

Nationwide to Acquire Virgin Money for £2.9bn

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Deal Overview:

Bidder: Nationwide

Target: Virgin Money

Deal Size: £2.9 Billion

Buy Side Advisors: UBS (Financial); Slaughter & May (Legal).

Sell Side Advisors: Goldman Sachs and JP Morgan (Financial); Clifford Chance (Legal).

Expected Completion: Q4 2024

Nationwide Overview:

Nationwide is a British building society offering a variety of services for consumers such as personal banking products, investment accounts and mortgages. Nationwide's current account market share reached 10.4% in 2023. Nationwide saw £2.229bn in statutory profit in 2023, a £632m increase compared to 2022. This increase in profits is impressive especially as base rates and inflation continues rising. Nationwide is one of the UK's largest building societies as it boasts that 1 in 10 current accounts are with them. Nationwide enticed customers to save with them by offering high interest rates on savings accounts and adjusted rates to base rate changes. Nationwide saw an extra £9.1 billion saved with them in 2023 compared to 2022's £7.7 billion.

Founded: 1884

HQ: Swindon, England

CEO: Debbie Crosbie

No. Employees: 18,000

Market Cap: £1.42 Billion

Virgin Money Overview:

Virgin Money similarly offers a variety of services such as insurance, pensions, savings accounts, and current accounts. Virgin Money has 6.6 million customers who can use their digital banking and physical banking locations. Virgin Money offers two types of current accounts, one being a zero cost "M Plus Account" where some benefits are £0 fees when using their card overseas and 2.02% AER on current account balance up to £1,000. And an Easy Access Cash ISA at 4.76% AER. Alternatively, Virgin Money offers a "Club M Account" for a monthly fee of £12.50 which offers benefits such as tools within the Virgin Money app to "track, budget, save and pay", no fees when withdrawing cash abroad, breakdown cover, worldwide family multi-trip travel insurance, and emergency medical treatment cover. Their Club M Account is optimal for families that travel often as the benefits outweigh the fees.

Founded: 1995

HQ: Newcastle Upon Tyne, England

CEO: David Duffy

No. Employees: 7,300

Market Cap: £2.7 Billion

Deal Summary and Structure

Nationwide has agreed to acquire Virgin Money for a total transaction value of £2.9 billion. Nationwide offered 220p, which includes a 2p final dividend, for each of Virgin Money's shares. The offered price is a 38% premium to the bank's closing price on the 6th March (Date of announcement). The deal will combine Nationwide's £274 billion and Virgin Money's £92 billion in assets to total £366 billion. Furthermore, Nationwide will acquire Virgin Money's 91 branches which brings the building society's total to 696 and have promised their customers that there will be no closure of branches until 2028. Lastly, Nationwide will see a significant increase in their deposits as their £191 billion increases to £257 billion after the transaction. Nationwide looks to increase their competitiveness against banks like HSBC, Lloyds and Barclays in consumer and business banking therefore this strategic acquisition allows them to significantly increase their market share.

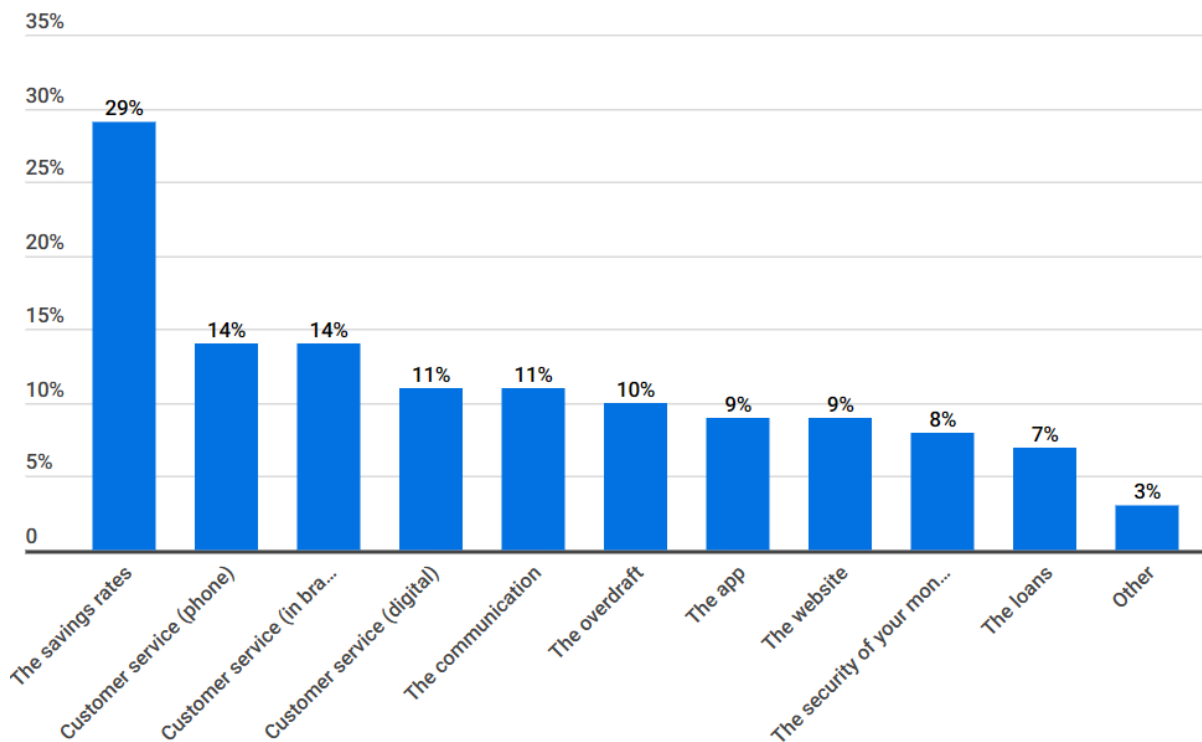


Industry Analysis

HSBC is the largest UK bank by market capitalisation at £117.8 billion in April 2024. It is over 4.5x larger than the second largest bank, Lloyds. Nationwide saw 16.3m customers in 2022 while Barclays saw 48m, a difference of 31.7m customers. However, Nationwide makes up for this statistic with their 90% customer satisfaction rate, the second best in the UK in 2023 behind Starling bank.

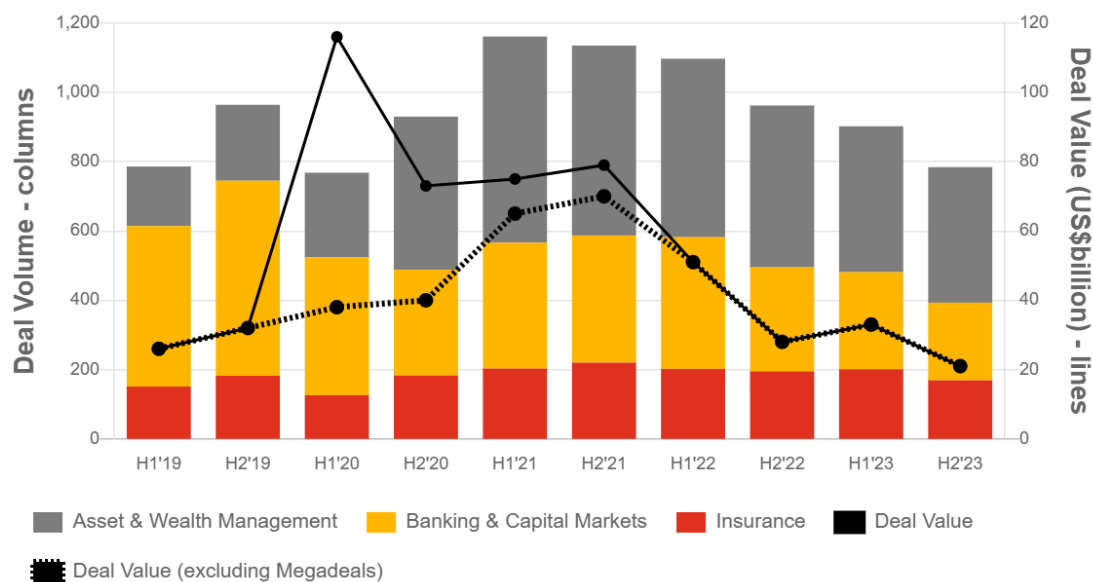
In the UK, more than 50% of customers reported they felt negatively towards their provider. Banks are criticised for their poor customer service, a factor that is extremely important to customers in special circumstances such as fraud attempts and errors. Data also shows that every 5 years at least 40% of the British population switch bank accounts therefore Nationwide is likely trying to capitalise on this market through a positive reputation.

Reasons high-street bank users feel negative about their bank



Source: Finder

Financial Services deal volumes and values, 2019-2023 EMEA



Source: PwC

There are some key drivers for M&A in 2024, with two being large cash balance sheets and the need for growth. When looking at Nationwide's capital structure it is an all-cash transaction meaning there is no debt or equity used in the deal. Additionally, two of the main reasons for the transaction is to grow their mortgage market share and to enter business banking and given that the market is saturated by large competitors, Nationwide felt that inorganic growth was the best option. However, some inhibitors are the geopolitical events happening this year which are likely going to affect the volatility of interest rates, inflation and corporate profits.

Many corporations are concerned about the future economic environment, which is emphasised by US companies rushing to sell corporate bonds to take advantage of current interest rates in case they increase later in the year. Depending on the outcome of the elections, there could be an uptick in economic performance, meaning that valuations of companies could rise if performance reflects it. Consequently, this may be why Nationwide has decided to begin acquiring Virgin Money in early 2024, because later in the year their valuation could increase, therefore becoming more expensive.

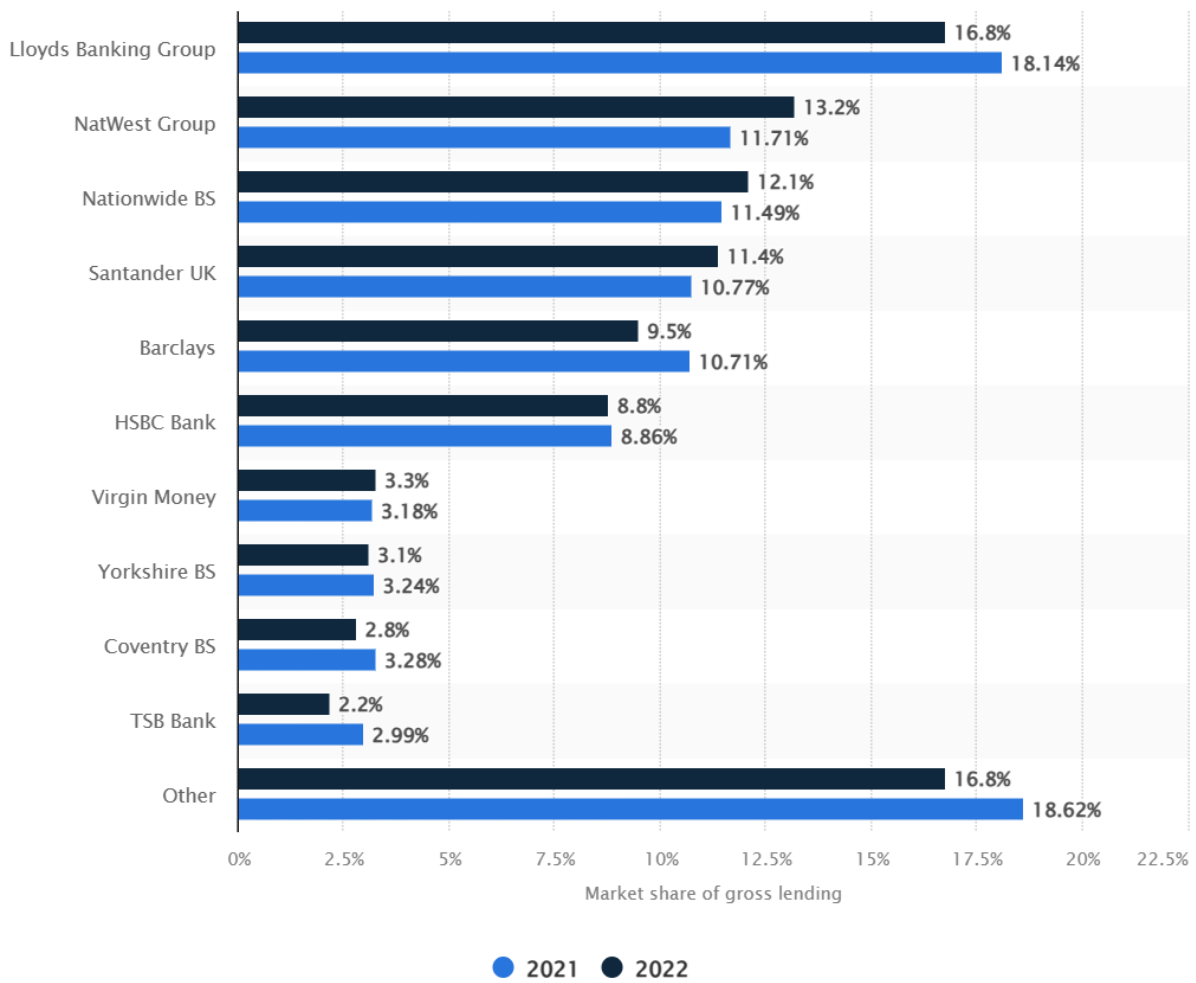
Financial Services players are under significant pressure to address current and future challenges and M&A can be seen as a catalyst for transformation therefore

driving its demand. Financial Services companies are focusing on digital transformation and technology integrations to compete with disruptive fintech companies entering the market. Hence, deals in 2024 may focus on companies that hold significant data, provide cyber security solutions, drive operational efficiency or speed up transaction processes. Economic instability may lead to cheaper acquisitions of fintech companies as many may be financially distressed due to the lack of new capital and liquidity access, consequently being an attractive target.

Deal Rationale

The acquisition will allow Nationwide to provide a wider range of products/service to consumers, one of which is business banking. Nationwide previously considered moving into business banking however abandoned due to coronavirus pandemic interruptions. Nationwide believes that Virgin Money's existing £9bn of business lending balances and "Business Current Account" will allow Nationwide to expand on their current products and diversify their sources of funding.

Largest mortgage lenders in the UK from 2021-2022, by market share



Source: Statista

| “Better value mortgages and savings, and leading customer service” |

Chairman – Kevin Parry

Additionally, the deal will result in Nationwide becoming the 2nd largest provider of mortgages and savings in the UK. Nationwide’s mortgage market share will increase from 12.2% to 15.7%, positioning them right behind Lloyds Banking Group by market share. Consequently, the interest rate on mortgages acts as a secure revenue stream that helps increase profitability and offset any losses elsewhere. Moreover, it could allow Nationwide to offer lower rates for customers which makes their products even more attractive.

Lastly, Nationwide’s lending and deposit space will expand considerably as they increase their number of customers from 17m to 23.6m and add Virgin Money’s

Total Lending of £72.8bn and Deposits of £67.3bn to their portfolio. Virgin Money has a strong presence in unsecured lending business with £6.7bn in balances and estimated 8.6% market share of the UK credit card market. Combining all these factors will allow for Nationwide to scale its core lending and deposit markets and leverage this growth to drive profitability.

Risks

A common issue that acquisitions face is the integration of employees. Virgin Money's 7,300 employees will join Nationwide's 18,000 to create a total of 25,300. As of now, there are no plans to reduce the workforce especially as the integration of companies is expected to take six years however duplication of roles is highly likely which will require redundancies to take place, leading to negative news reports, affecting Nationwide's reputation negatively.

As Virgin Money has an online banking platform, the technological integration between Nationwide's and Virgin Money's app may be particularly difficult. For example, cybersecurity issues could arise when transferring customer data. Nationwide must assure smooth transition from one app to another and keep Virgin Money customers informed in advance. This can result in a costly and time-consuming process, and consequently any technical difficulties could lead to Virgin Money customers wanting to move to a competitor with more reliable services.

Conclusion

Overall, the deal will likely result in positive impacts for Nationwide within Mortgage Lending, Deposits and Lending. They will have the capacity to offer a variety of products within Business Banking, which is what they have been looking to do since before 2020. The increase in assets considerably increases Nationwide's competitiveness against banks such as Barclays, Lloyds Bank, and HSBC which offer similar products. Their increased market share of mortgage lending may cause greater positive impact as net mortgage approvals rose to 60,400 in February from 56,100 in January, highest since September 2022. Despite some lenders raising their rates because of rising inflation in January and February demand still stayed strong. Assuming this activity continues throughout the year Nationwide could feel the positive impact of the transaction early after the deal completion. However, this all depends on whether they can navigate the risks stated above; they are critical in assuring Nationwide receives as much value from the deal as possible.

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