RETAIL BANKING SECTOR INQUIRY
PRELIMINARY REPORT II
CONSULTATION FEEDBACK FORM

Name of organisation : **Crédit Agricole SA**

Type of organisation: Credit Agricole SA is a fully licensed bank and a joint stock company, which acts as the central body of Credit Agricole Group and the holding company of a full array of subsidiaries specialized in banking, insurance and asset management business lines. Credit Agricole SA is a listed company in Paris Euronext Stock exchange.

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Have you received a request for information as part of the sector inquiry:

☑ Yes

☐ No

In response to the consultation instigated by the European Commission as part of its sector inquiry into the retail banking industry, the Crédit Agricole Group (hereinafter referred to as "**CA**") wishes to make some comments on the second interim report of the Directorate-General for Competition on current accounts and related services.

I. General observations

1) CA shares the Commission's objective of fair competition and a level playing field for all providers of banking and financial services, along with greater fluidity of these services across Europe. CA regards the European market as its future domestic market. It therefore fully supports any measure intended to remove artificial barriers to trade that are not justified by robust general-interest arguments, along with the fight against anti-competitive practices. It has fully co-operated with the sector inquiry and is prepared to supply the Commission with any further information it may require.

2) The Commission must, however, be aware that the development of the retail banking services covered by the report has been determined by each Member State's cultural and legal environment. Despite the rise of the internet, they remain local services in which direct contact between the client and his/her local branch enhances quality of service and builds trust. As a result, the distribution method and the pricing of these services differ between countries, resulting in differing business models and ultimately profitability patterns. These differences, which the report regards as "market fragmentation", should not necessarily be considered as entry barriers nor as indicators of abnormal market power. The report establishes no correlation between the concentration of the banking sector in a given country and the profitability of retail banking activities.

3) If a provider of banking and financial services wants to expand in other markets, it is not abnormal for it to learn the specific features of these markets and adjust its offering accordingly. This learning process forms part of the normal investments and risks that a company is prepared to assume as part of its development strategy. Efforts will always be required to adapt to local market conditions, even if customer behaviour converges and rules become more harmonised. This does not mean that a new entrant in a given market cannot make a significant contribution to product innovation, improve distribution methods and achieve greater coverage of the potential market. We have demonstrated this ourselves, particularly by rolling out our consumer credit offering in 13 European countries.

4) Neither is it abnormal that a de facto commercial advantage should be enjoyed by incumbent players that, over time, have accumulated in-depth knowledge of their domestic market and developed trusting relationships with their customers. This advantage is mostly offset by the need for a major national player to make its offering available throughout the country and address all consumers, whereas a new entrant can more easily limit its offering to the most profitable geographical areas and customer segments. The commercial franchise built up over time by domestic players cannot be regarded as a barrier to competition. This is because other players, particularly European ones, can enter the market either by setting up an entirely new business, making an acquisition or sealing a partnership, without encountering artificial barriers to their strategy or unequal treatment in terms of legislation, tax or technology. Merger and acquisition activity, which is accelerating in Europe and in which CA is actively involved, is undoubtedly a good way of achieving a more integrated market, while respecting each country's individual characteristics. From this point of view, the Commission's initiatives to prevent supervisory authorities abusing procedures for assessing new shareholders in banks, insurers or investment companies are welcome.

5) Differences in legal status between banks cannot be considered as impediments to healthy competition, provided that all banks are subject to the same rules for conducting their businesses and that none benefit from specific advantages or monopolies, particularly in distributing certain products. CA's French retail banking business is mainly organised through regional co-operative banks and their close-knit branch networks. It has traditionally been instrumental in giving access to banking and financial services to customer segments ignored by the traditional banking system. In line with its philosophy of serving its members and customers, CA has pioneered bancassurance products, in both life and property/casualty

segments. This has changed the competitive landscape among the traditional insurance players, leading to new products and distribution methods and substantially lowering the cost of these services. The diverse range of bank statuses should be fully preserved, since it is a vital aspect of healthy competition and is popular with customers. In France, there is competition not only between banks with different legal statuses (state owned, private, co-operative) but also within each legal status category. There are four national bank groups with co-operative status competing openly in the household, family business and SME segments.

6) CA makes constant efforts to diversify its range of banking and financial services, which include a comprehensive range of personal and property insurance services. It also strives to distribute this offering through all possible channels and to streamline its management. It is making the most of its universal bank model, which is the standard model in France and continental Europe. While limiting costs, particularly those associated with a dense branch network, this model allows high-quality products and services to be made available to the greatest number of people. It requires an active policy of cross-selling products and enhancing customer loyalty. Although the report does not demonstrate why, it suggests that equipment rates (the number of products from the same bank owned by each customer on average) and customer mobility (measured by the number of customers switching current accounts between banks) are indicators of structural competition problems. We do not share this view. We are open to improvements aimed at making it easier for customers to switch banks. However, we would draw the Commission's attention that a bias may arise if an approach based on other more specialised retail banking models is applied to the economics of the universal bank model, which is highly successful in terms of both economic performance and customer satisfaction. Our philosophy, which stems from our roots as a mutualist institution, is to serve our customers and establish long-term relationships with them. It is carried out by our marketing policy, which involves strengthening customer relationships and building loyalty, and is far removed from any attempt to retain customers artificially.

7) CA would suggest to the Commission that equating all kinds of co-operation between banks in the field of payment instruments as a threat to competition risks weakening service quality and increasing costs. If there is one area in which market fragmentation – which the report criticises – is particularly damaging to consumers, it is payment instruments. "Interbancarity" (co-operation between banks ensuring acceptance and exchange of all payment instruments) has existed in the French payment cards market for many years, through an economic interest group that is open to any new entrant. It is also very popular with consumers. Revenues from payment instrument usage in France are lower than the European average. This shows, if proof were necessary, that the model is beneficial for consumers. The SEPA, currently being implemented under the aegis of the EPC, represents an effort by the European banking sector to extend the combined benefits of intelligent co-operation between players and genuine price and product competition to the whole EU. It will result in very high costs for the banking industry, to allow the broadest possible migration of payment transactions relating to new pan-European products. The Commission must also be aware that disruptive changes to the rules underpinning the system's economics and security are not compatible with smooth implementation of the SEPA and its success among economic agents.

II. Answers to specific issues raised by the Commission

1) What are the main reasons for market fragmentation in Europe's retail banking sector? Please identify whether they are mainly of regulatory, structural or behavioural nature.

- It is hard to compare the structure of the retail banking sector with that of other sectors, since it relies heavily on local and trusting relationships with customers. Reputational issues are involved, and banks' relationships with consumer and small-business customers are developed on a long-term view.

- The wide variety of behaviours, languages, cultures and consumption habits should not be downplayed in a sector as sensitive as retail banking. It is the main reason why consolidation between banking and financial companies has taken place and continues to take place mainly within domestic markets. As the Commission emphasised in its statement on intra-EU investment in the financial services sector[1] the cost of adapting products and processes from one country to another is a major barrier to cross-border consolidation.

- There are significant differences in regulations, particularly as regards consumer protection and in taxation, for example concerning the benefits offered by certain savings products. These contribute to the fragmentation observed by the Commission, without being the main reason behind it. Similarly, certain supervisory authorities have used their prudential powers to protect their domestic market in an unjustified manner and to dissuade foreign players from moving into it.

- Nevertheless, consolidation is accelerating within the EU, and we are seeing the emergence of groups with genuine distribution capacity in several European countries. This trend is likely to continue, and there is no doubt that this will lead to more consistent consumer behaviour and convergence in banking practices.

- The CA can only support the Commission's efforts[2] to regulate assessments by supervisory authorities in the event that a company buys a qualified stake in a banking, insurance or investment company, based on strictly defined criteria and strict rules in terms of the timetable, procedures and transparency. However, these rules and criteria, while being fully justified in building a single European market, should not apply to purchases of stakes by investors or financial groups based in a non-European jurisdiction, unless there is an agreement between the EU and this jurisdiction ensuring <u>full reciprocity</u>. Clarification from the Commission on this crucial point would be welcome.

2) What are the main causes and implications of the different level of concentration in the EU retail banking markets?

[1] Communication C/2005/4080 of 21 October 2005
[2] Proposal for a directive concerning the procedures and evaluation criteria applicable when assessing acquisitions and stake-building in companies in the financial sector, published on 12 September 2006

Different levels of concentration in EU retail banking markets are caused mainly by the differing size of countries, differing levels of maturity in their retail banking markets and historical and political factors.

§ The banking and financial sector is logically more concentrated in small countries than in large ones. Geographical density and, to some extent, market maturity are also positively correlated with concentration.

§ Certain large countries, i.e. Spain, Italy and Germany, remain strongly attached to regional structures and specific local features, and this is at least partly reflected in their banking structures.

§ Economic policies also explain some of the differences. In France, successive policies of nationalisation followed by privatisation have helped to speed up concentration in the banking sector. In Germany, the government has favoured proximity between credit institutions and SMEs, helping the development of the "Mittelstand". In Italy, the government has gradually reformed savings banks, leading to an initial phase of consolidation. However, it has also put up obstacles to prevent foreign groups controlling Italian banks, hampering sector restructuring.

§ In some countries like Germany, three separate types of bank (private-sector banks, co-operative banks and savings banks) exist side-by-side. This has so far prevented greater consolidation, at least between entities with different legal statuses, unlike the situation in France, Belgium and Italy.

The level of concentration in most European countries, and France in particular, is relatively low by comparison with other goods and service industries. Banking sector consolidation allows more streamlined product development, information systems and branch networks, and gives access to cheaper financing by improving credit ratings. It has given Member States banks capable of carrying out the considerable investment needed to meet the challenges of the euro introduction, the on-going implementation of Basel II, the development of e-banking and international expansion. Consolidation must now continue at the European scale, to help banks deal with the new challenges of globalisation.

3) What are the main reasons for the varying rates of profitability and income in retail banking across the Member States?

- The report mentions varying rates of profitability in retail banking between countries. However, it does not establish a correlation between these variations and the degree of concentration or the relative size of players in a given country.

- The main reason for the observed variation in profitability is the dynamism of individual banks. This dynamism consists of efforts to streamline structures and tools, rigorous management, appropriate marketing decisions, product innovation capacity, service quality and policies for staff training and motivation, particularly as regards the sales force. A good example of a profitable strategy that benefits consumers is bancassurance, a field in which Crédit Agricole leads the French market.

- Aside from these microeconomic factors, the profitability of retail banking activities is clearly influenced in both directions by the general economic background, the quality of public infrastructure and services, the impact of certain regulations (particularly labour law) and by the tax and social security burden. Many of these factors fall outside the remit of the European legislator, making a fully integrated European market a long term objective.

- Differences between consumer protection systems cause differences in profitability, although this effect should not be overstated. These differences should be overcome by strenuous harmonisation efforts in key provisions. In the consumer credit area, this means rules concerning pre-contractual information, the definition of the APR (annual percentage rate), the right of withdrawal and cooling off period and out-of-court appeal mechanisms.

- The report rightly states that some Member States' governments intervene in a way that distorts competition. In particular, following a complaint filed by CA, the Commission initiated a formal procedure against France concerning Banque Postale and Caisses d'épargne's monopoly on the Livret A savings account and Crédit Mutuel's monopoly on the Livret Bleu savings account. We will naturally pay close attention to further developments in this case.

4) Are there other types of entry barriers in retail banking that have not been identified in the preliminary report?

In Europe, banking and insurance are currently supervised along a fundamentally national set up. This constitutes, if not a barrier, then at least a serious inconvenience. We would draw the Commission's attention to the need to adjust this system to the situation faced by financial groups, whose businesses and central functions are becoming increasingly pan-European. Apart from enhancing co-operation between supervisory authorities, a pragmatic way forward would be to give final decision-making power to the supervisory authority in the country of the group's head office, based on a consolidated view of the groups concerned.

5) Where and how does competition law have a role in tackling entry barriers in retail banking?

No particular comment.

6) Access to credit databases and payment infrastructures are sometimes cited as a barrier to entry in retail banking markets. Are there significant barriers to access which merit further investigation?

- <u>Credit data</u>: the report rightly states that credit databases vary widely in terms of ownership (with some credit registers being state-owned and some being privately owned), the nature and extent of information collected (with some showing positive data and some only default incidents) and pricing. Laws governing the protection of personal data included in credit registers also vary between countries. We share the Commission's objective of ensuring non-discriminatory access to data in a given country by credit institutions, whether or not they are resident in the country in question, provided that these institutions comply strictly with applicable personal data protection rules. However, we would encourage the Commission not to intervene in the debate over data ownership and type (positive or negative). No correlation has been established between the different types of databases in the EU and mobility rates of consumers.

- Payment infrastructure: Please refer to our comments on question 8.

7) What are the main reasons for the low mobility of retail banking customers?

The question refers to the mobility of retail banking customers – measured by the Commission through the "churn rate" – which rate is described as "low". This is a qualitative statement for which no demonstrable evidence has been provided. The churn rate is lower on average in EU-15 countries (8.91%) than in new Member States (11.96%), and varies little between EU-15 countries, except in Finland and the Netherlands, despite wide variations in banking structures.
These comparisons suggest that "low" mobility is a characteristic of fully mature markets. This is supported by a comparison between the length of customer relationships, which averages 8.56 years in EU-15 countries and 10 years in the US according to a survey quoted by the report.
In addition, "multi-banking" - i.e. customers holding current accounts with more than one bank - is a phenomenon that affects the most developed markets. Multi-banking is in some respects an alternative to mobility, but is not taken into account in the Commission's analysis.
The report was unable to establish any significant correlation between these indicators and the profitability of retail banking activities, or between these indicators and the level of banking sector concentration.
As a result, there is no justification for concluding that there is a lack of competition in the retail banking sector, as the report seems to suggest.

<u>This is confirmed by an analysis of the French market.</u> According to the Commission's report, France's "churn rate" has averaged 7.58% in the last five years (2001-2005). This should be regarded as high, rather than low, for the following reasons.

- The French banking market is mature. Some 98% of the population having bank accounts and there are 70 million sight deposit accounts, including those held with Banque Postale. We know that mature markets have low or zero churn rates, and that the churn rate automatically tends towards the population growth rate.
- Product obsolescence does not exist in the banking industry. In the consumer goods industry (automotive, telecoms, white/brown goods etc.) obsolescence – i.e. products wearing out or being overtaken by new designs – prompts consumers to buy new products, at which point they consider new suppliers. In the financial sector, a sight deposit account does not wear out, and product ageing, loss, theft or deterioration does not apply.

- A current account does not have a time limit for its use. Additionally, opening and closing accounts are totally free of charge in France.
- Customer satisfaction has been very high over the long term. The latest FBF survey shows a satisfaction rate of 86% (September 2006) as did the latest CSA/La Tribune survey (March 2006). This level of satisfaction means that customers' assessment of service quality is one of the highest seen in any industry. The satisfaction rate covers a range of services (current accounts, payment instruments, loans, savings, insurance etc.) and not just sight deposit accounts.
- French banks have developed services to help customers switch banks, and they bear exit costs such as the cost of sending new bank details to direct debit or standing order recipients.
- Banks compete aggressively with each other to win new customers. This is particularly true in the youth market. The churn rate is abnormally high among people aged 18-35, and even higher among students aged 18-25. Banks' promotional campaigns aimed at young people encourage them to change banks several times.

In a mature – not to mention fully saturated – market, the "normal" level of account switching should be the same as the population renewal rate, i.e. just over one million people per year. However, France's churn rate of close to 8% is the equivalent of the entire customer base of a large national bank like Société Générale changing banks every year.

8) Are there features of the payment industry that limit competition either at the level of provision of clearing and settlement services or the provision of retail banking services?

Clearing and settlement systems must comply with the regulator's security rules to ensure maximum confidence among all users.
As a result, as direct participants in these systems, we have size, performance and financial solidity constraints. The systems in which we are shareholders require heavy investment, and so certain credit institutions prefer not to bear these costs directly

9) Are interchange fees necessary for the development of payment instruments (credit transfers and direct debits) in the EU?

Interbank fees are necessary if a payment system requires all parties concerned to make investments and assume expenses and risk-related costs and if passing these directly on to their customers would disqualify the payment system.
We must therefore objectively examine and analyse these investments and costs, look at who bears them and strike a balance between the various players.
Such interbank fees have proven effective in France. In 15 years, cards have become the main electronic payment method. They give full satisfaction to both our cardholder and merchant customers.

10) Are there issues related to industry initiatives in the context of SEPA that should be assessed from a competition viewpoint?

We would like to be certain that we will not be criticised for the EPC's work on the introduction of the SEPA on 1 January 2008 and for the planned scheme development work.

11) Please provide comments on any other competition-related issues in relation to retail banking markets.

No specific comment.