is not known – e.g. borrowers and sponsors may have oversight at least of the most relevant information shared to enable investors to make correct decisions about their participation in the loan (i.e. that fact that borrowers/sponsors do not have complete oversight is a risk but does not provide evidence for information manipulation).

[210] As described in Chapter 2, there may be both a private and public version of the IM. The private version would include management forecasts whereas the 'public' version would not. The motivation for the public version is to enable those investors not wishing to wall-cross to (at least initially) consider participation based upon this document to avoid being brought prematurely onto the private side in way that might restrict ability to trade any securities associated with the offer.

Figure 42: Information sharing in general syndication phase



Source: Analysis of YouGov surveys of borrowers and sponsors, QS20/B19b

The timing and manner of distributing information to participants is another safeguard. Our lender fieldwork shows that a number of lenders make use of information portals – in particular Debt Domain – to share information among syndicate participants. These portals have the advantage of making the information sharing transparent, and ensuring that participants receive the same information at the same time. The use of Debt Domain is widespread (e.g. publicity from 2013 specified over 150 lead arrangers and agents using it to communicate with participants) but not necessarily used for all transactions.

Our fieldwork also provides some evidence for a further safeguard, in terms of the reliance of participant investors on the information provided by the MLAs and bookrunners. Participant lenders undertake their own due diligence as well as reviewing information received by the MLAs. Participant investors in LBO and PF/INFRA loans are sophisticated (large institutional investors with internal debt teams, CLO managers etc.) and decisions to participate in loans are passed through credit committees with strict requirements about information. These investors will also look at comparable information from internal deal flow or publicly available sources (including but not restricted to any comparable deals recently closed in the primary market or any recent secondary market activity), and they are able to request further information from bookrunners if they perceive there to be gaps in the information necessary to decide on their participation. In addition, once the loan has closed then all syndicate members (MLAs and participants alike) receive the same information about the progress of the loan, and any attempts to manipulate information in the general syndication phase will be noticeable, including any movements in secondary market pricing (i.e. after the loan is closed). Our examination of secondary pricing data (described in Chapter 3 in the section on secondary trading) shows there is no evidence of secondary loan pricing deviating significantly from par in the recent months after the loan close.

The above evidence suggests that the risk of MLAs exploiting information asymmetries cannot be eliminated - in that the various safeguards do not apply fully across the market - but that the risk is likely to be small. There is some evidence to suggest that there may be scope for MLAs to manipulate the information shared with participant inventors outside of borrower/sponsor oversight, and transparent document sharing portals cannot be assumed to be used across the board. However, given the ways in which participant investors gather and use information when deciding on participating in deals, their sophistication and the fact that mis-priced deals would be detectable after loan close, we do not consider the risk of the exploitation of information asymmetries to be significant.

The use of a lead left bookrunner
The use of lead left bookrunners was raised in our lender fieldwork by a small number of lenders (six out of 37). The view was that the use of a single lead left bookrunner is an increasing trend, but only in certain loan types (e.g. where a single message to the market is most helpful, or where the borrower/sponsor prefers to work with only one active bookrunner). The magnitude of this trend is not possible to estimate for the available evidence, but it remains a potential concern for the evolution of the market.

Our fieldwork indicates that in many cases where a borrower/sponsor appoints a lead left bookrunner they will also appoint a 'lead right' which would be another MLA shadowing the lead left and ready to take over if necessary. This provides in part a safeguard against the lead left practice resulting in only a few banks capable of undertaking this role.

In addition, at least one lender described how it had transitioned successfully to such lead left roles in the space of a few years, which implies that the market for lead left roles can be entered and mitigates against the risk that borrowers/sponsors are left with a restricted choice for these roles. The magnitude of this risk going forward will depend on the extent to which borrowers/sponsors use left leads in their transactions, and the ability of individual banks to enter into this market.

General syndication phase - Flex

Framework for competition analysis

In this section we consider the negotiations between syndicate members, with particular reference to flex (which can be market or documentation flex). Flex is a contractual feature used only in underwritten transactions. In line with the description in Chapters 2 and 3, this means that this analysis is currently of greater relevance to LBOs (but such flex clauses would not of necessity vary between PF/INFRA and LBO loans, i.e. the clauses are driven by the choice of distribution channel).

The flex terms are negotiated as part of the mandate in an underwritten transaction. The borrowers/sponsors also need to agree that the process around how flex is triggered should be set out clearly in advance by the relevant parties.

The main competition policy risk would be around any discussions between the MLAs on whether the flex should be triggered and any changes, which fall outside the agreed mechanism and where they do not reflect a direct reporting back of the outcomes of the approaches made to potential investors. There is scope for a breach of Article 101 if the bookrunners and underwriters discuss using the flex to increase the price in circumstances where the finance could in fact be raised without such

action being necessary or if they agree to go above a level that is necessary to secure the financing. These actions would be anti-competitive by object.[211]

As we note in Chapter 2, the borrower pays all costs, including for the banks' lawyers. This has resulted in sponsors and borrowers choosing the lawyers to be used by MLAs/banks. This feature may limit negotiating power of banks in terms of finalising documentation pre-general syndication. This could result in a greater incidence of documentation flex (stemming from feedback from the institutional investors approached). Even with such documentation flex, this market feature could mean that loan documentation standards are weaker than optimal.

Potential safeguards

The main safeguard is to ensure that t*he details of the flex mechanism and the process to be followed need to be agreed between borrower/sponsors and the book-running banks.* After that, the flex process as agreed by the borrower has to be followed, with no communication between lenders concerning the operation of the flex outside of that agreed process.

A further safeguard against the abuse of market flex are the economic disincentives on the bookrunners to use flex unless absolutely necessary.

[211] 'Upward flex' is an increase in the spread relative to LIBOR, or other market interest rate, and is made when the loan margin is too low to clear the market. 'Reverse flex' is the opposite, and involves a decrease in the spread which occurs when the loan is oversubscribed and the market clearing spread is lower than the original spread.

Evidence and analysis

Evidence for competition law risk or risk of sub-optimal outcomes in LBO and PF/INFRA segments

The inclusion of flex can be seen as enabling underwriting banks to be more aggressive in developing their offers, in that it provides a degree of flexibility should their reading of the market sentiment be overtaken by events. As we note in Chapters 2 and 3, the book-runner(s) control the marketing process. On the other hand, the borrowers/sponsors obtain regular feedback (characterised by lenders as every few days over a marketing process that would last 2-3 weeks). Investors provide feedback to the MLAs (essentially 'yes', 'no' or 'yes, if X changes'). It is the MLAs' analysis of the third of these that is most critical in the instance of flex (i.e. what needs to be changed to increase participant uptake). In the YouGov survey, borrowers and sponsors provided brief feedback on the marketing and flex processes. Several cited (unprompted) the transparency of the process, none criticised it on these grounds.

In addition, communication channels exist between the investors marketed to and the sponsors (particularly the private equity sponsors) – i.e. the process should not be a wholly 'black box' for the sponsors. On the minority of deals where a sponsor is absent, this particular check would likely be missing.

Any flex provisions are agreed in the contract signed by the MLAs with the borrower/sponsor. This is supported by our lender and borrow fieldwork, as well as in industry standards (such as LMA documentation and the Association of Corporate Treasures guidance on the LA documentation). (In current market conditions, some sponsors push to exclude flex provisions.[212]) Once negotiated into the contract, the use of flex is 'automatic' in that the bookrunners are free to use it if they feel it is necessary to the success of the syndication process, within the bounds set by the flex clause and provided the contractually agreed criteria have been met. In other words, the MLAs do not require further consent from the borrower/sponsor.

However, before market flex can be activated, MLAs would have to 'pay away' fees (either 25 or 50 basis points of the underwriting fee being cited by lenders). Such a fee pay-away acts as a disincentive for bookrunners to activate flex (or abuse it in order to change the economics of the loan to their advantage). Bookrunners also have reputational incentives not to abuse the flex provisions (i.e. that their initial reading of the market was not correct). MLAs can instead take the debt onto their balance sheets, seeking to sell it in the secondary market. However, if they are unable to then sell that debt at or near par, this has been shown to limit future arranging capacity.[213]

It is possible for borrowers/sponsors to agree to changes to the terms outside of the flex provisions. For example, bookrunners may recommend changes to documentation outside the scope of any documentation flex as a means of successfully syndicating the loan rather than using pricing flex. Borrowers/sponsors may well agree to this, which does potentially allow bookrunners some scope to secure changes in terms outside of the agreed flex provisions. In these cases, fees payable are also part of the discussion as to what aspects of the loan need to change, and the reputational incentives still apply. MLA(s) would need to demonstrate that the syndication cannot be successfully concluded on the original terms.

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[212] Around 10 per cent of sponsors/borrowers stated that they resisted inclusion of any flex provisions. This was a feature of the market also cited by many lenders. No lenders admitted to taking on underwriting mandates without some flex provisions.

[213] Bruche, M, Malherbe, F and Meisenzahl, RR (2017) "Pipeline Risk in Leveraged Loan Syndication".

In the fieldwork, 42 borrowers/sponsors had recent experience of flex with 93 per cent expressing satisfaction with the outcome of the process. Those that were dissatisfied were disappointed by the degree of movement from the terms (particularly documentation terms) that they had initially agreed and the terms that were eventually settled upon. (Lenders indicated that, where in place, documentation flex would not involve any economic penalty – i.e. documentation flex – within its contractual boundaries - could be effected without incurring the pay-away of fees).

Given the feedback loop when a sponsor is present, the nature of the pain-sharing agreements between borrower and MLAs, the reputational impacts of perceived over-reliance on flex and the inclusion of negotiated flex clauses (when it is applicable) in loan agreements (as described by lenders participating in our fieldwork), we consider the scope for bookrunners to use market flex to increase the pricing of a loan without good reason to generally be low. Where a sponsor is not present, this risk would be less.

In the EU market the borrower pays for the costs of the syndication process, including the banks' lawyers (this can be compared to the US for example where the banks pay for their own legal costs). A minority of lenders and institutional investors raised the point that borrowers/sponsors influence the selection of the lawyers used by the banks, potentially opening the door for borrower-friendly negotiations particularly around documentation (for example, covenants which place fewer restrictions on the borrower's future behaviour around e.g. taking on new debt or paying dividends). In an underwritten transaction, this may be partially tempered by institutional investors that seek to push back on the documentation as part of the general syndication phase. Some market participants expressed the view that leveraged deals experiencing documentation flex is the result of borrower/sponsors pushing documentation precedents to (or beyond) the limit. However, in our view, the overall effect of this market feature does look likely to be a contribution towards declining documentation standards, i.e. loan documentation containing sub-optimal creditor protections.

Ancillary services

Framework for competition analysis

As with the other elements of the loan process, we note here that the European Commission has not taken a position on what is falling within/outside the scope of 101(1) and/or what could be exempted under 101(3) as regards ancillary services in this area, and this discussion is based on our own assessment. "Ancillary" services in addition to the main loan facility may be provided by syndicate banks. These might include services directly related to the loan (such as hedging services) or activities such as cash management which are related to the activities being financed rather than the loan itself. The provision of ancillary services may be part of the initial competitive pitch by individual banks, and would be assessed alongside the main terms of the loan. Where the ancillary services were not pre-agreed, then the ability of the borrower to 'shop around' would be the key determinant of a competitive outcome. There may be a potential issue around collusion should the lending banks come together and decide how they might divide ancillary business between them.

Lenders may require, as a condition of the loan, that the borrower puts in place certain related services - such as hedging instruments - and include restrictions as to who can provide the services (e.g. that it must be lending bank(s)). Provided that the services in question can be considered to be directly related and necessary to the provision of the loan (as opposed to services that may be required by the borrower but are not connected to the loan itself, such as future M&A advisory activity) then the requirement of the lenders that the borrower purchase such services is unlikely in

itself to give rise to competition concerns. The conditions attached to the requirement may also be considered as directly related and necessary for the transaction or may not appreciably restrict competition (e.g. because there are a substantial number of lending banks who could compete to provide the service).

The conditions attached to the requirement may (exceptionally) also fall outside Article 101(1) altogether on the basis that they are directly related and necessary for the transaction or that they do not otherwise appreciably restrict competition. We note that whether there is an appreciable restriction on competition may depend on the number of participating banks who could provide the service. Where there are many lending banks it is unlikely that a restriction requiring that the related services be purchased from a lending bank would appreciably restrict competition. Alternatively, if the condition does appreciably restrict competition it may satisfy the conditions of Article 101(3). Any determination in respect of Article 101(1) and Article 101(3) requires an analysis of the restriction within its specific context – for example consideration of the purpose of the condition.

However there is a risk that, in an individual bid scenario, banks discuss and/or agree between themselves prior to making their bids that they will each make the provision of certain other services a requirement of their lending (as opposed to each individually responding and – independently - making this a condition of their participation).

Agreements between the lending banks and the borrower/sponsor relating to the fact that certain banks will supply certain related services *may* fall outside Article 101(1) altogether or benefit from the Article 101(3) exemption. Notably, similar considerations that apply to the setting of a single price and a single term sheet in respect of the provision of the lending may not apply to the provision of the ancillary service. Furthermore, there is a risk (again in an individual bid scenario as opposed to a situation where the borrower has requested a joint bid/single price) that the practice of agreeing a single price and term sheet in respect of the provision of the lending "spills over" into the provision of related services. In contrast to the provision of the syndicated lending it is not necessarily the case that the setting of a single price by a group of banks providing the related service is inherent to the provision of that service and the banks may be able to compete to provide such services on an individual basis. Similarly, there is a risk that the lenders jointly require that the borrower purchase services from them that are unrelated to the loan and in respect of which they can compete individually.

As we note in Chapter 2, MLAs can seek to make the award of connected services, such as hedging, one of the conditions attached to the provision of the loan. Potential risks around the provision of hedging services include the discussion among banks in order to share out the services between them and/or coordination on pricing, and uncompetitive bundling of the services with the initial loan terms which restricts the choice of borrower/sponsors.

MLAs can seek to make the award of future services one of the conditions attached to the provision of the loan. Such future services can range from leading any bond issuance undertaken to replace a bridging loan, to providing future M&A or IPO advisory services.

Potential safeguards

There are a number of potential safeguards that could be adopted which could reduce the abovementioned risks. Safeguards could be undertaken by the borrower/sponsor or the lenders.

- *Borrower clarity as to those required services that are to be considered directly related to the loan – and those that are not.* Banks generally compete separately for the provision of related services. Therefore guidance could be provided on the type of services that are likely to be related to the provision of the loan as opposed to those that are extraneous and which therefore the lenders should not generally (jointly) require be purchased from them.
- *Borrower clarity as to services required – and not required.* The borrower can seek to influence this by specifying which other services are required and which services are not required. If the RFQ specifies a particular approach, that approach should be respected by the banks.
- *Borrower clarity as to services needed for the loan.* The cross-sale of ancillary services needs to be carefully managed (or even avoided) in order to limit the risk of impairing competition conditions in neighbouring markets to that of syndicated loans, such as agreements on the provision of future M&A or IPO services.

Evidence and analysis

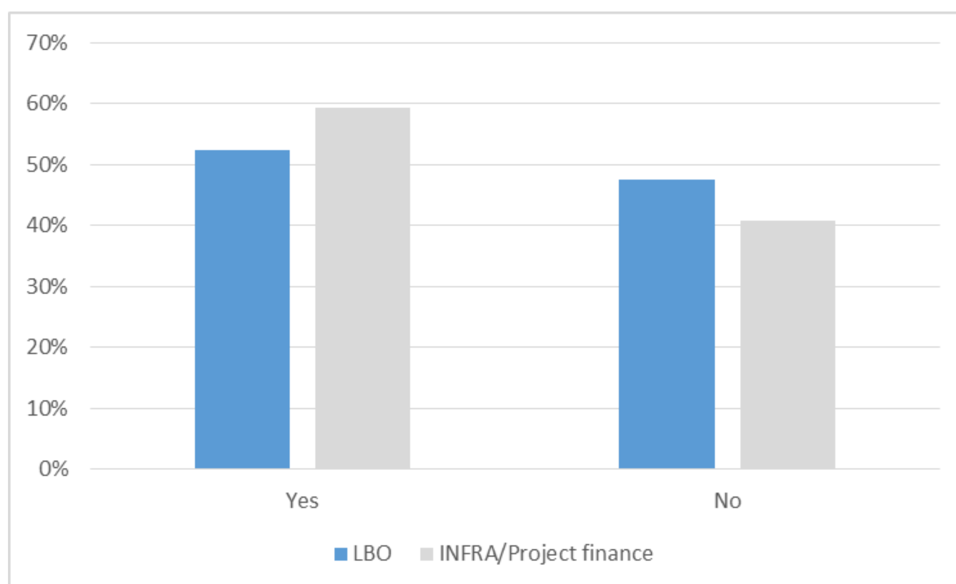
Evidence for competition law risk or risk of sub-optimal outcomes in LBO and PF/INFRA segments

As we set out in Chapter 2, various ancillary services are commonly acquired in conjunction with the loan, being:

- Hedging services, i.e. derivatives or other instruments to hedge against interest rate and/or FX exposure.
- Custodianship and/or collateral management services.
- Cash management services.
- FX services, i.e. foreign currency transfer and conversion.

The discussion of such ancillary services with MLAs is relatively commonplace in syndicated lending (and slightly more so in PF/INFRA than in the LBO segment).

Figure 43: Proportion of borrowers/sponsors negotiating with MLAs/syndicate about ancillary services

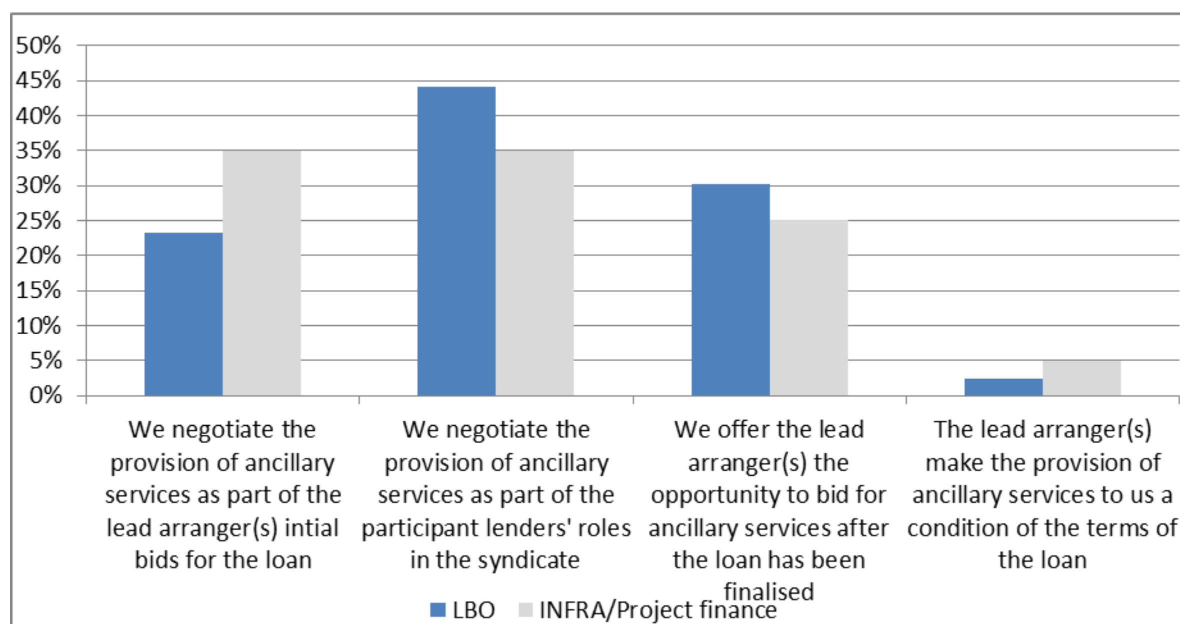


Source: YouGov survey of borrowers/sponsors.

Our focus here is on *how* those ancillary services are negotiated between borrowers/sponsors and lenders. The chart below focuses only upon those borrowers

or sponsors that acquired ancillary services, revealing that in the vast majority of cases (albeit not all), negotiation was either in parallel with the negotiations for the loan or else was part of a separate (implicitly competitive) process post-closure of the loan negotiations.

Figure 44: Provision of ancillary services connected to the loan



Source: Analysis of YouGov data, based upon a count of responses from 54 borrowers/sponsors. NB Respondents were not restricted to one response (since different ancillary services could be negotiated using different processes) – therefore the above chart does not sum across all categories to 100 per cent.

This is in line with past analysis based upon the US market where Christenfeld & Goodstein (2013) state "it is not unusual for loan syndicates to require that a derivative be purchased from a member of the lending syndicate" or else for the members be given the opportunity to compete for such services.[214]

Spain's Comisión Nacional de los Mercados y la Competencia's (CNMC's) investigation into the coordination by various Spanish banks into how interest rate derivatives were priced on various syndicated loans related to project finance in Spain in the period 2006–2016,[215], found that it was not possible to conclude on the unlawfulness of the fact that the banks forced clients of the syndicated loan to contract the coverage against the risk of interest rates with the same banks. On the other hand, the CNMC also considered it the case that the banks had failed to demonstrate that it is *essential* that derivatives are entered into by the banks party to the loan – indeed, the CNMC finding that such a requirement was disproportionate (additional analysis of this case is included at Appendix 5f). We consider such a feature as raising the risk of a borrower/sponsor achieving a sub-optimal outcome. We further note that all of the respondents that cited such provision being a condition of the loan were from Spain.

We note that sponsors (and by extension those deals with a sponsor) are much more likely to offer syndicate members the opportunity to bid for ancillary services after the finalisation of the loan terms, with almost 80 per cent of sponsors making use of that approach (making it the most likely approach adopted by sponsors). Borrowers were

[214] Christenfeld & Goodstein (2013) "Analyzing antitrust issues in lending" *New York Law Journal*, Volume 249 — No. 108, Thursday, June 6, 2013.

[215] Please see analysis at Appendix 5f and https://www.cnmc.es/novedades/2016-04-07-la-cnmc-incoa-expediente-sancionador-contra-banco-bilbao-vizcaya-argentaria.

more likely to roll the negotiation of the provision of ancillary services into the discussion around the loan itself.

As identified in the competition framework above, the MLAs making the provision of an ancillary service a condition of the loan's provision is not in itself problematic. In our lender fieldwork, the only ancillary service identified as at all likely to be discussed at this stage is the arrangement of hedging, e.g. a hedging letter could be agreed during the pre-mandate stage whereby an agreement to split hedging between all or some of the MLA banks is made. The lender fieldwork indicated that this is, at present, a feature of the PF/INFRA segment but not the LBO one. In addition, where banks agree with the borrower/sponsor the share in the future hedging of the loan during the initial stages of the process, there is more scope for them to discuss pricing and other strategic information and engage in collusive behaviour. In the CNMC case the banks took concerted action aimed at setting the price, above market prices, of the derivatives used as hedges for the interest rate risk associated with syndicated credits including in PF between 2006 and 2016. The banks communicated with each other, before the conversation with the client, to agree on a floor above the market level.[216]

Another form of coordination at play here is potential cooperation between banks in executing hedging arrangements. In the lender fieldwork, it was claimed that it was normal for hedging services to be delegated by the MLAs to 1–2 banks for execution of the hedging in the market place (on efficiency grounds, e.g. reducing transaction costs). Again in the Spanish case, the CNMC considered that some coordination between lenders was necessary firming up the price the prior agreement of the banks, completely unknown to the client, was an infringement of competition law– (please see elaboration in Appendix 5f).

More generally, the competitive dynamics related to the provision of ancillary services will depend on the way in which these are negotiated and awarded, particularly timing of when the services are discussed and awarded (e.g. in parallel to the loan being negotiated or after the primary loan has been concluded or as part of the negotiation of the initial loan terms), the process under which the services are allocated (via competitive bids from banks or allocated directly by the borrower/sponsor) and whether there is any limitation on bidding to syndicate members or whether they only have the opportunity to bid alongside other market participants.

When ancillary services are included in the initial competitive pitch by prospective lenders and negotiated before the borrower/sponsor has committed to the loan, then this need not raise concerns provided that the borrower/sponsor is using a competitive process (as noted, RFPs are applied by 93 per cent of borrowers/sponsors in the YouGov research) and the borrower/sponsor is sufficiently sophisticated to assess the offers made in order to determine its preferred terms. The problem, as in the CNMC case, was the prior agreement of the banks, completely unknown to the borrower, which is an infringement as it enabled the banks to eliminate the uncertainty resulting from an autonomous action under market conditions, to know the offers from the rest of banks beforehand and to illicitly agree on a price that is more beneficial for them. The conduct had a negative effect, through price fixing, on the quality of the derivatives, i.e. the value of the coverage for the client was negative instead of "at zero cost" as agreed. Clearly, in this case, the borrowers were not able to adequately

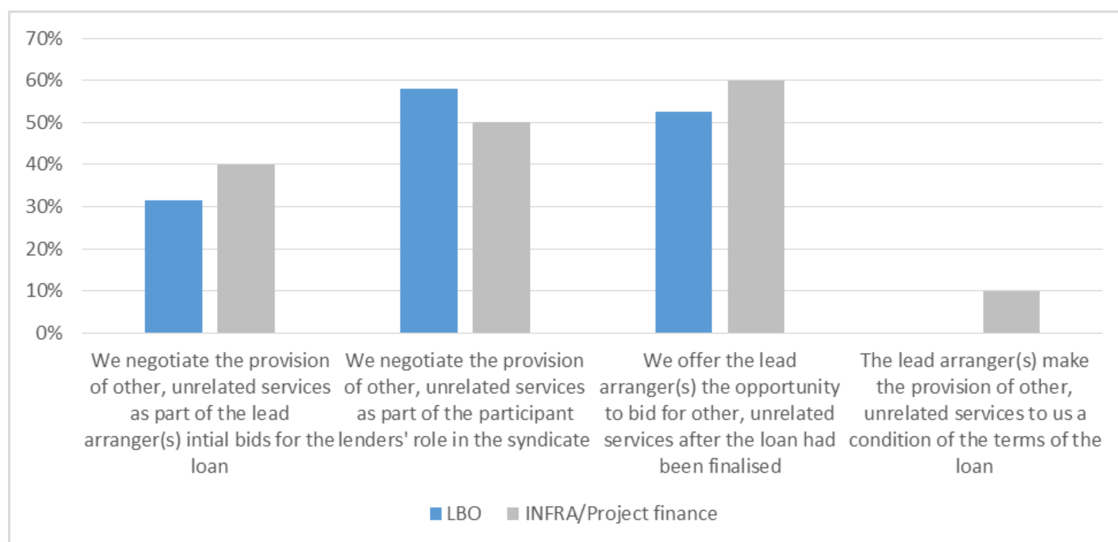
[216] The Spanish Competition Commission CNMC issued a decision imposing a fine on four of the largest Spanish banks for having agreed to fix the price of interest rate derivatives in the context of syndicated loans from 2006 to 2016. Case S/DC/0579/16 Derivados Financieros.

assess the terms presented to them.[217] This may be exacerbated in markets where the initial pool of lead banks is small.

It would also be possible for local banks, though, to establish a degree of market power in connection with services ancillary to loan where the service is (a) to be provided by a local lender, and (b) the provision of the service is restricted to within the MLA pool. On the other hand, any desire to bring in a local clearing bank into the syndicate (i.e. without including it in the competitive RFP process to act as MLA) to provide commercial cash management services is unlikely to affect the competitive dynamics of the loan itself (although where these services are awarded to an 'incumbent' local bank without a competitive process, then this could of course lead to sub-optimal results).

Ancillary services not directly related to the loan
The lenders can also seek to bundle services not directly related to the loan into the loan negotiation. This was considered a relevant feature by 35 per cent of the borrowers/sponsors participating in our research, i.e. (unsurprisingly) fewer than with ancillary services connected to the loan, but a substantial fraction.

Figure 45: Provision of ancillary services not connected to the loan



Source: Analysis of YouGov data, based upon a count of responses from 35 borrowers/sponsors. NB Respondents were not restricted to one response (since different ancillary services could be negotiated using different processes) – therefore the above chart does not sum across all categories to 100 per cent.

A broad mix of services were covered, but particularly focused upon (a) activities connected to further financing (e.g. around replacing a bridging facility), (b) advisory services and (c) investment research. In each case, 50–60 per cent of borrowers/sponsors cited each of these as types of ancillary service that had been provided to them.

As can be seen from the above, in most instances negotiation of the bundled service was part of the loan negotiation. Our lender fieldwork confirmed this, with lenders indicating that terms (including fees) would be part of the discussion at that time. The lender fieldwork also indicated that both "right of first refusal" and "right to match" clauses were in use. As we have described in Chapter 2, the UK's FCA formed a

[217] For example in the Spanish derivatives cartel case, the majority of clients included small and medium corporations, although larger corporations were also affected, including some very large borrowers.

view[218] on the utility of such clauses, determining that "right of first refusal" clauses that effectively prevented the client subject to the right from accepting offers from third parties and failed to identify any client benefit in them – with the important exception of services related to taking out a bridging loan. The FCA has banned the use of such clauses, except when relating to bridging finance, by regulated firms operating in the UK (irrespective of the client's location).

Both borrowers and sponsors referenced investment research as a service that could be bundled together with the loan negotiation. One further aspect for consideration here is the scope for a conflict of interest for the sponsor. Specifically, whether such investment research related to the borrower of the loan in question or to other existing (or potential) investments relevant only to the sponsor. This is, unfortunately, a level of detail that our research was not able to drill down to. Even so, we believe that the potential conflict here should be considered by sponsors to ensure that any such benefits arising due to the loan syndication process accrue exclusively to the borrowers to avoid sub-optimal outcomes arising.

Debt advisors

Framework for competition analysis

We have described in Chapter 2 how borrowers and sponsors may use debt and financial advisors in order to assist with all or part of the loan syndication and/or to provide advice on the adequacy of the terms secured. These advisors can provide expertise and/or additional resources to borrowers/sponsors. We note at Chapter 2 how it is a feature of the PF/INFRA segment in particular that such advice can be sourced from a lender that may also participate in the syndicated facility (including as an MLA).

Clearly, this market feature could give rise to significant conflicts of interest, potentially – if those conflicts are not well-managed - undermine the competitive nature of the syndication, and result in sub-optimal outcomes for the borrower/sponsor.

Potential safeguards

Potential safeguards are as follows.

- *Capacity of the borrower/sponsor to make own judgements as to outcomes and/or to have access to other advisors.*
- *Training and policies for relevant staff.* This could cover identification and management of conflicts of interest, clarity as to duty of care to provide neutral advice to clients.

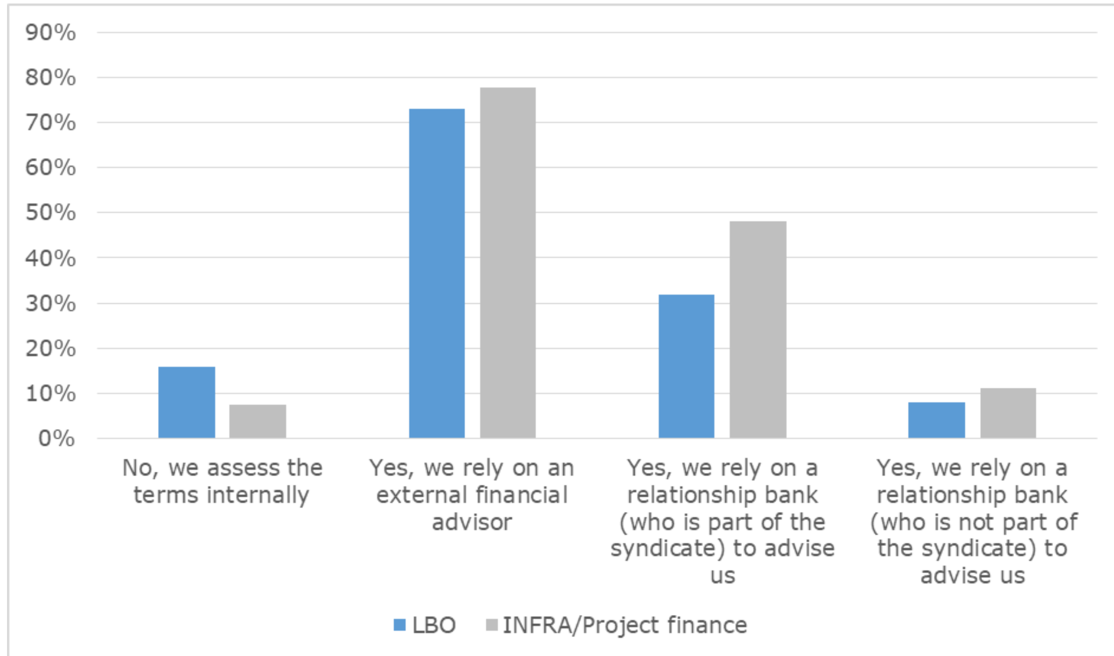
Evidence and analysis

Evidence for competition law risk or risk of sub-optimal outcomes in LBO and PF/INFRA segments

We describe below the comparative use across the LBO and PF/INFRA segments of external advice in assessing loan terms. (We described at Chapter 2 the same data analysed by borrowers and sponsors). This highlights how the vast majority do make use of external advisers to complement in-house knowledge (and internal resources can be highly sophisticated, but this may not apply across the board). Some borrowers/sponsors may make use of more than one of these forms of advisor.

[218] FCA PS17-13 "Investment and corporate banking: prohibition of restrictive contractual clauses", https://www.fca.org.uk/publication/policy/ps17-13.pdf.

Figure 46: LBO and PF/INFRA assessment of loan terms



Source: Europe Economics and YouGov fieldwork. B29/S31 "Do you usually receive any external aid in assessing the terms of the loan?"

Amongst the PF/INFRA segment sponsors/borrowers, 15 per cent had a relationship bank who is part of the lending group as an advisor – without any other source of external advice. The equivalent proportion was about 8 per cent in the LBO segment. Similarly, borrowers were much more likely to have a bank that was also part of the syndicate as the sole source of external advice (14 per cent of borrowers against 8 per cent of sponsors).

Where the borrower/sponsor is using a bank to provide debt advice (i.e. assessing how satisfactory the terms of the loan are) and securing debt from that same bank, there is potential for conflict. The analysis above, drawing on the views of sponsors and borrowers, indicates that this issue is more common in the PF/INFRA segment (but it is not non-existent in the LBO segment) and could represent a non-negligible fraction of transactions. This accords reasonably well with the views expressed by lenders in our interview programme.

Several of the lenders that we engaged with have such 'in-house' advisory teams in the PF/INFRA segment. In all cases where a lender had such a debt advisory team, it was functionally separate to the origination/syndication lending decisions. These banks were well aware of the potential conflict of interest. For example, the advisory unit would have no independent balance sheet capacity, and once mandated would be the other side of a Chinese wall from the origination and syndication units. Processes were described to us around the advisory teams having a duty of care to clients, such that the advice offered would be neutral with regard to debt products and the providers of those. Adherence to such protocols would mitigate the risk of sub-optimal outcomes to borrowers of not having a demonstrably independent advisor.

However, our lender fieldwork indicated that at least a couple of the banks interviewed do adopt a more relaxed take on the 'bundling' of such debt advice and the provision of debt to clients. There can be an expectation from the client that a substantial portion of the lending would come from the bank providing the advisory services,

particularly if raising the necessary funds for the deal proves difficult. For this reason, at least, such bundling by the bank could be an attractive feature to some borrowers/sponsors, at least for more marginal credits (because it would provide a cornerstone lender early in the process). (It could even be argued that, at least in current market conditions, such a pro-bundling strategy could result in adverse selection problems for the bank). However, there is also clearly scope for a sub-optimal outcome for the borrower. Bundling can be pro-competitive, but the way in which the advisory firm is appointed would then also be important. This could either be through a competitive process (e.g. RFP) or else the sponsor/borrower can approach the advisor directly. There would be a heightened risk that, where an advisor is appointed directly without a competitive process and combines the lending role with the advisory role, that the borrower/sponsor may not receive the best loan outcome.

A different form of concern would be where the advising bank attempted to influence the borrower/sponsor towards a strategy or debt structure that suited its lending arm, i.e. subverting the Chinese wall between the advisory and lending functions, and with this not being fully apparent to the borrower/sponsor. Based upon the description of their policies for managing such situations given to us by lenders, this would represent a significant breach of internal protocols.

Secondary loan market trading

Framework for competition analysis

Whilst co-ordination between the lead banking group to enable a successful syndication process is inherent to that process, co-operation post syndication could give rise to competition law risks. For example, if underwriting banks were to co-ordinate (subsequent to any coordinated sell-down agreed as part of the original loan negotiations with the borrower/sponsor) in relation to when to sell, what proportion to sell or at what price to sell the debt in the secondary market such co-ordination is unlikely to be justified and could be anti-competitive by object. In these circumstances the consent of the borrower to such activities would not be relevant as the borrower has already received the financing at the price agreed. In these circumstances the potential harm is to the purchasers of the debt in the secondary market.

In addition, as noted in Chapters 2 and 3, borrowers/sponsors can place restrictions on transfers on loans that may limit liquidity in the secondary market, potentially (but not necessarily) resulting in sub-optimal economic outcomes. The slowness of settlement processes could increase transaction costs, with equivalent consequences. The latter issue is discussed further at "back office inefficiencies" below.

Potential safeguards

There are a number of potential safeguards that could be adopted which could reduce the abovementioned risks to competition. Safeguards could be undertaken by the borrower/sponsor or the lenders.

- *Guidance and training.* This could cover not only the formation process but also ongoing co-operation between the lending banks post syndication and specifically highlight the risk of co-ordination in relation to secondary market activity.
- *Appropriate restrictions on post-closure sale by MLAs.* There may be a view that some co-ordination might be justified (as per equity markets) for a short period of time after the syndication. However, a borrower could also require that the underwriters hold a proportion of the debt for a period of time post syndication to avoid disruption - which would appear to be the legitimate way for the borrower to protect its interests, rather than co-ordination between the underwriters.

Evidence and analysis

Evidence for competition law risk or risk of sub-optimal outcomes in LBO and PF/INFRA segments

Our fieldwork indicates that hold levels are a wholly standard part of discussions between borrowers and MLAs/syndicate participants. Such hold levels may be time- or tranche- limited (e.g. in the LBO market, lenders will hold revolver facilities – as investors have no appetite for these – but may sell most or all of other tranches).

The only form of co-operation post syndication identified in our lender fieldwork (other than in connection to restructuring, as discussed in the next sub-section) relates to the coordinated sell down of debt post-close. This occurs in a short time-frame, within 2-3 months of closure, i.e. it is not sustained over the course of the loan.

The potential harm is to the purchasers of the debt in the secondary market. One of the key limitations in secondary trading is that the loans are private – the loan documentation contains commercially sensitive information about the borrower and thus is subject to strict confidentiality agreements. One implication is that only a limited number of market participants have access to all the relevant information at any one time. Lenders and investors stressed that the secondary market in loans remains in essence a caveat emptor market, i.e. the buyer needs to conduct its research carefully before the trade date. The buyer can seek information (under NDA) before that date, with the ability to ask for additional information to complete research before finalising the trade. In instances of distressed debt (i.e. where the value is not at or near par), this may even involve buying a small part of a loan in order to access additional information on the borrower before deciding whether (or not) buying more of the loan represents an attractive opportunity. Investors look at other loans (e.g. using data from recent primary market activity as well as any comparable secondary market trades) and other asset classes to assess the value proposition represented by a loan's pricing (i.e. investors are not under an obligation to buy a particular loan).

These features should act as limitations on any attempt by sellers to manipulate the price of the debt, unless they are able to simultaneously identify unsophisticated buyers of debt. However, as in any market, a significant overhang of supply, even if temporary, could potentially disrupt price formation.

We described (at Chapter 3) how the USA's secondary market "unambiguously lowers borrowing costs" in the primary market. We were not able to confirm that finding in our analysis of the less developed secondary market in Europe. It is also evident from the fieldwork with sponsors and borrowers that restrictions can be imposed on secondary trading (please see Chapter 3).[219] Equally, we were informed by lenders that the restrictive clauses in the LBO market tend to be based on LMA standard (i.e. borrower consent, not to be unreasonable withheld). As we have noted several times, secondary trading in PF/INFRA loans is significantly less (i.e. more banks adopt a take and hold strategy) than in the LBO segment. In our fieldwork, lenders stated it could even take 'months' to conclude a transaction in PF/INFRA from when interest in trading was expressed. The lenders described restrictions imposed by PF/INFRA sponsors/borrowers as potentially including: no small transfers; an embargo during the construction period and the transfer being subject to borrower approval (except in case of default). Whilst such restrictions may be reasonably motivated (e.g. restricting

[219] Parties must be made aware of any such restrictions in the loan documentation regarding to whom loans can be transferred (by novation) or assigned. There is generally less of an issue where the 'sale' is to be by way of participation, although occasionally credit documentation does impose restrictions on participations as well as transfers and assignments.

the dispersion of deal-specific information), these could limit the development and efficiency of the secondary market (at least at the margin). Given that secondary market pricing data are also used in the primary market, this could also affect the development and efficiency of the primary market.

Default and refinancing

Framework for competition analysis

Where current lending banks are aware that further lending opportunity is in contemplation, e.g. where there is a repeat financing, or refinancing, event – there is a risk that the banks commence discussions about the future lending opportunity prior to an RFQ being issued in circumstances where they may be competing for a role in the future lending. This would apply in both a voluntary refinancing (i.e. because the borrower believes that either its circumstances and/or market sentiment have changed sufficiently materially to motivate starting such a process) and also in an 'involuntary' refinancing where the borrower is on a pathway to default.

As we discussed in Chapters 2 and 3, as and when a borrower is in financial difficulties and faces an event of default, then there is a risk that the group of lending banks might together enjoy some sort of market power in that they jointly have the power to behave to an appreciable extent independently of their competitors and the borrower. This would be because the relevant market could then be defined very narrowly as the options available to a borrower may be very limited. This needs to be balanced against the needs of borrower for new capital.

There is a further risk that the lending banks together impose certain conditions on restructuring which are not objectively justified (e.g. to protect their investment or reflect a higher degree of risk in any restructuring). This could involve tying the purchase of other services to the refinancing and imposing excessive prices as a condition to the lending. In such cases, it cannot be excluded that these actions could constitute a breach of competition law.

Voluntary refinancing would not result in additional competition concerns over and above an initial syndicated deal. In PF/INFRA, lenders described how such a voluntary refinancing in the operational phase of a project is typically arranged following the standard syndication process with potential MLAs bidding for roles in the initial lending group and general syndication taking place after the agreement of loan terms. It is the reserve of the borrower whether to seek out such a process, and to agree (or not) to the offer. Therefore, we focus here only on default and restructuring.

Potential safeguards

There are a number of potential safeguards that could be adopted which could reduce the abovementioned risks to competition. Safeguards could be undertaken by the borrower/sponsor or the lenders.

- *Competition law guidance or training for banks about information exchange issues.* Tailored training and guidance could be put in place for the relevant functions within banks. In banks, management of portfolio loans will generally be separate from the origination function. The guidance on how to treat customers in a distressed situation would take into account the potential risks identified above.
- *Regulatory regime and banks' duties to clients.*

Evidence and analysis

Evidence for competition law risk or risk of sub-optimal outcomes in LBO and PF/INFRA segments

Where a bank is seeking to refinance at a certain (higher) price level, it should in the first instance discuss this with the borrower. If the borrower then instructs the bank to speak to other banks, the price level can be discussed among them. Any discussions between banks should be within the consent of the borrower.[220] Any discussion of key terms among the lenders ahead of such a refinancing would be analogous to MLAs sharing information ahead of submitting their competitive bids in the original syndication – i.e. clearly in breach of competition law and not necessary as part of the syndication process. We interviewed several restructuring teams based in lenders (as we have noted previously, these are functionally separate units), and these all professed to having undertaken some form of competition policy training, i.e. safeguards are used here.

An alternative available to a member of the syndicate is to decide to sell its loan share, based upon its analysis of declining credit (syndicate members naturally have regular access to performance data on the borrower and the loan). This would be determined independently and not discussed with other lenders (indeed, there is an incentive for lenders not to have such discussions, as these could impact price). If the potential buyer is on any pre-existing 'white list', the borrower would not need to be notified in such circumstances (although the lenders indicated that such notification was standard practice).

Syndicated loans are not financial instruments, and (provided the borrowers are private companies) fall outside the scope of the Market Abuse Regulation. Owners of the loan may have access to material non-public information, and this emphasises the importance of research and due diligence by potential buyers in what remains essentially a caveat emptor market. (Although we have noted at Chapter 3 that the draft NPL regulation could impact upon this.) However, such a transfer of a loan would not affect the fact of the syndicate being in existence (simply changing its composition). We do note, though, that the entry of additional lenders beyond the initial syndicate can complicate the resolution of problems. In particular, distressed debt funds (so called "vulture funds") are widely seen by both banks and borrowers/sponsors as potential disruptors of negotiations. (We understand from our fieldwork that such funds are often excluded from the 'white lists' with this motivation in mind.)

Once there has been a breach in the loan contract, or with the permission of the borrower, a committee will be formed amongst the lenders and vested with a degree of negotiating power. Discussions and negotiations of key terms typically take place between the borrower/sponsor and this committee representing the lenders in the syndicate. Decisions are ultimately taken either unanimously among lenders or by a majority (e.g. 75 per cent). A greater degree of collaboration between lenders is needed in restructuring compared to an initial loan formation, as the borrower/sponsor will not be negotiating bilaterally with individual banks. Whilst this may be efficiency enhancing as time is often pressurised, it equally enhances the risk of banks exercising some form of excess bargaining power. Again, we note that the bank restructuring teams that we interviewed had undertaken some form of competition policy training but clearly any subversion of the proper process would be problematic.

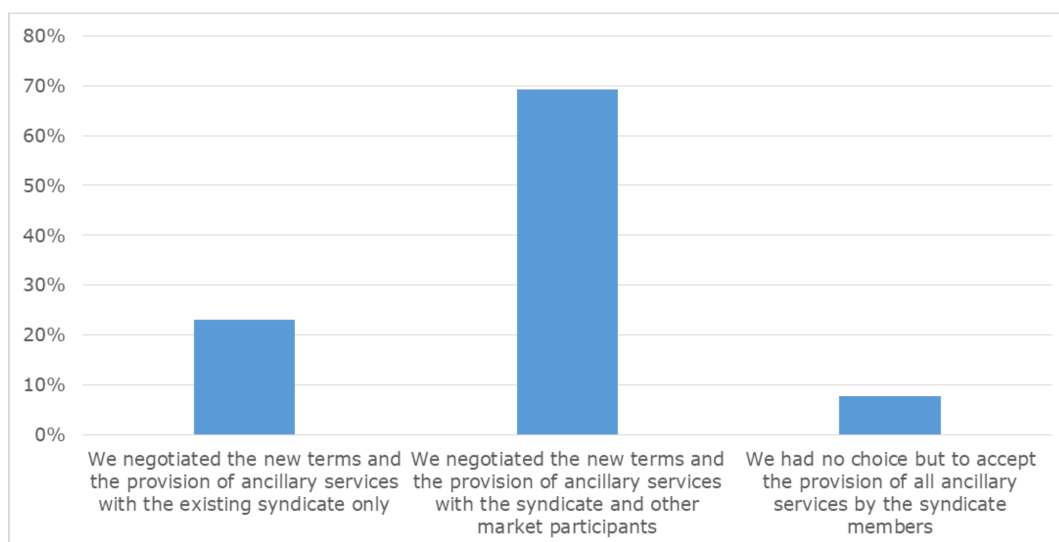
[220] Bretz, Oliver (2015) "Competition law and syndicated loans: identifying the regulatory risks" http://www.jordanpublishing.co.uk/system/froala_assets/documents/1553/CLJ_article_-_Comp_Law_and_Syndicated_Loans.pdf.

When restructuring works well, borrowers/sponsors work closely with lenders (in particular relationship lenders) to reach an agreement on mutually agreeable terms to avoid a default and/or keep the project/ business a going concern. That said, the lenders would have a legitimate need to protect their investment and terms must by necessity be negotiated jointly. It is also reasonable to expect the pricing to be higher than on the original loan as the credit risk has changed.

We investigated with borrowers and sponsors past experience of any required refinancing entered into or even of default. About one quarter of the sample (N=26) had some such past experience (not necessarily connected to current borrowing). In 38 per cent of these cases, negotiation was conducted only with members of the then syndicate, whereas in the balance (62 per cent) the refinancing negotiations were conducted with a mix of the existing syndicate members and other market participants. The willingness of the market to provide the new finance can be seen as a limit upon any excess bargaining power that the existing group of lending banks may have – on the other hand, there are a significant number of instances where the existing syndicate is the only option, i.e. there is scope to exert market power. We do emphasise, however, that we do not have evidence for its abuse.

A further dimension in this area relates to the potential for lenders to seek to exploit any market power through the bundling in of ancillary services as a condition of refinancing, or, even more baldly, through effecting the loan on 'punitive' terms (e.g. pricing excessively). The bundling in of additional services at the stage of involuntary refinancing would pose a competition concern as, unlike in the original syndication process, the borrower/sponsor would have little choice but to accept. We therefore investigated the basis of negotiation of any ancillary services (such as hedging) alongside the new loan terms, with results as presented below.

Figure 47: Negotiation of loan terms and ancillary services in restructuring



Source: YouGov survey of borrowers/sponsors, N=26.

As can be seen in Figure 47, in the majority of cases (almost 70 per cent), such negotiations also included other market participants. This should provide market discipline in those instances. However, it is also apparent that in a substantial minority of cases such negotiations took place only with the syndicate members. As with the restructured loan, there may be mitigating circumstances at work here – i.e. the absence of other market participants in the negotiations may be reflective of time constraints or else that market appetite outside the existing syndicate was expected to

be low. However, it is also clear that such distressed circumstances can create the opportunity to price such ancillary services on non-competitive terms.

Back office inefficiencies

Framework for competition analysis

Certain back office processes in the syndicated lending market are slow and/or inefficient. The focus of attention in our fieldwork has been on how KYC requirements are processed, and how settlement is handled. These factors increase transaction costs and potentially even reduce secondary market activity in consequence: the result would be potentially sub-optimal economic outcomes.

We investigated whether technology (in particular blockchain) could improve efficiency. A blockchain is a digital, distributed transaction ledger, with identical copies maintained on multiple computer systems controlled by different entities. Once entered into a blockchain, information can never be erased. Loans could be stored as smart contracts in the blockchain, together with the collateral ownership information.

With respect to the primary syndicated loan market, blockchain and smart contracts might allow for a syndicated loan to become a digital asset. In this scenario, the borrower, arranger and lenders would agree on the terms of a credit agreement, which would then be coded and entered on the blockchain. An arranger would broadcast that "smart loan" with public keys[221] of pre-authorized syndicate institutions. Only those institutions can accept or negotiate terms by broadcasting signed amendments for the arranger to approve. The arranger would accept or reject those conditions and sign the final loan commitments with its digital signature. That signing would cause the borrower's collateral to be assigned to syndicate members and for funds to be disbursed from syndicate members to the borrower (i.e. automating a process that is currently manual). The "smart loan" would automatically debit funds from the borrower's account and simultaneously extinguishes loan liability in the blockchain. Because permissions can be set to make the blockchain only available to some, as ownership of the loan changes, those permissions would change in turn. The existence of the loan as a digital asset would obviate the need for each institution to manually create the loan, and instead, could be automated on the blockchain.

Smart contract technology could benefit the borrower consent process, which could be completed on the blockchain, which could additionally facilitate secondary trade activity. Because blockchain requires that every network participant is represented by a digital identity, a token representing a party's approved information and creditworthiness could be stored on the blockchain.

A further claim for blockchain technology is that it could decrease the amount of time needed for clearing and settlement processes, which usually takes up to 20 days. It has been claimed that Distributed Ledger Transactions (DLT) could reduce this to about seven days by providing a secure database that all participants share across a distributed private network. This could yield immediate savings by reducing manual reviews, data re-entry and systems reconciliation.[222] It could also alleviate the hurdles imposed in LBOs by time constraints, considering that the average time required to

[221] Public key cryptography is the way that members in the blockchain identify themselves. Public and private keys make up a blockchain participant's digital signature.

[222] See e.g. FinExtra (2017) "Banks drive ahead with blockchain project for syndicated loans market" https://www.finextra.com/newsarticle/30366/banks-drive-ahead-with-blockchain-project-for-syndicated-loans-market/blockchain.

complete a transaction is roughly 60 days.[223] A faster settlement window in syndicated loans would reduce the difference between loans and bonds. Investors might be attracted to loans that are senior to bonds, but are currently put off by how long loan trades take to settle.

Additionally, proponents of the blockchain argue that it could enhance the secondary market for syndicated loans. Agent banks exert control in the secondary loan market over where assets trade, where the associated data sits and how customers receive it, and when two organizations trade a loan, they choose between them where it settles. One bank believes that the cost for participants in managing the whole life-cycle of a syndicated loan from origination to pay-off on blockchain could be up to 50 per cent below current trading costs.[224]

Savings might also come from reduced trade reconciliation cost, lower fees paid to third-party servicers and elimination of associated jobs handling settlement. A commercial DLT platform might charge half what current platforms charge with the added benefit of reduced reconciliation checking and clean data delivered in electronic form.

It is likely that widespread adoption is a pre-condition of applying blockchain technologies, since the first-mover banks may not have sufficient capacity or risk-appetite. This implies a degree of cooperation between (competing) banks in order to progress adoption. It also raises the risk that adopters could seek to sustain any associated advantage at the expense of late adopters.

Evidence and analysis

Evidence for competition law risk or risk of sub-optimal outcomes in LBO and PF/INFRA segments

There are two main barriers to the potential benefits described above, namely the development of the technology itself, and the potential of blockchain to overcome the real sources of inefficiency in the market.

The development of the technology

The first relates to the development of the technology. Whilst some banks have begun working on blockchain and associated (i.e. smart contract) technology and its application to loans, this is still in the early stages and is only beginning to be considered for syndicated loans.[225] One issue is the bespoke and flexible nature of the loans (which is a key benefit of syndicated lending). In order for, say, smart contracts to be created and executed, standardized forms and procedures would have to be adopted. Increased standardisation may not be appropriate for all deals – indeed at present it is not thought appropriate by the banks we interviewed for LBO, PF and INFRA loans. (PF/INFRA loans in particular are not likely candidates to benefit from smart contracts – the complexity and illiquidity of the loans means that this would add fewer benefits in terms of efficiency or time-savings whilst secondary activity remains quiescent and this may mean that the technology would not be investigated seriously.) This may even create potential for fragmentation of the market (between those 'simpler' deals suitable for standardisation, and the rest) may itself limit the appetite to adopt smart debt contracts.

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[223] Evidence suggests that the average period of time from a bank's commitment to provide funds until the finalisation of the LBO transaction (i.e. the execution of the cash transfer) is 60 days. See ECB (2007) "Leveraged buyouts and financial stability".

[224] See e.g. EuroMoney (2017) "Blockchain set to transform loan trading and collateral markets" https://www.euromoney.com/article/b14djmk97srdh5/blockchain-set-to-transform-loan-trading-and-collateral-markets.

225 Fusion LenderComm, from Finastra, was launched in late spring 2018 to aid with agent-to-lender administration. See https://www.finastra.com/solutions/lending/syndicated-lending/fusion-lendercomm.

Some banks are beginning to experiment with using distributed ledger technology in certain administrative processes (e.g. Fusion LenderComm provides such technology). In November 2018, BBVA, MUFG and BNP Paribas used a private blockchain to facilitate completion of a syndicated loan. More generally, those banks engaged in investigating blockchain are often focusing on other lending areas, e.g. trade finance.[226] Some recent German Schuldschein loans (which are a much simpler product) have recently used blockchain in distribution.

There are also risks in using blockchain technology, for example questions around its impact on settlement in times of crisis, and security issues. The use of blockchain technology would need to be embedded in other simpler loan areas before being widely extended to syndicated lending in LBO and PF/INFRA loans.

Drawing on our lender fieldwork there is no sign in the market that such an across-the-board shift towards digitalisation is at all imminent for the market, i.e. it is likely to remain peripheral for at least the short term.

The potential for blockchain to overcome inefficiencies

The nature of the inefficiencies in the market (especially around KYC processes) are unlikely to be fully addressed by blockchain technology, at least in the short term. However, we note that technology need not be the only solution. One alternative would be the pooling of resources by (competing) banks into a utility-style model (without necessarily adopting a novel technological solution in parallel). In particular, a group of five Nordic region banks are currently seeking to pool KYC processes for at least larger corporate clients in a utility-style model in a joint-venture (the Nordic KYC Utility). The stated objective is to shorten the duration of the affected processes. This initiative is subject to competition authority approval. This shows that there is at least some potential in market-based initiatives for resolving KYC issues (assuming that competition authority approval is granted). However, such piecemeal approaches may bring other issues, in particular that they will obviously not be a complete solution, and — because they will in themselves consume time and resources — may create disincentives for such a complete solution.

[226] HSBC completed the world's first commercially viable trade-finance transaction using blockchain in May 2018.

5. Conclusions

Based on the evidence and analysis presented in the preceding chapters, we now draw conclusions on the competition risks present in the EU loan syndication market. We begin by concluding on the comparability of the LBO and PF/INFRA segments, and then for each we present our further conclusions on the nature of these markets and the risks to competition law and of sub-optimal outcomes arising from the loan syndication process and market features relevant to each segment.

Comparing the LBO and PF/INFRA segments

The evidence gathered for this study shows a number of key differences between the LBO and PF/INFRA segments of the loan syndication market. These are summarised in the table below. As shown in Chapter 4, these differences warrant a separate consideration of the risks to competition law (although some risks are common across both segments).

Table 30 summarises the details of LBO and PF/INFRA loans. A description of the more general characteristics of the markets is presented as an introduction to the conclusions for each market below. The data in the table below is drawn from our analysis of Loan Connector database, and refers to the six sample Member States from 2010–2017, as well as from our fieldwork.

Table 30: Differences between LBO and PF/INFRA loans

	LBO	PF/INFRA
Total amount borrowed across sample (€m)	256,499	242,531
Average deal value (€m)	343	249
Total number of deals	748	973
Most frequent loan maturity	5-10 years	More than 10 years
Price range (margin over benchmark like Euribor)	400-500 bps, fairly standard across deals.	180-320 bps, with greater variation across deals.
Number of lenders*	309	363
Type of lenders	Investment and commercial banks. Geographic market presence relatively less important than PF/INFRA (often based in global/regional hubs). More likely than PF/INFRA to adopt an 'originate to distribute' lending strategy, although majority are still towards the take and hold end of the spectrum.	Investment and commercial banks. (Marginally) more concentrated than LBO market, and more evidence of 'home bias'. More likely to adopt a take and hold lending strategy.
Number of unique borrowers	651	867
Type of borrowers	Most common borrower type is a company/corporation. Sponsors tend to take the lead on the financing rather than the borrower. Loans fairly homogenous across market in terms of pricing, maturity, loan terms.	Borrower pool is more heterogeneous - most common borrower type is a special purpose vehicle but company/corporation also key. Loans more bespoke in terms of risk, pricing, maturity and loan terms.
Number of sponsors	312	322

Nature of sponsors	Typically private equity firms, many recurrently engaged in loan market, with notable expertise. Most LBO deals have a sponsor.	Mostly multinational companies and infrastructure funds, but also state-owned firms and government bodies. Less likely to engage in multiple market transactions. Minority of PF/INFRA deals have a sponsor.
Participant investors	Large number of loan participants (up to 100s per deal); some large investors granted 'early bird' access to loan but majority participate at sell down phase. Participants limited by white lists specified by borrower/sponsor.	Less involvement than in LBO segment, due to club deal nature of market and economics around PF/INFRA loans. Typically prefer operational phase to construction phase of loans. Institutional appetite increasing - becoming more familiar with risks and attracted by long-term maturities.
Loan process	Typically underwritten deals, with short timelines and commitment of funds necessary ahead of the buyout.	Typically club deals, with longer transaction timelines, including refinancing between construction and operational phases.
Ancillary services required	Hedging seldom mandated. Other services (cash management etc.) loan rather than segment specific.	Hedging often mandated as an ancillary service by lenders.
Secondary trading	Fairly active secondary market. Non-bank lenders particularly active, as well as lead banks (typically for portfolio management).	Not an active secondary market, given club deal nature of loan market and bespoke nature of loans.

Note: *The number of lenders does not include all participant lenders as the Loan Connector database primarily records lenders active in the initial arranging/underwriting of the loans.

Conclusions on risks in the LBO segment

We begin this section with a summary of the main characteristics of the LBO market, followed by our conclusions on the competition law risks.

Overview of the market

The LBO loan segment is a largely international market, particularly with respect to those loans raised in western European Member States, with most lenders active across all these countries. The market in Poland is qualitatively different than the other five reviewed – being less international, albeit still attracting a good range of foreign lenders in the LBO segment. Poland is smaller than the other markets, with a less mainstream currency and reference interest rate. The occurrence of such features in other markets (i.e. those not researched as part of this study) may make Poland an apposite proxy. A key driver of lender activity are the locations of the sponsors and investors. This results in many syndication and sales teams being based in London regardless of the overall geographic scope of the bank. These lenders might have local offices elsewhere in Europe and teams based in various countries (e.g. responsible for origination and structuring), or undertake origination from the central hub.

Lenders in the LBO segment include both investment and commercial banks. The key skill required by MLAs in this market is the ability to successfully syndicate a loan, and ready access to a broad institutional investor base and a track record of successful syndications are critical considerations in the award of a mandate. The relationships between MLAs and sponsors are also important.

Despite the international nature of the market, there is some evidence of “home bias” in as far as the top ranked lenders tend to be those with a parent in that country. However, this is less prominent in LBOs than in PF/INFRA, and we do not consider that this signals competition being undermined by restricting the pool of potential MLAs,

due to non-local banks being widely active across countries. Indeed, our analysis of the market shares of individual lenders in the LBO segment does not identify the markets as being very highly concentrated, with the HHI for the national markets in the LBO segments strongly confirming this.

There is high demand from non-bank institutional lenders for LBO loans (at least for Term Loan elements within the funding package). Such investors usually participate in the loan in the general syndication stage or else (post closure) via the secondary market, although some institutional investors may be included in the initial formation of the lead banking group as keystone or "early bird" investors.

On the demand side, private equity sponsors are often responsible for decision-making around the syndicated loan (as opposed to the ultimate borrower, which is the target of the LBO). Both borrowers and (in particular) sponsors in the LBO segment are sophisticated, with sufficient expertise to control the syndicate process and assess the price and terms of the loan. Larger sponsors may have dedicated debt-raising teams in-house. Third party debt advisors are also a common feature, providing additional advice on pricing and loan structure to the borrower/sponsor, and even playing a prominent role in the formation of the lead banking group and even the general syndication. In the LBO segment such third party advisors are largely characterised as being independent, even boutique-based.

Deal structures and processes

LBO transactions (in contrast to PF/INFRA) strongly tend to involve an underwritten loan coupled with a general syndication or sell down phase. This is driven by timing considerations and the certainty of funds required — the need of the sponsor to have committed funds when bidding for a target within a narrow time window. The initial underwriting phase is followed by a general syndication phase where (part of) the underwriters' loan shares are sold to other participants.

The formation of the lead banking (underwriting) group in the LBO segment involves the borrower/sponsor and/or their advisor, and a number of lead banks bidding for various MLA positions — this can be done individually or as a ready-made consortium. The process is designed to keep the competing banks separate for as long as possible, with negotiations occurring bilaterally between the borrower/sponsor/advisor and each bank or consortium. Information flows are subject to NDAs.

Once the lead banking group is formed, the banks are brought together to agree the general syndication strategy. The key negotiations during the general syndication phase take place between the (potential) participant lenders and the bookrunners, who relay the market response to the borrower/sponsor and the rest of the lead banking group. In some transactions (e.g. deals that are potentially more difficult to market) a single 'lead left' bookrunner could be appointed instead of there being multiple bookrunners. Participants to be approached are often drawn from a white list imposed by the borrower/sponsor (who wish to retain control over who can participate in the loan). Competition risks related to the general syndication phase will be largely limited to LBO loans given the predominant use of club deals in PF/INFRA loans.

At this stage in the process, ancillary services may also be negotiated between the lead banking group and the borrower/sponsor (participant banks may also be involved at this stage but our fieldwork shows that these services are more likely to be awarded to those in the lead group). In the LBO segment ancillary services can include hedging services, cash/collateral services, debt advisory services and M&A services. There is less need for ancillary services as an intrinsic part of the loan (e.g. hedging

services) in the LBO segment compared to the PF/INFRA segment, and therefore the associated risks will be less.

The above describes the primary phase in the syndicated loan market. Loan shares can also be sold on the secondary market, i.e. after the loan has closed. Secondary activity in LBO debt is substantially more important than in PF/INFRA, and therefore any associated risks to competition and market inefficiencies will be more important issues for this sector. Lead banks, participant lenders and non-syndicate lenders can all be involved in the secondary loan market. The borrower/sponsor's white list (if there is one) carries through to the secondary market, such that any non-syndicate (club) investors would either need to be on the white list or else the borrower/sponsors consent would be needed.

Pricing and information availability

LBO loans are systematically perceived as higher risk and are more expensive than Infrastructure and Project Finance loans. LBO margins tend to remain within the 400-500 bps band whereas a larger price variation over time is identifiable for Project Finance and Infrastructure. This pattern holds in each Member State.

Market participants draw on a range of information sources when assessing pricing and other loan terms. Both lenders and borrowers/sponsors have access to information from precedents of internal deal flows, comparator deals in similar sectors/countries, external data on deals they were not involved with from data vendors, and secondary market data. Market participants indicate that these sources together are sufficient in assessing deals, although external data are not always complete (e.g. from data vendors on primary and secondary market) as these are private markets. The homogeneity of LBO loans is a further factor enabling market participants to leverage off existing information.

Risks to competition law and loan outcomes

The tables below present a summary and conclusions on the risks of competition law breaches and sub-optimal outcomes across the stages of the loan syndication process in the LBO segment.

For each stage, we present a summary of the risks associated with its various features, the potential safeguards that could mitigate these risks, and our conclusions based on the evidence presented in the report as to the extent to which these safeguards are met in practice and the nature of the risk that remains.

Based on our analysis of the loan syndication market there are few areas where loan syndication processes in itself could represent a potential infringement of Article 101, i.e. where agreements between lenders have as their object or effect the prevention, restriction or distortion of competition; or Article 102 regarding the abuse of a dominant position. This is due both to the manner in which lenders typically cooperate, and to the wider contextual factors of the market. There are however some features which may raise competition risks, some which may benefit from the Article 101(3) exemption by virtue of being efficiency enhancing and indispensable to the pro-competitive benefits of the agreement, and others which may not. We highlight in the tables below where risks are *related* to the provisions governed by either Article 101 or 102 (even if we have not concluded that these risks pose an infringement of the Articles). We have also identified other areas which, while not directly related to Articles 101 or 102, point to inefficiencies in the market or more general risks for competition – in particular whether they could support collusive behaviour that would enable a group of banks to exert excessive bargaining power against the interests of the borrower/sponsor.

Appointment of the lead banking group in the LBO segment

Table 31: Summary and conclusions on risk to competition and sub-optimal outcomes for the formation of the lead banking group

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Competitive bidding process for appointing individual banks to the lead banking group	*Horizontal information exchange with risks of coordinated/collusive behaviour (related to Article 101).* The key competition risk at this stage is related to information sharing – i.e. information exchange between actual or potential competitors may result in a concerted practice which restricts competition where it facilitates alignment of their competitive behaviour (such tacit collusion, if sustained, could result in market power being exerted). Market soundings or inter-bank information exchanges could become a conduit for pricing information that may influence the banks' individual responses to the borrower's RFP. Some information exchange prior to the submission of bids may be necessary given the nature of the financing, such that it either does not have an anti-competitive effect or that it satisfies the conditions for exemption under Article 101(3). Where such information exchange takes place with the express consent of the borrower is good prima-facie evidence that the exchange is not anti-competitive by object and may further indicate that the exchange was considered and accepted by everyone as necessary in the circumstances.	A degree of separation between syndication and origination functions, such that syndication desks provide only consolidated anonymised views to origination desks could reduce the risk that information about other lenders' appetite is unduly passed onto the origination team and facilitates coordinated bidding. Competition law guidance or training for banks about information exchange issues. The structure of the bidding process to keep lenders separate for as long as possible or to separate them for specific purposes, with the use of NDAs to signal the intent to protect the bidding process from information exchange. The availability of external information to lead banks to help inform views on pricing will also reduce the risks of information sharing. Borrowers/sponsors to set clear parameters for information exchange where some market sounding is necessary for the successful completion of the transaction, e.g. identify specific investors to be	Safeguards around information sharing are present in the LBO market, in particular with respect to lead banks' access to information to inform their response to the RFQ; the structure of the bidding process in which the borrower/sponsor negotiates bilaterally with each bank and keeps them separate until the loan terms have been agreed; and the sophistication of borrowers/sponsors in the LBO market and their access to own and independent pricing data to assess the offers made by lead banks. However, risks do remain, even though we consider these relatively low in the LBO segment. The boundary between generic and specific sounding would need careful definition to ensure compliance (banks require explicit borrower/sponsor consent to conduct deal-specific soundings in a form whereby this would need to be demonstrable to compliance teams). In its strongest form, such consent should be specific as to who is contacted. There is evidence of generic market soundings by MLAs with investors prior to submitting bids, and whilst these discussions should not involve details of specific transactions information about specific lenders' appetite etc. may still be communicated back to the origination desks. This risk may be exacerbated where there is no significant functional separation between

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	In some cases, the borrower/sponsor may appoint a single lead arranger to set up the initial banking group and negotiate the loan terms with the other banks, and would mandate that the banks share information in order to reach a common loan price and terms. The interaction with the banks should be strictly within the parameters set by the borrower, otherwise here is a risk that information shared between the lead bank and other banks involved in setting the terms of the loan could lead to the loan terms moving against the borrower. *Coordinated agreements to limit supply (related to Article 101).* Any agreements between banks to limit supply (e.g. to agree not to participate or prevent other banks participating, or not to increase their participation where acting independently they would have done so) would be anti-competitive conduct related to collusion and coordination.	approached or specify the information to be shared and discussion (e.g. prohibiting discussions about limiting supply). The implications for investors of information exchange, such as Market Abuse laws about trading on information received about a loan. Borrower/sponsor sophistication regarding their expectations on price and the optimal structure for the bidding process.	the syndication and origination desks. Soundings (even generic soundings) with other MLAs (as opposed to exclusively with institutional investors without connections to MLAs) could be abused so as to facilitate collusive action, even potentially enabling a group of MLAs (particularly one with fewer substitute MLAs) to achieve, and sustain, some degree of collective market power. In addition, although the bidding process is set up to keep lenders apart, the prevention of information sharing is governed by NDAs, which can be difficult to enforce. Therefore although the process set up by the borrower/sponsor in LBO loans reduces the risk of anti-competitive information sharing, the risk remains that this may happen. Equally, once an NDA is signed, it is evident to the counter-party that the breach of that agreement is problematic (i.e. it puts banks on clear notice of borrower/sponsor expectations). The specific competition policy risks associated with a single lead arranger are not high: borrowers/sponsors control the formation of the lead banking group, keeping the individual banks separate until each has agreed the key terms with the borrower/sponsor and signed the initial loan agreement. In any event, the likelihood of a single MLA being appointed by the borrower/sponsor to set up the syndicate and negotiate the key loan terms with the rest of the lead banks is low in the LBO segment.

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Competitive bidding process for appointing initial banking group among consortia	*Horizontal information exchange with risks of coordinated/collusive behaviour (related to Article 101).* *Coordinated agreements to limit supply (related to Article 101).* Where a group of banks come together to submit a joint bid in response to an RFP at the request of a borrower then, provided that the bank group operates within the instructions of the borrower, it is likely that the any information exchange between the banks for the purposes of putting together that proposal and the ultimate agreement that the banks reach as to the terms of that bid, will either fall outside Article 101(1) altogether or satisfy the conditions of Article 101(3). To the extent that discussions or agreements go beyond what is required for the purposes of submitting the joint bid then, depending on their nature, such discussions may breach Article 101(1) and indeed may be anti-competitive by object. In particular, agreements to limit lending capacity e.g. by not inviting other lenders to participate, or not increasing their participation (where acting independently they could and would have done so) are likely to have an anti-competitive effect and could be anti-competitive by object. *Abuse of collective dominance to impose uncompetitive terms and pricing (related to Article 102).* If the banks coming together in a	Clear parameters for the consortium: the borrower/sponsor should ensure that there are clear instructions to the consortium as to what they should agree jointly and what information they can share. The borrower/sponsor can place limits on the interaction between bank, e.g. splitting up the consortium during the bidding process to negotiate certain terms bilaterally such as hold levels or price. If consortia are invited to submit bids that compete with other consortia (instead of bidding as the only consortium) then there is scope for the borrower/sponsor to compare bids and maintain competitive pressure. The regulatory regime could place a responsibility on lenders to highlight to the borrower/sponsor where the bidding process may lead to a sub-optimal outcome.	Consortia bids appear to be a feature of the LBO market based on borrower/sponsor fieldwork, although no lenders in our sample participated in consortia. The main safeguard for which there is evidence is that borrowers/sponsors almost always use a competitive RFP process when appointing the lead banking group (whether this is soliciting bids consortia) which implies that consortia at least compete and enable the borrower/sponsor to maintain competitive pressure (i.e. including such consortia in the RFP process could be pro-competitive). We do not have any evidence of there being regulations/requirements in place that place responsibility on banks bidding for the RFP to highlight to the borrower/sponsor where the process might not operate in their best interests. This could be a potential safeguard to explore further.

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	consortium have market power in the relevant market then there may be the risk of incompatibility with Article 102, subject to a finding that the consortium is able to unduly inflate the price through information sharing and coordination through its position of power. *Borrower's process leading to sub-optimal outcomes.* The borrower/sponsor could set up the consortium in a way that facilitates sub-optimal outcomes. For example, by stipulating that a certain bank be involved in the loan where this bank requires a higher price than the other banks in order to participate, this would limit the ability of the consortium to replace this bank and agree a lower price.		
Direct appointment of a single / relationship bank without competitive process.	*Borrower's process leading to sub-optimal outcomes.* *Abuse of asymmetric information by lead bank.* The direct appointment of a bank without a competitive process may result in sub-optimal outcomes for the borrower/sponsor – this is not considered to be a competition law risk as it is part of the structure imposed by the borrower/sponsor, but may have regulatory implications. The single bank could use its relationship with the borrower to create a situation of 'lock-in' and thereby extract rents through imposing higher prices on the borrower compared to a competitive situation.	If a relationship bank competes on reputation for the borrower/sponsor favour then this will limit its ability to negatively influence loan outcomes (depending on the sophistication of the borrower and availability of alternative relationship banks). If borrower/sponsors are not 'locked-in- to their relationship banks then this reduced the scope of these banks to underperform or negatively influence the loan process in their favour. A further safeguard would be the sophistication of the	In the LBO segment there is very little evidence of single MLAs being appointed without a competitive process, and thus the risks associated with a directly appointed MLA will be low in this market. The use of a competitive process also suggests that the value of relationship banks is considered in relation to competitors rather than due to a situation of 'lock-in'. The sophistication of most borrowers and sponsors increases their control of the syndication process and leaves them less susceptible to manipulation by a relationship bank, in particular in terms of selecting other participants.

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	A single relationship bank may also be able to unduly influence the syndication process in their favour, e.g. by excluding challenger banks from the wider syndicate in order to embed its position. These risks are influenced by the nature of the market - e.g. smaller geographic or product markets the borrower would have limited choice of eligible lead banks, and likelihood of repeat lending from the relationship bank and further information lock-in would be increased. Borrowers at the beginning of their 'life cycle' may also be more susceptible to the influence of relationship banks.	borrower/sponsor in driving the syndication process and the extent to which they relied on the advice or influence of the relationship bank (e.g. in selecting other loan participants). The ability of the borrower/sponsor to monitor the MLA's interaction with participant investors would also undermine undue influence or the risks of the relationship bank manipulating loan terms. The ability of the borrower to replace the MLA in case of underperformance would reduce the incentives for the MLA to underperform.	The ability of borrowers/sponsors to monitor and sanction MLAs behaviour once appointed is somewhat limited, limiting the applicability of one of the potential safeguards. However, given the repeat nature of interactions between sponsors and lenders and the competitive process used in appointing MLAs we consider it highly likely that poor performance would be punished in any subsequent transactions. Given the evidence on safeguards and the low likelihood of the direct appointment of a single MLA in the LBO segment, we consider this feature of the process to be overall a low risk.
Post-mandate to loan agreement	*Horizontal information exchange with risks of coordinated/collusive behaviour (related to Article 101).* At this stage the borrower/sponsor mandates that the lead banks meet and agree final loan terms – these discussions are an essential element of the loan syndication process and provided that the banks are operating within the terms of the mandate granted by the borrower then exchanges of information between them which are related to achieving that aim may fall outside Article 101(1) or alternatively benefit from an exemption under Article 101(3). *Coordinated agreements to limit supply (related to Article 101).* Banks must be careful not to go beyond	If the lead banking group is formed such that the key loan terms are discussed and negotiated bilaterally between the banks and the borrower/sponsor ahead of the post-mandate stage, then there will be less risk of the banks discussing these terms at this stage and moving against the borrower. The involvement of the borrower/sponsor in the post-mandate discussions would ensure that the communications were in line with the mandate. The strategy adopted by the borrower/sponsor should provide flexibility for banks to drop out of the	The scope for lenders discussing loan terms so as to move against the borrower at the post-mandate stage is low, given that in the LBO segment the process widely adopted is for the loan terms to be agreed bilaterally between the borrower/sponsor and individual lenders, and that joint discussions between lenders post-mandate should be limited to agreeing the loan documentation and syndication strategy. Borrowers/sponsors also aim to build in latency when obtaining loan commitments from the lead banking group. There is some, however, evidence that the loan process may not always work in the borrower/sponsor's favour in terms of it agreeing the overall price to the highest common denominator rather than

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	what is required under the borrower's mandate and reach any agreement or engage in any concerted practice to (artificially) raise the price or to restrict supply. Any such agreement should be viewed as anti-competitive by object. *Borrower's process leading to sub-optimal outcomes.* The process set up by the borrower/sponsor may lead to sub-optimal outcomes, e.g. if it stipulates that a particular bank(s) must be part of the syndicate and if that bank requires a higher price than the others to participate in the loan. A further risk at this stage when banks are brought together by the borrower is that repeat interactions among lenders on transactions may lead to inadvertent information sharing around each other's behaviour or strategies which could be used to align their bids in future transactions.	process to avoid having to agree to terms at the highest common denominator (e.g. by building latency into the process). The timing of information flows to the lenders would also reduce the risk of banks dropping out, i.e. by ensuring that all due diligence is provided before mandate. The risks of inadvertent information sharing and future coordination/collusion would be mitigated the lower the likelihood of repeat interactions between lead banks on syndicated loans. The information gained from such observations would also be influenced by the type of discussions that are held during this interaction (e.g. if pricing and hold strategies are not discussed then it will be more difficult for lenders to observe this information about each other).	negotiating a common price. This is not common and may, anyway, simply reflect the relative attractiveness of the credit itself. The evidence of the multiple interactions between lenders on transactions over time leads us to conclude that there is a definite risk that lenders can observe each other's behaviours and strategies, which may enable them to engage in some coordination on future loan transactions. We do not have direct evidence that this happens in practice. Given that fact that in most cases the discussions that occur at this stage do not involve detailed information about pricing and hold strategies, the amount of information that lenders are able to observe is likely to be limited. However this remains a risk area.

General syndication phase in the LBO segment

Table 32: Summary and conclusions on risk to competition and sub-optimal outcomes for the formation of the general syndication phase

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Selection of participant lenders	*Leverage of powerful position in syndicate. Collusive behaviour (related to Article 101).* If MLAs are able to influence the selection of participant banks into a syndicate, this could facilitate collusive behaviour by enabling reciprocal agreements between lenders in return for future business. Ultimately, this could even enable those banks to exert market power.	The degree of control retained by the borrower/sponsor in selecting the participant lenders will reduce the risk of undue influence of MLAs. Further, the risk of foreclosure raised by reciprocal arrangements is reduced if these agreements do not prevent other lenders from competing for or participating in syndicated loans.	MLAs exercise some influence over the selection of participant lenders. In the majority of cases this influence is controlled by the borrower/sponsor (e.g. through provision of a white list, direct feedback loops between investors and sponsors, regular feedback from the bookrunners), but there remain cases identified by borrowers/sponsors where the MLAs have the effective final say on which lenders participate in the loan. The allocation of loan shares across participants is done by the MLAs and, although subject to signoff by the borrower/sponsor, there remains the possibility than MLAs could favour certain participants in the allocation of loan shares.
Negotiation of final loan terms	*Horizontal information sharing (related to Article 101).* In so far as the banks are operating within the borrower/sponsor's mandate, inviting participant investors to participate in the loan on the basis of the terms agreed between the MLAs and the borrower/sponsor should fall outside Article 101(1) altogether or alternatively benefit from exemption under Article 101(3) on the basis that it is inherent to securing the financing. *Abuse of dominance by syndicate (related to Article 102).* A risk of sub-optimal outcomes exists if at this general syndication phase the syndicate as a whole uses its bargaining power as the	The process and timing for agreeing loan terms could reduce the risks of the syndicate coordinating and exploiting its bargaining power, i.e. if loan terms are agreed among the lead banking group before the general syndication phase, and if participant lenders are not given cause to interact then responding to MLAs. Borrower/sponsor control over information flows to participant investors, as well as mechanisms to ensure the transparency of these information flows, will reduce the risks associated with asymmetric	The evidence relating to the first safeguards shows that while the risk of the general syndicate coordinating their behaviour to move against the borrower cannot be eliminated – as some negotiation of terms during this phase is possible – the likelihood of this risk materialising is low given that in the vast majority of cases the final loan terms are agreed before the general syndication phase, that participants engage bilaterally with the bookrunners without the opportunity to discuss between themselves the loan (a process protected by NDAs), and, more so, and that there are large number of participant lenders engaging in this phase that effective coordination would be very challenging.

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	single (joint) provider of the loan to coordinate negotiations and move against the borrower/sponsor when agreeing final terms. *Exploitation of information asymmetries.* Information asymmetries may exist between the MLAs and the participant lenders, which the MLAs may exploit to distort the loan terms for their economic gain. *Exploitation of vertical relationships.* Any links between the MLAs and particular participant investors could also convey informational advantages onto these participants at the expense of their competitors.	information. Ensuring the separation of control between MLAs and participant investors will also reduce this risk. The reliance of participant lenders on information outside of that provided by the MLA will also reduce the risks associated with information asymmetry.	The risk of MLAs exploiting information asymmetries cannot be eliminated. The various safeguards do not apply fully across the market – there may be scope in some cases for MLAs to manipulate the information passed onto participant investors beyond borrower/sponsor oversight; and transparent information sharing portals (e.g. Debt Domain), though widely used, are not used in every transaction. This must be offset with the sophistication of participant investors in terms of their credit quality standards, and their use of information beyond that which is provided by the MLAs to inform their decisions about participating in loans. Further, mispricing of a loan through MLA manipulation should be detected shortly after the loan's close, e.g. on the secondary market. Such mispricing would also negatively impact upon the MLAs' reputation.
Market Flex	*Horizontal information exchange to impose higher prices (related to Article 101).* There is scope for a breach of Article 101 if the bookrunners and underwriters discuss using the flex to increase the price in circumstances where the finance could in fact be raised without such action being necessary, or if they agree to go above a level that is necessary to secure the financing. These actions would be anti-competitive by object.	The main safeguard is to ensure that the details of the flex mechanism and the process to be followed are agreed between borrower/sponsors and the book-running banks ahead of the general syndication phase. After that, the flex process as agreed by the borrower must be followed, with no communication between lenders concerning the operation of the flex outside of that agreed	Flex terms are agreed between the borrower/sponsor and the MLAs ahead of the general syndication phase, and thus the first key safeguard is met. Borrower and sponsors are sophisticated to negotiate flex provisions and also have access to guidance. A very high majority of relevant borrower/sponsors in our sample reported being satisfied with the transparency of the marketing and flex processes engaged by bookrunners, and the outcomes of the flex.

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	Borrower's process leading to sub-optimal outcomes. The practice of borrower/sponsors paying for the lawyers used by the lead banks also creates risks of sub-optimal outcomes if it weakens the loan documentation (as well as increasing the likelihood of documentation flex being invoked by participant lenders).	process. Economics disincentives on bookrunners could also prevent the unnecessary use of flex.	Bookrunners are subject to fee pay aways before they can use flex, which acts as a disincentive to invoke it unnecessarily. Our conclusion based on the extent to which the safeguards are met is that the risks of bookrunners abusing market flex is low. The market feature whereby borrowers/sponsors dictate the lawyers used by lead banks does – in our view - appear likely to be a contribution towards declining documentation standards, i.e. loan documentation containing sub-optimal creditor protections/outcomes. Another factor here the nature of current market conditions, with significant appetite amongst institutional investors and those managing their money to invest into LBO loans. A reduction in appetite amongst these could change the negotiating dynamic around such protections, i.e. shifting away from cov-lite – however there is no sign of such a shift in the market at present.

Ancillary services in the LBO segment

Table 33: Summary and conclusions on risk to competition and sub-optimal outcomes for the provision of ancillary services

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
The allocation of ancillary services across banks, and the pricing of such services.	Lenders individually requiring that a borrower put in place certain ancillary services, and including conditions as to who can provide the services (e.g. only a lending bank), is unlikely to give rise to competition concerns if the ancillary services are directly related and necessary to the provision of the loan, and the conditions are directly necessary to the loan or do not limit competition (e.g. if there are a large number of banks from whom the borrower could chose to provide the services). *Horizontal information sharing to collude on the provision of ancillary services (related to Article 101).* However, there is a risk that, in an individual bid scenario, banks discuss and/or agree between themselves prior to making their bids that they will each make the provision of ancillary services a requirement of their lending (as opposed to each individually responding and – independently - making this a condition of their participation). There is a risk in an individual bid scenario that the practice of agreeing a single price and term sheet in respect of the provision of the lending "spills over" into the provision of related services. It is not necessarily the case that the setting of a single price by a group of banks providing the ancillary service is inherent to the provision of that	Borrower clarity as to those required services that are to be considered related to the loan – and those that are not. Guidance could be provided to banks on the type of services that are likely to be related to the provision of the loan as opposed to those that are extraneous and which therefore the lenders should not generally (jointly) require be purchased from them. Borrower clarity as to services required – and not required. The borrower can seek to influence this by specifying which other services are required and which services are not required. If the RFQ specifies a particular approach, that approach should be respected by the banks.	Our borrower/sponsor fieldwork did not reveal significant differences in the types of ancillary services provided in LBO loans compared to PF/INFRA. The key services discussed are hedging services and cash management. Our lender fieldwork and data suggest that hedging services are more necessary and common in PF/INFRA loans compared to LBO loans. In the majority of cases from our lender and borrower/sponsor fieldwork, the allocation of ancillary services is decided as part of the initial agreement of loan terms, or as a competitive process after the loan has closed. In both cases the borrower/sponsor would be able to choose between banks' offers and maintain competitive pressure. However a small minority of borrower/sponsors identified that the MLAs make the provision of ancillary services by them a condition of the loan (the rest negotiate ancillary services as part of the initial loan agreement process, or after the loan close). Whilst competition law precedent (e.g. Spain's CNMC) has not concluded that it is unlawful for lenders to specify that ancillary services be purchased from them, we do consider such a feature as raising the risk of a borrower/sponsor achieving a sub-optimal economic outcome.

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	service, and the banks may be able to compete to provide such services on an individual basis. *Tying of ancillary services.* There is a risk that the lenders jointly require that the borrower purchase services from them that are unrelated to the loan and in respect of which they can compete individually. Where the provision of ancillary services by some lenders is restricted to the syndicate, or some sub-set of it, e.g. an obligation – or strong expectation – that purchase would be from the MLAs, especially if not all MLAs were able or willing to provide or quote for that service, then those particular lenders would be better able to exert bargaining power.		We further note that all of the respondents that cited such provision being a condition of the loan were from Spain. Ancillary services not directly related to the loan (e.g. further financing, investment services) can be negotiated as part of the loan negotiation, with both “right of first refusal” and “right to match” clauses being used. These have been found by the UK regulator as to have no client benefit – unless related to the replacement of bridging finance - and have been banned in the UK, but their use may be continued outside the UK (representing a continued risk to optimal outcome for borrowers/sponsors).

Debt advisors in the LBO segment

Table 34: Summary and conclusions on risk to competition and sub-optimal outcomes for the role of debt advisors

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
The use of debt advisors which are also involved in the syndicated loan	*Conflicts of interest and exploitation of information asymmetry.* This could give rise to significant conflicts of interest. If these conflicts are not well managed this could undermine the competitive nature of the syndication, and result in sub-optimal outcomes for the borrower/sponsor.	Capacity of the borrower/sponsor to make own judgements as to outcomes and/or to have access to other advisors. Training and policies for relevant staff, e.g. identification and management of conflicts of interest, clarity as to duty of care to provide neutral advice to clients.	The use of advisors who are also part of the syndicate is widespread among borrowers and sponsors, and in some cases with there being no other source of external advice. This issue is less common in the LBO segment that the PF/INFRA segment, but still occurs. Our lender fieldwork shows that where an advisory role is provided by a lending bank, this is functionally separate from the lending role, and adherence to such protocols should mitigate the risk of sub-optimal outcomes to borrowers of not having a demonstrably independent advisor. A different form of concern would be where the advising bank attempted to influence the borrower/sponsor towards a strategy or debt structure that suited its lending arm, i.e. subverting the Chinese wall between the advisory and lending functions, and with this not being fully apparent to the borrower/sponsor. Based upon the description of their policies for managing such situations given to us by lenders, this would represent a significant breach of internal protocols.

Secondary loan market trading in the LBO segment

Table 35: Summary and conclusions on risk to competition and sub-optimal outcomes for secondary trading

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Coordination by lenders on the sale of the loan on the secondary market	*Coordination and collusion in selling on the secondary market to influence supply and price (related to Article 101).* Co-operation between lenders post syndication could give rise to competition law risks, e.g. if underwriting banks were to co-ordinate in relation to when to sell, what proportion to sell or at what price to sell the debt in the secondary market, such co-ordination is unlikely to be justified and may well be anti-competitive by object. In these circumstances the potential harm is to the purchasers of the debt in the secondary market. *Borrowers' process leading to sub-optimal outcomes.* Restrictions placed by borrowers/sponsors on transfers on loans may limit liquidity in the secondary market, potentially (but not necessarily) resulting in sub-optimal economic outcomes.	Guidance and training to lenders and borrowers/sponsors, covering the formation process and ongoing co-operation between the lending banks post syndication, highlighting the risk of co-ordination in relation to secondary market activity. Appropriate restrictions on post-closure sale by MLAs. A borrower could require that the underwriters hold a proportion of the debt for a period of time post syndication to avoid disruption.	There is no evidence of co-ordinated secondary market activity in our fieldwork, and the safeguard relating to hold levels is widely upheld in practice (indeed, it is a key part of the process). The features of the secondary (i.e. post-closure trading) loan market (which remains a caveat emptor market with implicitly sophisticated buyers) should limit any attempt by sellers to manipulate the price of the debt, unless they are able to simultaneously identify a group of unsophisticated buyers of that debt. The economic benefit to lenders from any coordination may therefore be limited, reducing the plausibility of this risk. There is widespread evidence of borrower/sponsor restrictions on secondary trading, in terms of which institutions are eligible to participate in the loan. Given that secondary market pricing data are also used in the primary LBO segment (albeit not exclusively relied upon), this could also affect the development and efficiency of the primary market.

Back office inefficiencies

Table 36: Summary and conclusions on risk to competition and sub-optimal outcomes for back office inefficiencies

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Know-your-client and settlement processes.	*Increased transaction costs.* Certain back office inefficiencies increase transaction costs and potentially even reduce secondary market activity in consequence, potentially resulting in sub-optimal economic outcomes.	Blockchain technology may have the capacity to improve efficiency by creating the loan as a digital asset, automating the allocation of collateral, expediting the clearing and settlement process and speeding up the approval time for including additional investors (i.e. on the secondary loan market).	There are two main barriers to the potential benefits of blockchain, namely the development of the technology itself, and the potential of blockchain to overcome the real sources of inefficiency in the market. In relation to the first, our fieldwork shows that the technology to apply blockchain to syndicated loans has not been fully developed as yet (notwithstanding early adopters around loan completion) and that there is no sign that an across-the-market shift towards digitalisation is at all imminent. In relation to the second, other solutions to the problems of inefficient processes – in particular KYC – may be available without adopting novel technological solutions, such and banks pooling resources to create a centralised portal for KYC processes across shared clients. Therefore there is at least some potential in market-based initiatives for resolving KYC issues (assuming that competition authority approval is granted). However, such piecemeal approaches may bring other issues, in particular that they will obviously not be a complete solution, and — because they will in themselves consume time and resources — may create disincentives for such a complete solution.

Default and refinancing in the LBO segment

Table 37: Summary and conclusions on risk to competition and sub-optimal outcomes for default and refinancing

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Refinancing in conditions of default	*Horizontal information exchange leading to collusive behaviour (related to Article 101).* There is a risk that the banks commence discussions about the future lending opportunity prior to an RFQ being issued in circumstances where they may be competing for a role in the future lending. *Abuse of collective dominance to inflate loan price and terms and to bundle/tie additional services (related to Article 102).* When a borrower faces an event of default, there is a risk that the group of lending banks might together have market power, because the limited options available to the borrower could mean the market is defined very narrowly. There is a further risk that the lending banks together impose certain conditions on restructuring which are not objectively justified (e.g. tying the purchase of other services to the refinancing and imposing excessive prices as a condition to the lending).These actions could, in very exceptional circumstances, constitute an abuse of a collectively dominant position.	Competition law guidance or training for banks about information exchange issues and how to treat clients in a distressed situation. Regulatory regime and banks' duties to clients may reduce the likelihood that any abuses take place.	Competition policy training is undertaken by lenders' restructuring teams. These are functionally separate teams which take over the loan discussions from the origination teams in the case of a default risk, such that discussions between banks regarding the potential restructuring are not undertaken by teams involved in loan origination. Discussions between lenders are only possible under such policies at the instigation of the borrower. The discussions and negotiations of potential restructuring in the event of a default are performed collaboratively among the members of the syndicate. Whilst this may be efficiency enhancing, as time is often pressurised, it equally enhances the risk of banks exerting excessive bargaining power. We note that the bank restructuring teams that we interviewed had undertaken some form of competition policy training, but clearly any subversion of the proper process would be problematic. The extent to which the proper process had been subverted would need to be assessed on a case by case basis. Our fieldwork shows a majority of instances where refinancing discussions involved lenders from outside of the original syndicate. The willingness of the market to provide the new finance can be seen as a limit upon any collective market power that

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
			the existing group of lending banks may have. However, there is evidence of a non-trivial number of instances where the existing syndicate is the only option, i.e. there is scope to exert such market power. We do emphasise, however, that we do not have evidence for its abuse. In relation to the risk of the syndicate tying ancillary services to the refinancing, the fieldwork shows again that other, non-syndicate members are often involved in these discussions, which would provide market discipline against such coordinated tying behaviour. However, it is also apparent that in a substantial minority of cases such negotiations took place only with the syndicate members. There may be mitigating or efficiency enhancing circumstances, but it is also clear that such distressed circumstances can create the opportunity to price such ancillary services on non-competitive terms, and thus this is also an area deserving future monitoring.

Conclusions on risks in the PF/INFRA segment

We begin with a summary of the main characteristics of the PF/INFRA market, followed by our conclusions on the competition law risks.

Overview of the market

The market for PF/INFRA loans in western Europe is again largely an international one. In Poland, however, there is relatively less activity by foreign banks than in the LBO segment — most probably stemming from the low deal frequency and use of a non-mainstream currency. The features of Poland's market that drive this — that it is a smaller market, with non-euro currency — could also reflect the situation in other, smaller Member States.

Our evidence shows that national and project-specific risks are also relatively more important in the PF/INFRA segment compared to LBOs, and therefore local or product-specific presence is considered more valuable by many (although not all) lenders contributing to our study. For this reason, origination and syndication teams are more likely to be based within countries where the bank is active rather than operating centrally.

Banks active in the PF/INFRA sector include both investment and commercial banks. The role of relationship (commercial) banks is arguably higher in the PF/INFRA segment given the value of local expertise and the need for additional services such as cash management which need to be provided locally. This explains the greater degree of "home bias" found in the PF/INFRA segment compared to the LBO segment. Again, we do not consider this home bias to be restricting the pool of potential MLAs in the western European market (non-local banks are readily accessed). However, in Poland (and likely some other Member States outside our sample) the low deal frequency and use of a non-mainstream currency may make the pool of potential MLAs relatively small — with this more of a concern in the PF/INFRA segment than in the LBO one.

That said, our analysis of the market shares of individual lenders does not identify any of the national markets as being very highly concentrated, with the HHI for each of them in the PF/INFRA segment confirming this. In the PF/INFRA segment the HHI scores were higher than the LBO segment but only in Poland (where the HHI score is just below 1000) are there any signs of concentration. It is worth noting that the PF/INFRA segment is more heterogeneous than the LBO one, in that there are credit risks (say related to a particular type of infrastructure construction, such as specific forms of renewable energy) where knowledge could be less well distributed than the HHI-based analysis might suggest (i.e. in certain sectors the market could be more concentrated).

The participation of non-bank institutional investors in the PF/INFRA market is lower than the LBO market, particularly in the construction phase of projects. This is partly because they do not have the appetite for construction risk, and generally prefer tranches/deals where the full commitment is made on day one (i.e. all the money is put to work then). The lower pricing of these loans is also a factor. For this reason the financing of the construction of PF/INFRA is often characterised as being (still) a 'bank market'. However, certain institutional investors have emerged recently with revised (i.e. lower) expectations around yield in what continues to be a low real interest rate regime and displaying increased willing to take on construction risk. This has been facilitated by growing access to internal expertise at such investors (e.g. they have hired individuals or teams with the relevant skills as a pre-condition to increasing such investments).

Debt advisors are also a common feature of the market, providing additional advice on pricing and loan structure to the borrower/sponsor, and at times leading the formation of the club. Whilst such advisors can be independent, borrower/sponsors do engage advisors who are also part of a bank from within the lending group. Whilst our evidence suggests that the majority of these maintain a strict separation between the advisory business and the lending arm, there are cases where the advisory and lending services are explicitly bundled by the bank.

Deal structures and processes

The majority of PF/INFRA loans are structured as club deals. This reflects strong, sophisticated sponsors/borrowers able to put together the club coupled to the fact that the timing of most projects is long enough not to necessitate underwritten deals (indeed, underwriting could even act as a negative signal). In some circumstances, such as if a sponsor is in competition for a green- or brown-field site where timing is more pressurised then an underwritten deal may be considered, although this is the exception rather than the norm.

The process of forming the club in PF/INFRA deals is largely similar to the formation of the lead banking group in LBO loans, although there is a higher likelihood of relationship banks being involved at the pre-RFP stage. The borrower/sponsor/advisor typically puts the club together and negotiates directly with each lender, although there are cases where a coordinator might be appointed to form the club and negotiate with lenders on behalf of the borrower/sponsor.

The club banks typically agree and sign final terms with the borrower/sponsor before being brought together to agree documentation; however, there are also cases where the club would negotiate terms together and with the borrower/sponsor before signing the final terms. There is no formal general syndication phase to club deals (though the clubs' members may sell down some part of the debt post-close). Any negotiation of ancillary services would usually be towards the end of the club formation, although there is evidence of ancillary services being allocated as part of the initial negotiations to form the club. Hedging services are more often a pre-requisite by lenders in PF/INFRA loans and are thus an ancillary service integral to the provision of the loan. Cash management services are also frequently negotiated in PF/INFRA deals.

The role of the secondary market is much smaller than in the LBO segment, due to the fact primary lenders tend to hold their loan shares to maturity.

Pricing and information availability

PF/INFRA loans are systematically cheaper in absolute terms than LBO loans (we do not have the data to comment on the relative appeal in risk-return terms). This explains in part the lower appetite for these loans from institutional investors.

As in the LBO segment, market participants draw on a range of information sources when assessing pricing and other loan terms. Given the bespoke nature of some PF/INFRA projects, the availability of external comparator data will be lower in this segment, such that a greater reliance is placed on internal expertise (either past deal flow, or the expertise of individuals). This may raise the likelihood of lenders seeking to engage in forms of market sounding.

Involvement of state actors

Public sector actors can act as borrowers/sponsors (e.g. in the context of a public-private partnership, or PPP) and also potentially as lenders in the PF/INFRA segment (unlike the LBO segment where they are absent). The proportion of PF/INFRA

borrowers within the Loan Connector dataset is, however, rather low — at just 2 per cent of the total. Such public sector sponsors are not discretely identifiable.

PPP debt, with its reduced risk (e.g. due to stable, even potentially guaranteed income) and longer maturities, can be seen as contributing towards encouraging investors to respond positively to a partial gap in the market created by the withdrawal of some banks from longer-term PF/INFRA financing.

There are also public sector lenders in the PF/INFRA space. The main motivation for such involvement would be to resolve a market failure, i.e. providing capital to (narrowly) sub-marginal borrowers (i.e. those borrowers that could not afford debt priced according to their risk). We note that, especially in current market conditions, there is a risk that such actors will displace lending that could have come from commercial lenders.

Risks to competition law and loan outcomes

The tables below present a summary and conclusions on the risks of competition law breaches and sub-optimal outcomes across the stages of the loan syndication process in the PF/INFRA segment.

For each stage, we present a summary of the risks associated with various features of the stage, the potential safeguards that could mitigate these risks, and our conclusions based on the evidence presented in the report as to the extent to which these safeguards are met in practice and the nature of the risk that remains. We highlight in the tables below where risks are *related* to the provisions governed by either Article 101 or 102 (even if we have not concluded that these risks pose an infringement of the Articles).[227] We have also identified other areas which, while not directly related to Articles 101 or 102, point to inefficiencies in the market or more general risks for competition – in particular whether they could support collusive behaviour that would enable a group of banks to exert excess bargaining power.

[227] We note again that the assessment of the relevance to Articles 101 and 102 are based on our own judgements and that the European Commission has not taken a position on this.

Appointment of the lead banking group in the PF/INFRA segment

Table 38: Summary and conclusions on risk to competition and sub-optimal outcomes for the formation of the lead banking group

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Competitive bidding process for appointing individual banks to the lead banking group	*Horizontal information exchange with risks of coordinated/collusive behaviour (related to Article 101).* The key competition risk at this stage is related to information sharing – i.e. information exchange between actual or potential competitors may result in a concerted practice which restricts competition where it facilitates alignment of their competitive behaviour (such tacit collusion, if sustained, could result in market power being exerted). Market soundings or inter-bank information exchanges could become a conduit for pricing information that may influence the banks' individual responses to the borrower's RFP. Some information exchange prior to the submission of bids may be necessary given the nature of the financing, such that it either does not have an anti-competitive effect or that it satisfies the conditions for exemption under Article 101(3). Where such information exchange takes place with the express consent of the borrower is good prima-facie evidence that the exchange is not anti-competitive by object and may further indicate that the exchange was considered and accepted by everyone as necessary in the	A degree of separation between syndication and origination functions, such that syndication desks provide only consolidated anonymised views to origination desks could reduce the risk that information about other lenders' appetite is unduly passed onto the origination team and facilitates coordinated bidding. Competition law guidance or training for banks about information exchange issues. The structure of the bidding process to keep lenders separate for as long as possible or to separate them for specific purposes, with the use of NDAs to signal the intent to protect the bidding process from information exchange. The availability of external information to lead banks to help inform views on pricing will also reduce the risks of information sharing. Borrowers/sponsors to set clear parameters for information exchange where some market sounding is necessary for the successful completion of the transaction, e.g. identify specific investors to be	Safeguards around information sharing are present in the PF/INFRA segment, in particular with respect to the structure of the bidding process in which the borrower/sponsor negotiates bilaterally with each bank and keeps them separate until the loan terms have been agreed; and the sophistication of many borrowers/sponsors (and their debt advisors) in the PF/INFRA market to assess the offers made by lead banks. However, given the more bespoke nature of PF/INFRA loans the availability of information to assist banks in forming their views is likely to be lower than in the LBO segment. Therefore whilst there is no evidence to suggest that banks in this segment are more likely to engage in specific market sounding or breach NDAs, there is a heightened risk (relative to the LBO segment) that interactions between lenders that cross over the general/specific sounding boundary in the bidding stage. Other risks similar to the LBO segment also remain. The boundary between generic and specific sounding would need careful definition to ensure compliance (banks require explicit borrower/sponsor consent to conduct deal-specific soundings in a form whereby this would need to be

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	circumstances. In some cases, the borrower/sponsor may appoint a single lead arranger to set up the initial banking group and negotiate the loan terms with the other banks, and would mandate that the banks share information in order to reach a common loan price and terms. The interaction with the banks should be strictly within the parameters set by the borrower, otherwise here is a risk that information shared between the lead bank and other banks involved in setting the terms of the loan could lead to the loan terms moving against the borrower. *Coordinated agreements to limit supply (related to Article 101).* Any agreements between banks to limit supply (e.g. to agree not to participate or prevent other banks participating, or not to increase their participation where acting independently they would have done so) would be anti-competitive conduct related to collusion and coordination.	approached or specify the information to be shared and discussion (e.g. prohibiting discussions about limiting supply). The implications for investors of information exchange, such as Market Abuse laws about trading on information received about a loan. Borrower/sponsor sophistication regarding their expectations on price and the optimal structure for the bidding process.	demonstrable to compliance teams). In its strongest form, such consent should be specific as to who is contacted. There is evidence of generic market soundings by MLAs with investors prior to submitting bids, and whilst these discussions should not involve details of specific transactions information about specific lenders' appetite etc. may still be communicated back to the origination desks. This risk may be exacerbated where there is no significant functional separation between the syndication and origination desks. Soundings (even generic soundings) with other MLAs (as opposed to exclusively with institutional investors without connections to MLAs) could be abused so as to facilitate collusive action, even potentially enabling a group of MLAs (particularly one with fewer substitute MLAs) to achieve, and sustain, some degree of market power. In addition, although the bidding process is set up to keep lenders apart, the prevention of information sharing is governed by NDAs, which can be difficult to enforce. Therefore although the process set up by the borrower/sponsor in PF/INFRA loans reduces the risk of anti-competitive information sharing, the risk remains that this may happen. Equally, once an NDA is signed, it is evident to the counter-party that the breach of that agreement is problematic (i.e. it puts banks on clear notice of borrower/sponsor expectations). The use of a single MLA to set up a

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
			syndicate and negotiate with other banks is more likely to take place in PF/INFRA loans (although it is still not common). Whilst the fieldwork indicates that borrowers/sponsors retain control of this process, there remains the possibility that information sharing may occur such that the negotiations of the syndicate could be coordinated and the price and terms of the loan move against the borrower. The necessity of such information exchange would need to be assessed on a case-by-case basis, but this remains a risk area.
Competitive bidding process for appointing initial banking group among consortia	*Horizontal information exchange with risks of coordinated/collusive behaviour (related to Article 101).* *Coordinated agreements to limit supply (related to Article 101).* Where a group of banks come together to submit a joint bid in response to an RFP at the request of a borrower then, provided that the bank group operates within the instructions of the borrower, it is probable that the any information exchange between the banks for the purposes of putting together that proposal and the ultimate agreement that the banks reach as to the terms of that bid, will either fall outside Article 101(1) altogether or satisfy the conditions of Article 101(3). To the extent that discussions or agreements go beyond what is required for the purposes of submitting the joint bid then, depending on their nature, such discussions may breach Article 101(1) and indeed may be anti-competitive by object.	Clear parameters for the consortium: the borrower/sponsor should ensure that there are clear instructions to the consortium as to what they should agree jointly and what information they can share. The borrower/sponsor can place limits on the interaction between bank, e.g. splitting up the consortium during the bidding process to negotiate certain terms bilaterally such as hold levels or price. If consortia are invited to submit bids that compete with other consortia (instead of bidding as the only consortium) then there is scope for the borrower/sponsor to compare bids and maintain competitive pressure. The regulatory regime could place a responsibility on lenders to highlight	Consortia bids appear to be a feature of this market segment based on borrower/sponsor fieldwork, although no lenders in our sample participated in consortia. The main safeguard for which there is evidence is that borrowers/sponsors in PF/INFRA almost always use a competitive RFP process when appointing the lead banking group (whether this is soliciting independent bids or consortia) which implies that consortia at least compete and enable the borrower/sponsor to maintain competitive pressure (i.e. including such consortia in the RFP process could be pro-competitive). We do not have any evidence of there being regulations/requirements in place that place responsibility on banks bidding for the RFP to highlight to the borrower/sponsor where the process might not operate in their best interests. This could be a potential

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	In particular, agreements to limit lending capacity e.g. by not inviting other lenders to participate, or not increasing their participation (where acting independently they could and would have done so) are likely to have an anti-competitive effect and could be anti-competitive by object. *Abuse of bargaining power to impose uncompetitive terms and pricing (related to Article 102).* If the banks coming together in a consortium have excess bargaining power then there may be the risk of incompatibility with Article 102, if the consortium is able to engage in anti-competitive practices to inflate the price through information sharing and coordination, and thus abuse its position of power. *Borrower's process leading to sub-optimal outcomes.* The borrower/sponsor could set up the consortium in a way that facilitates sub-optimal outcomes. For example, by stipulating that a certain bank be involved in the loan where this bank requires a higher price than the other banks in order to participate, this would limit the ability of the consortium to replace this bank and agree a lower price.	to the borrower/sponsor where the bidding process may lead to a sub-optimal outcome.	safeguard to explore further.

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Direct appointment of a single / relationship bank without competitive process.	*Borrower's process leading to sub-optimal outcomes.* *Abuse of asymmetric information by lead bank.* The direct appointment of a bank without a competitive process may result in sub-optimal outcomes for the borrower/sponsor – this is not considered to be a competition law risk as it is part of the structure imposed by the borrower/sponsor, but may have regulatory implications. The single bank could use its relationship with the borrower to create a situation of 'lock-in' and thereby extract rents through imposing higher prices on the borrower compared to a competitive situation. A single relationship bank may also be able to unduly influence the syndication process in their favour, e.g. by excluding challenger banks from the wider syndicate in order to embed its position. These risks are influenced by the nature of the market - e.g. smaller geographic or product markets the borrower would have limited choice of eligible lead banks, and likelihood of repeat lending from the relationship bank and further information lock-in would be increased. Borrowers at the beginning of their 'life cycle' may also be more susceptible to the influence of relationship banks.	If a relationship bank competes on reputation for the borrower/sponsor favour then this will limit its ability to negatively influence loan outcomes (depending on the sophistication of the borrower and availability of alternative relationship banks). If borrower/sponsors are not 'locked-in- to their relationship banks then this reduced the scope of these banks to underperform or negatively influence the loan process in their favour. A further safeguard would be the sophistication of the borrower/sponsor in driving the syndication process and the extent to which they relied on the advice or influence of the relationship bank (e.g. in selecting other loan participants). The ability of the borrower/sponsor to monitor the MLA's interaction with participant investors would also undermine undue influence or the risks of the relationship bank manipulating loan terms. The ability of the borrower to replace the MLA in case of underperformance would incentivise the MLA to perform.	Similar to the LBO segment, the use of single MLAs is not widespread in the PF/INFRA segment and the appointment of these without a competitive process even less so. Similarly, repeat interactions between borrowers and lenders is low. Thus the magnitude of any risks will be small in this market. The sophistication and control of borrowers/sponsors in the PF/INFRA segment is more variable than in the LBO segment given their more heterogeneous nature and expertise, and MLAs on these transactions may be more likely to have the final say on which participants join the syndicate. Therefore in circumstances in which a single MLA *is* appointed it is likely to be relatively more able to influence the loan in its favour. This risk would be heightened further were the bank acting as MLA also be acting as debt advisor to the borrower/sponsor (see below). However, we note again the rarity with which a single MLA is appointed in the PF/INFRA segment.

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Post-mandate to loan agreement	*Horizontal information exchange with risks of coordinated/collusive behaviour (related to Article 101).* At this stage the borrower/sponsor mandates that the lead banks meet and agree final loan terms – these discussions are an essential element of the loan syndication process and provided that the banks are operating within the terms of the mandate granted by the borrower then exchanges of information between them which are related to achieving that aim will likely fall outside Article 101(1) or alternatively benefit from an exemption under Article 101(3). *Coordinated agreements to limit supply (related to Article 101).* Banks must be careful not to go beyond what is required under the borrower's mandate and reach any agreement or engage in any concerted practice to (artificially) raise the price or to restrict supply. Any such agreement should be viewed as anti-competitive by object. *Borrower's process leading to sub-optimal outcomes.* The process set up by the borrower/sponsor may lead to sub-optimal outcomes, e.g. if it stipulates that a particular bank(s) must be part of the syndicate and if that bank requires a higher price than the others to participate in the loan. A further risk at this stage when banks are brought together by the borrower is that	If the lead banking group is formed such that the key loan terms are discussed and negotiated bilaterally between the banks and the borrower/sponsor ahead of the post-mandate stage, then there will be less risk of the banks discussing these terms at this stage and moving against the borrower. The involvement of the borrower/sponsor in the post-mandate discussions would ensure that the communications were in line with the mandate. The strategy adopted by the borrower/sponsor should provide flexibility for banks to drop out of the process to avoid having to agree to terms at the highest common denominator (e.g. by building latency into the process). The timing of information flows to the lenders would also reduce the risk of banks dropping out, i.e. by ensuring that all due diligence is provided before mandate. The risks of inadvertent information sharing and future coordination/collusion would be mitigated the lower the likelihood of repeat interactions between lead banks on syndicated loans. The information gained from such observations would also be influenced	The scope for lenders discussing loan terms so as to move against the borrower at the post-mandate stage is low, given that in the PF/INFRA segment the process widely adopted is for the loan terms to be agreed bilaterally between the borrower/sponsor and individual lenders, and that joint discussions between lenders post-mandate should be limited to agreeing the loan documentation and syndication strategy. Borrowers/sponsors also aim to build in latency when obtaining loan commitments from the lead banking group. There is however some evidence that the loan structure may not always work in the borrower/sponsor's favour in terms of it agreeing the overall price to the highest common denominator rather than negotiating a common price. This may simply reflect the relative attractiveness of the credit itself. In the PF/INFRA segment there have been cases where the borrower/sponsor does bring lenders together at an earlier stage to discuss loan terms, e.g. in a club deal, and so this safeguard does not apply across the board. The exercise of control of the borrower/sponsor in these cases will therefore be more important i.e. by monitoring the discussions that take place. Whilst evidence gathered throughout the report indicates that borrowers/sponsors are sophisticated in this regard, some risk does remain than lenders may engage in discussions outside of the borrowers'

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	repeat interactions among lenders on transactions may lead to inadvertent information sharing around each other's behaviour or strategies which could be used to align their bids in future transactions.	by the type of discussions that are held during this interaction (e.g. if pricing and hold strategies are not discussed then it will be more difficult for lenders to observe this information about each other).	mandate. Any risk would be heightened considerably where borrowers were inexperienced or unsophisticated. The evidence of the multiple interactions between lenders on transactions over time leads us to conclude that there is a definite risk that lenders can observe each other's behaviours and strategies, which may enable them to engage in some coordination on future loan transactions. We do not have direct evidence that this happens in practice. Given that fact that in most cases the discussions that occur at this stage do not involve detailed information about pricing and hold strategies the amount of information that lenders are able to observe is likely to be limited. However this remains a risk area, albeit one we consider to be relatively immaterial.

Ancillary services in the PF/INFRA segment

Table 39: Summary and conclusions on risk to competition and sub-optimal outcomes for the provision of ancillary services

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
The allocation of ancillary services across banks, and the pricing of such services.	Lenders individually requiring that a borrower put in place certain ancillary services, and including conditions as to who can provide the services (e.g. only a lending bank), is unlikely to give rise to competition concerns if the ancillary services are directly related and necessary to the provision of the loan, and the conditions are directly necessary to the loan or do not limit competition (e.g. if there are a large number of banks from whom the borrower could chose to provide the services). *Horizontal information sharing to collude on the provision of ancillary services (related to Article 101).* However, there is a risk that, in an individual bid scenario, banks discuss and/or agree between themselves prior to making their bids that they will each make the provision of ancillary services a requirement of their lending (as opposed to each individually responding and – independently - making this a condition of their participation). There is a risk in an individual bid scenario that the practice of agreeing a single price and term sheet in respect of the provision of the lending "spills over" into the provision of related services. It is not necessarily the case that the setting of a single price by a group of banks providing the ancillary	Borrower clarity as to those required services that are to be considered related to the loan – and those that are not. Guidance could be provided to banks on the type of services that are likely to be related to the provision of the loan as opposed to those that are extraneous and which therefore the lenders should not generally (jointly) require be purchased from them. Borrower clarity as to services required – and not required. The borrower can seek to influence this by specifying which other services are required and which services are not required. If the RFQ specifies a particular approach, that approach should be respected by the banks.	Hedging is more frequently required as a condition of the loan in the PF/INFRA segment compared to LBOs given the nature of the project risks. In the majority of cases from our lender and borrower/sponsor fieldwork, the allocation of ancillary services is decided as part of the initial agreement of loan terms, or as a competitive process after the loan has closed. In both cases the borrower/sponsor would be able to choose between banks' offers and maintain competitive pressure. However a small minority of borrower/sponsors (in both the PF/INFRA and LBO segments) identified that the MLAs make the provision of ancillary services by them a condition of the loan (the rest negotiate ancillary services as part of the initial loan agreement process, or after the loan close). Whilst competition law precedent (e.g. Spain's CNMC) has not concluded that it is unlawful for lenders to specify that ancillary services be purchased from them, we do consider such a feature as raising the risk of a borrower/sponsor achieving a sub-optimal economic outcome. We further note that all of the respondents that cited such provision being a condition of the loan were from Spain. Where this feature occurs, we consider this an area of at least moderate competition concern.

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	service is inherent to the provision of that service, and the banks may be able to compete to provide such services on an individual basis. *Tying of ancillary services.* There is a risk that the lenders jointly require that the borrower purchase services from them that are unrelated to the loan and in respect of which they can compete individually. Where the provision of ancillary services by some lenders is restricted to the syndicate, or some sub-set of it, e.g. an obligation – or strong expectation – that purchase would be from the MLAs, especially if not all MLAs were able or willing to provide or quote for that service, then those particular lenders would be better able to exert bargaining power.		In the PF/INFRA segment it is more common for ancillary services to be allocated by the borrower/sponsor to lending banks at the initial stage of agreeing overall loan terms. The fact that the banks know who is to be providing the services provides them with scope to discuss and collude on pricing (i.e. makes it easier for them to subvert the proper, agreed process), even though the up-front allocation of ancillary services is not in itself an issue in terms of competition law. Restrictions placed by lenders on who can provide hedging services will be more problematic in markets where there is a limited number of lenders in the syndicate with the ability to provide such services, thus restricting borrower/sponsor choice. We do not have evidence of this occurring in practice, but note that smaller national markets (such a Poland in our sample) or else in more bespoke PF/INFRA deal will be more at risk. Ancillary services <u>not directly</u> related to the loan (e.g. further financing, investment services) can be negotiated as part of the loan negotiation, with both "right of first refusal" and "right to match" clauses being used. These have been found by the UK regulator as to have no client benefit – unless related to the replacement of bridging finance - and have been banned in the UK, but their use may be continued outside the UK (representing a continued risk to optimal outcome for

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
			borrowers/sponsors).

Debt advisors in the PF/INFRA segment

Table 40: Summary and conclusions on risk to competition and sub-optimal outcomes for the role of debt advisors

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
The use of debt advisors which are also involved in the syndicated loan	*Conflicts of interest and exploitation of information asymmetry.* This could give rise to significant conflicts of interest. If these conflicts are not well managed this could undermine the competitive nature of the syndication, and result in sub-optimal outcomes for the borrower/sponsor.	Capacity of the borrower/sponsor to make own judgements as to outcomes and/or to have access to other advisors. Training and policies for relevant staff, e.g. identification and management of conflicts of interest, clarity as to duty of care to provide neutral advice to clients.	The use of advisors who are also part of the syndicate is widespread among borrowers and sponsors, and in some cases with there being no other source of external advice. This issue is more common in the PF/INFRA segment than LBOs and could represent a non-negligible fraction of transactions. Our lender fieldwork shows that where an advisory role is provided by a lending bank, this is functionally separate from the lending role, and adherence to such protocols should mitigate the risk of sub-optimal outcomes to borrowers of not having a demonstrably independent advisor. There is (limited) evidence that some lenders do bundle – at the request of the borrower/sponsor – the advisory role with a lending role in PF/INFRA. The risks here would be heightened where the advisor is appointed directly without a competitive process and combines the lending role with the advisory role, whereby the borrower/sponsor may not receive the best loan outcome.

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
			A different form of concern would be where the advising bank attempted to influence the borrower/sponsor towards a strategy or debt structure that suited its lending arm, i.e. subverting the Chinese wall between the advisory and lending functions, and with this not being fully apparent to the borrower/sponsor. Based upon the description of their policies for managing such situations given to us by lenders, this would represent a significant breach of internal protocols. Where such controls were weak, this would be an area of high concern.

Secondary loan market trading in the PF/INFRA segment

Table 41: Summary and conclusions on risk to competition and sub-optimal outcomes for secondary trading

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Coordination by lenders on the sale of the loan on the secondary market	*Coordination and collusion in selling on the secondary market to influence supply and price (related to Article 101).* Co-operation between lenders post syndication could give rise to competition law risks, e.g. if underwriting banks were to co-ordinate in relation to when to sell, what proportion to sell or at what price to sell the debt in the secondary market, such co-ordination is unlikely to be justified and may be anti-competitive by object. In these circumstances the potential harm is to the purchasers of the debt in the secondary market. *Borrowers' process leading to sub-optimal outcomes.* Restrictions placed by borrowers/sponsors on transfers on loans may limit liquidity in the secondary market, potentially (but not necessarily) resulting in sub-optimal economic outcomes.	Guidance and training to lenders and borrowers/sponsors, covering the formation process and ongoing co-operation between the lending banks post syndication, highlighting the risk of co-ordination in relation to secondary market activity. Appropriate restrictions on post-closure sale by MLAs. A borrower could require that the underwriters hold a proportion of the debt for a period of time post syndication to avoid disruption.	There is no evidence of co-ordinated secondary market activity in our fieldwork, and the safeguard relating to hold levels is widely upheld in practice (indeed, it is a key part of the process). The features of the secondary (i.e. post closure trading) loan market (which remains a caveat emptor market with implicitly sophisticated buyers) should limit any attempt by sellers to manipulate the price of the debt, unless they are able to simultaneously identify a group of unsophisticated buyers of that debt. The economic benefit to lenders from any coordination may therefore be limited, reducing the plausibility of this risk. There is widespread evidence of borrower/sponsor restrictions on secondary trading. The lenders described restrictions imposed by PF/INFRA sponsors/borrowers as potentially including: no small transfers; an embargo during the construction period and the transfer being subject to borrower approval (except in case of default). Whilst such restrictions may be reasonably motivated (e.g. restricting the dispersion of deal-specific information), these do limit the development and efficiency of the secondary market. Given that secondary market pricing data are also used in the primary market this could also affect the development and efficiency of the primary market. The size and

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
			liquidity of the secondary market in the PF/INFRA segment is smaller than that in the LBO segment, i.e. the current value of secondary market information to the primary market is lower, and the impact therefore greater – albeit we consider such a knock-on effect relatively minor (financial intermediaries' key skill should be to assess credit risk).

Back office inefficiencies in the PF/INFRA segment

Table 42: Summary and conclusions on risk to competition and sub-optimal outcomes for back office inefficiencies

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Know-your-client and settlement processes.	*Increased transaction costs.* Certain back office inefficiencies increase transaction costs and potentially even reduce secondary market activity in consequence, potentially resulting in sub-optimal economic outcomes.	Blockchain technology may have the capacity to improve efficiency by creating the loan as a digital asset, automating the allocation of collateral, expediting the clearing and settlement process and speeding up the approval time for including additional investors (i.e. on the secondary loan market).	There are two main barriers to the potential benefits of blockchain, namely the development of the technology itself, and the potential of blockchain to overcome the real sources of inefficiency in the market. In relation to the first, our fieldwork shows that the technology to apply blockchain to syndicated loans has not been fully developed as yet (notwithstanding early adopters around loan completion) and that there is no sign that an across-the-market shift towards digitalisation is at all imminent. In relation to the second, other solutions to the problems of inefficient processes – in particular KYC – may be available without adopting novel technological solutions, such and banks pooling resources to create a centralised portal for KYC processes across shared clients. Therefore there is at least

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
			some potential in market-based initiatives for resolving KYC issues (assuming that competition authority approval is granted). However, such piecemeal approaches may bring other issues, in particular that they will obviously not be a complete solution, and — because they will in themselves consume time and resources — may create disincentives for such a complete solution.

Default and refinancing in the PF/INFRA segment

Table 43: Summary and conclusions on risk to competition and sub-optimal outcomes for default and refinancing

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
Refinancing in conditions of default	*Horizontal information exchange leading to collusive behaviour (related to Article 101).* There is a risk that the banks commence discussions about the future lending opportunity prior to an RFQ being issued in circumstances where they may be competing for a role in the future lending. *Abuse of collective dominance to inflate loan price and terms and to bundle/tie additional services (related to Article 102).* When a borrower faces an event of default, there is a risk that the group of lending banks might (in very exceptional circumstances) together be collectively dominant, because the limited options available to the borrower could mean the market is defined very narrowly. There is a further risk that the lending banks together impose certain conditions on	Competition law guidance or training for banks about information exchange issues and how to treat clients in a distressed situation. Regulatory regime and banks' duties to clients may reduce the likelihood that any abuses take place.	Competition policy training is undertaken by lenders' restructuring teams. These are functionally separate teams which take over the loan discussions from the origination teams in the case of a default risk, such that discussions between banks regarding the potential restructuring are not undertaken by teams involved in loan origination. Discussions between lenders are only possible under such policies at the instigation of the borrower. The discussions and negotiations of potential restructuring in the event of a default are performed collaboratively among the members of the syndicate. Whilst this may be efficiency enhancing, as time is often pressurised, it equally enhances the risk of banks acting with excess bargaining power. We note that the bank restructuring teams that we interviewed had undertaken some form of competition policy training, but clearly any subversion of

Element of process	Risk to competition law or sub-optimal outcomes	Potential safeguards	Findings and conclusions on safeguards and risks
	restructuring which are not objectively justified (e.g. tying the purchase of other services to the refinancing and imposing excessive prices as a condition to the lending). These actions could constitute an abuse of a collectively dominant position.		the proper process would be problematic. The extent to which the proper process had been subverted would need to be assessed on a case by case basis. Our fieldwork shows a majority of instances where refinancing discussions involved lenders from outside of the original syndicate. The willingness of the market to provide the new finance can be seen as a limit upon any collective market power that the existing group of lending banks may have. However, there is evidence of a non-trivial number of instances where the existing syndicate is the only option, i.e. there is scope to exert such market power. We do emphasise, however, that we do not have evidence for its abuse. In relation to the risk of the syndicate tying ancillary services to the refinancing, the fieldwork shows again that other, non-syndicate members are often involved in these discussions, which would provide market discipline against such coordinated tying behaviour. However, it is also apparent that in a substantial minority of cases such negotiations took place only with the syndicate members. There may be mitigating or efficiency enhancing circumstances, but it is also clear that such distressed circumstances can create the opportunity to price such ancillary services on non-competitive terms, and thus this is also an area deserving future monitoring.

Critical safeguards

We now draw upon the above analysis to identify the most important safeguards to ensure competitive outcomes in the loan syndication process.

- *Banks' duty of care to clients. There are two important safeguards here.*
  - Borrowers may source debt advice from the same lender that they wish to act as MLA (or, at least, consider acting an MLA). The critical safeguard here would be the adequate training and policies for the relevant staff at the potential MLAs. In particular, the training would need to cover topics such as the identification and management of conflicts of interest, and provide clarity as to duty of care to provide neutral advice to clients.
  - MLAs should ensure that there are not alternative options that could be put to the borrower, including inviting other lenders not previously involved in the process to participate (subject to obtaining borrower or sponsor consent), or considering a re-structuring of the loan, before aligning loan pricing or terms upwards to a highest common denominator. If the particular lender asking for the higher price is needed for the purposes of the joint bid (e.g. as explicitly required by the borrower), the price should be set at an acceptable level. The borrower (and its advisors, if relevant) can promote a beneficial outcome through ensuring a competitive bidding process (i.e. approaching more banks), building latency into the process and maintaining bilateral negotiations with individual lenders (or lender consortia) through to mandate award.
- *Avoidance of unwarranted information exchange.* In loan origination banks (and any other market players capable of forming the lead banking group) may need to exchange pricing information for the potential syndication while remaining competitors in the origination. The key safeguard would be that there are enforceable (and enforced) protocols around how – and in what form – any deal-relevant information obtained by the syndication function from other potential participants (who may also be competitors in the origination) may be transferred to the same bank's origination function in order to avoid anticompetitive alignment of prices.
- *Promotion of unbundled price competition.* Ancillary services not directly related to the loan (e.g. future M&A advisory services) can be negotiated as part of the loan negotiation, with both "right of first refusal" and "right to match" clauses being used. In the absence of market power, such a bundled offering may be pro-competitive but these have been found by the UK regulator as to have no client benefit – except when related to the replacement of bridging finance - and have been banned in the UK. It is advisable for syndicates to limit the cross-sale of ancillary services in order to avoid the risk of impairing competitive conditions in neighbouring markets to that of syndicated loans, and this should be kept outside the loan syndication process when these services are not directly linked to the loan.

1. Appendix: Glossary of Acronyms

Acronym	Description
CATI	Computer-Assisted Telephone Interview
CDO	Collateralized Debt Obligations
CLO	Collateralised Loan Obligation
Cov-lite	Covenant-lite
CSDR	Central Securities Depositories Regulation
EFSI	European Fund for Strategic Investments
EIB	European Investment Bank
Euribor	Euro Inter Bank Offered Rate
G-SIB	Globally Systemic Important Bank
IM	Information Memorandum
INFRA	Infrastructure
LBOs	Leveraged Buy-Outs
LIBOR	London Inter Bank Offered Rate
M&A	Mergers and Acquisitions
MiFID 2	Markets in Financial Instruments Directive 2
MLA	Mandated Lead Arranger
NDA	Non-Disclosure Agreement
OTC	Over-the-counter
PE	Private Equity
PF	Project Finance
RFP/RFQ	Request for Proposal/Request for quotation
S&P	Standard & Poor's
SME	Small to Medium-sized enterprise
SPV	Special Purpose Vehicle
TFEU	Treaty on the Functioning of the European Union

2. Appendix: Defining LBO, Project Finance and Infrastructure in the Thomson Reuters Loan Connector data

Our focus upon syndicated lending in particular market segments (LBO, Project Finance and Infrastructure) meant that we had to determine what data from the Thomson Reuters database fell within our research interest.

In the Loan Connector database, various labels are applied to private equity sponsor-related activity, including refinancing and recapitalizations. Our definition for LBO includes deals directly labelled as 'LBOs', as well those labelled as SBO (sponsored buyout) and MBO (management buyout, albeit representing a very small fraction of LBO deals).

Infrastructure is treated as a wholly subset of project finance and specifically includes projects in the following areas (in accordance with Loan Connector naming conventions):

- Electric/Cogeneration/Coal-fired/Gas-fired Electric/Geothermal/Hydroelectric
- Electric/Other
- Electricity transmission
- Gas/Oil Field Development Gas/Oil Processing Gas/Oil Storage
- Healthcare Infrastructure
- Infrastructure - Airports
- Infrastructure - Bridges/Tunnels
- Infrastructure - City Development
- Infrastructure - City Roads
- Infrastructure - Mass Transit
- Infrastructure - Ports
- Infrastructure - Toll Roads
- Other Pipelines Pulp & Paper Mills
- Recycling/Resource Recovery
- Telecommunications
- Water Facilities

The selection of the above project categories was based on the definitions provided by the exiting literature and working papers in the field. A recent publication from AFME for instance generally defines infrastructure as projects related to rail, roads, ports, telecoms,[228] whereas the European Fund for Strategic Investments (EFSI) also includes items such as broadband infrastructure, energy infrastructure and transport infrastructure as typical projects. Other sources also include gas and electricity networks in their definition, as well as wind and water infrastructure.[229]

Having specified the projects related to the infrastructure category, the project finance loan segment described in Chapter 3 is thus defined as the residual part of the whole project finance category, excluding infrastructure deals.

[228] AFME (2015) "Guide to infrastructure financing" https://www.afme.eu/globalassets/downloads/publications/afme_guide_to_infrastructure_financing2.pdf.
[229] ING (2013) "Syndicated lending and financing projects" https://www.ingwb.com/insights/newsletter/syndicated-lending-and-financing-projects.

Once data were downloaded from Loan Connector based on these criteria, some cleansing and refining was required in relation to: currency conversion, the presence of amended tranches and (exclusively) bilateral tranches. The approach we followed in dealing with these aspects is described below.

Loan Connector provides data on tranche and deal amounts either in national currency or in US dollars. In those cases where the amount was expressed in a currency different than euro, we applied the monthly exchange rates provided by Eurostat. More specifically:

- We converted national currency figures to euro for our core sample of six Member States. This guarantees more precision as it avoids a double conversion process (i.e. from national currency to US dollar and from US dollar to euro);
- We converted US dollar figures to euro for statistics related to the EU28 group, given the larger number of national currencies involved.

On the amendment feature, Loan Connector provides information on whether a tranche was amended during the life of the loan. Amendments are typically triggered by a change or extension in terms. As a result, the sample includes duplicated tranches (with the same identifier) every time a tranche is subject to an amendment. In order to address this issue, we kept in the sample only the original tranches when these were amended. The rationale was to make a consistent choice over the whole sample and see results based on the original conditions of loan issuance.

Loan Connector includes (some) bilateral loans (i.e. there is a sole lender) as well as syndicated loans. Therefore, deals that appear in the Loan Connector dataset as exclusively bilateral (i.e. comprising only bilateral tranches, all of which are with the same lender), and which Loan Connector lists as having a “Bilateral” distribution method, have been excluded from our analysis. However, some bilateral tranches are still part of the data set used in our analysis where (a) they are part of deals including also non-bilateral tranches or (b) the deal include only bilateral tranches but with different lenders.

3. Appendix: Mechanics of secondary loan market transfers

We describe here in more detail the types of transfer that can take place in the secondary loan market.

There are several mechanisms available for trading loans on the secondary market which differ in the degree to which they transfer the rights and obligations of the existing lender to a third party (i.e. buyer).[230] Starting from the most to least "complete" transfers these are:

- Novation.
- Legal assignment.
- Equitable assignment.
- Sub-participation.

With the first two methods, i.e. novation and legal assignments, the third party enters into a direct contractual relationship with the borrower (i.e. joining the syndicate ex post), while with the other two the third party's involvement in the loan is (to a larger or lesser extent) intermediated by the existing lender.

Novation is a complete transfer of the lender's obligations as well as rights specified in the loan agreement to a third party. Effectively, the buyer replaces the existing lender by taking on a position in the loan identical to that of the existing lender. All the current syndicate members as well as the borrower need to consent to a novation. That said, loan agreements usually include conditions, which – if satisfied – mean that the syndicate members and the borrower cannot withhold their consents. The original loan agreements also often include a separate schedule with the form of the transfer certificate. Thus, for any transfer by novation the transfer certificate is often already prepared and could be straightforwardly executed. The parties required for the execution (once the borrower's consent is obtained) are the agent bank, the buyer and the existing lenders.

In general, *assignment* is a transfer of rights but not obligations. It is often accompanied by an indemnity that the new lender will also assume those obligations "as if named as a lender under the facility agreement".[231] As opposed to a transfer by novation, assignment generally does not require obtaining the consent of the borrower (or other syndicate members).[232] *Legal assignment* is more complete and requires the transfer: to be unconditional, to cover the whole of the existing lender's share of the debt, to be in writing and signed by the existing lender, and to be disclosed in writing to the borrower (and other lenders, if the loan agreement specifies so). If any of those conditions is not satisfied, the transfer is an *equitable assignment*. The main difference between legal assignment and equitable assignment is that the assignee (i.e. the new

[230] LMA (2016) "Guide to secondary loan market transactions".
[231] LMA (2016) "Guide to secondary loan market transactions".
[232] There is some inconsistent evidence in the literature as to whether consent is required in the case of assignments:
- S&P (2014) "A Syndicated Loan Primer" says consent is 'typically' required, but that the consent cannot be withheld unless there is a reasonable objection. This is equivalent to what the LMA (2016) guidelines say on novation.
- Thomson Reuters glossary (cited below) states that assignments generally do not require consent.

Our interpretation is that assignments (as we define above) do not require consent. We are of the view that the S&P statement that consent is 'typically' required is the result of their using the terminology slightly differently, namely by grouping novation and assignment together, and collectively referring to them as assignment.

lender) often cannot bring any action against the borrower or other syndicate members and has to join the assignor (i.e. the existing lender).[233]

Sub-participations are agreements between an existing lender ('the grantor'), and a third party ('the participant'), which are independent from the primary loan agreement. Sub-participations generally do not require the borrower's consent, and could be kept confidential (however, borrowers/sponsors can make effecting such silent sub-participation more difficult). The general idea behind sub-participations is for the existing lender to mitigate the risk of the borrower defaulting on debt. The two main types of sub-participations are: funded and risk participations. In the first, the participant deposits money with the grantor, and agrees that it will be serviced and repaid only if the borrower services and repays the loan to the grantor. In the latter case, the participant does not deposit any money with the grantor upfront, but agrees to do so in certain circumstances (e.g. if the borrower defaults on any interest payments). In exchange for bearing that risk, the participant receives a fee from the grantor. In either case, although the participant is not in any contractual agreement with the borrower, the participant may obtain rights of subrogation, i.e. in case of the borrower's default the participant has the right to use any legal remedies available to the grantor against the borrower.

The majority of academic literature in this area relates to the US market, for which assignment is seen to constitute the majority of secondary loan trading (see, for example, Gupta et al. (2008)[234] and Bushman and Wittenberg-Moerman (2009)[235]). Assignment is also the most common form of secondary loan trading in several EU Member States, though it does vary on a country-by-country basis dependent on the precise legal context of that country. Table 44 below describes the most common forms of secondary loan trading for each of our sample Member States.

Table 44: Most common form of secondary loan trading by Member State

	Most common form of secondary loan trading
DE	The assignment and transfer by assumption of contract.
ES	Transfer of contractual position.
FR	Assignment.
NL	By Dutch law, only rights under a contract can be assigned by way of assignment, so assignments are rarely used. Instead, loans are typically transferred by way of a transfer of rights and an assumption of obligations.
PL	Assignment.
UK	Where debt is traded at par, novation is the usual method of transfer. Where distressed debt is traded, assignment or participation is the usual method.

Source: Clifford Chance (2014).[236]

[233] Thomson Reuters, "Assignment", Practical Law Glossary, https://uk.practicallaw.thomsonreuters.com/1-107-6442.
[234] Gupta et al. (2008) "Liquidity in the pricing of syndicated loans", *Journal of Financial Markets* 11 (2008) 339-376.
NB. Gupta et al. define only two types of transfer mechanism: assignment and participation. Thus it is our understanding that novation is grouped under assignment in their classification.
[235] Bushman, R. and Wittenberg-Moerman, R. (2009) "Does secondary loan market trading destroy lenders' incentives?"
[236] Clifford Chance (2014) "Loan trading across the globe".

4. Appendix: Regulatory interventions

CRD IV

Basel III is a package of reforms put together by the Basel Committee on Banking Supervision (BCBS), largely in response to what is now seen as insufficient prudential regulation responsible for the escalation of the recent financial crisis. The Basel III package was implemented in the European Union via the Capital Requirements Directive IV (CRD IV) and the Capital Requirements Regulation (CRR), effectively replacing the previous Capital Requirements Directives (2006/48/EC and 2006/49/EC). Broadly, CRD IV and the CRR impose requirements in three areas: capital, leverage and liquidity. The key areas of change from CRD III (and Basel II) are the liquidity coverage ratio (LCR), net stable funding ratio (NSFR), leverage ratio and also increased requirements on the quality and quantity of capital. The CRR became applicable as of 1 January 2014, whilst the CRD had to be transposed by Member States by 31 December 2013 – albeit that some provisions were gradually phased in by as late as January 2018.

Capital requirements

The capital requirements stipulate the ratio between the qualifying capital of a bank and the sum of its risk-weighted assets' value. This requirement acts as a buffer against potential future losses and is a measure of the difference between the value of an institution's assets and liabilities. All banks are also required to hold a capital conservation buffer and a countercyclical capital buffer, to ensure that they accumulate a sufficient capital base in prosperous times to enable them to absorb losses in the event of a crisis. The capital requirements set by CRD IV are more stringent than those in its predecessor, and the impacts on the syndicated loan market are likely to manifest primarily through the appetite for lending.

Leverage requirements

The leverage ratio is the ratio between the qualifying capital (Tier 1 capital) of a bank and the sum of the gross (not risk-weighted) assets' value. It is designed to restrict a bank's total indebtedness and contain the build-up of leverage in the banking sector. This ratio applied as a strict rule from 1 January 2018. Article 429(5) (c) of the CRD IV imposes an absolute prohibition on the ability of lenders to "net"[237] a loan against deposits for the purpose of calculating the leverage ratio. Industry associations have commented that the prohibition of netting would negatively affect appetite to participate in the loan market.[238]

Liquidity requirements

The **liquidity cover ratio (LCR)** requires banks and investment firms to hold high quality assets in quantities sufficient to meet their anticipated cash outflows (including undrawn lending commitments) over a 30 day stressed period. Under the LCR, the institution must therefore hold a 'pool' of high quality liquid assets which is at least equal to total net cash outflows. Article 412 of the CRR sets out the general LCR framework, and the LCR Delegated Regulation sets out rules governing which assets qualify as high quality liquid assets (HQLA) and how cash outflows and inflows should be calculated.[239] Loans are not eligible for inclusion in this liquid asset pool, although corporate bonds under certain haircuts could be included.

[237] Netting is a type of a quasi-security, arising when both parties hold debt of the other. It allows the debtor to apply the amount owed to it by the other party (the creditor) against the amount the debtor owes to the creditor, enabling the debtor to reduce or extinguish its liability.

[238] LMA (2015) "Regulation and the Loan Market".

[239] It should also be noted that although both banks and investment firms are subject to the general liquidity requirement under Article 412(1), only banks are directly subject to the detailed LCR set by the LCR Delegated Regulation.

The **net stable funding ratio (NSFR)** recommended by Basel III and implemented in the EU in January 2018, requires banks to hold stable funding in excess of a required amount in order to fund "illiquid" assets (i.e. those assets which are not deemed capable of being liquidated within a 12 month period). This means that many loan facilities with maturities of more than one year — in other words, most syndicated loan facilities — would need to be funded by stable funding. The amount of funding required depends on the asset held, any off-balance sheet contingent exposures incurred and/or activities pursued by the relevant institution.

Solvency II

Solvency II is an EU Directive that seeks, amongst other things, to establish new risk-based capital requirements for most insurers and reinsurers. Under Solvency II, affected firms must hold sufficient capital reserves to meet any expected future contractual liabilities, known as “technical provisions”.

In addition to holding capital to cover technical provisions, firms must also hold enough capital to comply with both a "minimum capital requirement" (MCR) and a "solvency capital requirement" (SCR). The MCR sets the minimum threshold for capital that a firm is required to maintain, meaning anything below is deemed "insolvent" for regulatory purposes. The SCR reflects a level of funds which should allow the insurer to absorb significant losses in a range of scenarios and continue to meet its obligations to clients.

Solvency II would have implications for the loan market through impacting the investment strategy of some loan market investors, i.e. regulated insurers and reinsurers.

Under previous legislation, insurers were only permitted to count assets against their capital requirements that were on a pre-determined list. The Solvency II requirements are not as prescriptive, and assets are now assessed in compliance with broader principles relating to general prudence, security and overall liquidity.[240]

Under the new rules, insurers are given greater freedom to invest. However, insurers also have to assess various categories of risk in relation to the specific asset held and hold additional capital to cover these. For example, the capital charge for an exposure to debt varies depending on the duration of the debt and the rating of the counterparty, similar to CRD IV.

MiFID 2

The MiFID 2 package regulates investment firms carrying out investment business throughout the EEA. The package seeks to provide a European-wide legislative framework for regulating the operation of financial markets in the EU. The legislation has several core objectives, including:

- increased investor protection;
- alignment of regulation across the EU in certain areas;
- increased competition across the financial markets; and
- introduction of reinforced supervisory powers.

Both MiFID and MiFIR were published on 12 June 2014 with an implementation date of 2018.

[240] See (2015) “LMA Regulation and the Loan Market”.

5. Appendix: Competition case law review — Introduction

The following appendices contains the list of cases reviewed by Euclid Law, covering the six Member States of interest to the study, and also Italy. Here we present the synthesis of these cases.

Introduction

The analysis was focused on competition policy issues around five categories of potential mischief:

- Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract.
- Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors).
- Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement).
- Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies).
- Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract.

Cases in these categories were sought across all industries. In addition, relevant cases were sought specifically in three segments: loans specifically, wholesale banking and in financial services as a whole.

These issues apply at different stages of the syndicated loan's life cycle, as summarised below.

Table 45: Competition law issues by phase of syndication

Syndication phases	Competition law issues
Pre RFQ	**Information exchange between banks** can be anti-competitive. ➢ E.g.: specific, detailed information about other banks future intentions, which could influence their competitive behaviour vis-à-vis the borrower
Post RFQ responses but pre-bid	

Individual bid scenario	**Information exchange between banks** could adversely impact the competition process, if beyond what is strictly required to have an understanding of the market's appetite for the transaction. ➢ E.g.: a lender understanding whether, how much and at what price level the other potential lender would be interested in participating **Agreement or Understanding between banks on related services** ➢ E.g.: agreement between banks to make the provision of services a requirement of their lending when the service is not directly related and necessary to the provision of the loan
Consortium bid scenario	**Information exchange between banks** on terms they are willing to participate could adversely impact the competition process, if beyond what is strictly required for the purposes of submitting a joint bid. **Agreement between banks on related services** ➢ E.g.: the lenders jointly require that the borrower purchase services from them that are unrelated to the loan and in respect of which they could compete individually **Agreements to limit supply** ➢ E.g.: discussions or agreements between banks not to invite other banks to participate or not to increase their participation
Post RFQ responses but pre-mandate	**Information exchange between prospective participating banks** can lead to price fixing or restriction of supply if without the express consent of the borrower. ➢ E.g.: prospective banks exchange information on the terms of their respective RFQ, their respective willingness to participate or adjust the amount they are willing to lend. **Only in circumstances where it is established that there could be market power (e.g. if a market is defined very narrowly, in distress situations or refinancing)[241]:** **Excessive bargaining power which could lead to an abuse** ➢ E.g.: a group of leading banks can use anti-competitive practices against a borrower in financial difficulties and facing an event of default, or if the market can be defined very narrowly due to the limited options available to the borrower.

[241] We note that we are not aware of any competition authority which has defined the market so narrowly.

	Abuse of market power through the imposition of refinancing conditions which are not objectively justified. ➢ E.g.: lenders tie the purchase of other services to the refinancing ➢ E.g.: lenders impose excessive prices as a condition to the lending
Post mandate but pre-finalised agreed terms	**Information exchange,** beyond the borrower's mandate can lead to price fixing or restriction of supply. ➢ E.g.: A flow of information to other banks concerning its requirements for continued participation, if beyond what is required under the borrower's mandate, specifically exchanging information on price and margin to achieve a better outcome for the group as a whole.
During syndication (in relation to flex clauses)	**Exchange of information, especially with regard to the operation of any flex** and outside the agreed process. ➢ E.g. discussions between the banks on how or whether the flex should be triggered and the level of the price which fall outside the agreed mechanism and where they do not reflect a direct reporting back of the outcome of the banks approaches to potential investors
Post-syndication	**Co-ordination between underwriting banks** ➢ E.g.: underwriting banks coordinate in relation to the time, proportion and price to sell the debts in a secondary market without proper justification

Cases directly relevant to loan syndication

The case law review revealed that in only one Member State within the scope of the review, the Netherlands, had the specific issue of syndicated loan market activity and its compatibility with Article 101/Article 102 (or Member State equivalent competition law provisions) been examined.[242] The NMA concluded that, whilst there were structural issues impacting the competitiveness of the markets in the period under examination, its review did not reveal any evidence giving rise to concerns about breaches of competition law.

In the UK the FCA considered syndicated loan markets as part of a wider market study into investment and corporate banking[243]. The FCA did not identify any specific competition law concerns with these markets but did note generally in respect of syndication that it has benefits for borrowers where it enables greater access to investors. The FCA examined whether the size or composition of syndicates (for example because the syndicate is too large) might lead to material detriment through inefficiencies but concluded there was evidence of such.

The FCA also considered whether certain reciprocal arrangements between banks might cause competition concerns and specifically any foreclosure concerns. The reciprocal arrangements under examination concerned a practice whereby a bank

[242]https://www.acm.nl/en/publications/publication/6254/NMa-limited-choice-for-undertakings-when-seeking-syndicated-loans.
[243]Financial Conduct Authority: Investment and Corporate Banking Market Study – MS15/1. https://www.fca.org.uk/publications/market-studies/investment-corporate-banking.

issuing its own financing might award mandates to another bank in part based on return business. The FCA found that this practice was most common in bank financing and in particular in covered bonds. However the FCA found no evidence that this practice excluded other banks from competing for such mandates at the time of its review.

The FCA raised concerned about certain cross-selling activities restricting costumers' future choices and ultimately decided to prohibit certain provisions included in appointments and mandates (which could include a mandate/appointment relating to loan syndication) which give banks rights to future appointments on primary market and mergers and acquisitions transactions.

Cases related to bid-rigging

In so far as the review of cases related to bid rigging is concerned we note that in several Member States there have been cases where, unsurprisingly, a feature of the bid-rigging arrangement is a mechanism to "compensate" any agreed loser of a bid/tender process, either by way of assistance in winning future bids or through appointment as a sub-contractor on the then bid in question. In some cases the compensation payment has been more direct e.g. by way of a direct payment between competitors[244] or by way of another mechanism such as payment of a higher rent.[245]

Syndicated loans markets may display similar characteristics to those present in these cases in so far as the way in which banks are appointed to the various roles within a syndicate may facilitate a compensation mechanism. The frequency with which similar groups of banks participate in tenders in respect of loan origination or are otherwise involved in participating in syndicated loans together could facilitate compensation arrangements between them, either through arrangements related to future tenders or to the allocation of roles on a syndication (or a combination of the two). This might be further facilitated by the arrangements agreed with the borrower for the allocation of fees as between the various banks depending on their roles in the syndication process. The extent to which collusion might be facilitated or frustrated is likely to depend on various factors, notably the regularity and predictability of tenders, the number and stability of the group of banks participating in tenders in any particular market, the degree of engagement of the borrower or sponsor and the tender design and the terms of appointment of the MLA(s).

Cases related to information exchange

Several of the cases reviewed also demonstrate that, where competitors come together for legitimate purposes, such as a response to a regulatory change or other legitimate co-operation, then the frequency of contact and familiarity resulting from such proximity can sometimes result in information being exchanged and agreements being reached that go beyond what is necessary to achieve the legitimate purposes at hand.

In syndicated loan markets competing banks have frequent and close contact and co-operation with each other through both the individual syndicated loans that they participate in together and through trade bodies such as the LMA. In certain circumstances there may also be a need for contacts between banks to ascertain

[244] For example, UK case on bid rigging in construction http://www.matrixlaw.co.uk/wp-content/uploads/2016/03/18_05_2011_02_32_17_Christopher-Brown-Construction-Judgments-paper.pdf.

[245] Decision 13-D-09 of 17 April 2013 relating to practices implemented in a public procurement for the reconstruction of watchtowers at the Prison of Perpignan http://www.autoritedelaconcurrence.fr/user/standard.php?id_rub=483&id_article=2074&lang=en

appetite for participation in syndications. What might be necessary and in the interests of the borrower, in terms of contacts, information exchange and other forms of co-operation between competing banks and at what stage may also vary from transaction to transaction and depending on market conditions.

In this context there are various ways in which the arrangements between competing banks might extend beyond what is necessary to achieve the legitimate aims for example:

- discussions preceding the submission of bids which might alter the competitive outcome of the bid;
- discussions and arrangements relating to other products/services offered by the banks to the borrower;
- discussions and arrangements during the syndication process which might alter the outcome of the syndication process for the borrower e.g. inappropriate discussions relating to operation of a market flex arrangement; and
- discussions related to other lending opportunities outside the particular transaction in question.

Awareness of appropriate boundaries may be more difficult to embed and monitor where multiple individuals have frequent contact with competitors and where what is necessary and appropriate may vary depending on numerous factors.

Cases relevant to abuse of dominance

The case law review did not reveal any cases where a dominant position was found to result from an appointment or grant of a contractual right on a transactional basis akin to the appointment of MLA(s) for the purposes of origination and syndication of loans. In the cases reviewed those entities found to have abused a dominant position were found to have had sustained market power and customers had limited ability to switch to alternative suppliers.

In syndicated loans markets the scenario where a customer is most likely to have limited ability to switch to alternative lenders is in the event of a default by the borrower. In such a situation there may be a potential for existing lenders to abuse that position by, for example, extracting excessive prices or tying/bundling other services into any further financing arrangements.

5a. Appendix: Competition case law review — France

Identification of relevant cases

Platform: French Competition Authority ("FCA")
Period: 2010-2017

Segment 1. Loan product search

No case available

Segment 2. Wholesale Banking services

No case available

Segment 3. Financial services, including insurance

No	Case Title	Case Reference	Date of closure/decision	Market Sector	Legislation
1	Opinion on competition conditions in the real estate bank guarantee sector	15-A-09	9 July 2015	Real estate bank guarantees	Articles L. 420-1 and L. 420-2 of the commercial code
2	Decision related to prices and associated conditions applied by banks and financial institutions for processing cheques submitted for encashment purposes	10-D-28	20 September 2010	Banking	Article L. 420-1 of the commercial code and article 101 TFEU

<u>Category A.</u> Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract.

No	Case Title	Case Reference	Date of closure/decision	Market Sector	Legislation
1	Decision related to practices in the sector of operating tables	10-D-04	26 January 2010	Operating tables	Article L. 420-1 of the commercial code, article 101 TFEU

2	Decision related to practices identified in the context of a call for tenders launched by the General Council of the Alpes-Maritimes for landscaping work on a road junction	10-D-10	12 March 2010	Agriculture	Article L. 420-1 of the commercial code
3	Decision related painting services for naval equipment and engineering structures	11-D-07	24 February 2011	Industrial painting	Article L. 420-1 of the commercial code
4	Decision related to practices implemented in a public procurement for the reconstruction of watchtowers at the Prison of Perpignan	13-D-09	17 April 2013	Prison watchtowers	Article L. 420-1 of the commercial code
5	Decision related to practices in the school bus transport sector in Bas-Rhin	16-D-02	27 January 2016	Transport	Article L. 420-1 of the Commercial code
6	Decision related to practices implemented in the market for land assistance of public land agency of Ouest Rhône-Alpes	16-D-27	2 December 2016	Construction	Article L. 420-1 of the Commercial code

Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors)					
No	**Case Title**	**Case Reference**	**Date of closure/decision**	**Market Sector**	**Legislation**
1	Decision related to delivery	15-D-19	15 December 2015	Delivery services	Article L. 420-1, 101

	services				TFUE

Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement)					
No	**Case Title**	**Case Reference**	**Date of closure/decision**	**Market Sector**	**Legislation**
1	Decision related to related to the launch of overseas DTT	15-D-01	5 February 2015	Telecoms	Article L. 420-2, 102 TFUE
2	Decision 15-D-06 of 21 April 2015 related to practices implemented by Booking.com B.V., Booking.com France SAS and Booking.com Customer Service France SAS in the online hotel booking sector	15-D-06	21 April 2015	Hotel	Articles L. 420-1 of the Commercial Code and Article 101, § 1 TFEU and / or Articles L. 420-2 of the Commercial Code and 102 TFEU

Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies)					
No	**Case Title**	**Case Reference**	**Date of closure/decision**	**Market Sector**	**Legislation**
1	Opinion related to crossed usage of client databases in the context of convergence between fixed-line and mobile telecoms	10-A-13	14 June 2010	Telecoms	Article 101 and 102 TFEU

Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract

No	Case Title	Case Reference	Date of closure/decision	Market Sector	Legislation
No case found.					

Summary of decisions

Segment 3. Financial services, including insurance

Opinion 15-A-09 of 9 July 2015 on competition conditions in the real estate bank guarantee sector[246].

- Following a referral from French consumer organisation UFC-Que Choisir, the FCA issued an opinion which recommends that more information on the guarantee rate be provided by real estate borrowers. However, separating credit offers and guarantee offers appears difficult to implement in practice.
- The market needs greater transparency as there is a structurally limited choice for borrowers in terms of real estate credit guarantees.
- The FCA recommends that consumers be better informed on bank guarantee rates in order to encourage banking institutions to choose the most competitive guarantee bodies. Transparency of rates could be planned for the transposition of the directive on real estate credit.

Decision 10-D-28 of 20 September 2010 on prices and associated conditions applied by banks and financial institutions for processing cheques submitted for encashment purposes[247]

- The FCA opened ex officio proceedings into the competitive situation concerning the prices and associated conditions applied by banks and financial institutions for processing cheques submitted for encashment purposes.
- The exemptability of the CEIC is examined below as regards the first two conditions provided for by article L 420-4 of the Commercial Code and article 81 EC: while the banks' agreement that enabled the switch to the ECHANGE IMAGE CHÈQUES (EIC) contributed to the achievement of economic progress, i.e. the implementation of a dematerialised system for exchanging cheques, the parties do not demonstrate, however, that the establishment of a fee such as the "Commission d'échange image-chèque" ("**CEIC**") was necessary to bring about these efficiency gains.
- The FCA analysed the arguments put forward by the parties to demonstrate the necessity of the CEIC through several stages:
  - The framework of the agreement (The context of the euro changeover, The required consensus for establishing a new interbank payment system, Factoring in the individual incentives of the banks to agree to dematerialised cheque exchanges)
  - the lack of demonstration by the parties that, at the time of the CIR negotiations.
  - introduction of a fixed fee per transaction was not in any event liable to offset the treasury losses claimed.
  - an economic assessment of the switch to the EIC will be presented for each of the banks.
  - CEIC was not adjusted at the end of the three-year period stipulated in the agreement of 3 February 2000.

[246] http://www.autoritedelaconcurrence.fr/user/standard.php?id_rub=607&id_article=2690
[247] http://www.autoritedelaconcurrence.fr/doc/10d28_en.pdf.

- The parties have not proved that the introduction of a clearing mechanism, in the form of a fixed interbank fee paid per transaction by the remitting bank to the issuing bank, was necessary to give all the banks the essential incentives to switch to the EIC.
- Consequently, this practice cannot be exempted.

Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract.

Decision 10-D-04 of 26 January 2010 on practices in the sector of operating tables[248] (upheld by the Paris Court of Appeal, 28 October 2010[249])

- ALM and Maquet are two manufacturers of operating tables which belong to the same group and offered separate bids.
- According to the FCA, two companies agreed to coordinate their offers and exchanged information prior to the date of the call for tenders.
- The bids were not independent but concerted which mislead public purchasers.
- As a consequence, ALM and Maquet agreed to offer distinct bids which were not independent using various methods simulating the autonomy of offers and companies.
- The FCA imposed a fine of EUR 750,000 to ALM and EUR 750,000 to Maquet.

Decision 10-D-10 of 12 March 2010 related to practices identified in the context of a call for tenders launched by the General Council of the Alpes-Maritimes for landscaping work on a road junction[250]

- The two companies SAS La Nouvelle Sirolaise de Construction SARL Provence Jardins shared information before the end of the tender process.
- The FCA considered that it amounts to a collusion between bidders and constitutes an infringement of article L. 420-1 of the French commercial code.

Decision 11-D-07 of 24 February 2011 related to the industrial painting sector[251]

- Four companies rigged bids for procurement contracts in the sector of painting services for naval equipment and engineering structures between 2005 and 2006.
- The companies exchanged information on their prices before the submission of tenders and submitted sham bids
    - In practice, before submitting tenders, companies informed each other of their prices by fax, phone or electronic means. Sham bids were submitted to the contracting entities in order to leave an impression of genuine competition and to secure projects for one of the companies which appeared consequently as the best bidder.
- Contractors were misled and overcharged.
- Purchasers calling for tenders were misled through these practices which contributed to the restriction of competition and drove up prices. When some invitations to tender proved unsuccessful, new tenders had to be organized, involving new costs.

[248] http://www.autoritedelaconcurrence.fr/pdf/avis/10d04.pdf.
[249] http://www.autoritedelaconcurrence.fr/doc/ca10d04.pdf.
[250] http://www.autoritedelaconcurrence.fr/user/avisdec.php?numero=10D10.
[251] http://www.autoritedelaconcurrence.fr/user/standard.php?id_rub=389&id_article=1557.
http://www.autoritedelaconcurrence.fr/user/avisdec.php?numero=11-D-07.

Decision 13-D-09 of 17 April 2013 relating to practices implemented in a public procurement for the reconstruction of watchtowers at the Prison of Perpignan[252]

- The FCA fined 4 companies of the Eiffage group and the Vilmor company for entering into an anticompetitive agreement within the framework of a public procurement for the reconstruction of watchtowers at the prison of Perpignan.
- Eiffage Construction Roussillon and Vilmor Construction had exchanged information before submitting their bids in response to the invitation to tender. This took the form of a cover bid by Vilmor Construction that was designed to make Eiffage Construction Roussillon's bid appear more attractive. For its part, Eiffage Construction Roussillon agreed to pay extra rent for the land that was adjacent to the site of the works and belonged to a property development company, in which the CEO of Vilmor Construction was one of the main partners.
- The contracting authority was misled as to the intensity of competition.
- The FCA imposed fines of € 960,000 to four companies in the Eiffage group and € 5,000 to Vilmor Construction.

Decision 16-D-02 of 27 January 2016 related to practices in the school bus transport sector in Bas-Rhin[253]

- Members of a group of companies sought to limit competition between them, and also vis-à-vis non-member companies through a non-aggression pact between the members of the cartel.
- Such practices had the object of distributing the school bus routes contracts among members to the detriment of the public purchaser.

Decision 16-D-27 of 2 December 2016 related to practices implemented in the market for land assistance of public land agency of Ouest Rhône-Alpes.[254]

- The object of the agreement was market sharing through an exchange of sensitive information prior to the award of the markets.
- The FCA imposed to EURL SETIS and Groupe Degaud a fine of €40,000.

Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors)

Decision 15-D-19 of 15 December 2015 related to Delivery services[255]

- In this case, the FCA found two anticompetitive agreements in the delivery service industry (through roundtable discussions during the trade council's meetings, Bilateral discussions between companies consolidated the agreement).
- The principal agreement concerns 20 companies as well as the professional trade associations TLF (transport and logistics trade association) and involved, during the period between 2004 and 2010, repeated collusions between competitors regarding annual price increases.

[252] http://www.autoritedelaconcurrence.fr/user/standard.php?id_rub=483&id_article=2074&lang=en
[253] http://www.autoritedelaconcurrence.fr/pdf/avis/16d02.pdf.
[254] http://www.autoritedelaconcurrence.fr/pdf/avis/16d27.pdf.
[255] http://www.autoritedelaconcurrence.fr/pdf/avis/15d19.pdf.

- A smaller-scale agreement involving 15 of the same companies as well as TLF was also fined.
- It concerned defining a common method for passing on the costs of a "diesel surcharge" during the course of seven annual price increase campaigns held between September 2004 and September 2010, the delivery service and express delivery service companies shared, within a multi-party context, in particular during TLF meetings, sensitive business information relating to their annual pricing increases.
- This process of sharing information was often backed up by communications between two or more of the companies involved.
- By way of example, during the 2006-2007 trade negotiations, the majority of the companies that had initially envisaged a price increase of approximately 5%, after sharing information, increased their demands to a higher level – around 7%
- The FCA imposed an overall penalty of €672 million.

Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement)

Decision 15-D-01 of 5 February 2015 related to the launch of overseas DTT[256]

- In 2010 France télévision published nine calls for tender for the award of DTT broadcasting contracts in the overseas territories and communities (five-year contracts).
- Three operators responded to these calls for tender including TDF, the incumbent terrestrial Hertzian broadcaster and OMT, the leading alternative overseas telecommunications operator.
- Before and during the competitive dialogue required under tender regulations, TDF did not publish any technical and pricing information concerning access to its infrastructures. This information was however necessary for its competitors to respond to the calls for tender. The nine contracts were awarded to TDF.
- The FCA imposed a fine to TDF of € 4.2 million.
- The case is pending (appeal before the French Supreme Court).

Decision 15-D-06 of 21 April 2015 related to practices implemented by Booking.com B.V., Booking.com France SAS and Booking.com Customer Service France SAS in the online hotel booking sector[257]

- The FCA noted that:
  - In a given market, when a platform with market power implements a parity clause, competing platforms are encouraged to implement similar clauses in order to guard against the risk of have higher retail prices on their sales channel than their competitors.
  - It is not excluded that the fact for Booking.com, or any other platforms, to impose parity clauses to hotels could be considered as an exclusionary practice which could amount to an individual or collective abuse of dominance under Articles 102 TFEU and 420-2 of the Commercial Code.
  - In conclusion, it appears that these practices raise competition concerns and may be qualified as anti-competitive under Articles L. 420-1 of the

[256] http://www.autoritedelaconcurrence.fr/user/standard.php?id_rub=607&id_article=2533
[257] http://www.autoritedelaconcurrence.fr/pdf/avis/15d06.pdf http://www.autoritedelaconcurrence.fr/user/standard.php?id_rub=607&id_article=2535

Commercial Code and Article 101, § 1 TFEU and / or Articles L. 420-2 of the Commercial Code and 102 TFEU.

- Booking.com thus committed to amend the price parity clause and remove any clause imposing parity obligations in terms of the availability of rooms or commercial conditions. This is not only in relation to competing platforms but also hotels' direct offline channels as well as some of their online channels.

Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies)

Opinion 10-A-13 of 14 June 2010 related to crossed usage of client databases in the context of convergence between fixed-line and mobile telecoms [258]

- The considered that crossed usage of client databases is possible, even for Orange and that bundling offers by Orange should be assessed on a case-by-case basis.
- The convergence movement between fixed-lines and mobiles is leading to the appearance of a "universal" operator model, resulting in the emergence of new commercial practices.
- This evolution is prompting operators to make crossed usage of their client databases and to propose "all in one" bundled offers, referred to as convergence offers.
- The FCA issued recommendations in order to improve the market fluidity.
- The main risks of such offers are the following:
  - the generalisation of bundling offers could further increase the cost for a consumer to change operators,
  - bundling offers may lead to a risk of foreclosure, no longer only of customers, but also of households,
  - concerning entry barriers in the mobile market, the generalization of convergence offers could distort competition for the benefit of the three existing mobile operators, and to the detriment of other operators.
- The FCA recommends the adoption of measures in order to improve the market fluidity and to prevent foreclosure risks. The measures could relate to the commitment terms, the re-commitment conditions for customers subscribing for a bundling offer, synchronizing the terms of the subscriptions for the high speed and mobile services, the standardisation of certain functionalities in order to ensure interoperability, as well as the portability of the current and future convergent services.
- As for efficiency justifications, the FCA notes that even though not directly related to competition law, certain measures are favourable to consumers, and tend to ease the process of changing operators. It could also improve the market fluidity and prevent foreclosure.

Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract

None.

[258] http://www.autoritedelaconcurrence.fr/pdf/avis/10a13.pdf. , http://www.autoritedelaconcurrence.fr/user/standard.php?id_rub=368&id_article=1416.

5b. Appendix: Competition case law review — Germany

Identification of relevant cases

Platform- Bundeskartellamt (BKA) Period- 2010-2017					
No	**Case Tile**	**Case Reference**	**Date of closure/decision**	**Segment**	**Legislation**
Segment 1. Loan product search *-Syndication loan, loan agreement, bank facility, multilateral loan, club deal, syndicated deal, corporate lending, loan (search terms)* *-(Kreditsyndizierung, Syndizierung, syndizierter Kredit, Kreditkonsortium, Konsortialkredit, Kreditvertrag, Darlehensvertrag, Bankeinrichtung, Bankenfazilität, multilaterales Darlehen, multilateraler Kredit, Club Deal, Firmenkreditgeschäft, Unternehmenskredit)*					
None					
Segment 2. Wholsesaale Banking services *-Market studies/Investiagtions/cases, relevant to categories A-E, and the loan syndication process.*					
None					
Segment 3. Financial services, including insurance *-Market studies/Investiagtions/cases relevant to categories A-E, and the loan syndication process.*					
None					
Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract. *-bid suppression and the promise of a sub-contract, collusive tendering, subcontractor collusion, cover pricing, contractual offer, collusion between bidders, tender, information exchange (search terms)* *- (Angebotsabsprache, Angebotsmanipulation, Angebotsentstörung, Untervertragzusage, Ausschreibungsabsprache, Unterlieferanten, Scheinangebote, Vertragsangebot, Absprache zwischen den Bietern)*					
1	Bid-rigging in the ophthalmological industry[259]	B3-130/11	2 May 2012	Ophthalmolo-gical Products	§ 1 of the GWB & § 73c of the SGB V[260]
2	Collusion in the TV and film production industry[261]	B12-23/15	26 July 2016	TV and Film Production	not available
3	Bid-rigging in the rail industry[262]	B12–11/11	July 2012	Rail Products	not available

[259] http://www.bundeskartellamt.de/SharedDocs/Entscheidung/DE/Fallberichte/Kartellverbot/2012/B3-130-11.pdf?__blob=publicationFile&v=4

[260] Sozialgesetzbuch, Fünftes Buch - Gesetzliche Krankenversicherung

[261] http://www.bundeskartellamt.de/SharedDocs/Entscheidung/DE/Fallberichte/Kartellverbot/2016/B12-23-15.pdf?__blob=publicationFile&v=3.

[262] http://www.bundeskartellamt.de/SharedDocs/Entscheidung/DE/Fallberichte/Kartellverbot/2012/B12-11-11.pdf?__blob=publicationFile&v=4.

<table>
<tr><td colspan="6">Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors)
–Exchange of commercially sensitive Information, concerted practice, price-fixing, coordinating commercial and promotional strategies between competitors, information exchange between bidders, efficiency enhancing discussions between competitors
- (Informationsaustausch, Austausch von Informationen, Austausch sensibler Geschäftsinformationen, abgestimmtes Verhalten, Preisfestsetzung, Preisabsprache, Koordinierung von Strategien, Informationsaustausch zwischen den Biedern, Effizienzsteigerung durch die Gespräche)</td></tr>
<tr><td>4</td><td>Joint marketing of pine wood[263]</td><td>B1–72/12</td><td>9 July 2015</td><td>Pine Wood</td><td>Article 32(1) of the GWB & Article 101 of the TFEU</td></tr>
<tr><td>5</td><td>Cooperation in the fast connection broadband market[264]</td><td>B7–46/13</td><td>4 November 2014</td><td>Telecommu nications</td><td>§ 1 of the GWB & Article 101 of the TFEU</td></tr>
<tr><td colspan="6">Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement)
-exploitative abuses, excessive pricing, price discrimination, contractual abuses, vertical restraints, contractual power, abuse of dominance, market power conferred by contract (Ausbeutungsmissbrauch, überhöhte Preise, Preisdiskriminierung, missbräuchliche Vertragsvorschriften, vertikale Beschränkungen, Marktmacht, Missbrauch einer beherrschenden Stellung, Missbrauchs einer marktbeherrschenden Stellung, Marktstärke)</td></tr>
<tr><td colspan="6">None</td></tr>
<tr><td colspan="6">Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies)
-abuse of dominance, market power, bundling and appetite, tying, efficiencies and bundling, validations for tying and bundling
-(Missbrauch einer beherrschenden Stellung, Missbrauchs einer marktbeherrschenden Stellung, Marktmacht, Bündelung, Appetite, Bindung, Knüpfen, Kopplungsbindung, Effizienz, Validierung)</td></tr>
<tr><td>6</td><td>Deutsche Bahn[265]</td><td>B9-136/13</td><td>24 May 2016</td><td>Rail Transport</td><td>§ 19 of the GWB & Article 102 of the TFEU</td></tr>
<tr><td colspan="6">Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract
-Abuse of dominance, agreement to vary contract price/terms, change of existing terms, alterations to existing contract (Vereinbarung die Preisen/die Bedingungen zu verändern, Veränderung von bestehenden Bedingungen, Abwechslungen des bestehenden Vertrags)</td></tr>
</table>

[263] http://www.bundeskartellamt.de/SharedDocs/Entscheidung/DE/Entscheidungen/Kartellverbot/2015/B1-72-12.pdf?__blob=publicationFile&v=5.

[264] http://www.bundeskartellamt.de/SharedDocs/Entscheidung/DE/Entscheidungen/Kartellverbot/2015/B7-46-13.pdf?__blob=publicationFile&v=2.

[265] http://www.bundeskartellamt.de/SharedDocs/Entscheidung/DE/Entscheidungen/Missbrauchsaufsicht/2016/B9-136-13.pdf?__blob=publicationFile&v=2.

None

Jurisdictional Review

Segment 1. Loan product search

None.

Segment 2. Banking services

None.

Segment 3. Financial services, including insurance

None.

Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract.

1. **Bid-rigging in the ophthalmological industry**

- A number of ophthalmologist associations colluded in the tender process for the supply of ophthalmological products organised by AOK Bayern, a health insurance company.
- The companies' conduct consisted of proposing a joint offer (instead of individual ones) and thus considered a restriction of competition.
- The investigation closed due to the application of a *lex specialis* provision of § 73c(3)(1)(4) SGB V allowing for collective offers in the field of medical products.

2. **Collusion in the TV and film production industry**

- Two German TV and film studios colluded and exchanged commercially sensitive information, which influenced their participation in tender processes.
- The companies exchanged information related to: prices, costs, content of offers, details on their participation in tenders and other commercially sensitive information.
- The companies colluded in two tender processes.
- The communications took place prior to and during the tender proceedings.

3. **Bid-rigging in the rail industry**

- Four German rail product manufacturers colluded in tenders organized by Deutsche Bahn, a holder of German railway infrastructure.
- The collusion consisted of coordinating the companies' participation in tenders and the content of their offers, particularly prices and volumes.
- The information was exchanged via phone, e-mail and during personal meetings.

Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors)

4. Joint marketing of pine wood

- Baden-Württemberg State exchanged commercially sensitive information and conducted marketing agreements with private and corporate holders of forests in order to jointly market pine wood.
- The exchange of information and the agreements related to production volumes, product ranges, prices and time schedules of sales.
- The BKA found that Baden-Württemberg, as an owner of forests, is a competitor of private and corporate holders of forests.
- The exchange of information and agreements resulted in a restriction of competition- by fixing prices and production quotas.
- Such agreements bring efficiencies by improving the marketing of pine wood. However, this was true only with respect to the forest holders of less than 100ha. Baden-Württemberg went beyond this threshold by having contacted larger forest holders.

5. Cooperation in the fast connection broadband

- Telefónica Germany GmbH & Co. OHG and Telekom Deutschland GmbH intended to implement an agreement, which would help them offer faster broadband connection. They reported their intended agreement to the BKA asking for validation.
- The cooperation involved the exchange of commercially sensitive information and the potential restriction of infrastructure competition.
- The BKA concluded that the agreement did not restrict competition, as the cooperation to develop faster broadband connection could not be achieved without the exchange of information.
- The BKA did not assess the efficiency reached by the cooperation, however, it reserved its right to do so if the exchange would exceed the objectives reported.

Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement)

None.

Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies)

6. Deutsche Bahn

- Deutsche Bahn, a holder of the German railway infrastructure, established with private railway operators agreements giving the latter access to its infrastructure.
- Deutsche Bahn bundled the agreement on tariffs with the agreement on sales cooperation.
- The extent of obligations imposed by Deutsche Bahn on railway operators was extensive. This was considered to be the abuse of Deutsche Bahn's dominant position.

Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract

None.

5c. Appendix: Competition case law review — Italy

Identification of relevant cases

Platform - Autorita Garante Della Concorrenza E Del Mercato (AGCM) Period- 2010-2017					
No	**Case Tile**	**Case Reference**	**Date of closure/decision**	**Market Sector**	**Legislation**
Segment 1. Loan product search *-Syndication loan, loan agreement, bank facility, multilateral loan, club deal, syndicated deal, corporate lending, loan (search terms)*					
1	**Banca Popolare di Vicenza**[266]	PS10363	*12 September 2016*	Finance	Article 101 TFEU & Law No. 287/90, Section 3
2	**Mortgage interest rate collusion**[267]	I777	4 March 2016	Finance	Article 101 TFEU & Law No. 287/90, Section 2
Segment 2. Wholesale Banking services *-Market studies/Investigations/cases relevant to categories A-E and the loan syndication process.*					
None					
Segment 3. Financial services, including insurance *-Market studies/Investigations/cases relevant to categories A-E and the loan syndication process.*					
None					
Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract. *-bid suppression and the promise of a sub-contract, collusive tendering, subcontractor collusion, cover pricing, contractual offer, collusion between bidders, tender, information exchange (search terms)*					
3	Public school cleaning services[268]	I785	20 January 2016	Home Services	Article 101 TFEU & Law No. 287/90, Section 2
4	Asbestos[269]	-	18 November 2015	-	Article 101 TFEU & Law No. 287/90,

[266] http://www.agcm.it/en/newsroom/press-releases/2352-ps10363-forced-to-become-shareholders-to-obtain-a-soft-loan-a-heavy-eur-4-5-million-fine-on-banca-popolare-di-vicenza.html.

[267] http://www.agcm.it/en/newsroom/press-releases/2313-i777-mortgage-interest-rate-collusion-in-the-provinces-of-trento-and-bolzano-the-ica-imposed-a-27-million-euro-fine-on-banks-and-cooperatives.html.

[268] http://www.agcm.it/en/newsroom/press-releases/2300-i785-a-110-million-fine-imposed-on-four-companies-providing-public-school-cleaning-services.html.

[269] http://webcache.googleusercontent.com/search?q=cache:-afOa4giqfUJ:www.agcm.it/concorrenza-delibere/sanzioni/download/41256297003874BD/F864FA14306D9A9FC1257F1B005FE9F7.html%3Fa%3Dp25739.pdf+&cd=2&hl=en&ct=clnk&gl=uk.

					Section 2
5	Public Transport Insurance Sector[270]	I744	26 March 2015	Vehicle Insurance	Article 101 TFEU & Law No. 287/90, Section 2
6	Vending Operators[271]	I783	14 June 2016	Food and Beverages	Article 101 TFEU & Law No. 287/90, Section 2
7	Sky, Mediaset Premium, Lega[272]	I790	20 April 2016	Media	Article 101 TFEU & Law No. 287/90, Section 2
8	Telecom Italia	I761	23 December 2015	Telecom	Article 101 TFEU & Law No. 287/90, Section 2
9	Gerling, Faro, Navale and Primogest[273]	I731	3 October 2011	Healthcare	Article 101 TFEU & Law No. 287/90, Section 2
Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors) *–exchange of commercially sensitive information, concerted practice, price-fixing, coordinating commercial and promotional strategies between competitors, information exchange between bidders, efficiency enhancing discussions between competitors*					
None					
Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement) *-exploitative abuses, excessive pricing, price discrimination, contractual abuses, vertical restraints, contractual power, abuse of dominance, market power conferred by contract*					
None					
Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies) **-***abuse of dominance, market power, bundling and appetite, tying, efficiencies and bundling, validations for tying and bundling*					
- Banca Popolare di Vicenza (see above, No1)					

[270] http://www.agcm.it/en/newsroom/press-releases/2211-i744-insurance-companies-two-fines-for-29-million-euros-against-unipolsai-and-generali-due-to-an-anti-competition-agreement.html.

[271] http://www.agcm.it/en/newsroom/press-releases/2308-i783-a-fine-exceeding-one-hundred-million-euros-for-an-anti-competitive-agreement-among-vending-operators.html.

[272] http://www.agcm.it/en/newsroom/press-releases/2290-a-66-million-euro-fine-imposed-on-sky,-mediaset-premium,-lega-and-infront-by-the-italian-competition-authority.html.

[273] http://www.agcm.it/en/newsroom/press-releases/1967-i731-insurance-13-million-in-fines-for-competition-restricting-agreement-by-three-companies-and-one-multi-firm-agency.html.

Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract -*agreement to vary contract price/terms, change of existing terms, alterations to existing contract,*
None

Jurisdictional Review

Segment 1. Loan product search

1. **Banca Popolare di Vicenza**

- Customers who wished to obtain a soft loan, were forced to become shareholders so as to finance capital increase transactions.
- In order to obtain the "shareholder loans" - characterised by concessional financial terms when compared to ordinary loan products - consumers were conditioned:
  i) to purchase the Bank's minimum share packages (equal to 100 shares) and
  ii) not to sell these share packages in order to continue to benefit from the concessional financial terms.
- The ICA noted that the practices carried out by Banca Popolare di Vicenza considerably limited consumers' freedom to choose in relation to financing products.
  - that is, subscription to the Bank's securities (securities could not be negotiated or liquidated, given the non-listed nature of the company Banca Popolare di Vicenza, and which could not be disinvested during the loan period under the penalty of losing the soft financial terms provided).
- By obliging consumers to open even a shareholders' bank account linked to the loan with the same Bank, Banca Popolare di Vicenza implemented a practice whereby loans have been bound to bank accounts which is prohibited by the Consumer Code.

2. **Mortgage Interest Rate Collusion**

- The ICA imposed a series of fines on several Banks belonging to Federazione Cooperative Raiffeisen and Federazione Trentina della Cooperazione, for two distinct anti-competitive agreements aimed at setting a minimum mortgage interest rate among Banks in the provinces of Bolzano and Trento.
- In essence, the mentioned Banks agreed to coordinate their commercial policies, also through the exchange of sensitive information (interest rates and other economic conditions of the loans), with the aim to limit competition in the mortgage market in the province of Bolzano.
- The collusion was carried out for about seven years (2007-2014).

Segment 2. Wholesale banking services

None.

Segment 3. Financial services, including insurance

None.

Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract.

3. Public school cleaning services

- CNS (Consorzio Nazionale Servizi società cooperative), Manutencoop Facility Management, Roma Multiservizi and Kuadra, all provide cleaning services in public schools.
- The ICA ascertained the existence of an anti-competitive agreement that conditioned the outcome of the public tender called by Consip, the Public Administration's purchasing organization.
- Through this agreement, the four companies – two of which are the largest operators on the market – actually annulled the competition in Consip's tender allocating the most interesting lots among each other and winning the maximum number allowed.
- Although formally participating autonomously, the CNS and the consortium Manutencoop Facility Management agreed on a strategy - concurring with the other parties involved in order to achieve shared aims and thus alter the outcome of the tender.
- To this end, they also made use of subcontracts for the protection of their respective market positions.
- CNS subcontracted to Roma Multiservizi, with reference to the lots in Lazio, in exchange for the latter's commitment not to participate in the tender.

4. Asbestos

- The Italian Antitrust Authority (IAA) adopted a decision against 12 undertakings for their participation in a bid-rigging cartel.
- The cartel related to tenders conducted by the Italian Ministry of Defence for the disposal of hazardous materials (asbestos) present in the military arsenals located in the cities of Taranto, La Spezia and Augusta.
- The 12 undertakings colluded to agree on the allocation of tender lots between 2011 and 2013.
- This conduct led to market-sharing and the preservation of the companies' positions, as well as to a steady reduction of the rebates offered to the Italian Ministry of Defence.

5. Public Transport Insurance Sector

- The ICA conducted an investigation into some of the leading Italian insurance companies, namely Assicurazioni Generali S.p.A. and Generali Italia S.p.A. (both belonging to the Generali Group), Unipol Assicurazioni S.p.A. and Fondiaria SAI S.p.A.
- These companies entered into an anti-competitive agreement concerning 58 tenders in the Italian vehicle insurance market for public transport.
- 15 local public transport companies throughout Italy invited insurance companies to participate in public tenders.
- The ICA found that Generali and UnipolSai either did not participate in these calls for tenders (39 cases) or that they were the only insurers to bid when the calls were issued by transport companies they were already insuring (19 cases).
- In 18 out of the 58 tenders under investigation, the call for tenders allowed participants to offer prices higher than the reference price. Nevertheless, no bids were made for these calls.

- This conduct was facilitated by contacts/exchanges of information among the undertakings concerned in the context of an ad hoc working group on public transport set up by ANIA (the Italian insurance companies association), allowed each insurance company to keep its customers and negotiate directly with them, without competing with other insurers on the market.

6. Vending Operators

- The ICA fined the main vending operators in the food and beverage sector and on their category association.
- The agreement aimed at maintaining high prices and at preserving the companies' profitability- allocating the market and customers, as well as coordinating sale prices.
    - In practice, the companies defined each other as "competing friends," avoiding submitting offers to each other's customers on the occasion of calls for tenders on the basis of a "non-belligerence agreement." The latter provided for a compensation mechanism based on giving back customers of equivalent value (in terms of allocation) to each "competing friend" in case of possible subtractions of customers within the ambit of the companies' commercial activity.

7. Sky, Mediaset Premium, Lega

- The ICA imposed fines on Sky and RTI/Mediaset Premium, the main television operators in the pay-tv market, and on the Italian Football League (Lega Calcio) and its advisor In front.
- The parties entered into a bid-rigging agreement concerning the award of the Serie A broadcasting rights for the following three years (2015-2018). The parties agreed to alter the outcome of the tenders for the A, B and D lots, following the presentation of their bids.
- Lega Calcio - advised and supported by Infront – instead of awarding to Sky the broadcasting rights in line with the submitted bids, engaged in a negotiation with the bidders, aimed at altering the outcome of the tender. As RTI/Mediaset Premium would not be awarded any lots on the basis of their bids, they were ready to join the collusive agreement since the very first moment.

***8.* Telecom Italia**

- The ICA imposed a cumulative fine on seven companies - Alpitel, Ceit Impianti, Sielte, Sirti, Site, Valtellina and Telecom Italia - for an anti-competitive agreement.
- The Companies agreed to coordinate their economic offers and contractual terms in relation to the tenders for the selection of suppliers made by the companies Wind and Fastweb; and in relation to information regarding the supply of corrective maintenance services.
- The anti-competitive conducts consisted in the agreed coordination of contractual economic terms and information transmitted to the regulator, with the aim to limit competition and prevent competing operators from providing other ancillary technical services.
- The fined Companies had numerous meetings and contacts in order to agree on the economic offers to be submitted to Wind Telecomunicazioni and Fastweb for the end-to-end corrective maintenance disaggregate

service; and, in general, to identify a single communication plan concerning the conditions for supplying the service.
- The ICA found that the investigated conducts were capable of altering OLO's and stakeholders' incentives, prejudicing market competition.

9. Gerling, Faro, Navale and Primogest

- Gerling (from Talanx, a German multinational), Faro, Navale (UGF) and Primogest (a multi-firm agency) divided up tenders for healthcare liability coverage in Campania.
- The agreement, lasting from 2003 to 2008, affected 18 procedures and 9 different procurement entities.

Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors)
None.

Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement)
None.

Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies)
Banca Popolare di Vicenza (see above, No1)

Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract
None.

5d. Appendix: Competition case law review — Poland

Identification of relevant cases

Platform- Urząd Ochrony Konkurencji i Konsumenta (UOKiK) Period- 2010-2017					
No	**Case Tile**	**Case Reference**	**Date of closure/decision**	**Segment**	**Legislation**
Segment 1. Loan product search *-Syndication loan, loan agreement, bank facility, multilateral loan, club deal, syndicated deal, corporate lending, loan (search terms)* *-(syndykacja, konsorcjum kredytowe, konsorcjum, kredyt, pożyczka, instrument finansowy, club deal, konsorcjalny, korporacyjne, dla przedsiębiorstw, biznesowy)*					
None					
Segment 2. Wholsesaale Banking services *-Market studies/Investiagtions/cases, relevant to categories A-E, and the loan syndication process.*					
1	Consumer mobility in the national market for savings and settlement accounts[274]	-	October 2010	Savings and Settlement Accounts	Market Study
Segment 3. Financial services, including insurance *-Market studies/Investiagtions/cases relevant to categories A-E, and the loan syndication process.*					
None					
Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract. *-bid suppression and the promise of a sub-contract, collusive tendering, subcontractor collusion, cover pricing, contractual offer, collusion between bidders, tender, information exchange (search terms)* *- (zmowa przetargowa, przetargowa, zmowa, przetarg, oferent, oferujący, wspólny udział, manipulacja, blokowanie, ustalanie cen, oferta, zaproszenie)*					
2	Bid-rigging in the market for municipal waste collection[275]	RLU 40/2013	24 December 2013	Waste Collection	Article 6(1)(7) of the UOKiK[276]
3	Bid-rigging in the market for military textiles[277]	DOK– 9/2014	30 December 2014	Military Textiles	Article 6(1)(7) of the UOKiK

[274] https://uokik.gov.pl/download.php?plik=9339.

[275] https://decyzje.uokik.gov.pl/bp/dec_prez.nsf/0/3C74B3F2AC1B3449C1257EC6007BA48A/$file/bia_263ystok%20przetarg%20decyzja%20%20_bip_.pdf.

[276] Ustawa o ochronie konkurencji i konsumentów (Dz. U. Nr 50, poz. 331 ze zm.)

[277] https://decyzje.uokik.gov.pl/bp/dec_prez.nsf/43104c28a7a1be23c1257eac006d8dd4/853b4211138c6d31c1257ec6007ba8f4/$FILE/Decyzja%20DOK%209_2014%20w%20sprawie%20porouzmienia%20%5BAgrotur-Marko-Texpol%20%5Dwersja%20BIP.pdf.

<table>
<tr><td colspan="6">Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors)
–exchange of commercially sensitive information, concerted practice, price-fixing, coordinating commercial and promotional strategies between competitors, information exchange between bidders, efficiency enhancing discussions between competitors (wymiana informacji, informacja handlowa, poufna informacja, poufny, uzgodnione praktyki, ustalanie cen, koordynacja, uzgodnienie, uzgadnianie, uzgodnienia, uzgodnienie strategii, strategia, efektywność, zwiększenie efektywności, poprawienie efektywności, poprawa efektywności, polepszenie efektywności, porozumienie)</td></tr>
<tr><td>4</td><td>Collusion in the telecommunications[278]</td><td>DOK -8/2011</td><td>30 December 2014</td><td>Telecommunications</td><td>Article 101 of the TFEU</td></tr>
<tr><td>5</td><td>Market sharing in the insurance[279]</td><td>RBG -28/ 2011</td><td>30 December 2011</td><td>Insurance</td><td>Article 6(1)(3) of the UOKiK</td></tr>
<tr><td colspan="6">Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement)
-exploitative abuses, excessive pricing, price discrimination, contractual abuses, vertical restraints, contractual power, abuse of dominance, market power conferred by contract
- (wyzysk, nadużycie cenowe, zawyżone ceny, nadmierne ceny, dyskryminacja cenowa, klauzule umowne, warunki umowy, siła przetargowa, nadużycie pozycji dominującej, pozycja negocjacyjna)</td></tr>
<tr><td>6</td><td>Abusive enforcement of the contract for street lighting operation[280]</td><td>RKT – 17/2010</td><td>19 July 2010</td><td>Street Lighting</td><td>Articles 9(1) and 9(2)(6) of the UOKiK</td></tr>
<tr><td>7</td><td>Unfair terms in the contract for street lighting operation[281]</td><td>RGD. 36/2011</td><td>30 December 2011</td><td>Street Lighting</td><td>Article 9(1) of the UOKiK</td></tr>
<tr><td>8</td><td>Exploitative conduct of housing cooperatives[282]</td><td>RKR- 1/2016</td><td>18 April 2016</td><td>Housing</td><td>Articles 9(1) and 9(2)(3) of the UOKiK</td></tr>
</table>

[278] https://decyzje.uokik.gov.pl/bp/dec_prez.nsf/43104c28a7a1be23c1257eac006d8dd4/aa4443cb93a73fb2c1257ec6007b9768/$FILE/decyzja%20DOK-8_2011.pdf.

[279] https://decyzje.uokik.gov.pl/bp/dec_prez.nsf/43104c28a7a1be23c1257eac006d8dd4/ee3d242e9cff95cdc1257ec6007b986d/$FILE/decyzja_nr_rbg_28_2011-2.pdf.

[280] https://decyzje.uokik.gov.pl/bp/dec_prez.nsf/43104c28a7a1be23c1257eac006d8dd4/7ecbebc567e13bd3c1257ec6007b8f62/$FILE/Decyzja%20Nr%20RKT-17-2010%20z%2019.07.2010r.%20-%20EnergiaPro%20S.A.pdf.

[281] https://decyzje.uokik.gov.pl/bp/dec_prez.nsf/43104c28a7a1be23c1257eac006d8dd4/f31d07be097e854fc1257ec6007b9889/$FILE/RGD-36-11-IW%20z%20dnia%2030%20grudnia%202011%20r.pdf.

[282] https://decyzje.uokik.gov.pl/bp/dec_prez.nsf/43104c28a7a1be23c1257eac006d8dd4/09333947f6364f32c1257fbc004bb142/$FILE/antymonopol%20decyzja%20RKR_411_2_15_BR%20Nowotarska%20Sp%C3%B3%C5%82dzielnia%20Mieszkaniowa%20BIP.pdf.

9	Exploitative conduct of housing cooperatives[283]	RLU – 13/2012	14 August 2012	Housing	Articles 9(1) and 9(2)(5) of the UOKiK
10	Unfair terms in the contracts for fuel gas supply[284]	DOK 1/2012	13 April 2012	Fuel gas	Article 9(2)(5) of the UOKiK & Article 102 of the TFEU
Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies) -*abuse of dominance, market power, bundling and appetite, tying, efficiencies and bundling, validations for tying and bundling (pakietyzacja, sprzedaż pakietowa, pakiet, łączenie, wiązanie, efektywność i pakiety, efektywność, zgodność z prawem, zgodna z prawem)*					
None					
Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract - *Abuse of dominance, agreement to vary contract price/terms, change of existing terms, alterations to existing contract (ustalanie zmian w umowie, ustalanie zmian w warunkach, zmiana warunków, zmiana umowy, modyfikacje umowy, modyfikacje warunków)*					
None					

Jurisdictional Review

Segment 1. Loan Product search

None.

Segment 2. Wholsesale Banking services

1. **Consumer mobility in the national market for savings and settlement accounts**

Segment 3. Financial services, including insurance

None.

Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract.

2. **Bid rigging in the market for municipal waste collection**

[283]https://decyzje.uokik.gov.pl/bp/dec_prez.nsf/43104c28a7a1be23c1257eac006d8dd4/a7af1b9c191c1681c1257ec6007b99ac/$FILE/decyzja%20SM%20Podlasie5bip.pdf.
[284]https://decyzje.uokik.gov.pl/bp/dec_prez.nsf/43104c28a7a1be23c1257eac006d8dd4/2d3e060324b0a95cc1257ec6007b991b/$FILE/decyzja%20DOK%201%202012%20z%2013.04.2012%20%5BPGNiG%5D%20wersja%20BIP.pdf.

- Four companies active in the market for municipal waste collection colluded prior to and during multiple tender processes.
- The mechanism of collusion consisted of submitting incomplete offers for tenders, refusing to submit required documents, overestimating proposed prices and other failures, which led to the exclusion of some competitors from tender processes.
- The collusion was supported by the fact that the companies were intertwined in terms of capital. They shared premises and the employees could cooperate and collude on the terms of their offers and on their participation in tenders.

3. Bid rigging in the market for military textiles

- Three companies active in the market for military textiles engaged in bid-rigging prior and during multiple tender processes.
- The mechanism for collusion consisted of positioning and withdrawing offers. The parties agreed on the offered prices and ensured that their prices are differentiated. If their offers were placed on the top and took following positions, bidders with lower prices dropped out by failing to submit required documents.
- The existence of collusion was supported by the fact that the companies reciprocally subcontracted the services provided as a result of tenders. They cooperated on many projects and recommended each other to customers. In addition, the companies used the same insurers and they concluded their respective insurance agreements at the same time. The signatures present in the forms were similar.

Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors)

4. Collusion in the telecommunications

- Four mobile retailers created a consortium in order to develop the Polish market for mobile TV services based on DVB-H technology.
- The consortium was reported to the UKE (Office of Electronic Communications). It was approved since it aimed at achieving following efficiencies on the wholesale market: joint testing, setting up a common technology standard, developing new business models, improving knowledge of DVB-H technology, creating a wholesale company providing DVB-H services. The companies were allowed to bid jointly for the 470-790 MHz frequencies.
- The companies went beyond what was necessary to achieve these objectives. They colluded on retail level in order to foreclose a competitor, which did not participate in the consortium.
- The anti-competitive collusion at the retail level started prior the bid for the 470-790 MHz frequencies and continued after. The employees of the companies met, exchanged communications and set-up a common strategy towards their other competitors.

5. Market sharing in the insurance

- The UOKiK stated that an insurance broker and an insurance company engaged in illegal exchange of information and allocated consumers.

- The companies claimed that their relationship is vertical and they achieve efficiencies in terms of improved distribution. The UOKiK disagreed and stated that the insurance broker had its own insurance offer.

Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement)

6. Abusive enforcement of the contract for street lighting operation

- EnergiaPro S.A., an electricity company, concluded an agreement with Opole Municipality, the owner of street lighting network, according to which EnergiaPro S.A. operated the street lighting system of Opole.
- EnergiaPro S.A. became dominant in the market for street lighting services as a result of the agreement concluded with Opole Municipality.
- The abuse consisted of imposing on Opole an obligation to pay the costs of repairing the lighting system, whose failures were not connected to breakdowns of light points, which was not covered by the agreement.

7. Unfair terms in the contract for street lighting operation

- ENERGA-OPERATOR S.A., an owner of street lighting network in Bytów Municipality, concluded with the latter the agreement to operate and to maintain the street lighting system.
- ENERGA-OPERATOR S.A was dominant in the market for street lighting services, as the owner of street lighting network.
- The abuse consisted of imposing on Bytów unfair terms of agreement, which limited its freedom to choose an electricity provider and to organise tenders in this regard. This prevented Bytów from meeting its regulatory obligations and breached its right to independently choose an electricity provider.

8. Exploitative conduct of housing cooperatives (RKR- 1/2016)

- Housing cooperatives ("spółdzielnia mieszkaniowa") are the entities of Polish law, which are created by future residents, in order to collectively satisfy their housing needs. Housing cooperatives are in charge of the real estate construction and/or its maintenance.
- Nowatorska Spółdzielnia Mieszkaniowa was dominant in the market for managing 155 buildings in Nowy Targ.
- Nowatorska Spółdzielnia Mieszkaniowa abused its dominant position by including differentiated and discriminative terms and charges in its agreements with telecommunications operators.

9. Exploitative conduct of housing cooperatives (RLU – 13/2012)

- Similar case to RKR- 1/2016.
- The housing cooperative - Spółdzielnie Mieszkaniowa „Podlasie" - abused its dominant position by denying a telecommunication operator access to its buildings.

10. Unfair terms in the contracts for fuel gas supply

- PGNiG, a dominant company in the retail market for fuel gas supply, abused its position by imposing on its consumers' long termination periods, which locked them in existing contracts.
- PGNiG's practices exploited its consumers and prevented the development of retail market for fuel gas supply.

Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies)

None.

Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract

None.

5e. Appendix: Competition case law review — Netherlands

Identification of relevant cases

Platform- Autoriteit Consument & Market Period- 2010-2017

No	Case Tile	Case Number	Date of closure/decision	Sector	Legislation
Segment 1. Loan product search *-Syndication loan, loan agreement, bank facility, multilateral loan, club deal, syndicated deal, corporate lending, loan (search terms)*					
1	NMa: syndicated loans[285]	-	25 January 2010	Finance	Market Study
2	Municipal pawnshops[286]	ROT 15/2993 en ROT 15/2994	28 January 2016	Finance	-
3	Dutch SME loan market[287]	14.0889.25	30 June 2015	Finance	Market Study
Segment 2. Wholesale Banking services *--Market studies/Investigations/cases relevant to categories A-E and the loan syndication process.*					
4	Brink's[288] (appeal)	7512	13 August 2015	Finance	Article 6 and 24 (Mededingingswet)
5	Switching banks and tying[289]	-	30-03-2010	Finance	Market Study
Segment 3. Financial services, including insurance *-Market studies/Investigations/cases relevant to categories A-E and the loan syndication process.*					
None					
Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract. *-bid suppression and the promise of a sub-contract, collusive tendering, subcontractor collusion, cover pricing, contractual offer, collusion between bidders, tender, information exchange (search terms)*					
6	Enforcement auction[290]	6538/7237/7268	03 July 2017	Housing Market	Article 6 (Mw)
7	Taxi transport[291]	7130-7131	05 March 2013	Transport	Article 6 (Mw)

[285] https://www.acm.nl/en/publications/publication/6254/NMa-limited-choice-for-undertakings-when-seeking-syndicated-loans.
[286] https://uitspraken.rechtspraak.nl/inziendocument?id=ECLI:NL:RBROT:2016:569.
[287] https://www.acm.nl/sites/default/files/old_publication/publicaties/14681_report-competition-on-the-dutch-sme-loan-market-june-2015.pdf.
[288] https://www.acm.nl/nl/publicaties/publicatie/14665/Uitspraak-rechtbank-in-beroep-Brinks.
[289] https://www.acm.nl/en/publications/publication/6400/NMa-study-reveals-switching-banks-easier-than-expected.
[290] http://deeplink.rechtspraak.nl/uitspraak?id=ECLI:NL:CBB:2017:204.
[291] https://www.acm.nl/nl/publicaties/publicatie/11221/Boete-kartel-aanbesteding-taxivervoer-RMC-en-IJsselsteden.

8	Demolition companies Rotterdam[292]	7249	20 December 2012	Construction	Article 6 (Mw)
9	Southern Dutch construction companies[293]	6494 & 6836	04 September 2010	Construction	Article 6 (Mw)
Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors) *–exchange of commercially sensitive information, concerted practice, price-fixing, coordinating commercial and promotional strategies between competitors, information exchange between bidders, efficiency enhancing discussions between competitors*					
10	Federation Textielbeheer Nederland[294]	7245	29 December 2011	Healthcare	Binding Commitme nts
11	Forklift truck batteries[295]	7615-11	05 July2017	Tech and Construction	Article 6 (Mw)
12	Prefab concrete garage boxes[296]	14.0409.31	17 February 2016	Building and Construction	Article 6 (Mw)
13	Concrete mortar sector[297]	15.0959.29	29 June 2016	Construction	Article 6 (Mw)
14	Destruction fields First year onion sets[298]	6987	18 December 2012	Food	Article 6 (Mw)
15	KPN, T-Mobile and Vodafone (appeal)[299]	(C-8/08)	26 October 2011	Telecommuni cations	Article 81(1) EC & Article 6
16	Readmaps[300]	7244	31 August 2015	Media	Article 6 (Mw)

[292] https://www.acm.nl/en/publications/publication/11028/NMa-fines-demolition-firms-for-illegal-activities.
[293] https://www.acm.nl/nl/publicaties/publicatie/14622/Boete-Janssen-de-Jong-en-WBL-manipulatie-aanbestedingen-Limburg.
[294] https://www.acm.nl/nl/publicaties/publicatie/4572/Toezeggingsbesluit-Federatie-Textielbeheer-Nederland.
[295] https://www.acm.nl/en/publications/publication/17434/Fines-for-price-fixing-agreements-involving-forklift-truck-batteries.
[296] https://www.acm.nl/nl/publicaties/publicatie/15708/Besluit-op-bezwaar-kartel-prefab-betonnen--garageboxen.
[297] https://www.acm.nl/nl/publicaties/publicatie/15976/Besluit-bindend-verklaring-toezeggingen-in-de-betonmortelsector.
[298] https://www.acm.nl/nl/publicaties/publicatie/11182/Boete-afspraak-vernietiging-akkers-Eerstejaars-plantuien.
[299] https://www.acm.nl/en/publications/publication/6710/NMa-confirms-Dutch-mobile-operators-engaged-in-cartel-activities-in-2001.
[300] https://www.acm.nl/nl/publicaties/publicatie/14789/Besluit-op-bezwaar-boete-in-kartelzaak-Leesmappen.

Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement) *-exploitative abuses, excessive pricing, price discrimination, contractual abuses, vertical restraints, contractual power, abuse of dominance, market power conferred by contract*					
17	Dutch Railways NS	16.0691.31	29 June 2017	Transport	Article 6 & Article 24 (Mw)
18	KPN misuse of position in tendering (objection)[301]	11.0007.37	20 June 2014	Telecommunications	Article 24 (Mw)
19	AstraZeneca[302]	7069/1832	24 September 2014	Pharmaceuticals	Article 24 (Mw)
Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies) **-***abuse of dominance, market power, bundling and appetite, tying, efficiencies and bundling, validations for tying and bundling*					
-	Switching banks and tying (see above, No 5)				
20	Sandd complaint against TNT (appeal)[303]	6207	26-09-2013	Finance	Article 6 and 24 (Mw)
21	Bundling of telecom services[304]	-	July 2017	Telecommunications	Market Study
Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract **-** *Abuse of dominance, agreement to vary contract price/terms, change of existing terms, alterations to existing contract,*					
None					

Jurisdictional Review

Segment 1. Loan product search

1. **Netherlands Competition Authority (NMa): limited choice for undertakings when seeking syndicated loans (study)**

- The NMa analysed the market for syndicated loans and club deals.
- The NMa found that the number of banks that are active in the Dutch market for syndicated loans has fallen.

[301] https://www.acm.nl/sites/default/files/old_publication/publicaties/13064_besluit-op-bezwaar-inzake-boete-kpn-voor-misbruik-positie-bij-aanbesteding-2012-07-09.pdf.
[302] https://www.acm.nl/sites/default/files/old_publication/publicaties/13595_no-abuse-of-a-dominant-position-by-astrazeneca-2014-12-02.pdf.
[303] https://www.acm.nl/en/publications/publication/6748/NMa-rejects-Sandds-complaint-no-abuse-by-PostNL.
[304] https://www.acm.nl/sites/default/files/old_publication/publicaties/17560_bundling-of-telecom-services-and-content-in-the-netherlands.pdf.

- The primary reason for this drop is the decrease in the number of mergers and acquisitions that have taken place in the Dutch banking industry. In addition, as a result of the financial crisis, foreign banks have withdrawn from this market to focus on their home markets instead.
- NMa noted how a return of these foreign players, that used to be active on the Dutch market, might positively affect competition because it would increase the number of players.
- Banks that are still active on this market have become more prudent when it comes to giving individual undertakings substantial loans, in part because they have limited resources.
- The number of international syndicated loans has seen a slight increase, which may prove to aid market recovery.
- Undertakings that have experience with syndicated loans benefit because this knowledge strengthens their bargaining positions, and it enables them to better assess what loan conditions are in line with market conditions.
- The NMa found no indications of violations of the Dutch Competition Act on the market for club deals and syndicated loans.

2. District Court of Rotterdam rules in appeal of municipal pawnshops

- The District Court of Rotterdam overturned the decisions of the Netherlands Authority for Consumers and Markets (ACM) that contained binding instructions on municipal pawnshops with regard to pawn contracts.
- In this case, the ACM imposed two binding instructions on the municipal pawnbroker in Amsterdam (Stadsbank van Lening) and one in The Hague (Gemeentelijke Kredietbank).
- ACM disagreed with the way these two municipal pawnbrokers extended pawn loans if consumers were unable to repay these loans at the end of their pawn contracts.
- The two pawnbrokers demanded that customers pay interim interest payments.
- According to ACM, such demands would violate not only the regulations but also the spirit of the law.
- The court held that ACM had interpreted the statutory standard incorrectly, and that the business practices of said municipal pawnbrokers are in accordance with the regulations.
- Another of the court's considerations was that it had been stated in parliamentary history that the conditions of the municipal pawnbrokers would remain largely unaltered in the transition to the new scheme as of July 1, 2014.
- The court ruled that ACM only incorrectly interpreted the statutory standards with regard to one aspect of the new pawnshop rules, which is demanding immediate repayment of the pawn loan when extending the contract. The court's verdict does not apply to the other pawnshop rules such as the interest rate and the minimum loan term.

3. Dutch SME loan market (market study)

- ACM investigated competition among banks active in the Dutch market for SME loans.
- Period: January 2007 to September 2014
- ACM concluded that there is insufficient competition among banks in this market. In addition, the margin calculation has revealed that competition has decreased in recent years. There are a number of reasons as to why banks experience relatively little competitive pressure in this market:

   1. Barriers to entry in the Netherlands are high.

2. Increased capital requirements reduce the opportunities for the three major banks to exert competitive pressure on each other.
3. SMEs shop around and switch to a very limited extent.
4. There is a risk of tacit coordination among banks
5. Competitive pressure from alternative forms of financing is currently still limited

Segment 2. Wholesale Banking services

4. Brink's (appeal)

- The ACM reassessed Brink's complaint about possible unfair competition by Geldservice Nederland (GSN).
- Brink's stated that the partnership of banks for the counting and processing of banknotes and the joint purchasing of cash transportation hinders competition.
- The GSN partnership is an initiative of ABN AMRO Bank, Rabobank and ING Bank.
- These banks want to realize savings through cooperation, such as fewer counting centres and more efficient journeys by money cars. Because there is less cash in circulation, it is efficient for banks to centrally regulate the counting and processing of banknotes.
- ACM believes that the cooperation between the banks in GSN does not restrict competition
- ACM rejects Brink's objections and maintains its decision.

5. Switching Banks and tying (market study)

- A majority of small and medium-sized business owners (SMBs) stated that the switching process was not that 'complex'.
- Only on a limited scale do banks coerce SMBs into purchasing one or more additional financial products when they take out a business.
- These are the most important findings of a study into tying among banks, carried out by Dutch market research firm TNS NIPO, which had been commissioned by the NMa.
- The study found that at least one out of four small-business owners that take out a commercial mortgage, a business line of credit or any other form of business loan is either coerced (5-8 per cent) or encouraged (18-23 per cent) to purchase an additional financial product.
- Most of the time, these additional products include business insurances or merchant accounts. The NMa currently does not have any indications pointing to a breach of the Dutch Competition Act.
- The market study had been launched because of media reports, tip-offs and indications SMBs about tying arrangements by banks when offering business loans.

Segment 3. Financial services, including insurance

None.

Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract.

6. Enforcement auctions (appeal)

- The Trade and Industry Appeals Tribunal (CBb) annulled fines for the traders in the Execution Auctions.
- The ACM imposed fines on more than 70 traders on execution auctions, for involvement in a system of prohibited cartel agreements in the period 2000-2009.
- Traders cooperated with at least 200 executory auctions to frustrate price formation and thus kept the price for the property at the official auction as low as possible.
- The ACM noted the cooperation between traders on more than 2,300 foreclosure auctions as one continuous violation.
- The CBb held that the ACM has not shown that the cooperation in all those foreclosure auctions was always aimed at frustrating price formation.

7. Tender for taxi transport

- The Taxi company RMC signed two agreements with two other taxi companies, IJsselsteden and BIOS, in which they made agreements about which of them would register in the Rotterdam region for tenders for contractual taxi transport. RMC and IJssel cities came to a definition of "home markets" that they would respect reciprocally.
    - In practice; they worked out who could approach which customer and then they would discuss whether or not to register.
- RMC and IJsselsteden also agreed that they would not work as sub-contractors for other companies.
- In the agreement between RMC, BIOS and a joint subsidiary, the parties included the clause that they would not bid for contracts in the Rotterdam region for which one of the taxi companies involved already arranged the transport.
- They also agreed to consult with each other to divide new assignments in advance.

8. Demolition Companies Rotterdam

- Between 2005 and 2009, two Rotterdam-based demolition firms engaged in bid-rigging activities in four tenders for demolition contracts in Rotterdam.
- Hofstede and Struijk distorted the tender procedures of these four projects by way of cover pricing.
    - In Practice, one firm places a bid, known to the other firm, even though it does not have any actual interest in the contract. Its bid is higher than that of the other firm, thereby eliminating mutual competition.
- The firms' real objective behind these cover bids is, with an eye to future tenders, to remain on the client's long list.

9. Southern Dutch construction companies

- The NMa imposed individual fines on three executives of two construction companies based in the southern Dutch province of Limburg.
- Manipulation of tender.
- Companies deliberately misled clients by way of cover pricing.
- The construction companies in question are Janssen de Jong Infra BV and contracting and road-construction company Aannemings- en Wegenbouwbedrijf Limburg BV.

Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors)

*10.*Federation Textielbeheer Nederland

- The Federation of Textile Management Netherlands (FTN) is a trade association for textile care providers.
- NMa's investigation revealed that the FTN regularly gave its members advice on how to pass on specific costs for textiles to health care institutions. Since the members of the FTN represent virtually the entire market, such advice can produce a noticeable price effect that would directly disadvantage customers- in this specific case healthcare institutions.
- In addition, FTN repeatedly commented negatively on a current tender for textile care organized by 14 healthcare institutions.
- In consequence of this members of the FTN decided not to register, as a result the client's search for the company with the best price-quality ratio is made more difficult.
- The FTN deleted the words "coordinate and coordinate the activities of its members" from its statutory objective. The FTN revokes its advice to pass on specific costs for textile care.

11.Forklift truck batteries

- The ACM imposed fines on importers of batteries for forklift trucks, among other vehicles, and on their trade association BMWT.
- These companies and the association agreed on using a so-called ‘lead surcharge.’ The objective of this ‘lead surcharge’ was to incorporate in a structural manner the widely fluctuating price of lead into the retail price of batteries.
- The companies also shared competition-sensitive information among each other.

12.Prefab concrete garage boxes

- Van Bon Coldstores Beneden-Leeuwen (now H & S Coldstores) and Kloosbeheer exchanged competition-sensitive information.
- Both companies examined since December 2005 whether they could merge or cooperate intensively. At the same time, however, far-reaching agreements were also made about existing customers, tariffs and capacity. The merger talks lasted more than four years and ultimately led to nothing.

13.Concrete mortar sector

- A number of concrete motor companies made extensive and far-reaching commitments for structural changes.
- One of the risks was that competition-sensitive information could be exchanged through intensive cooperation between competing concrete mortar companies.
    - For example, there are concrete mortar plants that are managed and used by competing companies. This can lead to less competition. Within three years, therefore, partnerships will be terminated between concrete mortar companies that together have a market share of 40%

or more in a specific area. These concrete mortar plants can no longer be operated together.

- Another risk is if a company carries out work together with a competitor.
- The concrete companies promise to do so and this must also be reported to the client.
- If there are business contacts between the competitors, this must be registered.

14. **Destruction fields First year onion sets**

- Seven companies who cultivate, process and market first-year onion sets in 2009 violated the prohibition of cartels by making agreements about the destruction of parts of already sown fields.
- In order to agree on the destruction of onion sets and to ensure that the cartel participants complied with the agreements, competition-sensitive information was exchanged by the companies concerned.

15. **KPN, T-Mobile and Vodafone**

- A meeting took place in June 2001 between five Dutch mobile phone operators (T-Mobile Netherlands, KPN Mobile, Orange Nederland, Vodafone Libertel and Telfort Mobile BV).
- The operators allegedly exchanged information about the commission paid to dealers for post-paid subscriptions.
- The case came before the ECJ on a preliminary reference from a Dutch court.
- The national court sought guidance on whether there can be a breach of Article 81(1) even where there is only a single instance of shared sensitive information.
- The Dutch Trade and Industry Appeals Tribunal (CBb) confirmed that the companies engaged in cartel activities in 2001.
- 'In this matter, we are supported by the ECJ, which has made it clear that mobile operators are never allowed to exchange information about the dealer remuneration levels, not even once,'.

16.Readmaps (objection)

- ACM maintains that the reading directory companies have made anti-competitive agreements.
- On 7 November 2013, ACM fined 13 companies that distribute reading folders because they had cartel agreements.
- These companies had divided the market among themselves. They agreed not to recruit each other's customers and made agreements about each other's work area. The various reading directory companies regularly exchanged information about this.

Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement)

17.Dutch Railways NS

- Dutch Railways NS abused its dominant position in the 2014 tender process for the public-transport contract in the southern Dutch province of Limburg.

- ACM fined NS for two violations.
  - (i) The first violation is that NS submitted a lossmaking bid in the 2014 tender process for the public-transport contract in the province of Limburg
  - (ii) The second violation is a combination of several related actions:
    - NS used confidential information that it had obtained from a former director of rival operator Veolia, which operated the regional rail services in Limburg at the time of the regional tender process. At the time, this director was working indirectly for NS.
    - NS put its competitors at a disadvantage by responding slowly and providing incomplete answers in response to their requests for access to certain services and facilities at stations.
    - NS passed on confidential information about its competitors Veolia and Arriva to its own subsidiary Abellio, through which NS participated in the tender process. Furthermore, NS withheld useful information about passenger revenues from its competitors, while its own subsidiary Abellio was allowed to use said information.

18. KPN misuse of position in tendering (Decision on objection)

- KPN objected to the decision to impose a fine for violations of the Telecommunications Act.
- In the framework of a tendering procedure for fixed government telephony, KPN had charged the government lower tariffs than those charged to other comparable large corporate customers.
- With this, KPN abused its position because KPN had significant market power on this market, it had to charge the same rates to comparable customers. For that reason KPN had to publish the tariffs that it charged to the government for this service.

19. AstraZeneca

- The undertaking allegedly abused a dominant position with respect to the drug Nexium.
- However, the NMa could not sufficiently determine that AstraZeneca enjoyed a dominant position.
- Further, it could not be established that a sufficiently substantial group of patients that were prescribed the expensive branded drug Nexium outside of hospitals could also have benefited from a cheaper generic version of the drug.

Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies)

20. Sandd complaint on abuse of dominant position TNT (appeal)

- The complaint addresses four possible violations of the Dutch Competition Act by TNT: predatory pricing, tying and bundling, exclusive long-term contracts, and price discrimination.
- The NMa did not find any indications of tying and bundling nor any exclusivity provisions (provisions in a contract prohibiting customers from buying services from competitors) between TNT and its customers. In addition, the NMa considered the durations of the contracts to be reasonable.
- Finally, the NMa has established that TNT did not engage in selective price-cutting.

21. Bundling of telecom services

- ACM notes that the importance of fixed-mobile bundles is increasing. The number of consumers with such bundles is growing. In addition, ACM sees increasing integration between ISPs and content providers.
- Although bundling can be advantageous for consumers, ACM also sees a number of risks to competition in the longer term. Partly as a result of bundling, consumers will switch less quickly, making it difficult for smaller providers to grow.
- Ultimately it may even lead to departures from the market, resulting in a decrease in competition. ACM will monitor these developments closely.
- The ongoing market analysis will devote explicit attention to the role played by 29 fixed-mobile bundles and the competition potential for smaller providers.

Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract

None.

5f. Appendix: Competition case law review — Spain

Identification of relevant cases

<table>
<tr><th colspan="6">Platform- National Commission of the Markets and the Competition)
Period- 2010-2017</th></tr>
<tr><th>No</th><th>Case Title</th><th>Case Reference</th><th>Date of closure/decision</th><th>Market Sector</th><th>Legislation</th></tr>
<tr><td colspan="6">Segment 1. Loan product search
-Syndication loan, loan agreement, bank facility, multilateral loan, club deal, syndicated deal, corporate lending, loan (search terms)</td></tr>
<tr><td>1</td><td>Sanction proceedings against Banco Bilbao Vizcaya Argentaria, Banco Sabadell, Banco Santander and Caixabank[305]</td><td>-</td><td>07 April 2016</td><td>Finance</td><td>Article 1 of the Law 15/2007</td></tr>
<tr><td colspan="6">Segment 2. Wholesale Banking services
-Market studies/Investigations/cases relevant to categories A-E and the loan syndication process.</td></tr>
<tr><td colspan="6">None</td></tr>
<tr><td colspan="6">Segment 3. Financial services, including insurance
-Market studies/Investigations/cases relevant to categories A-E (i.e. completion concerns-see methodology) and the loan syndication process.</td></tr>
<tr><td colspan="6">None</td></tr>
<tr><td colspan="6">Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract.
-bid suppression and the promise of a sub-contract, collusive tendering, subcontractor collusion, cover pricing, contractual offer, collusion between bidders, tender (search terms)</td></tr>
<tr><td>2</td><td>Road tendering[306]</td><td>S/0226/10</td><td>19 October 2011</td><td>Construction</td><td>Article 1 Law 15/2007 & 101 TFEU</td></tr>
<tr><td>3</td><td>Engineering companies[307]</td><td>S/0287/10</td><td>08 February 2012</td><td>Engineering</td><td>Article 1 Law 15/2007 & 101 TFEU</td></tr>
<tr><td>4</td><td>Railway Bearings[308]</td><td>S/0453/12</td><td>04 December 2014</td><td>Transport</td><td>Article 1 Law 15/2007 & 101 TFEU</td></tr>
<tr><td>5</td><td>Waste cartel[309]</td><td>S/0429/12</td><td>January 2015</td><td>Waste and urban sanitation</td><td>Article 1 Law 15/2007 & 101 TFEU</td></tr>
</table>

[305] https://www.cnmc.es/novedades/2016-04-07-la-cnmc-incoa-expediente-sancionador-contra-banco-bilbao-vizcaya-argentaria.
[306] https://www.cnmc.es/buscador?t=S/0226/10.
[307] https://www.cnmc.es/expedientes/s028710.
[308] https://www.cnmc.es/en/node/344046.
[309] https://www.cnmc.es/expedientes/s042912.

6	Modular construction[310]	S/0481/13	03 December 2015	Construction	Article 1 Law 15/2007 & 101 TFEU
Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors) *–exchange of commercially sensitive information, concerted practice, price-fixing, coordinating commercial and promotional strategies between competitors, information exchange between bidders, efficiency enhancing discussions between competitors (search terms)*					
7	AENA Commercial services[311]	S/0404/12	02 January 2014	Transport	Article 1 Law 15/2007 & 101 TFEU
8	Car manufacturers	S/0482/13	28 July 2015	Vehicles	Article 1 Law 15/2007 & 101 TFEU
Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement) *-exploitative abuses, excessive pricing, price discrimination, contractual abuses, vertical restraints, contractual power, abuse of dominance, market power conferred by contract (search terms)*					
9	Agedi/Aie-Rdio[312]	S/0500/13	26 November 2015	Intellectual rights	Article 2 Law 15/2007 & 102 TFEU
10	Endesa Instalación[313]	S/0446/12	10 July 2014	Distribution of Electrics	Article 2 Law 15/2007 & 102 TFEU
Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies) **-***abuse of dominance, market power, bundling and appetite, tying, efficiencies and bundling, validations for tying and bundling (search terms)*					
None					
Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract **-***agreement to vary contract price/terms, change of existing terms, alterations to existing contract, horizontal agreement to vary contractual terms (search terms)*					
None					

Jurisdictional review

Segment 1. Loan product search

1. Financial derivatives

- The Comisión Nacional de los Mercados y la Competencia (the "**CNMC**") fined four banks, Banco Bilbao Vizcaya Argentaria S.A. ("**BBVA**"), Banco

[310] https://www.cnmc.es/buscador?t=S/0481/13.
[311] https://www.cnmc.es/expedientes/s040412.
[312] https://www.cnmc.es/expedientes/s050013.
[313] https://www.cnmc.es/expedientes/s044612.

Sabadell S.A. ("**Sabadell**"), Banco Santander S.A. ("**Santander**") and Caixabank S.A. ("**Caixabank**") for a single and continuous infringement of the provisions of Article 1 of Law 15/2007, and Article 101 of the Treaty on the Functioning of the European Union ("**TFEU**"), consisting of a concerted action aimed at setting the price, above market prices, of the derivatives used as hedges for the interest rate risk associated with syndicated credits in project finance between 2006 and 2016.

- The CNMC separately analysed two conducts: i) the coordination to set the economic conditions of the derivatives for interest rate risk coverage of syndicated loans related to project finance and ii) the link between derivatives for the coverage of the interest rate and the syndicated banks by forcing the client to contract with them.

    - Regarding the first conduct, the CNMC considered that the banks coordinated to set a price above the one agreed in the contract with the client in both interest rate swaps and collars derivatives.
        - The derivative contracts were set at "zero cost" or "no cost" or "market value", i.e. at the time of contracting, none of the parties must made any disbursement, given that the price of the purchase and sale of options are the same. "Market value" refers to the fact that the price of the options purchased and sold (in the case of the collar) is made at market prices and that therefore there is no type of margin charged by the financial institution.
        - In the case of collars, the operation of contracting and fixing the caps and floors was as follows: the debtor of the syndicated credit went to the notary to sign while the representatives of the banks were in communication through teleconference from their respective entities to carry out the calculation of caps and floors. In general terms, the agent bank performed the calculations and offered values that needed to be accepted (or rejected) by the debtor of the syndicated credit and by the rest of the banking entities.
        - The banks communicated with each other, before the conversation with the client, to agree on a floor above the market level.
        - The CNMC concluded that the banks coordinated to set economic conditions for the coverage of risk of adulterated interest rates, with implicit margins imposed in a multilateral and concerted manner, and higher to what was agreed with the client in the contract "under market conditions", amounting to a restriction by object.
    - As for the second conduct, the CNMC considered that it was not possible to conclude on the unlawfulness of the fact that the banks forced clients of the syndicated loan to contract the coverage against the risk of interest rates with the same banks.

- According to the banks, coordination amongst competitors to jointly fix the price of derivatives in the context of a syndicated loan is common practice in all jurisdiction. Indeed, the banks confirmed the existence of a coordination.
    - Sabadell justified the coordination amongst banks by the fact that they are interested in controlling the level of the floor of the derivatives offered by each of them due to the guarantee system that comes with this type of contract. Absent a single floor or fixed rate fixed by all banks, there would be non-proportional settlements between banks, the incentive to offer higher floor and fixed rates, instability and uncertainty of cash-flow, and it would discourage banks from participating in the

operation. Sabadell also considered that agreeing on the level of the floor allows banks to improve the production and distribution of financing services and does not affect competition outside these operations.
  - According to Santander, the coordination is explained by the nature of syndicated coverage and the need of proportionality between banks, i.e. banks are in favour of having the floor level and the fixed rate at the same level for all banks, in case of expiration of voting rights. If the floor or fixed rate was negotiated between the client and each bank, there would be a clear incentive for banks to set a higher level than the other entities.
  - According to an expert report submitted by one of the parties, it is usual market practice for banks to agree on the same conditions for both the syndicated loan and its coverage. The experts explained that it cannot be assumed that the banks acted in such way to harm the client given that the concentration of prices is usual in this kind of operations.
- The CNMC considered that, although coordination is necessary to set the price and eliminate the differences between banks due to different calculation methods, in this case, it is the prior agreement of the banks, completely unknown to the client, which is considered as an infringement, and not the final negotiation with the client through teleconference. This is due to the fact that it is the first agreement which enables the banks to eliminate the uncertainty resulting from an autonomous action under market conditions, to know the offers from the rest of banks beforehand and to illicitly agree on a price that is more beneficial for them.
- The CNMC rejected the parties' arguments that the practices could be considered as ancillary restrictions to derivative contracts, i.e. the legal exemption of article 1.3 of Law 15/2007 or 101.3 of the TFEU. Fixing prices higher than the ones agreed with the client did not allow "consumers or users to participate equally in their benefits", and the parties failed to demonstrate that it is essential that derivatives are entered into by the banks party to the loan – indeed, the CNMC considering such a requirement to be disproportionate.
- Finally, although it was not necessary to prove anti-competitive effects, the CNMC noted that the conduct had a negative effect, through price fixing, on the quality of the derivatives, i.e. the value of the coverage for the client was negative instead of "at zero cost" as agreed.
- The banks announced that they will appeal the fine of 91 million euros imposed by the CNMC.[314]
- The CNMC's decision is the first infringement decision by an EU competition authority in connection with a product related to syndicated lending.[315]

Segment 2. Wholesale Banking services

None.

Segment 3. Financial services, including insurance

None.

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[314] MLex press round-up, 16 April 2018, http://www.expansion.com/empresas/banca/2018/04/15/5ad327b7e2704e59188b45a8.html

[315] Cadwalader, "The Spanish competition authority fines four banks for fixing derivative prices", available at: https://www.cadwalader.com/index.php?/resources/newsletters/antitrust-and-financial-services/the-spanish-competition-authority-fines-four-banks-for-fixing-derivative-prices

Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract.

1. Road Tendering

- 46 companies in the construction sector agreed to allocate and fix prices on government tenders for roadway maintenance works.
- The companies were in contact with each other and met to exchange. information on the discounts off the base price that they planned to propose.
    - In practice, they would agree on the amount of the winning reduction and of the rest of the bids. These discounts (between 1% and 6%) were much smaller than those normally applied in competitive conditions (15% to 30%). The winning bidder thus obtained a higher budget at the expense of the Administration having to pay a higher price and would pay economic compensation to the rest of the competitors in the tender for having modified their offers.

2. Engineering companies

- Companies in question operated in the civil engineering field, offering post-tensioning and geotechnical systems.
- Together they are the main operators on the market and, in some cases, they are subsidiaries of large construction companies
- The following infringements took place- On the post-tensioning systems markets, agreements to share out contracts for post-tensioning systems including various large projects and supply of bars.
- The companies held periodic meetings amongst themselves (sometimes monthly) in order to proceed with the sharing out of potential contracts and the monitoring of the sharing arrangements.
- Quotas were defined per company, which reflected their weight on the market, and potential contracts were shared out by reference to these quotas. Companies colluded on the price to be submitted to customers seeking the services in order to ensure the designated company would obtain the contract. Mechanisms were also defined for compensation between companies by reference to the quotas.

3. Railway Bearings

- The CNMC fined companies SCHAEFFLER, SKF and NSK, which are manufacturers of industrial bearings for railway vehicles, for constituting a cartel in the supply of these products to Spanish railway operator Renfe, almost the exclusive buyer of this type of products.
- The companies agreed to fix prices and share the Spanish market for industrial bearings for railway vehicles, which affected the tenders called by Renfe in 2004, 2007 and 2011.
- The cartel was organised and developed through meetings and telephone calls between the managers of the companies, which were carried out at the same time as the announcement of each tender. The managers contacted each other through meetings or by telephone, so as to agree on the offers to be submitted, fixing prices and distributing the mentioned tenders, at all times maintaining the allocation of supply of each reference of the product that historically had been supplied to Renfe by each of these companies.

4. Waste cartel

- The case concerned a national agreement for the distribution of the waste management and urban sanitation market.
- This agreement consisted of commitments to respect the respective clients; the distribution of new clients; the exchange of commercially sensitive information (clients, offers submitted to them, etc.); distribution of public tenders by means of the submission of joint offers or the non-concurrence of one part of the tender; use of sectorial associations to implement market distributions or coordinate actions; and collective recommendations issued by sectorial associations to persuade their associates to respect the overall market distribution agreement in the scope of their actions.

5. Modular construction

- The CNMC issued a decision concluding that nine undertakings had engaged in fixing prices and had entered into agreements to share customers and rig tenders organised by both private and public bodies in the Spanish market for modular constructions.
- The authority found that the anticompetitive practices had been taking place from 2008 to 2013 and affecting the territory of different Spanish autonomous regions.

Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors)

6. AENA Commercial services

- Self-drive car rental companies and authorised dealers at airports in several cities in Spain exchanged commercially sensitive information between April 1996 and September 2012 in collaboration with the public company in charge of airport management (AENA).
- The fined public company sent monthly reports that contained invoicing, the number of contracts and the conditions of the self-drive car rental companies that operated in 31 airports in their network.
- This allowed the involved companies to have an accurate knowledge of market quotas, the number of disaggregated contracts, and the evolution of their competitors, which facilitated coordination, as uncertainty was eliminated.

7. Car manufacturers

- The CNMC fined 21 companies and two consulting companies as a result of a cartel in the market for the distribution and marketing of motor vehicles and in the provision of after-sales services.
- The infringing companies implemented a systematic exchange of confidential and commercially sensitive information, both current and future, which was highly disaggregated and which covered almost all of the activities carried out by the sanctioned companies through their distribution and after-sales network.
- The exchanges of information were structured around three areas or exchange forums, although it was all part of a complex agreement.

Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation

process (e.g. because of contractual/commercial constraints on replacement)

8. Agedi/Aie Radio

- The intellectual property rights management entities AGEDI and AIE were fined for fixing inequitable rates and for applying more advantageous terms to some operators than to others.
- AGEDI and AIE were responsible for abusing their dominant position by setting unfair and discriminatory rates in relation to phonogram's radio broadcasting in Spain.

9. Endesa Instalación

- Endesa Distribución abused its dominant position in the electrical installations market reserved for the distributor between 2009 and 2012.
- The abuse consisted of inappropriate charges for the execution of installations for new network extensions, in cases where the distributor company would be in charge of executing such installations, only charging the extension rights in force thus abusing its dominant position in the reserved electrical installations market in the distribution areas it managed.

Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies)

None.

Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract

None.

5g. Appendix: Competition case law review — United Kingdom

Identification of relevant cases

Platform- Competition Market Authority & LexisNexis Period- 2010-2017

No	Case Title	Case Reference	Date of closure/decision	Market Sector	Legislation
Segment 1. Loan product search *-Syndication loan, loan agreement, bank facility, multilateral loan, club deal, syndicated deal, corporate lending, loan (search terms)*					
1	Royal Bank of Scotland Group plc v Barclays Bank plc[316]	CE/8950-08	20 January 2011	Finance	Chapter I of the CA98 & Article 101 of the TFEU
2	Payday lending market investigation[317]	-	13 August 2015	Finance	Order under Enterprise Act 2002
Segment 2. Wholesale Banking services *-Market studies/Investigations/cases relevant to categories A-E and the loan syndication process.*					
3	Dahabshiil Transfer Services Ltd v Barclays Bank plc; Harada Ltd and another v Barclays Bank plc[318]	[2013] EWHC 3379 (Ch.)	5 November 2013	Banking services	Chapter 2 of the CA98 & Article 102 of the TFEU
Segment 3. Financial services, including insurance *-Market studies/Investigations/cases relevant to categories A-E and the loan syndication process.*					
4	FCA statement of objections to four asset management firms[319]	-	29 November 2017	Finance	Chapter I of the CA98 & Article 101 of the TFEU
5	Private motor insurance market investigation[320]	-	18 March 2015	Finance	Market Investigation
6	Private motor insurance: exchange of data[321]	CE/9388/10	2 December 2011	Transport	Chapter I of the CA98 & Article 101 of the TFEU

[316] https://assets.digital.cabinet-office.gov.uk/media/555de2a0e5274a74ca000023/CE8950_08_dec.pdf.
[317] https://www.gov.uk/government/news/cma-publishes-final-motor-insurance-order.
[318] http://lexisweb.co.uk/cases/2013/november/dahabshiil-transfer-services-ltd-v-barclays-bank-plc-harada-ltd-and-another-v-barclays-bank-plc.
[319] https://www.fca.org.uk/news/press-releases/fca-issues-first-statement-objections-four-asset-management-firms.
[320] https://www.gov.uk/cma-cases/private-motor-insurance-market-investigation.
[321] https://www.gov.uk/cma-cases/private-motor-insurance-exchange-of-data.

Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract. *-bid suppression and the promise of a sub-contract, collusive tendering, subcontractor collusion, cover pricing, contractual offer, collusion between bidders, tender, information exchange (search terms)*					
7	Supply of products to the furniture industry (drawer wraps)[322]	CE/9882-16	27 March 2017	Household goods, furniture and furnishings	Chapter I of the CA98 & Article 101 of the TFEU
8	Galvanised steel tanks for water storage (Main Cartel)[323]	CE/4327-04	19 December 2016	Building and Construction	Chapter I of the CA98 & Article 101 of the TFEU
9	Access control and alarm systems[324]	CE/9248-10	6 December 2013	Fire, police and security	Chapter I of the CA98 & Article 101 of the TFEU
10	Bid rigging in the construction industry (appeal)[325]	[2011]CAT 3 (Kier Group plc and Others v OFT)	11 March and 27 April 2011	Construction	Chapter I of the CA98 & Article 101 of the TFEU
Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors) *–exchange of commercially sensitive information, concerted practice, price-fixing, coordinating commercial and promotional strategies between competitors, information exchange between bidders, efficiency enhancing discussions between competitors (search terms)*					
Private motor insurance: exchange of data (see above, No 5)					
11	Conduct in the ophthalmology sector[326]	CE/9784-13	20 August 2015	Healthcare and medical equipment	Chapter I of the CA98 & Article 101 of the TFEU
12	Dairy retail price initiatives[327]	CE/3094-03	26 July 2011	Retail and service	Chapter I of the CA98 &

[322] https://assets.publishing.service.gov.uk/media/592ea4f3ed915d20fb000122/non-conf-decision-drawer-wraps.pdf.
[323] https://assets.publishing.service.gov.uk/media/58db91e440f0b606e3000046/ce-9691-12-main-cartel-decision.pdf.
[324] https://www.gov.uk/cma-cases/access-control-and-alarm-systems-collusive-tendering.
[325] http://www.matrixlaw.co.uk/wp-content/uploads/2016/03/18_05_2011_02_32_17_Christopher-Brown-Construction-Judgments-paper.pdf.
[326] https://assets.publishing.service.gov.uk/media/55d5989f40f0b609ff000009/Conduct_in_the_ophthalmology_sector_decision_v2.pdf.
[327] http://webarchive.nationalarchives.gov.uk/20140403003913/http://www.oft.gov.uk/shared_oft/ca-and-cartels/dairy-decision.pdf.

					Article 101 of the TFEU
13	Galvanised steel tanks for water storage (information exchange decision) [328]	CE/9691/12	19 December 2016	Building and construction	Chapter I of the CA98 & Article 101 of the TFEU
14	Airline passenger fuel surcharges for long-haul flights[329]	CE/7691-06	19 April 2012	Transport	Chapter I of the CA98 & Article 101 of the TFEU
Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement) *-exploitative abuses, excessive pricing, price discrimination, contractual abuses, vertical restraints, contractual power, abuse of dominance, market power conferred by contract (search terms)*					
15	Health and fitness clubs[330]	MP - G & C/0004	10 September 2013	Recreation and leisure	Chapter 2 of the CA98 & Article 102 of the TFEU
16	Domestic bulk LPG suppliers: unfair contract terms[331]	MP-SIP18-21, MP-SIP23	1 March 2012	Oil and gas refining and petrochemicals	Chapter 2 of the CA98 & Article 102 of the TFEU
17	Vehicle service, maintenance and repair platforms[332]	CE/9496-11	9 September 2014	Communications	Chapter 2 of the CA98 & Article 102 of the TFEU
Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies) **-***abuse of dominance, market power, bundling and appetite, tying, efficiencies and bundling, validations for tying and bundling (search terms)*					
Dahabshiil Transfer Services Ltd v Barclays Bank plc; Harada Ltd and another v Barclays Bank plc (See above, No 3)					
18	BSkyB[333] (appeal)	1158/8/3/10	May 2013	Service provider	Chapter 2 of the CA98 & Article 102 of the TFEU

[328] https://assets.publishing.service.gov.uk/media/58db746440f0b606e300003c/ce-9691-12-information-exchange-decision.pdf.
[329] https://www.gov.uk/cma-cases/airline-passenger-fuel-surcharges-on-long-haul-flights-price-fixing.
[330] https://www.gov.uk/cma-cases/health-and-fitness-clubs-unfair-contract-terms.
[331] https://www.gov.uk/cma-cases/domestic-bulk-lpg-suppliers-unfair-contract-terms.
[332] http://webarchive.nationalarchives.gov.uk/20140402163550/http://oft.gov.uk/news-and-updates/press/2014/12-14.
[333] http://www.catribunal.org.uk/238-6549/1158-8-3-10-British-Sky-Broadcasting-Limited.html.

19	IDEXX Laboratories Ltd[334]	CE/9322/10	1 November 2011	Agriculture, environment and natural resources	Chapter 2 of the CA98 & Article 102 of the TFEU
Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract *-agreement to vary contract price/terms, change of existing terms, alterations to existing contract, horizontal agreement to vary contractual terms (search terms)*					

Jurisdictional Review

Segment 1. Loan product search

1. **Royal Bank of Scotland Group plc v Barclays Bank plc**

- Loans to large professional services firm
- RBS staff provided pricing data to counterparts at Barclays
- Barclays used the provided information to determine the pricing on its own loans.
- Notably, the provided information detailed a proposed structure for two new loan facilities

Segment 2. Wholesale banking services

2. **Investment and corporate banking market study**

- In 2015-2016, the FCA carried out a market study in relation to investment and corporate banking services, focusing on primary markets and related activities provided in the UK. It published a final report in October 2016.
- While the FCA found that the universal banking model of cross-selling and cross-subsidisation from lending and corporate broking services to primary market services worked well for large corporate clients, it found that there were some practices that could have a negative impact on competition, particularly for smaller clients.
- It made note of two key points relevant to loan syndication: reciprocity and restrictive contractual clauses:
  - Reciprocity is a practice whereby a bank issuing its own financing awards mandates to another bank partly based on how much business it will receive in return. The FCA analysed book-runner and co-manager roles awarded to reciprocal and non-reciprocal banks and concluded that reciprocity did not appear to be excluding non-reciprocal banks from competing because they could win mandates. It decided not to carry out further analysis by fees earned. The FCA did not propose any remedies related to reciprocity.
  - The FCA noted that banks used clauses in contracts, mandates or engagement letters that forced clients to award or offer future primary market services to that bank. It found that these clauses were restricting a client's ability to use an alternative bank or adviser on a subsequent transaction. In June 2017, the FCA published a separate policy statement[335] following the final report on its market study. The FCA

[334] https://assets.publishing.service.gov.uk/media/555de29e40f0b669c4000011/OFT1387.pdf.
[335] https://www.fca.org.uk/publications/policy-statements/ps17-13-investment-and-corporate-banking-prohibition-restrictive, https://www.fca.org.uk/publication/policy/ps17-13.pdf.

decided that "right of first refusal" clauses (i.e. a contractual right to be given the opportunity to enter into a business transaction with a company before anyone else can, the client subject to the right is prevented from accepting offers from third parties) should be banned; and "right to match" clauses (i.e. the right for the firm to be approached following a third-party offer, to match that offer with the client ultimately deciding which firm to select to provide the services) are acceptable. The ban will apply to agreements entered into from 3 January 2018.

3. **Dahabshiil Transfer Services Ltd v Barclays Bank Plc; Harada Ltd and another v Barclays Bank Plc**

- Barclays was in a dominant position in the market for banking services.
- Each of the Claimants carries on a "money **service** business", defined as "an undertaking which by way of business operates a currency exchange office, transmits money (or any representations of monetary value) by any means or cashes cheques which are made payable to customers."
- Following an internal review in late 2012 and early 2013, Barclays decided that it wished to reduce its exposure to this sector. The implementation of that decision forms the background to the present applications.
- They were subsequently given notice by Barclays of its intention to withdraw banking services from their businesses.
- The claimants contended that, Barclays had acted unlawfully because it was alleged to be in a dominant position in the market for the provision of banking services (Article 102 TFEU & Chapter II - Abuse of dominance).
- They sought interim injunctions to restrain Barclays from withdrawing its services.

Segment 3. Financial services, including insurance

4. **FCA statement of objections to four asset management firms**

- The FCA alleged that four firms shared information by disclosing the price they intended to pay in relation to one or more of two Initial Public Offerings (IPOs) and one placing, shortly before the share prices were set.
- The sharing generally occurred on a bilateral basis and allowed firms to know the others' plans during the IPO or placing process when they should have been competing for shares.

The FCA's main allegations were as follows:

- In 2015, Newton Investment Management Limited ('Newton') and Hargreave Hale Ltd and River & Mercantile Asset Management LLP disclosed and/or accepted information about the price they intended to pay for shares in relation to one IPO and a placing;
- In 2014 Artemis Investment Management LLP and Newton shared information about the price they intended or were willing to pay for shares in relation to another IPO.

5. **Private motor insurance market investigation**

- The CMA published its final report into the private motor insurance market which said that it would:

- ban agreements between price comparison websites (PCWs) and insurers which stop insurers from making their products available more cheaply on other online platforms;
- ensure there was better information for consumers on the costs and benefits of no-claims bonus protection.

6. Private motor insurance: exchange of data

- The OFT accepted formal commitments from six insurance companies and two IT software and service providers to limit the data they exchange between them.
- The commitments ensured that the companies would exchange pricing information through the analysis tool only if that information met certain principles agreed with the OFT.
- These principles required the information, if less than six months old, to be anonymised, aggregated across at least five insurers and already 'live' in broker-sold policies.

Category A. Bid-rigging/information exchange between bidders during the course of tender process, with particular focus on persuading rivals to drop out in return for a role on sub-contract/future contract.

7. Supply of products to the furniture industry- drawer wraps

- BHK UK and TATL exchanged competitively sensitive information prior to tendering
- Bid rigging occurred during the tender process and parties would ‘back off’ from, each other’s customers
    - *In practice when BHK was approached by a TATL customer, BHK would inform TATL by telephone and it would be agreed that BHK would either i) quote high in order not to win order, (ii) decline*
- Pricing information was shared for the purposes of submitting tactical quotes to customers, thus enabling the parties to maintain their respective customer bases; putting less downward pressure on prices than would otherwise be expected.

8. Galvanised steel tanks for water storage (main cartel)

- The practices in this case were bid-rigging and market sharing by way of customer allocation. The parties agreed which customers ‘belonged’ to which party and agreed benchmark prices for a range of tanks.
- Agreements were made and reinforced in regular meetings attended by the parties’ representatives, as well as in bilateral exchanges concerning particular bids.
- The fixing of the Parties’ prices, rigging of bids and allocation of customers in relation to the supply of CGSTs could not be said to have contributed to improving the production or distribution of goods, or promoting technical or economic progress.

9. Access control and alarm system

- Infringements comprised of three separate bilateral collusive tendering arrangements.

- In practice, when bidding for these contracts, Cirrus shared its proposal with one of O'Rourke, Owens or Jackson with the aim that they would submit higher bids, thereby enabling Cirrus to win the contracts.
- Parties exchanged confidential pricing information.

10. Bid rigging in the construction industry (appeal)

- Corporations engaged in bid-rigging activities on 199 tenders, mostly in the form of 'cover pricing', (which occurs when a company obtains a price from a competitor in the tender process).
- Certain instances involved bidders paying an unsuccessful bidder an agreed sum (compensation payment).
- When communicating with one another regarding a compensation payment, the Parties disclosed, and received, information regarding their respective bidding intentions.
- Even where the Parties did not exchange details of their tender prices, the exchange of information regarding the level of compensation to be paid also had an influence on the pricing of the contracts.

Category B. Information exchange in circumstances where some discussion between competitors is necessary and efficiency-enhancing, but which goes beyond what is necessary (including between buyers and sellers where they are also competitors)

11. Conduct in the ophthalmology sector

- A membership organisation was formed to represent the interests of 37 limited liability partnerships (LLPs) and their 200 consultant members.
- The platform provided members with a number of services including access to CESP Limited negotiated contracts with private medical insurers.
- Information provided to members is for efficiency purposes but went beyond legal boundary as the organisation recommended that its members refused to accept lower fees offered by an insurer, and that they charged insured patients higher self-pay fees.
  - Further, infringements included;
    - Circulating amongst its members' detailed price lists for ophthalmic procedures.
    - Sharing of consultants' future pricing and business intentions.

12. Dairy retail price initiatives

- Arla, Asda, Dairy Crest, McLelland, Safeway, Sainsbury's, Tesco, The Cheese Company and Wiseman co-ordinated increases in the prices consumers paid for certain dairy products
- This co-ordination was achieved by supermarkets indirectly exchanging retail pricing intentions with each other via the dairy processors - so called A-B-C information exchanges.
- Efficient supply chains required a degree of communication.
- Certain meetings/interactions were held for legitimate market discussions

13. Galvanised steel tanks for water storage (information exchange decision)

- By way of a separate decision, this information exchange took place at a single meeting, in the context of a market which was already subject to a long-running cartel involving price fixing, bid rigging and market sharing by way of customer allocation (the main cartel)
- Balmoral was not a party to the main cartel infringement, and members of the main cartel were forced to compete with Balmoral Tanks for the supply of CGSTs.
- Balmoral Tanks attended a meeting at which it disclosed and received commercially sensitive information.

14. Airline passenger fuel surcharges for long-haul passenger flights

- BA and VAA co-ordinated their surcharge pricing on long-haul flights to and from the UK through the exchange of pricing and other commercially sensitive information.
- The contact between the Parties allowed each to make its decisions on PFS changes with foreknowledge of its main UK competitor's reaction.
- There were two channels of communication between the Parties in respect of the PFS changes; one at a communications level and the other at a commercial level.
- Interactions between the company's senior managers involved joint industry wide media initiatives on behalf of their airlines.

Category C. Abuse of dominance by contract counterparty/bidder as a result of market power conferred by contract or during contract negotiation process (e.g. because of contractual/commercial constraints on replacement)

15. Health and fitness clubs- consumer enforcement case

- Companies which operated in the health and fitness sector were using similar unfair contract terms or business practices, namely tying consumers into minimum membership periods with limited rights to cancel should their circumstances change and/or using misleading debt collection practices (unreasonable contract terms-customers were commercially constrained by the contract).
- OFT secured an enforcement order which prevented Ashbourne Management Services Limited (AMS), a gym management company, and its directors from recommending, using or relying on certain unfair contract terms and prohibited a number of its former debt collection practices which amounted to unfair commercial practices.

16. Domestic bulk LPG suppliers- consumer enforcement case

- In the O**ff-Grid Energy Market Study**, the OFT received complaints that some people may be locked into domestic bulk LPG contracts with significant and unavoidable price increases.
- The concerns raised by the OFT varied by supplier and primarily related to two areas:
  - improved and/or clearer termination/switching/cancellation rights.
  - consistency with the Competition Commission (CC) Orders.

17. Vehicle service, maintenance and repair platforms

- Certain provisions in Epyx's contracts restricted its service, maintenance and repair platforms, customers - particularly those that manage vehicle fleets - from evaluating, developing, marketing and using alternative systems
- Epyx offered commitments that would relax or remove these contractual restrictions, giving Epyx's customers the freedom to work with, develop and sponsor alternative systems while also enjoying more frequent opportunities to switch supplier.

Category D. Abuse of dominance by bundling but where there may be efficiency justifications (but no technical efficiencies)

18.BskyB

- BSkyB was in a dominant position (Media Industry).
- The alleged anticompetitive behaviour was bundling practices of sports and film channels.
- OFT disagreed with this argument and closed the case.

19.IDEXX Laboratories Ltd

- There were no grounds for action related to abuse of dominance, since it was unlikely that INDEXX's bundling of animal diagnostic testing equipment and external laboratory tests would foreclose competitors.

Category E. Agreement or understanding between contract sellers as to the exercise of contractual rights to vary contractual terms (e.g. price) pursuant to an existing contract

None.

6. Motivation and description of fieldwork

Table 46: Motivation of information sought from lenders (through structured interview-based fieldwork)

Question category	Information sought	Relevance to study
Overview of activity in syndicated lending	Market-positioning and strategy, segments covered (LBO/PF/INFRA and geographic), geographic location of decision-making	Contextual understanding of answers to other questions. Contribution to consideration of market segmentation.
Transaction mechanics	Step by step description of deal process, including details on:	
	1. Origination of transaction to bank, functionality of different teams in the bank and interaction between these	Contextual understanding of answers to other questions.
	2. Processes and governance around internal and external information flow	Understanding information exchange throughout origination and syndication process.
	3. Appointment as MLA and formation of bank group	Understanding nature of the appointment process (e.g. competitive), use/nature of any market soundings, scope for (abuse of) dominance.
	4. Role in general syndication (where applicable)	Understanding information exchange, market flex and any subsequent negotiation/allocation.
	5. Basis for price-setting of loan	Understanding nature and availability of information sources used.
	6. Activity in and price-setting of any ancillary services	Understanding scope for bundling, timing and nature of such ancillary services.
Secondary trading	Scale of activity, functional location within bank	Understanding role in primary market price formation, scope for abuse of informational advantage by MLAs, impact on MLA incentives.
Market evolution	Evolution of non-bank lenders and investors	Understanding broader competitive dynamics.
	Market inefficiencies and the scope for technological or regulatory	Identifying market features that might generate sub-optimal economic

	change to resolve these	outcomes.
Refinancing and restructuring	Functional location of restructuring within bank and description of processes in restructuring and scope for sale	Understanding scope for abuse of informational advantage by MLAs, impact on MLA incentives

Table 47: Motivation of information sought from non-bank lenders and investors (through structured interview-based fieldwork)

Question category	Information sought	Relevance to study
Overview of activity in syndicated lending	Market-positioning and strategy, segments covered, geographic location of decision-making	Contextual understanding of answers to other questions. Contribution to qualitative interpretation of market segmentation.
Transaction mechanics	Step by step description of deal process, including details on:	
	1. Origination of transaction	Contextual understanding of answers to other questions, nature and form of interaction with MLAs/borrowers/sponsors.
	2. Processes and governance around internal and external information flow	Understanding information exchange throughout origination and syndication process.
	3. Role and approach to general syndication	Understanding information exchange, market flex and any subsequent negotiation/allocation.
	4. Approach to loan pricing	Understanding nature and availability of information sources used.
Secondary trading	Scale of activity and role	Understanding role in primary market price formation, scope for abuse of informational advantage by MLAs.
Market evolution	Evolution of non-bank lenders and investors	Understanding broader competitive dynamics.
	Market inefficiencies and the scope for technological or regulatory change to resolve these	Identifying market features that might generate sub-optimal economic outcomes.
Refinancing and restructuring	Differentiation in processes between refinancing and origination, in restructuring and	Understanding scope for abuse of informational advantage by MLAs, impact on MLA incentives.

	scope for sale	

Table 48: Motivation of information sought from borrowers (through survey-based fieldwork)

Question category	Information sought	Relevance to study
Market experience	Quantity and type(s) of transactions involved with	Contextual understanding of answers to other questions.
Substitutes for syndicated loans	Availability of substitutes and reasons for selection of syndicated loan	Contribution to qualitative interpretation of market segmentation.
Process	1. Approach to appointment of MLA, e.g. number of banks approached and relationship of these to borrower	Understanding nature of the appointment process (e.g. competitive), use/nature of any market soundings, scope for (abuse of) dominance.
	2. Approach to formation of syndicate, e.g. identification of lenders, nature of approach	Understanding role vis-à-vis MLAs on selection and process.
	3. Approach to setting of terms, including experience with flex	Understanding frequency and views of market flex.
	4. Approach to assessing satisfaction with outcomes, e.g. use of independent advisers	Understanding use of third party advisors, particularly if any potential conflicts of interest involved.
	5. Approach to negotiating any ancillary services	Understanding scope of bundling, timing and nature of such ancillary services, both those directly linked to loan and not.
	6. Nature of fees, i.e. scale of contingent elements	Understanding MLAs' incentive structure.
Market evolution	Market inefficiencies and the scope for resolution of these	Identifying market features that might generate sub-optimal economic outcomes.
Restructuring	Experience and satisfaction with outcomes	Understanding scope for abuse of informational advantage by MLAs.

Table 49: Motivation of information sought from sponsors (through survey-based fieldwork)

Question category	Information sought	Relevance to study
Market experience	Quantity and type(s) of transactions involved with, including with stapled finance	Contextual understanding of answers to other questions.
Substitutes for syndicated loans	Availability of substitutes and reasons for selection of syndicated loan	Contribution to qualitative interpretation of market segmentation.
Process	1. Approach to appointment of MLA, e.g. number of banks approached and relationship of these to borrower and actions to replace MLA	Understanding nature of the appointment process (e.g. competitive), use/nature of any market soundings, scope for (abuse of) dominance.
	2. Approach to formation of syndicate, e.g. identification of lenders, nature of approach	Understanding role vis-à-vis MLAs on selection and process.
	3. Approach to setting of terms, including experience with flex	Understanding frequency and views of market flex.
	4. Approach to assessing satisfaction with outcomes, e.g. use of independent advisers	Understanding use of third party advisors, particularly if any potential conflicts of interest involved.
	5. Approach to negotiating any ancillary services	Understanding scope of bundling, timing and nature of such ancillary services, both those directly linked to loan and not.
	6. Nature of fees, i.e. scale of contingent elements	Understanding MLAs' incentive structure.
	7. Views on balance of bargaining power between borrowers, sponsors and lenders	Contextual understanding of answers to other questions.
Market evolution	Market inefficiencies and the scope for resolution of these	Identifying market features that might generate sub-optimal economic outcomes.
Restructuring	Experience and satisfaction with outcomes	Understanding scope for abuse of informational advantage by MLAs.

Table 50: Detailed borrower and sponsor questions

Sponsor (S) and Borrower (B) question reference	Question	Answer options
S1; B1	What are your current funds under management (to nearest €100m)?	Open
S3; B2	Considering your business, which of the following types of debt financing have you (i.e. your firm) engaged in in the past 3 years?	Loan with a single bank (i.e. a bilateral loan)
		Loan with a group of banks (i.e. a syndicated loan or a club deal)
		Private placement of debt
		Bond financing
S4	How would you describe your experience in selecting banks (e.g. lead arrangers) to lead syndicated loans?	We tend to approach the same lead bank(s) because our established relationship guarantees the most efficient loan.
		We tend to approach the same lead bank(s) due to lack of suitable alternatives.
		We select the most relevant lead bank(s) based on the nature of the specific loan and the banks' expertise.
		We aim to use different banks in order to ensure competitive bids.
S5; B3	Where you do use syndicated loans, how close a substitute for syndicated lending are each of the following usually (1 being not a close substitute to 5 being the closest possible - if the option was not a substitute, mark separately as NA) ?	Bilateral lending
		Bond financing
		Private placement of debt (including Schuldscheine, etc.)
		Other (please specify)
		There were no substitutes to syndicated borrowing

Sponsor (S) and Borrower (B) question reference	Question	Answer options
S6; B4	Compared with the closest substitute in the previous question, what were the reasons for choosing to take out a syndicated loan?	Only means of securing necessary volume of lending
		Cheapest source of funding
		More flexible loan terms
		Less risk
		Faster
		More privacy of the transaction
		To maintain or make use of relationships with a number of banks
		Non-availability of substitutes
		Other (please specify)
S7; B5	Which of the following best describes the typical syndicated loan transaction your organisation engages in? **We use throughout the term 'mandated lead arranger' to include all lead banks such as agents, bookrunners, underwriters etc.**	Club deal without a mandated lead arranger (MLA)
		Club deal with MLA also appointed
		Fully underwritten deal with one MLA
		Fully underwritten deal with more than one MLA
		Best efforts deal with one MLA
		Best efforts deal with more than one MLA
S8; B6	Which procedure(s) do you usually follow when the MLA(s) are appointed in this transaction?	We appoint the MLA directly without receiving competing bids
		Request proposal for funding from various individual banks
		Request proposal for funding from various individual banks and also pre-formed, pre-determined groups of banks
		Issue a public request for proposals
		Other (please specify)

Sponsor (S) and Borrower (B) question reference	Question	Answer options
S9; B7	How many candidate banks do you typically approach to act as the MLA(s)?	One
		2 – 3
		4 – 5
		6 – 10
		More than that
S10; B8	Thinking about the banks approached to act as MLA, please say whether all, most, some or none are...	The banks approached are ones with whom the borrower had a pre-existing relationship
		The banks approached are ones with whom the sponsor had a pre-existing relationship
		The banks approached are based in the country of the borrower
		The banks approached are based in the country of the sponsor
		The banks approached are based in neither the same country as the borrower nor the sponsor
S11; B9	Thinking about your MLA appointment, which of the following usually applies?	We usually appoint one MLA
		We appoint more than one MLA if the complexity of the transaction requires this
		We appoint more than one MLA if the transaction is to be fully underwritten and a single MLA was not able to bear the risks on its own
		We appoint more than one MLA if each lead arranger is well-placed to execute different tasks
		Other (please specify)
S12; B10	Do candidate MLAs typically know the identity of the other MLA candidates?	No, as there are specific NDAs
		Not to our knowledge
		Yes, the process of appointment sometimes requires this

Sponsor (S) and Borrower (B) question reference	Question	Answer options
		Yes, this is a standard part of our process
S13; B11	Which of the following, if any, best represent(s) your attitude to the MLAs engaging in market sounding activities (this refers to the informal scouting of interest - both pre and post-appointment of the MLAs - in participation in the loan from other market players)?	It could lead to some privacy and information leaks concerns
		We do not have much choice but to allow it in order to ensure the success of the syndication
		It allows the lead arranger to gain market information which he may use to inflate the terms of the loan
		We do not allow market sounding pre-appointment of the MLA, but allow it post-appointment
		We do not allow it at all
		We place restrictions on the amount/type of information that can be discussed between banks (please specify)
		Other (please specify)
S14; B12	Have you ever been dissatisfied with the performance of an appointed MLA during the formation of the syndicate? What actions did you take?	Yes, and we replaced the MLA with another bank
		Yes, but there was not another suitable bank to replace it with
		Yes, but it was to contractually difficult or too costly in terms of other resources to replace the MLA
		Yes, but the other MLAs and/or loan participants ensured the MLA performed adequately in the end.
		No, all the MLAs have been satisfactory
S15; B13	What institutions are usually approached to be part of the general syndicate?	Commercial banks
		Investment banks
		Mutual funds
		Insurance companies
		Pension funds
		Multilateral financial institutions

Sponsor (S) and Borrower (B) question reference	Question	Answer options
		EU agencies
		National public sector agencies
		Other (please specify)
S16; B14	How would you best characterise those institutions typically considered to participate in the loan? Please indicate in terms of all / most / some / none your views of the following characterisations:	The institutions approached are ones with whom the borrower has a pre-existing relationship
		The institutions approached are ones with whom the sponsor has a pre-existing relationship
		The institutions approached are based in the country of the borrower
		The institutions approached are based in the country of the sponsor
		The institutions approached are based in the country of the MLA
		The institutions approached are based in neither the same country as the borrower, nor sponsor nor MLA
S17; B15	And how would you best characterise those institutions that actually do participate in the loan? Please indicate in terms of all / most / some / none your views of the following characterisations	The institutions approached are ones with whom the borrower has a pre-existing relationship
		The institutions approached are ones with whom the sponsor has a pre-existing relationship
		The institutions approached are based in the country of the borrower
		The institutions approached are based in the country of the sponsor
		The institutions approached are based in the country of the MLA
		The institutions approached are based in neither the same country as the borrower, nor sponsor nor MLA
S18; B16	What procedure is typically used when forming the bank syndicate (i.e. including participant lenders)?	Candidate participants are relationship lenders and approached directly by the borrower/sponsor (or their advisors)

Sponsor (S) and Borrower (B) question reference	Question	Answer options
		Candidate participants are approached by the MLAs who agree terms with them.
		Competitive procedure between candidate participants
		Some of the participant lenders are approached, while others compete for a position
		A "roadshow" was organised where the loan is marketed to interested parties
		Other (please specify)
S19; B17	Who has ultimate say on which institutions join the syndicate?	The borrower and the sponsor (or their agent) do
		The MLA(s)
		Both we and the MLA(s) have a say
		Other party has a say (please specify)
B18	We now turn to the stage where participant lenders negotiate and agree terms with the lead arranger(s), before the final syndicate is formed. What is the typical process for negotiating the terms of the loan (fees, margin, covenants, adverse situations) where there is a main group of banks involved and further participant lenders?	We negotiate and agree the terms with the lead banks/lenders and finalise all or nearly all of the term sheet before further syndication to participant banks.
		We negotiate and agree the terms with the lead banks, but these are subject to re-negotiation once participant banks engage in the syndicate.
S20; B19b	At the stage during participant lender negotiation and before the final syndicate is formed, what kinds of information are typically shared between your firm and the participant lenders?	The same information as that is shared with the lead arranger(s)
		Information agreed upon with the MLA
		We do not have insight into all the information that is shared with the participant banks.
S21; B19	How do you negotiate key terms with MLAs? Please rate the following:	We use past precedent to secure the best terms available

Sponsor (S) and Borrower (B) question reference	Question	Answer options
		We rely on advisers to secure the best terms available
		We rely on a competitive process (i.e. involving multiple lenders) to secure the best terms available
		There is not much negotiation as we agree on relatively standard loan terms
		Other (please specify)
S22; B20	What terms are liable to change between mandate and final syndication? Please check all that apply on LIKERT scale (no change, minor change, medium change, major change)	Margin
		Fees
		Covenants
		Terms of ancillary services
		No terms are negotiated with participant banks
		Other (please specify)
S23; B21	Are formal flex processes used by the lead arranger(s) in order to close the syndication?	Yes / No
	If yes, were you satisfied with the outcomes of the flex process in terms of risk-sharing with leading lenders? (Yes/No and explain)	Yes/No - Open
	If no to the first question, why?	The terms of the loan are not flexed, as we generally explicitly prohibit this in the mandate letter/other official documents
		There is usually no need for market flex but there can be provision for this in the contract
S24; B22	Did the negotiation with the lead arranger and/or participant institutions include arrangements about provisions of ancillary services related to the loan (e.g. hedging services, insurance, advisory services etc)?	Yes/No
	If yes, why / how?	We negotiate the provision of ancillary services as part of the lead arranger(s) initial bids for the loan
		We negotiate the provision of ancillary services as part of the participant lenders' roles in the syndicate

Sponsor (S) and Borrower (B) question reference	Question	Answer options
		We offer the lead arranger(s) the opportunity to bid for ancillary services after the loan has been finalised
		The lead arranger(s) make the provision of ancillary services to us a condition of the terms of the loan
	If no to the first question, what was the process?	We are able to make our own arrangements for ancillary services wholly independently of the loan syndication process
		We are able to make our own arrangements for ancillary services independently of the loan syndication process, but in the first instance gave the leading banks in the syndicate the right to bid
		We are able to make our own arrangements for ancillary services independently of the loan syndication process, but awarded the business to the leading banks in the syndicate
		Ancillary services are usually not relevant to our transactions
S25; B23	If you answered yes at S24; B22, which ancillary services do you typically agree to purchase?	Hedging services
		Insurance
		Advisory services
		Custodianship and related services
		Cash/collateral management
		Foreign exchange services
		Other (please specify)
S26; B24	Do the negotiations with the lead arrangers and/or other participant institutions ever include arrangements about provisions of services not connected to the scope of the loan (i.e. cross-selling, such as participation in another loan)?	Yes/No
	If yes, why / how?	We negotiate the provision of other, unrelated services as part of the lead arranger(s) initial bids for the loan
		We negotiate the provision of other, unrelated services as part of the participant lenders' role in the syndicate
		We offer the lead arranger(s) the opportunity to bid for other, unrelated services after the loan had been finalised

Sponsor (S) and Borrower (B) question reference	Question	Answer options
		The lead arranger(s) make the provision of other, unrelated services to us a condition of the terms of the loan
	If no, why / how?	We are able to make our own arrangements for other, unrelated services independently of the lead arrangers / syndicate participants
		We do not discuss such arrangements
S27; B25	If yes to S26; B24, exactly what kind of provisions were made?	Arrangement in another loan
		Participation in another loan
		Underwriting of other security
		Advisory services
		Custodianship and related services
		cash/collateral management
		Insurance
		Foreign exchange services
		Investment research and financial analysis
		Hedging services
		Other (please specify)
S28; B26	How is the final price of the loan typically negotiated per tranche?	Highest common denominator amongst all participant propositions to secure the necessary volume
		Negotiate common price
		Negotiate common price, based on initial talks between MLAs and us as the borrower
		The borrower/sponsor/adviser sets the price and requests interest from lenders
S29; B27	In your view, what are the main factors affecting the current pricing of syndicated loans?	Interest rate environment
		The risk profile of the borrower / sponsor
		The nature of risk of the project
		Market liquidity
		Appetite among non-bank lenders
		Regulatory changes

Sponsor (S) and Borrower (B) question reference	Question	Answer options
		Other (please specify)
S30; B28	How do you assess the price and terms on loans to ensure that these are satisfactory?	We use a predetermined benchmark price, based on our own assumptions and negotiate a price close enough to that
		We use a predetermined benchmark price, based on some industry standard and negotiate a price close enough to that
		We are willing to accept a higher than expected loan price, if the other terms of the loan (maturity, covenants, etc.) are good enough to compensate
		We are sometimes not very satisfied with the loan price, however we are not able to negotiate a lower one
		Other (please specify)
S31; B29	Receive any additional help in assessing price/terms?	No, we assess the terms internally
		Yes, we rely on an external financial advisor
		Yes, we rely on a relationship bank (who is part of the syndicate) to advise us
		Yes, we rely on a relationship bank (who is not part of the syndicate) to advise us
		Yes, we rely on some other institution (please specify)
S32; B30	Do the loan agreements include any provisions preventing secondary trading of the loan?	Always/Sometimes/Seldom/Never/We sometimes have provisions limiting secondary trading rather than prohibiting it
	If yes, what is the motivation for this?	Secondary market trading could complicate the repayment procedure, as the identity of the secondary lender may be ambiguous
		It could complicate a potential defaulting procedure
		We have some concerns about the distribution of our confidential information
		There are specific lenders we do not want to borrower from
		Other reason (specify)
S33; B31	How much, if any, of the MLA's fees are contingent on successful	All

Sponsor (S) and Borrower (B) question reference	Question	Answer options
	conclusion of the loan?	
		A large amount
		A reasonable amount
		A small amount
		None
S34; B32	In terms of the operation of the syndicate post-closure, has there been any default on the loan terms or need for refinancing?	Y / N
S35; B33	If Yes at S34; B32, please assess the following statements:	We negotiated with the original syndicate only
		We negotiated with the original syndicate and other market participants
S36; B34	If Yes at S34; B32 were ancillary services bundled in at this stage?	We negotiated the new terms and the provision of ancillary services with the original syndicate only
		We negotiated the new terms and the provision of ancillary services with the original syndicate and other market participants
		We had no choice but to accept the provision of all ancillary services by the syndicate members.
S37; B35	How, overall, would you rate the success of the loan syndication transaction in meeting your financing needs?	LIKERT scale
S38	In your view, are you aware of any risks to competition in the SL market arising from MLA or lender behaviour?	Open-ended
S39; B36	What, if any, improvements in the functioning of the SL market would you like to see?	Open-ended
S40	Was there was stapled financing?	Often/Sometimes/Never/Not applicable (i.e. if not an LBO deal)
	If yes, how did the final terms executed match up?	The final terms were more borrower-friendly, with the bank(s) offering the stapled financing
		The final terms were more borrower-friendly, with a different lender/ syndicate
		The final terms were the same, with the bank(s) offering the stapled financing

Sponsor (S) and Borrower (B) question reference	Question	Answer options
		The final terms were the same, , with a different lender/ syndicate
S41	When selecting lead arrangers, how important is the existence of an existing relationship?	Very important/ quite important / not very important /not important at all
	What benefits do you achieve from acting with the same institutions on multiple transactions?	Price benefits on loans
		More borrower-friendly terms on loans
		Better response in the case of default/ refinancing
		Price benefits to other services related to loans
		Price benefits to other services not related to loans
		More responsive in qualitative ways (e.g. timing)
S42	How do you consider the balance of power in a syndication to be evolving between sponsors, borrowers and lenders?	It's deal specific, so no trends are identifiable
		It's a borrower market and sponsors and borrowers are gaining additional power
		It's a borrower market and stable
		It's a borrower market but lenders are gaining additional power
		It's a lender market but sponsors and borrowers are gaining additional power
		It's a lender market and stable
		It's a lender market and lenders are gaining additional bargaining power

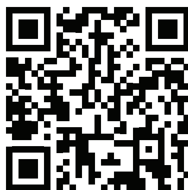
Abstract

Debt is a critical source of finance for the European economy. The syndicated loan market is a major contributor of debt finance, particularly in terms of large-scale debt.

This study by Europe Economics investigates whether the syndicated loans market in six selected countries – France, Germany, the Netherlands, Poland, Spain and the United Kingdom – is working well and efficiently. This research focused on two, important, segments within the overall syndicated lending market – loans supporting Leveraged Buy-outs (LBOs) and those financing project and infrastructure investment.

Our work identifies some areas of potential competition concern, particularly around aspects of information exchange between lenders, the provision of ancillary services (such as hedging) by banks that are part of the syndicate, the combination of advisory and debt arranging activities and in refinancing situations. We describe how these risks differ between the LBO and PF/INFRA segments. We identify those features in the market and within market participants that can influence the likelihood of these risks being actualised.

We also identify an area of inefficiency in the loan syndication market, not directly related to the competition policy risks, around settlement processes, which could be another area for future regulatory attention.



KD-04-19-330-EN-N
doi: 10.2763/738938