

***Case No IV/M.1413 -
THOMSON-CSF /
RACAL
ELECTRONICS***

Only the English text is available and authentic.

**REGULATION (EEC) No 4064/89
MERGER PROCEDURE**

Article 6(1)(b) NON-OPPOSITION
Date: 15/03/1999

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COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 15.03.1999

In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EEC) No 4064/89 concerning non-disclosure of business secrets and other confidential information. The omissions are shown thus [...]. Where possible the information omitted has been replaced by ranges of figures or a general description.

PUBLIC VERSION

MERGER PROCEDURE
ARTICLE 6(1)(b) DECISION

To the notifying parties :

Dear Sirs,

Subject: Case No IV/M. 1413 – THOMSON-CSF / RACAL ELECTRONICS

Notification of 01.03.1999 pursuant to Article 4 of Council Regulation No 4064/89

1. On 15.02.1999, the Commission received a notification of a proposed concentration pursuant to Article 4 of Council Regulation (EEC) No 4064/89 by which the undertaking Thomson-CSF (“Thomson”) and Racal Electronics Plc. (“Racal”) acquire within the meaning of Article 3(1)(b) of the Council Regulation joint control of a newly created company constituting a joint venture.
2. After examination of the notification, the Commission has concluded that the notified operation falls within the scope of Council Regulation (EEC) No 4064/89 and does not raise serious doubts as to its compatibility with the common market and with the EEA Agreement.

I. THE PARTIES' ACTIVITIES AND THE OPERATION

3. Thomson is a French company, active in professional electronics and defence systems. Racal is a British company active in defence and industrial electronics and in telecommunication services.
4. Following the signature of a joint venture agreement, Thomson and Racal will create a joint venture, MBN Ltd (“MBN”). MBN will be active in the prime contracting of High Performance Local Area Systems (“HP LAS”), which form part of the more general sector of military ground communication systems and are used by military land forces to transmit voice, data and images between headquarters and vehicles.

II. THE CONCENTRATION

Joint control

5. The shares of the MBN will be equally held by the parties. Moreover, major decisions, including, *inter alia*, the approval of the business plan and the annual budget and the appointment of upper level managers, will be made by unanimous approval of the Board, consisting of six members equally appointed by the parties. Presiding over the Board will be a Chairman with no casting vote.
6. It is therefore concluded that the joint venture will be jointly controlled by the parties.

Full function joint venture operating on a lasting basis

7. MBN, which will be established on an indefinite basis, will be active in the prime contracting of HP LAS. Its business will include all activities in connection with research and development, system integration and testing, marketing, sales and support of HP LAS. It will have access to sufficient resources including finance, staff and intellectual property rights.
8. MBN's first activity will concern the supply of a HP LAS under the first phase of the so-called Bowman Project. This project covers the refurbishing of the tactical communication networks of the British army, it includes the development and the production of a HP LAS, and its customer is the UK Ministry of Defence (MOD). The first phase of the overall project has been contracted to the UK company Archer Communication Systems Ltd ("Archer"), which is a joint venture set up between BAe, ITT and Racal for the sole purpose of performing the Bowman project. Archer has decided to subcontract the HP LAS part and, after a selection process, has awarded this subcontract to a joint team between Thomson and Racal. This subcontract will be transferred to MBN.
9. However, MBN will not be established merely for the implementation of this subcontract. MBN will also compete for other and future projects relative to the supply of HP LAS, a number of which have already been identified by the parties.
10. MBN will have no manufacturing capacity, and will have to source the components of its products from subcontractors, including its parent companies. As a result, its own activities will only account for a relatively small proportion (between [10-30]%) of their total value. However, MBN will also be responsible for the specifications of the main equipment (which accounts for around [40-60]%), for the selection of the suppliers and for the definition of the overall costs and contract terms. Consequently, it will have decisive influence on and bear the responsibility of all aspects of the projects it will compete for. Furthermore, other companies (such as Hunting Engineering Ltd, BT Syntegra, Dytechna, etc.) specialise in system integration without being vertically integrated in equipment.
11. MBN might source components or services (such as R&D) from its parent companies, and, in some cases, MBN might work either in co-operation or under the prime contracting of Thomson and/or Racal. However, such relationships appear to be relatively limited, they will be carried out under competitive market conditions, and MBN will remain free to choose its suppliers.
12. In the light of the above, MBN will perform on a lasting basis all the functions of an autonomous economic entity. Therefore, the proposed operation constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

III. COMMUNITY DIMENSION

13. Thomson and Racal have a combined aggregate worldwide turnover in excess of EUR 5,000 million (Thomson, EUR 5,846 million; and Racal, EUR 1,361 million). Each of them has a Community-wide turnover in excess of EUR 250 million (Thomson, EUR 2,920 million; and Racal, EUR 891 million), but they do not achieve more than two-thirds of their aggregate Community-wide turnover within one and the same Member State. The notified operation therefore has a Community dimension, and does not constitute a cooperation case under the EEA Agreement, pursuant to Article 57 of that Agreement.

IV. THE RELEVANT MARKETS

A. Relevant product markets

14. The parties state that within the sector of military ground communication systems, a distinction should be made between fixed networks and mobile networks, because of differences in terms of product characteristics and use between these two types of products. They also indicate that mobile networks should be categorised in Wide Area Systems (WAS), which serve the subscribers of higher level military entities and are generally deployed over large areas (typically, more than 2,500 km²), and Local Area Systems (LAS), which cover small areas (typically, 25 km²) and serve limited military formations.
15. Finally, the parties consider that, within LAS, HP LAS forms a distinct product market, insofar as the design of such systems, the technologies they use, their performances and their prices differ significantly from those of standard LAS. They also insist that standard LAS cannot easily be upgraded into HP LAS.
16. HP LAS are a new generation of LAS, which use modern telecommunications technologies, such as Asynchronous Transfer Mode (ATM) or Time Division Multiplexing (TDM). It appears that, although the capabilities (and the prices) of HP LAS are significantly higher than those of standard LAS, both products fulfil the same basic functions. Moreover, even though HP LAS and standard LAS are not substitutable with each other once the customer has specified the level of performance required, they may directly compete with each other at an earlier stage, when the customer has to decide on the level of performance it needs and the prices it is prepared to pay for its LAS.
17. Finally, the results of the investigation carried out by the Commission suggest that there is no clear borderline between standard LAS and full HP LAS : capabilities between genuine HP LAS and standard LAS can be achieved through upgrades of existing LAS, or through the use of technologies different from ATM or TDM.
18. Consequently, it would appear that HP LAS and standard LAS are part of the same product market. This is further indicated by the fact that many of MBN's competitors are likely to be standard LAS contractors.
19. Similarly, LAS and WAS are now increasingly based on the same underlying technologies. There is therefore increasing supply-side substitutability between these two types of systems. Adversely, there is clearly no demand side substitutability between WAS and LAS, as these two types of systems remain very different in terms of number and nature of subscribers served, of size of the areas covered and of nature of the data transmitted.

20. However, it is not necessary to further delineate the relevant product market as, in all alternatives considered, the operation will not lead to the creation or strengthening of a dominant position.

B. Relevant geographic markets

21. The notifying parties state that the relevant geographic markets for HP LAS should in principle be regarded as national.
22. Military ground communication products are defence products. In past decisions¹, the Commission has indicated that, despite a trend towards a more international approach to procurement over the recent years, governments in countries where a strong supplier exists generally wish to support their national suppliers and thereby their country's military independence, and that therefore, markets remain national in these countries; it has also indicated that, in countries where no domestic suppliers exist, and subject to other barriers such as export restrictions and other barriers connected with national security, competition generally takes place world-wide.
23. In this context, the impact of the proposed operation has to be measured in particular in France and the UK as well as in the rest of the world, taking care to exclude those producers which are not significantly present outside their domestic markets.

V. ASSESSMENT

A. Dominance

Horizontal aspects

24. Insofar as Racal is not active in military ground mobile communication networks, the horizontal aspects of the proposed concentration do not appear to affect materially competition in that sector.

Vertical aspects

25. Thomson and some of its subsidiaries are active in military switching equipment, and Alcatel, one of Thomson-CSF's parent companies, is active in cables and connectors. All of these products are components of HP LAS systems.
26. However, Thomson's share of military switching equipment does not exceed 15%, and Alcatel's share of cables and connectors is below 10%. Furthermore, the operation does not materially change the competitive conditions on either the upstream or the downstream markets, as Racal is neither active in military ground communication systems or in components of these systems.

Conclusion

27. In view of the above, the proposed concentration does not create or strengthen a dominant position as a result of which effective competition would be significantly impeded in the EEA or any substantial part of that area. This is further indicated by the fact that none of the

¹ See, inter alia, case IV/M.1198 - British Aerospace Plc/SAAB AB

customers or of the competitors who responded to the investigation carried out by the Commission expressed any concerns about the operation.

B. Coordination of competitive behaviour

28. Pursuant to Article 2(4) of the Merger Regulation, a joint venture having as its object or effect the coordination of the competitive behaviour of undertakings that remain independent has to be appraised in accordance with the criteria of Article 85(1) and 85(3) of the EC Treaty. In order to establish a restriction of competition in the meaning of Article 85(1), it is necessary that the coordination of the parent companies' competitive behaviour is likely and appreciable and that it results from the creation of the joint venture be it as its object or its effect.
29. Thomson and Racal will keep competing businesses in military mobile radiocommunication systems, in military naval, aeronautical and space communication systems, in airborne radar and in electronic warfare. All of these sectors are therefore candidates for examination under Article 2(4) of the Merger Regulation.
30. The activities of MBN will remain limited to the field of HP LAS, where, except for the completion of existing contracts which cannot be transferred to MBN, Thomson and Racal have agreed not to compete with the joint venture. Therefore, there are no indications that the creation of MBN has as its *object* the coordination of the competitive behaviour of Thomson and Racal. It should therefore be examined whether the notified operation might have as its *effect* the coordination of the competitive behaviour of the parents.
31. In general terms, it should be borne in mind that, in defence markets, a limited number of contracts is awarded each year. Most of these contracts are very important in value and duration and, given the considerable lifetime (up to 20 years) of military products, they often provide the only opportunity for defence companies to compete for the supply of a given generation of the product concerned to the same customer. Moreover, these contracts are generally not transparent, either in terms of price, quantities, or both. And finally, defence products are usually sophisticated and differentiated products. Consequently, it is likely that the structure of defence markets, whether at a national or at worldwide level, provides no incentives for defence companies to coordinate their competitive behaviours.
32. In addition, although military mobile radiocommunication systems form part of military communication systems and are therefore related to HP LAS, Thomson and Racal are not active on the same national markets, their combined worldwide market share does not exceed 31%, and they remain submitted to the competition of a number of suppliers like ITT, Tadiran or Harris.
33. The other products mentioned above are different from HP LAS, whether in terms of technical characteristics or in terms of customers. Furthermore, the parties often have very dissimilar market positions and often propose substantially distinct types of products. Finally, in all these markets, the parties will remain submitted to the competition from other and large companies. It follows that there are no indications which would allow the conclusion that the setting up of MBN will lead to the coordination of the parents' competitive behaviour on any of the markets concerned.
34. Consequently, both the structural characteristics of the defence sector and the activities and market positions of the parties in the markets concerned indicate that the creation of MBN

will not lead to any coordination of the parents' competitive behaviour in these markets. In any case, in view of the presence of strong competitors and of the countervailing buying power of the MODs, there is no indication that such coordination would be appreciable.

VI. ANCILLARY RESTRAINTS

35. The parties have agreed not to compete with MBN during the duration of the Joint Venture agreement. This restriction aims at preserving the ongoing investment made by the parent companies in the joint venture. It can, therefore, be considered ancillary and is covered by the present decision

VII. CONCLUSION

36. For the above reasons, the Commission has decided not to oppose the notified operation and to declare it compatible with the common market and with the EEA Agreement. This decision is adopted in application of Article 6(1)(b) of Council Regulation (EEC) No 4064/89.

For the Commission,