

*Case No COMP/M.1709 -
PREUSSAG / BABCOCK
/ CELSIUS*

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

Article 6(1)(b) NON-OPPOSITION
Date: 19/01/2000

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COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 19-01-2000

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PUBLIC VERSION

MERGER PROCEDURE
ARTICLE 6(1)(b) DECISION

To the notifying parties

Dear Sirs,

Subject: Case No COMP/M.1709 – Preussag/Babcock/Celsius

Notification of 9 November 1999 pursuant to Article 4 of Council Regulation No 4064/89

1. On 9.11.1999, the Commission received the notification of a transaction whereby the Swedish state-owned defence company Celsius AB (“Celsius”) acquires joint control together with the German privately owned consortium Preussag Aktiengesellschaft (“Preussag”) over Howaldtswerke-Deutsche Werft AG (“HDW”), a subsidiary of Preussag active in the fields of conventionally powered submarines and large defence naval vessels. As part of the same operation, HDW acquires 100% of Kockums AB (“Kockums”), hereto Celsius’ subsidiary active in the fields of conventionally powered submarines and small defence naval vessels.
2. The notification was declared incomplete on 25 November 1999. On 9 December 1999, the parties completed their notification.
3. After examination of the notification, the Commission has concluded that the notified operation falls within the scope of the Merger Regulation and does not raise serious doubts as to its compatibility with the common market and with the functioning of the EEA Agreement.

I. THE PARTIES

4. The notification mentioned that the notifying parties are Preussag, Celsius and Babcock Borsig Aktiengesellschaft (formerly “Deutsche Babcock Aktiengesellschaft”) (“Babcock”).

5. **Preussag** is head of a group of undertakings active world-wide within the fields of energy, trading, plant engineering, building engineering, logistics, transport, tourism and, through its subsidiary HDW, shipbuilding.
6. **Babcock** is head of a group of undertakings with business activities within mechanical engineering and power plant engineering, power transmission engineering, building technologies, power and process engineering and industrial services.
7. In the *Preussag/Babcock Borsig* decision¹, the Commission concluded that, Preussag's acquisition of a minority shareholding of approximately 33 per cent in Babcock amounted to Preussag acquiring sole control over Babcock on a de facto basis. Consequently, the Commission considers that Babcock is not a separate "undertaking concerned".
8. **Celsius**, a Swedish company owned by the Swedish state, is active in three core areas; defence, with a focus on electronics, IT and smart weapon systems; aerotech services, which comprises advanced services, consultancy and maintenance, primarily for defence-sector customers; and aviation services which is focused on engine and component maintenance and asset management services for the commercial market. Celsius is also active in shipbuilding through its subsidiary Kockums and its interest in the Australian Submarine Corporation ("ASC").
9. **HDW**, a German company ultimately controlled by Preussag, is active within the field of construction of conventionally powered submarines and large naval surface vessels as well as merchant ships. HDW used to be a 100% direct subsidiary of Preussag. However, in an agreement, executed prior to the current operation, Babcock acquired 25% from Preussag and is obliged and intends to acquire a further 25 per cent plus one share in HDW from Preussag (the voting rights are already granted to Babcock).
10. **Kockums**, a wholly-owned subsidiary of Celsius, is active within the field of construction of conventionally powered submarines and small naval surface vessels. Kockums also develops and manufactures mobile military bridges.

II. THE OPERATION

11. The notified operation results in HDW acquiring all shares in Kockums from Celsius, and Celsius acquiring 25% plus one share in HDW from Preussag. After completion of the transaction, Babcock will hold 50% plus one share, Celsius will hold 25% plus one share and Preussag will hold 25% minus two shares in HDW.

The Australian operation that is not part of the notification

12. HDW intends to acquire the shares in two Australian companies, Kockums Pacific Pty Ltd. ("KP") and Kockums Pacific Technology Pty. Ltd. ("KPT"), which are indirectly owned by Celsius. KP has a 49 per cent holding in Australian Submarine Corporation ("ASC"), an Australian company active within the construction of conventionally powered submarines and other naval vessels[, which has the Australian Government as

¹ See Case IV/M.1594 – Preussag/Babcock Borsig

another major shareholder]. The parties consider that ASC is jointly controlled by KP and [the Australian Government].

13. The negotiations concerning the acquisition of KP and KPT by HDW still continue. However, it is most likely that HDW will acquire all shares in KP and in KPT within the next months. ASC is almost entirely active within Australia, with [negligible] turnover within the EEA.
14. The acquisition by HDW of the shares currently held by the Celsius subsidiaries in ASC is not a part of the notification.

III. CONCENTRATION

Joint control of HDW

15. The Supervisory Board ("Aufsichtsrat") of HDW will comprise sixteen members, eight of which represent the workers. Eight members will be elected by the shareholders: Babcock will nominate three members, Preussag one member and Celsius two members. The remaining two shareholders' members of the Supervisory Board shall be elected unanimously by Preussag, Babcock and Celsius. Babcock shall be entitled to nominate the Chairman of the Supervisory Board. The Chairman has a casting vote in case of a deadlock situation.
16. Celsius shall have the right to appoint always at least one member of the Executive Board. Babcock shall have the right to appoint the other three members including the chairman.
17. The shareholders' agreement between Preussag, Babcock and Celsius provides that unanimous agreement between each of the parties is required for, a.o., any change to the initially agreed business plan and contracts exceeding a contract value of [...] million DM.
18. The veto rights given to Celsius in the shareholders' agreement constitute the acquisition of joint control by Celsius over HDW as (a) the initial business plan sets out the strategy for [several] years and (b) contracts with values exceeding [...] million DEM accounted, during each of the last five years, for more than 85% of the combined aggregated contract value of HDW and Kockums.
19. It can, therefore, be concluded that Preussag and Celsius acquire joint control over HDW.

Joint control over Kockums

20. As HDW acquires all the shares of Kockums, previously a 100% subsidiary of Celsius, the outcome is that Preussag and Celsius, having joint control over HDW, acquire also joint control over Kockums.

Autonomous economic entity

21. HDW will furthermore perform on a lasting basis all the functions of an autonomous economic entity, and will especially have access to the necessary assets, personnel,

manufacturing facilities and commercial and service networks in order to conduct on a lasting basis its business activities.

One concentration

22. As the transaction whereby Celsius acquires an interest in HDW is the necessary condition for the accomplishment of the transaction whereby HDW acquires Kockums, these two transactions constitute one concentration whereby Preussag and Celsius acquire joint control over the businesses of HDW and Kockums.
23. The operation thus constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

IV. COMMUNITY DIMENSION

24. The combined aggregate world-wide turnover of the undertakings concerned exceeds EUR 5 000 million and the aggregate Community wide turnover of each party exceeds EUR 250 million. They do not achieve more than two-thirds of their turnover in one and the same Member State. The notified operation therefore has a Community dimension. It does not constitute a co-operation case under the EEA agreement.

V. MARKET DEFINITION

A. Relevant product markets

Submarines

25. The parties argue that submarines have to be distinguished from other naval vessels in view of both demand-side (operational particularities, stealth characteristics, deterrence efficiencies) and supply-side (distinct know-how, in particular design) characteristics. These views have been widely confirmed by the results of the Commission enquiry.
26. According to the parties, the only affected product market is that of conventional powered submarines with a surface displacement over 300 tons. The market is said to include new submarines, used submarines refurbished before delivery and the mid-life conversion of submarines. The inclusion of all these activities in one market has been contested by some of the market participants, but it is not necessary, for the purposes of this case, to decide this issue.

Nuclear submarines is a distinct market

27. Nuclear submarines have to be distinguished from conventionally powered submarines given technical differences, different purposes of use and price differences and that the export of nuclear submarines is prohibited just as purchasing countries would not consider buying them abroad for political reasons. These views have been confirmed by the market investigation. The parties do not produce nuclear submarines.

Mini submarines is a distinct market

28. The parties have also argued that conventionally powered submarines with a surface displacement below 300 tons constitute a separate product market as such small

submarines serve a different purpose (e.g. covert special mission operations in coastal areas). These views have been confirmed by the market investigation although some market participants consider that the relevant ‘triggering point’ should be 400 or 600 tons.

29. It is not necessary to define this market precisely as of the parties only Kockums has developed some activity. Kockums has conducted a [...] technical study on the feasibility of a small submarine resulting in a product concept named ‘Sea Dagger’, a small submarine (70 tons) of modular design to allow for different mission configurations. The concept has been generally distributed at various exhibitions over the last three years [...].

New, modernised and used submarines

30. The parties argue that the conventionally powered submarine market (with a surface displacement over 300 or so tons) includes (a) new submarines (and the related services such as production documents, instructions and training) built by the seller and the sale of complete material packages for production in the buyer’s country; (b) used submarines refurbished before delivery to another navy and (c) substantial reconstruction and modernisation (mid life conversion) of submarines which will remain in service in the same navy.
31. A refurbishment of used submarines before delivery to another navy than the original owner normally occurs after the intended operational life of the submarine and allows a safe operation of the submarine beyond the intended life. It involves replacement of worn out parts and in some cases of obsolete equipment which can no longer be supported by the logistic chain. A mid life conversion involves a much more substantial operation as it consists of a concerted act to improve the vessel’s original performance in the light of intensified or changed mission requirements, occurring when new technology has become available.
32. The sale of used submarines and the mid life conversion belong, according to the parties, to the same market as the one for new submarines because the submarines involved are, from the point of view of the purchasing entities, largely substitutable for new submarines as all submarines involved are designed for the same general purpose duties and they are all able to fulfil a variety of missions. The parties have given several examples of bids where both used and new submarines were offered as well as navies that negotiate to buy new submarines but in the end bought used submarines. Furthermore, there are several examples of navies that purchase used submarines after having previously purchased new submarines and navies starting off with used submarines that purchase later new ones.
33. On the other hand, there are substantial differences in price, performance (the overall operational capability of the submarine) and duration (operational life after sale) between each of the categories. A further distinction is that new submarines are offered by the manufacturer and second hand submarines are offered by the Governments by means of a Government-to-Government agreement whereby the shipyard in a way performs the service of refurbishing the submarine, but does not control the decision process.
34. The Commission considers that it is not necessary, for the purposes of this decision, to decide whether the supply of new and used submarines as well as mid-life conversion

can be combined into a single product market, or whether a further distinction should be made. For the reasons that will be indicated further below, the key element for the competitive assessment is whether producers are able to offer up-to-date designs in the future. This assessment will not be fundamentally different whether or not used submarines and/or mid life conversions are taken separately.

Patrol and Ocean going Conventional Submarines

35. Patrol submarines have a surface displacement of less than 2000 tons, whereas the ocean going submarines have a size up to 3000 tons. The “ocean going” submarines are much bigger and have deeper diving capacities, a longer mission duration, a wider cruising range, a higher submerged endurance and a lower indiscretion rate (time needed to charge the battery requiring the intake of air via a snorkel) than patrol submarines.
36. A respondent has argued that these performance differences and the fact that a development by a patrol sized submarine producer of an ocean going submarine is not without incurring high extra costs and risks should lead to the conclusion that there are distinct markets for these two types of submarines.
37. However, the parties and the other respondents have stated that the *missions* that can be fulfilled by coastal and ocean going submarines do not differ greatly. Both can be used for surveillance, anti-submarine warfare, anti-surface ship warfare and coastal actions and mine-laying. Hence, navies of ‘ocean countries’ have, in view of the price impact, opted very often for patrol submarines.
38. However, it is not necessary for the purpose of the present decision to decide this issue as the competitive assessment is not fundamentally different.

Other naval vessels : frigates, corvettes and mine counter measure vessels constitute distinct markets

39. The parties submit that there are three distinct product markets for naval vessels:
 - (a) Frigates: they are to be distinguished from other naval vessels due to their specific operational purpose such as long sea endurance, world-wide operation, heavy anti air warfare and/or anti submarine warfare combat systems. The parties indicate that the prices for frigates are substantially higher than those for corvettes and other small naval vessels.
 - (b) Corvettes and other small naval vessels like fast patrol boats and other surface combatants. The parties consider that this market can be distinguished from frigates by their size, limited sea endurance, general purpose or anti surface warfare combat system and in some cases different materials for hull and superstructure.
 - (c) Mine counter measure vessels (MCMV) : due to their operational capability (clear navigation routes from mines) they cannot be substituted by other naval vessels.
40. Finally, the parties submit that for each of the above ‘naval vessels’-markets, the relevant market consists of all such vessels, whether new, substantially modernised or simply refurbished.

41. The market investigation has confirmed the distinction between the three types of ships. With regard to the question whether used ships and/or substantially modernised ships are part of the same market, the same reasoning as described above for submarines can be applied.

B. Relevant geographic markets

Submarines

National markets where domestic producers exist

42. The parties argue, in line with the approach that the Commission has taken in a number of defence cases, that where domestic producers exist, there is a national market as governments wish to support national suppliers and thereby the country's military independence. However, a market can only be considered as really national (i.e. not open for competition from suppliers from other countries) if the national producer has the ability to design and produce himself products satisfying actual and future demand.
43. According to the parties, the following are national markets within the EU: France, Germany, Italy, the Netherlands, Spain, Sweden and the UK. Outside the EEA: USA, Japan, Australia, Russia and China.
44. It can be noted that there are no conventionally powered submarines in operation in France, the UK and in the USA. However, the French and UK producers sell conventionally powered submarines on the export market. The American and Japanese producers do not themselves develop activities outside their domestic market and are not expected to do so in the future.
45. Although the Australian navy considers the Australian producer, ASC, as a new submarine producer, it can be doubted whether Australia constitutes a national market. ASC, is, as mentioned above, a JV consisting of the Australian Government and Kockums. The only submarine produced, the Collins class, is a Kockums design to which Kockums owns the intellectual property rights. In addition, the parties consider that whilst ASC currently has [...]% of the design capability required to undertake changes to the Collins submarines, it has [...]% of the capability to develop a new design for the Australian navy or for export markets.[...]
46. The current Spanish submarines have all been produced by the local shipyard (Bazan) on the basis of a licence of French designs. However, Bazan has recently developed together with DCN, the French producer, a new submarine design (Scorpène) that has already been sold to Chile. Whilst Bazan will always be the building yard, it is not a foregone conclusion that the Spanish navy will acquire the Scorpène. Hence, other competitors may bid with their design.
47. All Italian submarines have been designed and built so far by the local producer, Fincantieri. However, the latest purchase of the Italian navy consists of two submarines of German design (HDW) to be built by Fincantieri. The design has been supplied to Fincantieri in the framework of an agreement between the Italian and German States (the design in question is not offered by HDW to export clients). Such an agreement is quite atypical and does not allow a firm conclusion that Italy can no longer be considered as a national market. On the other hand, it illustrates that even on national markets, the position of other competitors can have an impact.

Other markets

48. The parties argue that there are three other distinct markets: (a) markets inaccessible to western submarine manufacturers; (b) markets only accessible to western submarine manufacturers; and (c) open world market for submarine exports. The first market consists of countries such as North Korea, Iran and Libya. The second market consists of the EU Member States, NATO member states, Brazil, Argentina, Chile and Pakistan. The open world market is the remainder consisting of countries like South Korea, South Africa and India. The only affected markets would then be (b) and (c).
49. This market definition differs from the geographical market definition that the Commission has taken in a number of defence cases which is to identify national markets and a world market albeit that competitors from certain countries such as China and Russia may be excluded from supplying to some of the candidate buyers, especially NATO countries.
50. It results from the market investigation that the classification of the countries as proposed by the parties may not always be complete or correct. In addition, the classification may change.
51. The Commission considers that it is not necessary, for the purposes of this decision, to decide whether the relevant geographic markets consist of those proposed by the parties or the approach that the Commission has taken in a number of defence cases. The assessment of the concentration will not be fundamentally different whether one assesses the parties' proposed markets (b) and (c) or one world market but excluding the Chinese and Russian competitors as they are the only other actual competitors to the European companies.

Other naval vessels

52. Substantially the same reasoning as developed above for submarines can be applied for the other naval vessels.

VI. ASSESSMENT

National markets

53. Kockums is active on the Swedish market for submarines, corvettes and MCMV. In the period 1990-1999, the Swedish navy contracted for 3 new submarines in 1990 and 2 mid life conversions in 1999; 2 corvettes in 1995 and 2 in 1996; and 2 MCMV in 1994. HDW is active on the German market for submarines and frigates. On the German submarine market, HDW co-operates since 1990 in consortium with Thyssen Nordseewerke ("TNSW"). The German government contracted 4 submarines in 1994 and paid for 2 submarines in 1991 to be delivered to Israel. On the frigates market, HDW co-operates with Blohm + Voss and TNSW for the supply of 3 frigates (contract of 1996). HDW has started recently design work for corvettes.
54. The operation does not change the parties' existing positions on these markets.

The open world markets for corvettes and frigates

55. With regard to corvettes, Kockums has received one export order in the last decade, namely for refurbishing a used corvette for supply to Chile. HDW has recently started design work. The total number of units ordered in the last decade by countries accessible to Western producers totals 91.
56. With regard to frigates, the partnership between Blohm+Voss and HDW received orders for 4 Turkish frigates. The total number of units ordered in the last decade by countries accessible to Western producers totals 58.
57. On this basis, it can be concluded that the operation will not lead to the creation of a dominant position on either of these neighbouring markets.

The open world market for conventional submarines

Characteristics of the market

Demand

58. As for most other defence markets, there are very few contracts. There are, in the whole world, less than 300 conventional submarines in operation. In countries accessible to Western producers, 11 contracts are currently signed for the delivery of 35 submarines and it is expected that in the coming ten years between 50 and 100 new submarines will be ordered. The price for a new submarine varies, depending on the size, between around EUR 150 to 350 million. The life-time of a submarine varies typically between 20 to 30 years. The navies therefore expect that their new submarines consist of state-of-the-art technology and even used submarines are expected to remain operational for a decade or more.
59. The bidding procedure is normally based on the overall procurement rules in place in the buying country, and can take place over several phases (customer's request for proposal; concept design and definition phase; bidder's quotations, contract award). This can take several years. After a contract is awarded, it may take further a long time to finalise the detailed design (depending on the changes required by the customer of the basic design) and the actual production of several submarines will also be spread over many years. A whole contract cycle can thus be longer than 10 years.
60. The market investigation indicates that an important factor in the purchasing decisions of the navies and their respective governments other than the technical performances of the submarine and its intrinsic price relates to the capacity of the supplier to offer compensation schemes. Diplomatic relations involving the support of the domestic government and/or navy also can play an important role. With regard to the demand of countries that request a transfer of technology, typically involving a local shipyard in the construction process, there appears to be a high degree of loyalty to the incumbent supplier.

Design capacity

61. A traditional feature of the defence markets is that the local defence industry works in close co-operation with the local armed services for the development of new infrastructure via so-called programmes (national market). The customer requires

tailor-made products but funds design, development and production works and he may have certain rights over the supply of the resulting products to third parties.

62. Such an available design (or a design largely based on it) is then also offered by the supplier on the export market. The export customer may require further changes, but then he is expected to provide the funding for such changes.
63. It is less common but not unusual (eg. the Scorpène design of DCN and Bazan) for submarine producers to develop a design specifically for the export market. What is needed to enter the export market is a concept design. Whilst this does not imply the detailed design (this is only done when a contract has been awarded), a new concept design implies costs in the order of EUR 25-50 million.
64. Such a new design can easily remain up-to-date for 15 years. Existing designs can be continuously improved, up to certain limits, so that a design can be offered successfully during 25-30 years.
65. Many navies apply a form of risk reduction by requesting that only sea-proven designs are offered, i.e. a submarine that is already in operation (typically with the local navy of the producer). However, there are examples of navies that have stated that a proven design is preferred or even required, but, in the end, opted for a new design. Such a new design will only be acceptable if it is offered by reputable manufacturers.
66. The possibility for conventional submarine producers to develop new designs and to keep existing designs up-to-date depends on their possibility to acquire new contracts. However, the manufacturers of conventional submarines all produce other naval and/or commercial vessels. As such they do not solely depend on gaining orders for conventional submarines and they can benefit, to a certain extent, of the know-how developed on these other ships for their conventional submarines. There are, however, certain specific conventional submarine skills that need to be “kept alive” by a certain continuity of, especially, design and R&D work. It has been indicated that, as the submarine design and built cycle is 6 to 10 years, the best way to conserve the know-how is to have a new project following on the preceding one. However, depending on how much other substitutable work can be obtained, the preservation of knowledge can bridge an extra period in the order of 4 to 8 years.

Conclusion: competitors are those able to offer up-to-date designs in the future

67. On the basis of the above, the Commission concludes that competition in the submarine markets depends on the availability of credible bidders in future contract rounds, in the first place on the open export markets. This credibility depends on the availability of up-to-date designs that can be offered now and the likelihood that a company can continue to generate new designs when the current designs will be obsolete.

Market position of the parties on the market

Overview of past performance (orders, deliveries)

68. In view of the above characteristics, the Commission agrees with the parties that the relevant time period to assess past performance is not every single year, but consists of

a longer period. In the notification, the parties provided information on the contracts that have been concluded² in the period 1990-1999 (hereafter “orders”). In addition, the Commission requested the parties to provide information on actual submarine deliveries³ in the period 1990-1999 (hereafter “deliveries”).

69. In describing the past performance, it must be noted that HDW and TNSW have concluded a co-operation agreement setting up the “German Submarine Consortium” whereby the companies jointly bid for contracts outside the EEA. The design and production work for individual contracts that are won are shared between the two companies.
70. Of the 28 (new, modernised and used) submarines ordered in non-national markets accessible to Western producers, HDW and TNSW won the contract for 11 new submarines (Brazil, Israel, Turkey and South Korea). Kockums refurbished 4 old Swedish submarines for supply to Singapore. The UK producer, Marconi Marine (VSEL) Ltd, now part of the BAe Systems Operations organisation, refurbished 4 UK submarines (that have been in operation for around 5 years only) sold by the UK Government to Canada. DCN and Bazan contracted the supply of 2 Scorpène submarines to Chile and DCN received the order for 3 Agosta 90 submarines from Pakistan. The Russian producer is believed to have sold 4 submarines to India (although some publications indicate that India ordered only 2 submarines). This would give the parties a market shares of 53% (HDW+TNSW 39%; Kockums 14%). The nearest competitor is DCN involved in 18% of the submarines ordered. It should be mentioned that HDW/TNSW recently signed a contract with South Africa for the supply of 3 class 209 submarines. However, this contract is not yet effective.
71. According to the parties, there were 28 submarines delivered in non-national markets in the period: 5 by TNSW (alone) to Norway; 1 by HDW (alone) to Brazil; 13 by HDW and TNSW to Turkey and South Korea ; 2 by DCN to Pakistan; the 4 submarines refurbished by Marconi Marine for sale to Canada and 3 by the Russian producer to India. The only deliveries outside Sweden in which Kockums was involved during the last decade, are the 3 Collins class submarines delivered to the Australian navy (that the parties consider to be a national market). Taking into account these Australian submarines, the parties would achieve a market share of 55% (HDW+TNSW⁴ 45%; Kockums 10%).

Description of some likely future orders

72. Within the EEA, Portugal has short-listed HDW and DCN-Bazan (Scorpène) for the supply of 3 submarines (bidders were also Fincantieri, Kockums and RDM). The Greek

² This is defined as the date the contract became effective. This date can be between two and 12 months later than the contract signature date.

³ This is defined for submarines being manufactured by the submarine designer as the year in which the submarine has been delivered to the customer’s navy, i.e. “changing the flag”. This does not necessarily coincide with the commissioning date which is an internal affair of the navy concerned. Deliveries for material packages for local manufacture have been defined as the year in which the last main item of the material package has been delivered.

⁴ Not including the 5 submarines supplied by TNSW to Norway, an activity in which HDW was not involved.

navy is generally expected to order 3 submarines from HDW (bidders were also DCN, Kockums and RDM). Spain is expected to order 4 new submarines where the Scorpène (DCN-Bazan) seems to have reasonably strong chances. Kockums has developed a concept study (Viking design) for the Swedish, Danish and Norwegian navies that are expected to order 10 new submarines.

73. Outside the EEA, reasonable opportunities arise, according to the parties, in [...]. Kockums is generally expected to have a strong advantage with respect to [...] in view of the previous supply of used [...] submarines, and HDW is expected to have the strongest position in [one country] in view of [previous contracts]. Other bidders for the other countries and for some other potential opportunities are, based on the market investigation, likely to involve DCN at almost all cases, whereas RDM is expected to participate at most of them and Fincantieri at several and Marconi Marine only at some.

Description of competitors' current position

74. **HDW**, in co-operation with TNSW, has a very successful sea-proven design (class 209), that will remain up-to-date for [...], and a new design for the export market (class 214). Its order book involves ongoing work for the production of the new German submarines (class 212) and the supply of submarines to several navies.
75. **Kockums** has a sea-proven design for the export market based on the Swedish submarine designs. Whilst it has obtained no export contracts for these designs, it won the important Australian contract with its new design (Collins). Its Viking design is expected to be marketable [...]. Ongoing work involves the refurbishing of the used Swedish submarines for Singapore and the mid life conversion of Swedish submarines. Kockums concluded in 1997 an agreement with DCN for the development of a new generation submarine [...]. The agreement will be terminated [...].
76. **DCN** (France) has two designs (Agosta 90 and Scorpène) and it has won an export order for both of them (Pakistan and Chile). Work on these orders is ongoing. It can be noted that the Scorpène design is the only “new design” that has won an export order so far (meaning the only design that will enter into detailed design). The Scorpène is the result of a co-operation agreement with **Bazan** (Spain).
77. **RDM** (Netherlands) has not obtained a new production contract in the last 10 years, but supplied 4 (ocean going) submarines to the Dutch navy in the period 1990-1994. RDM started project definitions, that were partially funded by the Dutch Navy, for patrol size submarines. This has resulted in the period 1991-1993 and 1994-1997 in project definitions for its Moray classes 1800 and 1400. The results are two new designs.
78. **Fincantieri** (Italy) has two sea-proven designs on offer for the export market that are upgrades of the Longobardo and Sauro class submarines in operation with the Italian navy. The last Longobardo has been supplied in 1995. It can also offer a modified version of the 212A (German design based submarine currently under construction) submarine for the export market. Its ongoing work involves a combat system modernisation of the two Longobardo submarines, a mid life conversion of two Sauro submarines and the supply of the two 212A submarines, all for the Italian navy.
79. **Marconi Marine** (UK) is the builder of the UK's nuclear submarines. The UK has phased out its four ocean going conventional submarines (Upholder Class) that have been sold (as refurbished used submarines) to Canada in 1997. Marconi Marine used to

have a marketing agreement with RDM for RDM's Moray class, but this has now expired. The company offers the Upholder design with options for an AIP system.

Consequences of the proposed operation

80. It is clear from the above that HDW is the major player on the market and that the merger with Kockums will reinforce this position further. However, the Commission considers that the parties will remain for the foreseeable future subject to competition from the above competitors and that especially DCN, but also RDM and Fincantieri, will have the capacity to effectively compete with the parties' products.
81. This conclusion is based on the fact that DCN and RDM both have a new design available that can be considered to remain up-to-date for some 15 years to come. The Commission recognises that DCN cannot rely on national programmes of the French navy for the development of conventional submarines, and therefore has to invest into specific export designs, so that it could be argued that DCN will only maintain such investments if the export market *per se* is sufficiently profitable and could otherwise withdraw from the market. However, this argument does not appear to play any substantial role in the foreseeable future, as both of DCN's designs have been sold, and especially its new Scorpène design, so that the design costs will be amortised to a large extent, and as there appear to be reasonably good opportunities for DCN in foreseeable future (e.g. Spain or Pakistan). In addition, as the only producer so far having concluded a contract for the existing new designs, this will give DCN the advantage of having the first sea-proven new submarine design.
82. The existing new design of RDM will enable it to remain a credible competitor in future bidding rounds. Also Fincantieri can still offer a recent sea-proven design (Longobardo) and may offer a new design based on a modified version of the 212A. It can be noted that to a large extent the costs involved in maintaining its know-how and R&D investments is covered by the ongoing Italian programmes.
83. In the light of the above, it therefore appears that the competitors to the parties can offer credible alternatives to the parties' products.
84. Furthermore, it appears highly unlikely that, after the operation, the parties will be in a position to substantially undermine these producers' competitiveness.
85. This is because, firstly, designs remain up-to date for very long periods (up to 15 years) and are amortised over a very limited number of contracts (typically no more than 2 or 3 contracts).
86. Secondly, it appears that larger sales volumes do not confer substantial competitive advantages in the submarines market, as i) the amortisation of sunk costs over a limited number of contracts also means that economies of scale are not all that important in the supply of submarines; ii) it appears from the Commission enquiry that past sales records are not a decisive factor in the selection of a submarine supplier (provided that the other competitors have a recognised capability and reputation); and iii) it also appears that, even in the absence of sales for several years, submarine producers can maintain their competitiveness, because they usually receive funding from their national customer in order to carry out sufficient R&D activities through other submarine and naval work.

87. And thirdly, as indicated above, the selection of suppliers on the export market is not based on performance and price only, but also appears to be largely dependent on a number of other considerations, relative a.o. to diplomatic relationships with the governments of the potential suppliers, the funding scheme offered, the possibility for offsets or technology transfers, etc. This implies that even suppliers offering products that have not been purchased by their national or other foreign navies (not sea-proven) have reasonable chances to be awarded certain export contracts.
88. In the light of the above, it appears that the parties could not successfully engage in selective actions aimed at other competitors or, more generally, derive market power from their current market shares. Consequently, the notified operation does not create or strengthen a dominant position in conventional submarines, as a result of which effective competition would be significantly impeded in the EEA or any substantial part of that area.

VII. CONCLUSION

89. 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,