EN

Case No COMP/M.4956 - STX/ AKER YARDS

Only the English text is authentic.

**REGULATION (EC) No 139/2004
MERGER PROCEDURE**

Article 8 (1)
Date: 05/05/2008

COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 05/05/2008

C(2008) 1693 final

PUBLIC VERSION

Commission Decision
of 05/05/2008
declaring a concentration to be compatible with the common market
and the EEA Agreement

(Case No COMP/M.4956 - STX/ Aker Yards)

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(Text with EEA relevance)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,
Having regard to the Treaty establishing the European Community,
Having regard to the Agreement on the European Economic Area, and in particular Article 57 thereof,
Having regard to Council Regulation (EC) No 139/2004 of 20 January2004 on the control of concentrations between undertakings[1], and in particular Article 8(1) thereof,
Having regard to the Commission's Decision of 20 December 2007 to initiate proceedings in this case,
Having regard to the opinion of the Advisory Committee on Concentrations[2],
Having regard to the final report of the Hearing Officer in this case[3],
WHEREAS:

(1) On 16 November 2007, the Commission received a notification pursuant to Article 4 of Regulation (EC) No 139/2004 ("the Merger Regulation") of a proposed concentration by which STX Corporation Co., Ltd ("STX", South Korea) acquires within the meaning of Article 3(1)(b) of the Merger Regulation control of the whole of Aker Yards A.S.A ("Aker Yards", Norway) (Aker Yards and STX are together referred to as "the parties").

(2) By Decision dated 20 December 2007, the Commission found that the notified operation fell within the scope of the Merger Regulation. and decided to initiate proceedings in this case pursuant to Article 6(1)(c) of the Merger Regulation.

I. THE PARTIES

(3) STX is a South Korean holding company listed on the South Korean Stock Exchange. The STX group is active in three main areas: shipbuilding and marine equipment (including engines), shipping and logistics and energy and construction. As part of its shipbuilding activity, STX designs and builds various types of commercial vessels such as containerships, product tankers, chemical and oil tankers, bulk carriers and liquid national gas ("LNG") carriers. STX currently operates in commercial shipbuilding through two shipyards located in South Korea and it has another shipyard under construction in China.

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1 OJ L 24, 29.1.2004, p. 1.
2 OJ C ...,...200. , p....
3 OJ C ...,...200. , p....

(4) Aker Yards is a Norwegian limited company. Aker Yards is a shipbuilding group focusing on sophisticated vessels. Its product range includes cruise ships and ferries, commercial vessels, offshore production and specialised vessels. Cruise ships and ferries accounted for approximately 44% of Aker Yards' total sales in 2006. Aker Yards comprises eighteen shipyards in Norway, Finland, Germany, Romania, France, Ukraine, Vietnam and Brazil.

II. THE CONCENTRATION

(5) The notified transaction consists of the acquisition by STX of a minority shareholding of 39.2% in Aker Yards on the Oslo Stock Exchange. STX acquired the shares on 23 October 2007.

(6) Given the shareholding structure of Aker Yards and the exercise of voting rights in Aker Yards at its last three shareholders' meetings, the minority shareholding of 39.2% is highly likely to allow STX to exercise the majority of the represented voting rights in Aker Yards, and, thereby, to acquire effective *de facto* control of Aker Yards[4].

(7) It is noted that attendance at the shareholders' meetings of Aker Yards between 2005 and 2007 never exceeded 60.44%. If STX had exercised the voting rights attached to all of its newly-acquired shares in Aker Yards at the shareholders' meetings in 2005 and 2006, it would have accounted for 66% of the total shares represented in 2005 and 65% of the total shares represented in 2006.

(8) At the date of notification, the remaining 60.8% of shares and votes in Aker Yards (that is those not acquired by STX) were widely dispersed among a large number of small shareholders, with none of the remaining shareholders holding a stake in excess of 5%. Past experience indicates that it is unlikely that a sufficient number of small shareholders will participate at future shareholders' meetings to form a majority[5]. There are no indications that this trend will change.

(9) The notified transaction therefore constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

III. COMMUNITY DIMENSION

(10) The undertakings concerned have a combined aggregate worldwide turnover of more than EUR 5 000 million[6] (EUR 3 214 million for Aker Yards in 2006; EUR 3 965 million for STX in 2006). The aggregate Community-wide turnover of each of the undertakings concerned exceeds EUR 250 million (EUR 857 million for STX in 2006; EUR 715 million for Aker Yards in 2006) and they do not achieve more than two-thirds

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4 See paragraph 59 of Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings, (http://ec.europa.eu/comm/competition/mergers/legislation/en.pdf): "A minority shareholder may also be deemed to have sole control on a *de facto* basis. This is in particular the case where the shareholder is highly likely to achieve a majority at the shareholders' meetings, given the level of its shareholding and the evidence resulting from the presence of shareholders in the shareholders' meetings in previous years." See also, for example, Commission Decision of 26 June 2001 in Case COMP/M.2404 Elkem/Sapa; Commission Decision of 11 July 2003 in Case COMP/M.3091 Konica/Minolta; or Commission Decision of 12 March 2004 in Case COMP/M.3330 – RTL/M6.

5 Less than 10% of small shareholders participated at the shareholders' meeting in 2005 and 2006 and less than 17% in 2007.

6 Turnover calculated in accordance with Article 5(1) of the Merger Regulation and the Commission Consolidated Jurisdictional Notice.

of their aggregate Community-wide turnover within one and the same Member State. The notified operation therefore has a Community dimension *within the meaning of Article 1(2) of the Merger Regulation.*

IV. COMPETITIVE ASSESSMENT

A. RELEVANT PRODUCT MARKETS

COMMERCIAL SHIPBUILDING

Introduction

(11) The activities of the parties overlap in the area of shipbuilding of commercial vessels, in the following categories of ships: container ships and LNG carriers (these are both non-affected markets), chemical and oil tankers and product tankers. In addition, Aker Yards is a major player in cruise ships and ferries.

(12) In previous Commission decisions, some differences between the various categories of commercial vessels were pointed out, but at the end, the question was left open whether the construction of all categories of commercial vessels belong to one relevant product market. For example, in Case No COMP/M.2772 - HDW/Ferrostaal/Hellenic Shipyard[7], it was stated that the market for commercial shipbuilding could be divided into several separate product markets according to the main groups of ships such as bulk carriers, container ships, product carriers, chemical and oil carriers, LNG carriers, liquefied petroleum gas ("LPG") tankers, roll-on roll-off vessels, ferries, cruise ships, offshore/specialised vessels (see recital 37). In addition, in Case No COMP/M.4104 – Aker Yards/Chantiers de l'Atlantique, it was accepted that, both on the basis of demand and supply side considerations, the market for cruise ships and the market for ferries were product markets distinct from other commercial vessels (see recitals 10 and 11).

(13) In this case, STX submitted that there is a general dividing line between the various types of commercial vessels, as was suggested in earlier Commission decisions. This general distinction was also confirmed by most of the market participants questioned during the market investigation.[8]

(14) The vessels transporting cargo are distinguished according to the nature of the cargo transported, which determines the specific features of the categories of ships such as bulk carriers, container ships, product tankers, chemical /oil tankers, LNG carriers, LPG carriers, roll-on roll-off vessels. The demand-side substitutability of these various types of cargo ships is very limited (with some exceptions such as chemical/oil tankers and product tankers, as e explained in Recital 17). Specific categories of products require special facilities and a special design of the ships, and they cannot be transported other than by dedicated vessels. For example, liquid natural gas (LNG) is only transported on

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7 Commission Decision of 25 April 2002.

8 See Questionnaire to customers of 28 November 2007, question 6, and questionnaire to competitors of 27 November 2008, question 7. Most of the respondents agreed that there is a clear diving line between the various categories of ships (some referring to a nuance relating to product tankers and chemical/oil tankers, which are discussed in Recital 17 of this Decision). However, one competitor of the parties, Fincantieri, argued in the market investigation that commercial shipbuilding constitutes one big single market, without any distinctions as to the types of vessels, mainly relying on the supply-side substitutability of various types of ships.

LNG tankers, which require strict safety measures and specific building criteria. Similarly, roll-on roll-off vessels are specifically designed for transporting vehicles. There is another category of ships distinguished in the industry, which are not purely for the transportation of cargo, such as offshore and specialised ships, which are used for special functions such as serving offshore-platforms. In addition,, cruise ships and ferries carry passengers on board; the distinction between those two types is based mainly on the purpose of the transportation (namely holidays and leisure for cruise ships versus transporting people between specific ports for ferries).

(15) From the supply side, shipbuilders generally do build various types of vessels and switching between the production of these categories is not uncommon. Once a shipbuilder possesses the technology and necessary know-how to build a specific type of ship, and there are no physical limitations regarding its yards for the building of ships of certain sizes, it can quite easily adjust its production according to market needs. However, in the case of very sophisticated ships, in particular cruise ships (on which the market investigation was mainly focused), there are considerable entry barriers linked to technology and the development of the know-how necessary for the technical design and project management, a necessary shipyard infrastructure and skilled working force and a network of geographically close subcontractors.[9] As a result of those barriers, it is not easy to switch to the production of cruises ships from other categories of ships.

(16) Taken into account the matters referred to above, it is appropriate to distinguish various types of ships such as cruise ships from the overall market for commercial shipbuilding.

Product tankers and chemical/oil tankers

(17) In addition to the general delineation of markets according to the various types of ships, the notifying party, STX, also submitted that in practice chemical/oil tankers and product tankers can be used for the transportation of several types of substances and, therefore, these categories of ships could be considered as a single product market. The market investigation seems to confirm some demand side substitutability amongst these two categories of tankers.[10] Several customers have indicated that oil tankers can be used (albeit at a certain transaction cost) to transport chemicals and that product tankers can be used (after some adjustments and at a certain transaction cost) for the transportation of oil and chemicals, but the market investigation was not conclusive in this respect. However, the question whether chemical/oil tankers and product tankers should be considered as forming one single product market may be left open in this case, since the notified transaction does not give rise to any competition concerns under either alternative market definition.

Cruise ships and ferries constitute relevant markets separate from the overall commercial shipbuilding market

(18) In Case COMP/M.4101 Aker Yards/Chantiers de l'Atlantique, a distinction was made between the market for the construction of cruise ships and the market for the construction of ferries from the overall commercial shipbuilding market, taking into account both demand and supply side considerations (see recitals 10 and 11). The

9 See Questionnaire of 14 January 2008 to cruise ship competitors, question 41, and questionnaire of 11 January 2008 to cruiser ship customers, question 20.

10 See Questionnaire to customers of 28 November 2007, questions 8 and 9 and questionnaire to product tankers customers of 11 January 2008, question 8.

notifying party also proposes to delineate separate markets for those two categories of ships. However, the market investigation showed that there are no reasons to depart from previous Commission practice.

(19) Cruise ships are primarily intended for holiday makers, passengers on vacation who spend several days or even weeks on board for leisure. The design and the composition of cruise ship must therefore meet very high standards in terms of accommodation, common facilities (which can include theatres, swimming pools, or casinos), but also in terms of technical features such as reduced vibration or noise. The direct customers of shipyards building cruise ships are mainly large international companies operating globally and specialised in cruise holidays. The four largest customers account for about 80% of the entire demand for cruise ships. The characteristics of the demand are thus very *easily distinguishable* from other types of vessels.

(20) Similarly, ferries are also very specific from the demand-side perspective. Ferries are intended for transporting passengers (often in combination with cars or other goods) between fixed locations. The main purpose of a ferry is thus not leisure activity but transport. The customers, ferry operators, are also distinct from the customers of other types of ships. They are private or public companies operating certain marine routes in a certain geographic location.

(21) The market investigation indicated that there are in general important differences between ferries and cruise ships. The main difference, on the demand side, is precisely the different purpose of the ship, namely leisure versus transport, which consequently means that there is very limited substitutability of demand between cruise ships and ferries. These different needs are translated into differences in the setup and design of the ships. Alongside technical characteristics such as reduced vibration and noise levels, the absence of car-desks and other design features, cruise ships usually have much more sophisticated outfitting standards of public spaces and cabins and level of services offered on board. Although a niche of so-called 'cruise ferries' (more sophisticated ferries with higher standards) exists, where certain overlaps with smaller cruise ships can be observed, in general the characteristics of the two categories of ships are largely different. In addition, the demand for cruise ships is, in contrast to ferries, characterised by long-term established relationships between the ship owner and the main shipbuilders, who often have a *de facto* 'preferred shipbuilder' relationship.

(22) From the supply side, there are three main suppliers of cruise ships, and two of these companies also build ferries. Nevertheless, all other shipbuilders which are active in the market for the construction of ferries (up to 20 companies) are virtually absent in the cruise segment. The market investigation has shown that there are effectively significant barriers to entry into the cruise ship market in terms of technology and the know-how needed for the significant level of complexity involved in cruise ship building projects and also in the ability to coordinate a network of a large number of cruise ship subcontractors.[11] It is thus evident that supply-side substitutability would only work one-way (from ship cruise to ferries, but not the other way), unless the significant barriers could be overcome by the shipbuilders. However, despite the strong indications for separate markets for cruise ships and ferries, for the purposes of the assessment of the notified transaction, it is not necessary to decide whether cruise ships and ferries belong

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[11] See Questionnaire of 14 January 2008 to cruise ship competitors, question 41, and questionnaire of 11 January 2008 to cruiser ship customers, question 20.

the same relevant product market or constitute two separate markets since the transaction does not give rise to any competition concerns even under the narrower product market definition.

No need to distinguish between the different sizes of cruise ships

(23) Within the area of cruise ships, the market investigation provided indications that small (usually very luxurious) cruise ships of capacity below 20 000 -30 000 gt (gross tons) form a different market from medium and large size cruise ships of above 30 000 gt. There are several smaller customers ordering smaller cruise ships and they differ from the large cruise ship operators. Also on the supply side, there are a number of smaller shipyards capable of producing small cruise ships but which are not active at all in the segment of larger cruise ships which demand a considerably higher degree of sophistication.

(24) Based on the data collected during the market investigation, it appears that (i) not one single order for a cruise vessel between 20 000 gt and 30 000 gt was placed after 1998 (and no delivery took place after 2001), (ii) of the 12 cruise vessels of less than 20 000 gt delivered from 2000 onwards (two of which were ordered well before 2000) only one was built by a shipbuilder also building larger ships (namely Fincantieri). These facts demonstrate a clear break in a possible chain of substitution going from smaller to larger cruise vessels. It clearly appears that orders are concentrated either on medium and large sized vessels (above 30 000 gt) or on small cruise vessels (below 20 000 gt), with a gap in between and that, while large shipbuilders cover 95% to 98% of the orders in the upper segment (and large cruise operators place around 80% of the orders), they are (as well as large cruise operators) virtually absent from the lower segment, which therefore remains available for other, smaller shipbuilders.

(25) However, it is not necessary to decide the exact scope of the product market definition, as the assessment would not change. It is noted that the volumes and values related to the small cruise ship segment are negligible with respect to the segment of larger cruise vessels (respectively, 86 000 gt against 7 880 000 gt in volume and EUR 600 million against EUR 35 000 million in value). For these reasons, the possible consideration of a segment specific to smaller cruise vessels does not significantly change the market assessment. For the purpose of the competitive assessment of the notified transaction, the cruise ship market of above 30 000 gt, where Aker Yards is active is analysed in Recitals 38 to 174. As there are no competition concerns even on this narrower market, the exact scope of the product market definition can be left open in this case.

Conclusion on the markets for commercial shipbuilding

(26) For the purposes of the assessment of the notified transaction, the competitive assessment focuses on the market for the construction of cruise ships (of above 30 000 gt). In addition, the effects of the merger are assessed on the markets for ferries (either considered separately or within a hypothetical market comprising both ferries and cruise ships) and chemical/oil tankers and product tankers (either considered separately or as one single market). As regards the other categories of ships, there is no need to decide on the exact definition of the relevant markets as these markets are not affected by the notified transaction.

SHIP ENGINE MANUFACTURING

(27) STX is active in the area of ship engine manufacturing, through its subsidiaries, STX Engine Co., Ltd. and STX Heavy Industries Co., Ltd. STX produced diesel engines suitable for various types of vessels, on the basis of a licence agreement with MAN Diesel SE, under which […]*. Aker Yards is not active in the manufacturing of ship engines.

(28) According to the notifying party, the market for ship propulsion main engines forms one single product market. The notifying party submits that in general engines are technically interchangeable for all types of commercial vessels and producers typically manufacture the whole range of marine engines. The only exceptions mentioned by the notifying party are specific dual fuel engines suitable for LNG carriers. STX does not produce this type of engines.

(29) In Case No COMP/M.4596 – Wärtsilä Technology/Hyundai Heavy Industries/JV, the Commission recognised that dual fuel engines and those engines which are substitutable for LNG carriers might constitute a relevant product market, but left the definition open.

(30) The market investigation indicated that ship propulsion engines could be divided into two main categories according to the fuel used for the propulsion: diesel engines and dual fuel engines.

(31) Some market participants stated that the most relevant division might be a distinction between two-stroke engines and four-stroke engines, which differ by size and performance. Four-stroke engines are typically used for cruise ships and ferries propulsion, electric power plants for commercial vessels and propulsion of smaller commercial vessels while two-stroke engines are mainly used for large commercial vessels propulsion. However, the market investigation also provided indications that despite differences between two-stroke and four-stroke diesel engines, the two different types of diesel engines can be generally interchangeable from the demand side point of view. As one ship-builder explained, it is technologically possible to replace several less powerful four-stroke engines by a single two-stroke engine. In addition, the market investigation indicated that the main manufacturers are generally able to produce the whole range of diesel engines.

(32) In the present case, the exact scope of the product market definition may, however, be left open, due to absence of any competition concerns.

B. RELEVANT GEOGRAPHIC MARKET

(33) The notifying party has submitted that the relevant geographic market for commercial shipbuilding and for ship engine manufacturing is global in scope.

(34) In Case No COMP/M.2772 - HDW/Ferrostaal/Hellenic Shipyard[12], the Commission accepted the parties position that *"the market for construction (…) of all kinds of commercial vessels [is] world wide in scope, as the transportation costs for ships are comparatively low and there are no significant trade barriers"*.

12 See footnote 8.

* Parts of this text have been edited to ensure that confidential information is not disclosed; those parts are enclosed in square brackets and marked with an asterisk.

(35) The market investigation supports the view that the relevant geographic market for commercial shipbuilding is generally global in scope with suppliers taking orders from customers worldwide.[13] This conclusion is the same for all ship types considered in the present Decision.[14] Similarly, the results of the market investigation support a worldwide scope for the market of ship engines.[15]

(36) Therefore, for the purposes of the present Decision, the relevant geographic markets for the construction of commercial ships and for the manufacturing of ship engines are defined as world-wide markets.

C. ASSESSMENT - HORIZONTAL ASPECTS

(37) The parties' activities overlap in the area of shipbuilding of commercial vessels, for several types of vessels. In the potential markets for container ships, chemical /oil tankers, and LNG carriers, their combined market shares would not exceed 15%. These markets are thus not affected. In addition, the undertakings contacted by the Commission during the market investigation did not raise any concerns with respect to those markets. Therefore, the assessment is focused on the potential effects on competition in the markets for the construction of cruise ships and for the construction of ferries, where there is no horizontal overlap but where competition concerns were raised by some market participants, and in the only market affected by the transaction (and then only if considered separately from chemical/oil tankers), which would be the market for product tankers.

C.1. CONSTRUCTION OF CRUISE SHIPS

C.1.1. INTRODUCTION

(38) The cruise shipbuilding industry is highly concentrated and dominated by three large and experienced players: Fincantieri, Aker Yards and Meyer Werft. STX has no presence on this market.

(39) Smaller players are not in a position to compete for contracts for the largest ships and in most cases they do not manage to obtain contracts for medium-size vessels either. The capacity of these suppliers tends to be used for small ships for which the three largest manufacturers do not compete, or for refurbishing/renovating existing ships. On the demand side, smaller cruise operators tend to work with refurbished vessels *at the outset*, and only later buy new ships.

(40) For the period from 2003-2007 (market shares computed over a shorter period would not be a good proxy of market power, given the limited number of orders and deliveries) and as regards the orders for cruise vessels of 30 000 gt or more, the market shares obtained on the basis of the market investigation are summarised in Table 1.

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13 See Questionnaire to customers of 28 November 2007, question 14, questionnaire to competitors of 27 November 2007, question 14.

14 Although in the case of ferries, certain shipbuilders seem to distinguish between regional clusters, such as the Mediterranean or the Baltic region.

15 See Questionnaire to customers of 28 November 2007, question 16, questionnaire to competitors of 27 November 2007, question 16.

Table 1 - Worldwide market for Cruise ships based on orders for the period from 2003-2007[16]

	Based on ordered vessels	Based on gross tonnage (gt)	Based on value of orders (EUR)
Fincantieri	[40-45]*%	[40-45]* %	[40-45]* %
Aker Yards	[20-25]* %	[30-35]* %	[30-35]* %
Meyer Werft	[25-30]* %	[25-30]* %	[25-30]* %
Mariotti	[5-10]* %	[0-5]* %	[0-5]* %
Mitsubishi	-	-	-
Others	-	-	-
Total	100.00%	100.00%	100.00%

Source: Commission (market investigation)

(41) For a longer time scale, namely for the period from 2000-2007, it appears that Aker Yards used to have a stronger market position but lost market share in favour of both its main competitors (Fincantieri and Meyer Werft). The data are summarised in Table 2.

Table 2 - Worldwide market for Cruise ships based on orders for the period from 2000-2007

	Based on ordered vessels	Based on gross tonnage (gt)	Based on value of orders (EUR)
Fincantieri	[35-40]* %	[35-40]* %	[35-40]* %
Aker Yards	[30-35]* %	[35-40]* %	[35-40]* %
Meyer Werft	[20-25]* %	[20-25]* %	[20-25]* %
Mariotti	[5-10]* %	[0-5]* %	[0-5]* %
Mitsubishi	[0-5]* %	[0-5]* %	[0-5]* %
Others	-	-	-
Total	100.00%	100.00%	100.00%

Source: Commission (market investigation)

(42) A particular case seems to be the one of the Italian company Mariotti, which received orders in 2000 for a prototype and two sister ships of [30 000 – 35 000]* gt from Carnival, making Mariotti the fourth largest player on the market with a [0-5]* % market share in terms of tonnage volume and value. Before obtaining those orders, Mariotti had supplied smaller cruise vessels (before 2000) and one cruise vessel of around [35 000 – 45 000]* gt in 2003. As discussed in Recital 47, the notifying party submitted that Mitsubishi is also a competitor on the market for the construction of cruise ships, and effectively delivered very large ships ([110 000 – 120 000]* gt) in 2004, also ordered by Carnival (in 1999-2000). However, Mitsubishi is currently not active on the market and market participants do not perceive it as an existing competitor.

(43) Cruise ships are a differentiated product representing in most cases a difficult engineering and logistical cooperation between the shipbuilder, the customer and the network of subcontractors supplying the different components of the ship.

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16 Market share figures for the cruise ship market used in this Decision are a reconstruction of the market based on the responses to the Questionnaire to cruise ship competitors of 14 January 2008, question 9 and Annex 1. Data concerning Aker Yards include the companies it acquired in this period, that is Kvaerner and Chantiers de l'Atlantique.

(44) Due to its complexity (and to the fact that cruise vessels are highly customised products), the construction of a cruise vessel entails specific costs. There are various ways to reduce such costs, including relying on a consolidated relationship with a shipbuilder (namely, based on previous orders) and ordering "sister ships" of an existing "prototype". In particular, the latter phenomenon allows the spreading of the financial cost of the design over several ships, thereby reducing the average cost per ship. In addition, sister ships can be built in a shorter time scale (as the time for the design and for finding all technical solutions is necessarily reduced). The risk is also reduced due to the shorter time scale as well as of the possibility of learning from the use of the prototype ship to 'fine tune' the design of the sister ship(s). Moreover, sister ships can be ordered at the same time as the prototype, thereby allowing a possible rebate on the overall price.

(45) Nevertheless, the number of sister ships of the same prototype is limited as their design and/or specific technical solutions may become obsolete and/or less economic (or efficient) with respect to new designs which may emerge in the meantime, or they may simply no longer correspond to the demands of cruiser operators. At some point, the (financial and non-financial) savings which may provide an incentive for the ordering of a sister ship, rather than a new prototype, may outweigh the cost of pursuing obsolete solutions. At that point, cruise operators may therefore choose to order a new prototype rather than a sister ship of an existing prototype.

(46) As referred to in Recitals 38 to 41, the market is principally served by three large manufacturers of cruise vessels: Aker Yards, Fincantieri (the market leader) and Meyer Werft. However, demand is also very concentrated in the hands of four large cruise operators controlling around 80% of the market: Royal Caribbean Cruises Ltd. ("Royal Caribbean"), Carnival Corporation & plc ("Carnival"), Norwegian Cruise Line ("Star/NCL") and MSC Crociere SA ("MSC").

(47) Taking into account the absence of horizontal overlaps, the position of Aker Yards on the cruise ships market would not be reinforced as a direct result of the notified transaction. Two strong competitors to Aker Yards would remain: the Italian (state-owned) Fincantieri, the market leader, and the German company Meyer Werft. These two companies made deliveries in the period from 2004-2007 and competed (and obtained) new orders for the next few years. However, during the first phase market investigation concerns were raised concerning the elimination of STX as a potential entrant and the alleged state aid granted to the merged entity which could lead to a significant impediment of effective competition. The in-depth investigation has shown that such concerns are not justified, as discussed in the following sections.

C.1.2. ELIMINATION OF STX AS A POTENTIAL ENTRANT

Introduction

(48) During the first phase market investigation, the Commission received indications that STX might be about to enter the cruise ship market and that the notified transaction would therefore eliminate a potential new entrant to the market of cruise ships. Even though STX claimed to the Commission that it has no actual or potential plans to enter

the cruise ship market[17], the Commission found elements suggesting the contrary. In particular, it was revealed that since autumn 2007 STX has been involved in bidding for a new cruise ship building project for the company Saga Lines. Accordingly, a number of market participants regard STX as a potential new entrant on the market and concerns were raised about the loss of a potential competitive force, which would disappear from the market.[18] In addition, there were indications from the press which quoted STX officials as mentioning the company's ambitions to enter the cruise ship market.[19]

(49) The in-depth investigation sought to clarify whether the removal of STX as a potential competitor would have significant anti-competitive effects on the market. According to the Commission's Horizontal Guidelines[20] "For a merger with a potential competitor to have significant anti-competitive effects, two basic conditions must be fulfilled. First, the potential competitor must already exert a significant constraining influence or there is a significant likelihood that it would grow into an effective competitive force. Second, there must not be a sufficient number of other potential competitors, which could maintain sufficient competitive pressure after the merger.

STX does not currently exert a significant constraining influence and there is no significant likelihood that it will grow into an effective competitive force in the short term

(50) STX participated in the preliminary stages of a bidding process with one customer (Saga Line) for a cruise ship in late 2007. The market investigation confirmed that apart from that instance STX has not participated in any other bid, preliminary contacts or conversations for the construction of a cruise ship.[21] None of the cruise ship customers that responded to the market investigation, with the exception of Saga Lines, indicated having any contacts with STX regarding cruise ship building projects. STX has never built a cruise ship before and has never previously sought any cruise ship business. In addition, customers generally do not perceive STX as an actual competitor but rather as a potential entrant alongside other Asian players.[22] Customers seem to have only been made aware of STX's cruise ship involvement in the context of the Saga Lines tender. One large customer reported that "*until the acquisition of its stake in Aker Yards was announced, STX was not considered by* [the customer]* *as a potential cruise ship builder. If known at all, STX was regarded as a reputable builder of tankers and other, relatively unsophisticated, cargo ships of medium size, as well as engines under licence from European manufacturers. It is understood however that STX has recently approached one or more smaller European ferry and cruise operators…*"[23]

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17 Reply of STX of 29 November 2007 to question 11 of Commission's Questionnaire of 26 of November 2007.

18 See in particular the Minutes of the telephone conference with [name of customer]* of 12 December 2007.

19 Lloyd's List, Special Report-South Korea, article entitled: "STX chairman works within family to create bold vision". Published 6 October 2006.

20 Paragraph 60 of Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, (OJ C 31, 5.2.2004, p. 5).

21 Even though one competitor submitted that STX may have participated in more projects in the past, this claim was not confirmed by the relevant customers.

22 Questionnaire to cruise ship customers of 11 January 2008, questions 12, 15, 16 and 17.

23 Reply of [name of customer]* of 21 January to the questionnaire to cruise ship customers of 11 January 2008, question 12.

(51) With respect to the first and only tender in the area of cruise ships in which STX participated, it related to the construction of a relatively small cruise ship (42 000 gt) for a smaller customer, Saga Lines. By comparison, the average sizes of cruise ships built by the three main competitors are much larger (Fincantieri [100 000 – 110 000]* gt, Aker Yards [115 000 – 125 000]* gt and Meyer [100 000 – 110 000]* gt). In addition, according to STX, its participation in that tender was limited to the submission of very initial documents and the aim of participating in the bid was presented rather as an opportunity to start learning about the market in view of a possible entry in the longer term. STX admitted to the Commission that it has long-term plans to enter the cruise ship market. However, it seems to be only at the beginning of the process of developing the necessary know-how.

(52) STX explained that in the early stages of the tender for Saga Lines it submitted only a few very initial basic drawings of the ships. Whereas for the construction a cruise ship it would be necessary to develop several thousands drawings and technical documents. Although STX could, if selected in the bid, to certain extent rely on support from engineering consulting offices for the design, it appears that it clearly lacks the experience and the know-how necessary to build complicated cruise vessels, such as, in particular, the large ones built by the three incumbents on this market. In particular, unlike some of its Asian competitors, STX has only started to prepare its research and development activities in the area of cruise ships[24]. This acquisition of know-how can take a considerable length of time, given the complexity and specificities of the cruise ship design compared to that of cargo ships. The market participants mentioned they were not aware of any significant R+D efforts by STX which would bring it closer to mastering the know-how necessary for cruise ship construction.

(53) Experienced customers may cooperate with shipbuilders not yet present on the market, thereby helping them to gain know-how on cruise ship design in view of a possible future cooperation. The main customers confirmed, however, that no such technical cooperation is being undertaken with STX. It should be stressed that this is also a continuous process and this learning exercise, together with R+D efforts invested in-house can take a long time before they can be capitalised. STX is only at the very initial stages of this process.

(54) Previous experience in building other passenger ships such as ferries may also help to some extent in developing the know-how for cruise ships. While experience gained in building ferries is not seen by the market participants as a pre-condition for entering into the cruise ship market, it may be advantageous, although there seems to still be big gap between the two categories of ships. STX has never built ferries, unlike a number of its Asian competitors. In the past, STX has constructed one small training ship for the Korean Marine Academy with a tonnage of 5 900 gt. STX, however, explained that this vessel was intended to educate and train students of the Marine Academy and that, even though it can accommodate 246 passengers, it is not classified as a passenger ship but rather as a special-purpose vessel, having far less sophisticated standards in terms of outfitting, safety and technology and with a complexity far below that of cruise ships.

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24 STX explained that it has not undertaken any research, development and innovation activities on its own in the area of the construction of cruise ships and it only started in late 2007 to participate in a development project initiated by the South Korean government relating to elementary know-how on cruise ships. STX is participating in a working group focusing on R&D related to interior design, which has a budget of about [less than USD 5 million]* over a five-year period from 2007-2012, out of which STX will contribute about one quarter. For details of this South Korean R&D programme, see Recitals 95, 96 and 97.

(55) To conclude, during the market investigation no plans or specific evidence was found indicating a likely and timely entry by STX in the market in a significant way. The market participants associate STX with the cruise ship market mainly due to the recent isolated instance of bidding for Saga Lines. Although STX admits its intention to enter the market in the long-term, it has clearly not invested enough efforts into preparing a significant entry into the market for cruise ships. It should therefore be concluded that STX does not currently exert a significant constraining influence on builders of cruise ships and that there is no significant likelihood that it will grow into an effective competitive force in the short term.

There are a sufficient number of other potential competitors which are at least equally well placed as STX to enter the cruise ship market

(56) The market investigation confirmed that other shipbuilders from the Far East such as Mitsubishi from Japan and South Korean companies such as Samsung and Daewoo are at least as well placed as STX to become potential entrants into the cruise ship market. When asked about potential entrants, both customers and competitors referred to these three companies alongside STX.[25]

(57) Mitsubishi is probably the best known far-East shipbuilder in connection with cruise ships, as it was already active in the market in the past. It delivered smaller cruise ships in the beginning of 1990s and in 2004 it delivered two large cruise ships, Diamond Princess and Sapphire Princess, each with a tonnage of [110 000 – 120 000]* gt (more than 2 500 passengers) to P&O Princess (now part of the Carnival Corporation, the largest cruise operator worldwide). Therefore, Mitsubishi has a substantial know-how advantage over the other Asian shipbuilders as it already has the necessary know-how to build cruise ships. Although it is currently not active in the market, it is perceived by customers as a credible potential (re-)entrant[26].

(58) To date, the South Korean shipbuilders have never been awarded a cruise ship building project. It is understood by market participants that the South Korean shipbuilders are looking at the cruise ship market with some strategic interest for the future, as their Chinese competitors, which are expanding their shipyards, are slowly expected to move into the types of cargo ships which have been predominantly built in South Korean yards. Hence, the South Korean players may seek to explore markets with a higher degree of sophistication such as cruise ships.

(59) The market participants regard STX, Samsung and Daewoo as the potential entrants from amongst the South Korean shipyards. As one competitor noted, "*STX on a standalone basis is a potential new entrant. Daewoo (DSME) and Samsung might have a small advantage as they built ferries for the European market before*"[27]. Both of these South Korean companies have experience in building ferries, which may be a certain advantage in terms of know-how for a new entrant into the cruise ship market.

(60) Daewoo is reported to have "*acquired advanced technology for building sophisticated passenger car ferries, based on its past experience of building three 40-knot class ultra*

25 Questionnaire to cruise ship customers of 11 January 2008, questions 15 and 16. Questionnaire to cruise ship competitors of 14 January 2008, questions 37, 38 and 39.

26 Questionnaire to cruise ship customers of 11 January 2008, questions 12 to 16.

27 Reply of Meyer Werft of 21 January 2008 to the Questionnaire to cruise ship competitors of 14 January 2008, question 39.

speed ferries the 'Treasure Island' with 472 passengers capacity, the 'Blue Star' car ferry for a Greek owner with the capacity of 1 500 passengers and 200 cars and a very luxurious car ferry accommodating 1 800 passengers ordered by Moby Line in Italy. All these passenger ferries have received attention for their light and solid structured designs, elegance, and outstanding interior design features"[28]. While the ferry experience does not seem to be a pre-condition for entering the complex and sophisticated cruise ship market, it can certainly help to some extent.

(61) Although it may be still a long way from achieving its final objective, Samsung (SHI) has also been building ferries. In addition, on its website it gives information concerning its efforts to build up cruise ship know-how, stating in its section on "Products" and in its subsection "Cruise and Ferries" that "*SHI is steadily laying down the groundwork for design and construction of cruise ships*". It also presents some basic design outlines of cruise ships, including a 85 000 gt cruise ship for 2 500 passengers.[29]

(62) To conclude, other Far-East shipbuilders are more advanced than STX in their steps towards entering into the cruise ship market. In any event, there is nothing to suggest that STX would be more advanced than these companies in preparing a significant entry into the market.

The likelihood of a timely entry by Asian competitors into the cruise ship market

(63) As regards the possible entry of Asian competitors (be they STX or other companies) into the cruise ship market, it remains unclear when they would eventually overcome the know-how barriers (with the exception of Mitsubishi who already has experience in this area). More importantly, even if the specific know-how and project-management for constructing complex cruise ships was developed by the shipyards (internally or with the help of consultants or customers), the question remains when a significant entry of one or more of the yards could actually materialise. In addition, know-how is only one barrier to entry, and there are other elements that suggest that significant competition from Asia in the area of cruise ships in the short-term is quite unlikely.

(64) First, about 80% of the value of a cruise ship is produced by subcontractors (from marine equipment such as engines, fire security or air conditioning systems, to the outfitting of cabins, restaurants, theatres, swimming pools and casinos). At present, the majority of subcontractors are located in Europe. Accordingly, importing the material into Asia may have significant financial consequences on the price and profitability of the projects (additional transport costs, exchange rate risks). Usually, subcontractors, with their staff, complete a large proportion of the works in the shipyard, which would mean additional communication and increased travel costs. As one shipbuilder notes, "*the geographical proximity of the subcontractors is very important for the profitability of the project. In the long term, the subcontractors will follow the shipbuilder. A network cannot move overnight however, needs to build up over time*".[30] Certain subcontractors are already establishing in Asia, but it will clearly take time for a local network of cruise ships subcontractors to emerge in the Far-East. In addition, major cruise ship clients would have to be persuaded to accept Asian subcontractors with no 'track records', notably for critical marine equipment parts.

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28 www.cruiseshipportal.com

29 http://www.shi.samsung.kr/eng/

30 Reply of [name of shipbuilder]* of 28 January 2008 to Questionnaire of 14 January 2008, question 23.5.

(65) Second, the attractiveness of the cruise ship market, as compared to the cargo ship market, might be reduced by the fact that the number of cruise ships ordered per year is much lower and the delivery times longer than is the case for cargo ships. Consequently, the risks associated with an entry into the cruise ship business are also higher. The economies of scale in the cruise ship market (related to sister-ships) are much more limited in comparison to the production of cargo vessels which are produced in large series in a more automated production.

(66) Another factor is the current market situation in the area of cargo ships, where the Japanese and South Korean shipbuilders are specialised and engaged in mass production. The market investigation indicated that, due to the current boom in the cargo ship market, the South Korean and Japanese shipbuilders currently do not have any incentive to enter new market segments, in particular when they are faced with the entry barriers described above.. The Commission estimates that this situation might change in light of the growing capacity in China and the possibility of a downturn in the shipbuilding market. It is, however, impossible to forecast when this situation might change and thus predict the timeliness of the entry of Asian competitors in the cruise ship market. On the basis of the current market situation, it appears that this entry is not likely in the short-term.

(67) Undertaking investments and efforts to overcome the barriers (research and development, the development of a local subcontractor network) and production inefficiencies along the learning curve and to profitably build cruise ships in the long term, instead of cargo ships, is not an obvious choice for Asian competitors at the present time.

Conclusion on potential entry

(68) The above findings show that STX does not currently exert any significant competitive constraint in the cruise ship market and that there are no reasons to believe that, without the merger, STX would become an effective competitive force in the near future. In addition, a number of other possible entrants are more advanced and at least as well placed as STX to enter the market.

(69) To conclude, the merger would not have significant anti-competitive effects as a result of the elimination of STX as a potential competitor of the three current large builders of cruise ships.

C.1.3. COMPETITION CONCERNS ON THE BASIS OF SUBSIDIES

(i) Introduction

(70) During the market investigation[31], Fincantieri complained that together with a number of other alleged advantages, such as low labour, energy and steel costs[32], the merged entity would benefit from state subsidies from South Korea. It would, therefore, be able to use such unfair subsidies to undercut prices, with the result of marginalising the

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31 Reply of 28 January 2008 to the Questionnaire to cruise ship competitors of 14 January 2008.

32 These alleged competitive advantages are realised within the overall competitive strategy of each company and can clearly be distinguished from subsidies, which, as it is claimed, would not be based on competition on the merits but have a disruptive character.

existing competitors and driving them out of the cruise ship business, monopolising it and creating thus a dominant position on the market for cruise ships.[33]

(71) According to the complainant, the current situation where Aker Yards' position in the cruise ships market is not a dominant position may change due to the immediate acquisition of know-how by STX combined with the alleged ability of STX to access unfair subsidies, which would create an immediate opportunity for a significant impediment of competition. In particular, the complainant stated that "*Because of the support it is likely to continue to receive from the Korean state, Aker/STX will be able to withstand any period of losses (or low profitability) without the need to restructure or rationalise capacity. This will in turn put strong pressure on other shipbuilders, such as Fincantieri, competing instead on market terms, and in the end likely force them to respond by retrenching their own capacity. As a result, it is realistic to anticipate the structure of capacity for instance in the cruise and ferry segments would likely become much more asymmetric (as in the LNG case cited below) than would have occurred without subsidies, and without the acquisition of Aker Yards. The likely result will be very significant market power for STX, de facto marginalization of European players, and higher prices despite the cost advantages.*"[34] According to the complainant, this situation may made be even worse by the alleged advantages of South Korean shipbuilders in terms of lower production costs (mainly lower labour, energy and steel costs), the fact that STX would be vertically integrated into ship engine manufacturing and the wider product portfolio that the combined entity would enjoy.

(72) According to the complainant, the subsidies to the combined entity would mainly be granted in the form of pre-shipment loans and advanced payment refund guarantees for the merged entity's prospective ship-building projects. Both STX and the South Korean public bank KEXIM, which is allegedly involved in the granting of these production loans and guarantees, have claimed that these instruments have been extended on market terms[35]. In addition, the complainant submitted that STX has in the past benefited from advantageous investment loans and state programmes in support of research and development. In essence, it argued that South Korea has already granted subsidies to shipbuilders in the past and that such a practice would, therefore, be likely to continue in the future. The complainant states[36] that the Commission has an obligation to make an independent assessment even of potential subsidies in the framework of merger control in order to fully appreciate the effects of such subsidies on the merged entity's financial strength and refers in this respect to case law, in particular the judgement of the Court of First Instance of the European Communities in Case T-156/98 RJB Mining plc v Commission of the European Communities[37].

(73) The concern that the merged entity would make use of such subsidies/state aids liable to distort competition has only been raised by two out of the five respondents, among the

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33 Fincantieri argues that the cruise ship market is not to be regarded as a separate market from other commercial vessels which all form one single wider market. This implies that the merged entity is claimed to monopolise a market even larger than for cruise ships only. Given that the market investigation supports the view of a separate market for cruise ships, Fincantieri claims are analysed on that narrower market.

34 Reply of 28 January 2008 to the Questionnaire to cruise ship competitors of 14 January 2008, question 45.

35 Reply of 5 February 2008 to the Questionnaire for STX of 30 January 2008. Letter of 5 February 2008 addressed by KEXIM to SXT, Annex 2 to the Reply of 5 February 2008 to the Questionnaire for STX of 30 January 2008.

36 Submission of Fincantieri of 15 February 2008, *Relevance of Subsidies/State aid in EC Merger Control*.

37 Case T-156/98 RJB Mining plc v Commission of the European Communities [2001] ECR II-337.

competitors: Fincantieri and another smaller player[38], and only Fincantieri's complaint has, at least partially, been substantiated during the procedure. No such concerns have been raised by other companies which could become potential entrants. Finally, from the customers' point of view, only two out of the seven respondents (including the four largest customers) have indicated that the notified transaction may lead to some anti-competitive concerns[39]. However, the concerns raised by those two respondents related to the elimination of potential competition (as referred to in Recitals 48 to 69), and the weakening of the European market and loss of know-how, which were not further substantiated. It is worth noting that three out of the four largest customers (representing a large share of the cruise ship demand) did not raise any concerns and one of them even indicated that the transaction would increase the number of suppliers[40], suggesting therefore that it would be pro-competitive.

(74) Fincantieri’s claims should be rejected. First, the principles laid down by the Court of First Instance in Case T-156/98, the RJB Mining judgment, mainly concern the need to avoid inconsistencies in different Community policies and are therefore of limited relevance to the present case. Second, the results of the market investigation show that STX does not have a financial position that is such as to render the merged entity dominant on the market for the construction of cruise ships, regardless of whether or not the financial instruments mentioned by the complainant constituted past or current subsidies by South Korea. Third, there is no evidence to conclude that South Korea is likely to grant subsidies to the merged entity in the future. Fourth, even if the alleged future subsidies were granted, such subsidies would not lead to a dominant position by the merged entity in the market for cruise ship.

(ii) State aid in the framework of merger control

(75) In the framework of a merger analysis, the Commission must assess all relevant criteria which may lead to a significant impediment of competition. Among numerous elements, the financial strength of the merged entity may also come into play[41].

State aid and financial strength

(76) State aid could potentially increase a company’s financial strength if financial means are allocated to the company, for example by a reduced price for a state-owned target, by a simple transfer of money or in the form of loans or guarantees provided at conditions which do not correspond to market terms. By way of illustration, a loan granted by a state does not constitute state aid if it is granted on market terms. If the interest rate required is, however, lower as compared to the conditions available on the market, such an advantage (the difference between the advantageous rate and the market rate) is a form of state aid.

(77) In 2001, the Court of First Instance found in Case T-156/98, concerning *RJB Mining*[42], that the Commission had not analysed the effect of supposed state aid (that is a financial

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[38] Reply of Fincantieri of 28 January 2008 to the Questionnaire to cruise ship competitors of 14 January 2008. Reply of [competitor]* of 23 January 2008 to Questionnaire to cruise ship competitors of 14 January 2008.

[39] Reply of 18 January 2008 to Questionnaire to cruise ship customers of 11 January 2008, question 43. Reply of 30 January 2008 to Questionnaire to cruise ship customers of 11 January 2008.

[40] Reply of 21 January 2008 to Questionnaire to cruise ship customers of 11 January 2008.

[41] See the Commission's horizontal merger guidelines, paragraph 36.

[42] Case T-156/98 RJB Mining plc v Commission of the European Communities [2001] ECR II-337.

transfer which had not been identified as state aid at that stage) on the merged entity's financial strength. Accordingly, it annulled the Commission's decision in Case IV/ECSC.1252 *RAG/Saarbergwerke/Preussag Anthrazit*[43], which had been assessed under the Treaty establishing the European Coal and Steel Community (ECSC).

(78) However, the *RJB Mining* judgement relates to very specific circumstances, which are not present in this case. First, it is worth noting that contrary to the state aid addressed in the *RJB Mining* judgement, the alleged government subsidies in question in the present case are not directly 'linked' to the merger. While in the *RAG/Saarbergwerke/Preussag* case, the state aid in question was not only connected to but even triggered by the merger. However, the alleged government subsidies in the present case do not show any significant link to the notified transaction.

(79) More importantly, that judgment by the Court of First Instance does not provide grounds for concluding that the Commission would be obliged to make a "pre-assessment" of alleged subsidies within a merger control procedure by conducting a *quasi* state aid investigation (comparable to the procedure under Article 88 of the Treaty) in order to identify whether subsidies were granted by a third country (namely "a non-Member State"). The judgment by the Court of the First Instance in Case T-156/98, concerning RJB Mining, reflects the Commission's parallel competence for state aid and merger control in the Community, and the consistent application of both procedures. However, potential subsidies granted by a third country, such as South Korea, do not fall under the Community state aid rules but may be subject to the applicable rules of international law. The main rules applicable to subsidies within the World Trade Organisation ("WTO") are defined in Articles VI and XVI of the General Agreement on Tariffs and Trade 1994 (“GATT 1994”) and in the WTO Agreement on Subsidies and Countervailing Measures (“the SCM Agreement”) that apply to all WTO Members, including the Community and South Korea[44]. The outcome of disputes before the WTO is decided by a WTO-panel in a procedure to which the Commission is only an actor, but not the ruling body.

(80) The *RJB Mining* judgment, therefore, does not provide grounds for concluding that the Commission is required to synchronise its merger investigation with other proceedings outside the sphere of Community law, and in particular the potential outcome of a possible dispute settlement before the WTO, involving an alleged breach of the SCM Agreement. It also does not support the conclusion that the Commission should conduct its own independent investigation in order to decide on the existence of subsidies within a merger control proceeding in cases which do not involve the parallel application by the Commission of two competition procedures based on Community law.[45] In addition, no WTO procedure is currently taking place against South Korea concerning

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43 Commission Decision of 29 July 1998 in Case IV/ECSC.1252 RAG/Saarbergwerke/Preussag Anthrazit http://ec.europa.eu/comm/competition/mergers/cases/decisions/ecsc1252_en.pdf

44 Concerning subsidies granted by a third country, the Commission could either investigate the alleged subsidisation and possibly impose countervailing duties if subsidies causing injury to the domestic industry are confirmed (according to Part V of the SCM Agreement and Council Regulation (EC) No 2026/97 of 6 October 1997 on protection against subsidized imports from countries not members of the European Community (OJ L 288, 21.10.1997, p.1). Regulation as last amended by Regulation (EC) No 461/2004 (OJ L 77, 13.3.2004, p. 12)), or bring a complaint to the WTO (according to Parts II & III of the SCM Agreement).

45 See also Case T-114/02 BaByliss vs. Commission [2003]* ECR II-1279, paragraph 441.

past individual subsidies for shipbuilding companies or concerning subsidisation programmes or schemes which could extend to the future.

Adequacy of WTO-procedures

(81) The complainant, however, argues that the Commission should not leave the assessment of foreign subsidies to the *ex post* control exerted by the WTO but instead it should use merger control and its *ex ante* assessment to efficiently address foreign subsidies. The complainant alleges that the WTO procedure is inadequate since its decisions are not binding, and the regulation of subsidization is not based on an "effects on competition test" and the WTO does not have own investigative powers[46]. The arguments raised by the complainant seem to suggest that the Commission should effectively assess subsidies granted by a third country within merger control where the WTO procedure, according to the complainant, does not appear to be sufficient.

(82) However, apart from the fact that a WTO ruling is binding under international law, it should be noted that the conclusion on serious prejudice or injury to the domestic industry, which are tests used in the SCM Agreement, would not be sufficient to 'block' a merger. It would, instead, be necessary to find a significant impediment of effective competition, which is the test applicable under Article 2 of the Merger Regulation. The test applied pursuant to the Merger Regulation is therefore stricter than the one used by the WTO.

(83) In addition, the Commission has investigative powers pursuant to the "Trade Barrier Regulation"[47] in accordance with which it will investigate allegations of subsidisation in breach of the SCM Agreement, which allows the presenting and substantiating of a complaint in the WTO. In addition, Annex V to the SCM Agreement provides for a procedure to gather the information to be examined by a Panel to establish whether a WTO Member has granted or maintained a subsidy which caused injury to the domestic industry, nullification or impairment of benefits of other members or serious prejudice to another member.

(84) Finally and most importantly, any alleged difference or alleged inadequacy in the WTO procedure would not be a sufficient reason to conclude, as the complainant seems to suggest, that the Commission could extend the limits of merger control proceedings in order to "correct" allegedly inadequate WTO procedures.

Conclusion on state aid and merger control

(85) In principle, the Commission is obliged to take into account in its merger analysis any subsidies as factors potentially increasing a merged entity's financial strength, in so far as evidence supports the existence or the likelihood of such subsidies. However, if there is no clear evidence of the existence of such subsidies provided by third countries, the *RJB Mining* judgement, contrary to what is claimed by the complainant, does not provide grounds for imposing a general obligation on the Commission in a merger

[46] Submission of Fincantieri of 15 February 2008 *Relevance of Subsidies/State aid in EC Merger Control*.

[47] Council Regulation (EC) No 3286/94 of 22 December 1994 laying down Community procedures in the field of the common commercial policy in order to ensure the exercise of the Community's rights under international trade rules, in particular those established under the auspices of the World Trade Organization,(OJ L 349, 31.12.1994, p. 71). Regulation as last amended by Regulation (EC) No 125/2008 (OJ L 40, 14.2.2008, p. 1).

control procedure to carry out an independent analysis – comparable to a state aid procedure under Article 88 of the Treaty - in order to establish whether financial measures extended by third countries are granted on non-market terms and therefore constitute subsidies. Any alleged inadequacies of the international procedures, such as the WTO procedures, are not relevant in this respect.

(86) As the description of the alleged subsidies set out in the following sections demonstrate, the financial transactions indicated by the complainant cannot generally be characterised as evident subsidies. It was, therefore, not established within the merger control investigation that subsidies in the form of the financial transactions, as described by the complainant, exist or are likely to be granted in the future. Even though this finding suggests that there is not sufficient evidence for any increase in financial strength on the basis of such financial transactions, the Commission has undertaken additional steps to evaluate the likelihood, and the potential effects of such alleged subsidies, on the basis of the available data. As shown below, even if the indicated financial transactions contained elements of subsidies their effect would, with a high likelihood, not significantly alter the financial strength of the merged entity.

(iii) Financial strength on the basis of past or current subsidies

STX' overall financial strength

(87) Generally, it is unlikely that a company which is not in a leading market position could become dominant on the basis of financial strength only. STX/Aker Yards will have a market share of [30-35]*% in the cruise ship market after the merger, with Fincantieri being the market leader (with a market share around [40-45]* %). The market investigation has not shown any indications that STX could currently enjoy a financial strength superior to that of most of its present or potential competitors.

(88) It should be noted that whilst under Article 2(1)(b) of the Merger Regulation, economic and financial power are important criteria for the appraisal of whether a concentration is compatible with the common market, in the absence of other indicators financial strength as such will not be sufficient to lead to the creation or strengthening of a dominant position as a result of which competition will be significantly impeded." [48]

(89) In any case, the argument that the financial strength of the merged entity would be significantly increased thereby allowing it to marginalise its competitors is not confirmed by the facts.

(90) The following Table 3 summarises the main financial indicators of both STX Group and Fincantieri[49].

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[48] See Recital 32 of Commission Decision of 21 October 2002 in Case M.2908 - Deutsche Post / DHL

[49] Reply of Fincantieri of 6 March 2008 to Questionnaire for Fincantieri of 22 February 2008; and Replies of STX of 26 February 2008 to Questionnaire for STX of 22 February 2008 and of 11 March 2008 to the Commissions' request for information of 10 March 2008.

Table 3 - Financial indicators in EUR million - 2006

	STX Group	Fincantieri	Aker Yards
Turnover	3 965	2 467	3 215
Gross profit	207	158	178
EBITDA	293	[…]*	179
EBITDA margin	7.4%	[…]*%	5.5%
EBIT	172	125	155
EBIT margin	4.3%	5%	4.8%
Net profit	25	52	129
Liquidity ratio	44%	[…]*%	34%
Net debt	804	(143)	988
Equity	922	779	764
Total assets	3 306	5 663	3 545

(91) As Table 3 shows, although STX is larger than Fincantieri in terms of turnover, the other financial indicators do not appear to reflect a greater financial power, even when allegedly STX would have benefited from unfair subsidies in the past. In particular, while Fincantieri has a positive net financial position (it has no net debt), STX has a net debt amounting to 2.7 times its earnings before interest, taxes, depreciation and amortisation (EBITDA).

(92) Taking account of the fact that finance is an important factor in the cruise ship business (since around 80% of the value of a cruise ship is financed by the shipbuilder), not having access to finance may constitute a barrier to entry into the market. However, in light of the data set out in Table 3, it is difficult to conclude that STX would be in a better financial position than Fincantieri to have access to the necessary production financing. On the contrary, it appears that Fincantieri is in a better position than STX both in terms of profits and debt. STX's weaker financial position is even explicitly recognised by Fincantieri in its assessment of the STX's credit rating (see Recital 98).

(93) In addition, this situation is unlikely to change post merger. Currently STX is active in the construction of the type of ships, for which the role of production financing other than advance payments from ship owners is less important than it is for cruise ships, where 80% of the value is financed by the shipbuilder, from its own resources or through external borrowing. Therefore, should STX start producing cruise ships in South Korea, it would lead to an additional increase in pressure on its level of debt. In addition, as indicated in Table 3, Aker Yards is also highly indebted and the more recent results for the fourth quarter of 2007 are also below the expected results with a negative EBITDA of EUR 146 million, which would have an additional negative effect on the overall financial situation of the merged entity considered as a whole[50].

(94) As shown below, it also cannot be assumed that the specific financial transactions, which have been described by Fincantieri and according to the complainant were granted to STX by South Korea, could significantly increase STX' financial strength even if they contained elements of subsidies.

50 STX derogation request of 5 March 2008.

Programme in support of technological knowledge

(95) The complainant identified the state programme by South Korea in support of technological knowledge as a possible source of reinforcing of the financial strength of the merged entity. According to the complainant, this publicly announced programme represents a support of KRW 222.8 billion (EUR 160 million) for the period between 2007 and 2014[51].

(96) The notifying party confirmed that such a programme existed but specified that it covered 21 projects in various industries. Only one of these projects concerns the shipbuilding industry, and has a budget of KRW 22 billion (EUR 16 million) for the period between 2007-2014, co-financed by South Korea (EUR 8 million) and the private sector participants to the project (EUR 8 million)[52]. According to the notifying party, approximately 20 shipbuilders and subcontractors are participating in this project, including all major South Korean shipyards. More specifically, the notifying party is involved only in one of the five sub-projects. The five-year budget allocated for this sub-project is [less than EUR 4 million]*, of which 50% is financed by South Korea and 50% by the participating companies (not only STX) in cash or in kind. STX itself contributes [less than EUR 2 million]*, supplemented by the South Korea's contribution of KRW 200 million (EUR 0.2 million)[53]. The notifying party confirmed that this project is the only research and development activity relating to the cruise ship market in which it has been involved[54].

(97) It follows from these considerations that there is no evidence to suggest that this technology programme partially supported by South Korea, which does not seem to be exceptional in the shipbuilding industry (comparable programmes have been developed in other regions of the world), would be such as to considerably strengthen the financial situation of STX to an extent which would lead to a significant impediment of competition.

Investment loan of USD 400 million

(98) The complainant submits[55] that STX received an investment loan of USD 400 million used for the purpose of constructing a shipyard in China and that this loan was on "very favourable conditions when compared to conditions available to European companies". According to Fincantieri, the interest rate charged was 130 basis points over six-months the London Interbank Offered Rate (LIBOR), which Fincantieri sees as very low, considering the amount of debt of STX and the credit rating of STX. Fincantieri submits that the rating BBB+ Stable granted to STX by two South Korean rating agencies in fact corresponds to "an international equivalent" Low BB/High B. Fincantieri submits that considering the financial results of STX, and in particular its debt/EBIDTA ratio, which shows that STX is a company with a high level of debt, it would be clear that STX would not have been able to raise sufficient financing on the free financial market.

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51 Reply of Fincantieri of 28 January 2008 to the Questionnaire to cruise ship competitors of 14 January 2008, question 45.

52 Reply of 7 February 2008 to Questionnaire for STX of 30 January 2008, question 1.

53 Reply of 21 January 2008 to Questions to the notifying party of 11 January 2008, question 2.

54 Reply of 21 January 2008 to Questions to the notifying party of 11 January 2008, question 2.

55 Reply of 6 February 2008 to Questionnaire for Fincantieri of 30 January 2008, question 3.

(99) Fincantieri then submits examples of allegedly similar USD-denominated loans granted to allegedly similar South Korean companies at the same time as the loan granted to STX and claims that the market rate for the loan to STX was in the range of 300-700 basis points above the benchmark government rate.

(100) The notifying party confirmed[56] that in November 2007 two of its subsidiaries in China (STX Dalian Shipbuilding and STX Dalian Heavy Industry) received a loan of […]* for the construction of a shipyard in China. The loan was granted by a consortium of four South Korean banks: […]* (one of largest commercial banks in […]*), […]* (a […]* commercial bank with a key shareholder being […]*), […]* (owned indirectly by […]*) and […]*. […]* the four banks lent […]* on the basis of the same terms and conditions and the respective banks confirmed that they shared the same rights and obligations relating to the loan on equal terms[57]. All four banks participated in the negotiation of the loan and its documentation; their respective credit committees independently approved the loan. According to the notifying party, the interest rate is […]* and has been determined considering various factors including project risk evaluation, prospects of the business, company ratings of the borrowers and the guarantor and the conditions of collateral. All four banks confirmed to the Commission that the loan was granted on market conditions at the time of granting the loan, considering the various factors on a commercial basis.[58] The loan was granted against collateral […]*. The borrowers requested also other financial institutions to submit their proposals for the loan and chose this consortium as the "most competitive offer"[59].

(101) The notifying party then submitted examples of other investment loans extended to companies comparable in terms of credit-rating in the same period and at similar or lower interest rates[60].

(102) In response to Fincantieri's claim that the loan constituted a subsidy, it is noted that the loan was, according to the information submitted by the notifying party, provided on a equal footing (on same terms and bearing the same risk) by four banks. The fact that the four banks, including two privately owned banks, of which one is partially owned by the European bank BNP Paribas, acted in the same way indicates *prima facie* that the loan was extended at arm's length.

(103) As to the link between a loan for the construction of Chinese production facilities and the possible future use of the alleged financial advantage to significantly undercut the prices of cruise ships that would be produced in the future by STX, it is very remote. There is no evidence or any indication in the present case that the newly developed capacity of STX in China could be used for the construction of cruise ships.

(104) Since the loan benefits two subsidiaries of STX, which are not likely to produce cruise ships, it is unlikely that the loan, even if it was to contain an element of subsidy, could increase significantly STX' financial strength to an extent which would lead to the creation of a dominant position or to a substantial impediment to competition on the cruise ship market.

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[56] Reply of 7 February 2008 to Questionnaire for STX of 30 January 2008, question 3.

[57] Confirmed by the four banks in their replies of 17, 18 and 19 March 2008.

[58] Replies of the four banks of 17, 18 and 19 March 2008.

[59] Reply of 7 February 2008 to Questionnaire to STX of 30 January 2008, question 4.

[60] Reply of 7 February 2008 to Questionnaire to STX of 30 January 2008, question 4.

(105) It should be noted that had the loan been obtained on conditions that were more favourable than the market conditions, the subsidy would not have corresponded to the whole loan of USD 400 million, but only to the difference between a higher market interest rate and a lower interest rate granted to STX Dalian Shipbuilding and STX Dalian Heavy Industry. The amount of the subsidy would therefore be only a small fraction of the USD 400 million. In addition, the loan was granted to two subsidiaries of STX and STX was only a guarantor of the loan repayment. Even if this loan had been granted on favourable terms and would consequently contain an element of subsidy, it would, therefore, be unlikely that STX' financial strength could be increased significantly on this basis.

Financing of the purchase of Aker Yards

(106) Finally, Fincantieri submitted[61] that since it is not clear how STX financed the USD 700 million necessary for the acquisition of Aker Yards[62], it should be assumed that the main source of funding was a financial loan. Fincantieri then pointed out at the financial situation of STX, and in particular the level of debt which would not be such as to permit STX to raise enough additional debt on the free financial market. On this basis, Fincantieri concludes that STX cannot sustain this level of debt on commercial terms. This submission of Fincantieri appears unfounded.

(107) The notifying party explained[63] that STX used, for the acquisition of Aker Yards, […]*.

(108) Based on this information, it appears that the acquisition of Aker Yards was financed through the internal resources of the STX Group and not through external financing.

Conclusion on financial strength and alleged past or current subsidies

(109) In light of the above, the it should be concluded that the financial position of STX is presently not such as to render the merged entity dominant on the market for the construction of cruise ships, regardless of whether or not the financial instruments referred to by the complainant constituted past or current state subsidies by South Korea.

<u>(iv) Assessment of alleged future subsidies</u>

(110) Fincantieri raised the concern that the merged entity would in the future engage in unfair pricing on the basis of subsidies received in the form of favourable conditions for project financing. The Commission is not aware of any particular plan for subsidies to be granted to STX in the future. However, the main competition concerns raised by the complainant are attributed to potential subsidies granted to STX in the future. The complainant submitted that STX will receive favourable loans from the South Korean state for project specific financing when bidding for future cruise ship projects. This instance of subsidisation is alleged to be such as to directly enable STX to artificially lower its production costs for cruise ship building projects and to undercut the market prices, with a result of monopolising the market.

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[61] Submission of Fincantieri of 22 February 2008 *Impact of Subsidies/State Aids in the Cruise and Ferry Segments*, part I.

[62] The remaining USD 100 million were provided by STX Engines.

[63] Reply of 15 February 2008 to the Questionnaire for STX of 13 February 2008, question 1.

Project specific loans and guarantees

(111) The complainant identifies two instruments that could potentially be used for this purpose: Pre-shipment loans (PSLs) and Advanced Payment Refund Guarantees (APRGs) extended by KEXIM, the state-owned South Korean Export Bank. PSLs ensure the financing of the construction before the totality of the price for a ship is paid by the customer. Through APRGs, a financial institution guarantees that an advance payment made by the customer before the delivery of the ship (amounting normally to 80% of the total price in the case of cargo vessels and to 15-20% of the total price in the case of cruise ships) are repaid in the event of non-performance of the building contract.

(112) The market investigation has shown that shipyards typically use similar types of instruments to finance their working capital. Due to the nature of ships as large capital products, most shipyards have to rely on external sources to finance their production: either in the form of advance payments by the buyers or external borrowing. Ensuring financing of working capital represents therefore a certain cost for the shipyards.

(113) If these financing instruments are offered by public institutions on terms that are more advantageous than those offered on the market, they contain a subsidy element in the form of a reduced interest rate or a reduced guarantee premium. This form of subsidy is specific to a bidding project and could only have the competitive impact alleged by the complainant when granted to the merged entity in the individual future tenders for cruise ships.

(114) The complainant submits[64] that STX currently finances its working capital with the use of both PSLs and APRGs offered by KEXIM. Despite the fact that the complainant was not in a position to identify on what terms these instruments, APRGs and PSLs, are currently offered to STX, it maintains that STX benefits and will benefit in the future from interest rates and guarantee premia below market rates due to subsidisation by KEXIM, namely state subsidisation by South Korea. Fincantieri submits that thanks to these favourable financing conditions STX will be able to decrease its production costs, offer "artificially favourable payment terms to customers" and "aggressively buy market shares through lower prices"[65].

(115) The notifying party confirms[66] that STX uses for the financing of its current shipbuilding production in South Korea the APRG programme and the PSL programme run by KEXIM. The notifying party submits that these programmes as such are not considered subsidies under the WTO Agreement on Subsidies and Countervailing Measures.

(116) According to the notifying party[67], APRGs are provided to it by KEXIM, but also by other commercial banks. KEXIM APRGs constitute only a part of the total APRGs that STX is using to finance its production (approximately […]* in 2005, […]* in 2006 and […]* in 2007). The notifying party submitted to the Commission lists of APRGs it had received from KEXIM and other commercial banks in the period from 2005-2007. Based on this data, the guarantee premia charged by commercial banks were similar or

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64 Reply of 6 February 2008 to the Questionnaire for Fincantieri of 30 January 2008, question 5.

65 Reply of 28 January 2008 to the Questionnaire to cruise ships competitors of 14 January 2008, question 45.

66 Reply of 21 January 2008 to the Questions to the notifying party of 11 January 2008, question 8.

67 Reply of 7 February to the Questionnaire to STX of 30 January 2008, question 7.

even lower than those charged by KEXIM[68]. The guarantee premium is said to be determined by taking into account various factors such as company credit rating and conditions of collateral.

(117) As to PSLs, the notifying party submits[69] that KEXIM has been charging an interest rate equal to […]* plus spread based on the credit rating of the company and on the conditions of the collateral. The notifying party provided the Commission with a list of PSLs, confirming that the interest rate charged by KEXIM for PSLs in the period from 2005-2007 was above the applicable KORIBOR rate[70].

(118) On the basis of the market investigation, it should be concluded that STX currently uses APRGs and PSLs partly extended by KEXIM. The evidence collected by the Commission in the framework of this merger control procedure does not show that these financial instruments are currently extended on more advantageous terms than those offered on the market and constitute subsidies. Having regard to this evidence, it cannot be assumed that the merged entity will in the future be able to have recourse to subsidised financing enabling it to engage in anti-competitive practices in the cruise ship market.

Forecasts of future state decisions by South Korea

(119) The Commission's market investigation did not provide evidence which would allow it to forecast future decisions by South Korea to extend the APRGs and PSLs on terms more advantageous than those offered on the market.

(120) The complainant alleges[71] a constant practice established by KEXIM in the past, which, according to the complainant, should be sufficient evidence that South Korea will pursue this practice in the future. The complainant makes reference to the case that the European Communities initialled in 2002 before the WTO, claiming, amongst other things, that the APRGs and PSLs programme run by KEXIM constituted a subsidy prohibited under the SCM Agreement[72].

(121) It is correct that in 2002, after a two-year investigation under the Trade Barrier Regulation, the Commission brought a complaint before the WTO[73] arguing that South Korea was granting prohibited export subsidies to major South Korean shipbuilders, including STX, in form of project financing extended by KEXIM below the market benchmark. The Commission notes that the WTO Panel established[74] that STX benefited in the late 1990's from some individual APRGs and PSLs which constituted prohibited subsidies. The WTO Panel, however, ruled that the Commission had failed to

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68 Annex 1 to the Reply of 7 February to the Questionnaire to STX of 30 January 2008.

69 Reply of 15 February 2008 to the Questionnaire for STX of 13 February 2008.

70 Annex 3 to Reply of 7 February 2008 to the Questionnaire for STX of 30 January 2008.

71 Reply of 28 January 2008 to the Questionnaire to cruise ships competitors of 14 January 2008, question 45.

72 Report of the Panel of 22 December 2004 in WT/DS 273 Korea – Measures affecting trade in commercial vessels.

73 WT/DS 273 Korea - Measures affecting trade in commercial vessels. On 21 October 2002, the Commission requested consultations with South Korea pursuant the Dispute Settlement Understanding, GATT 1994 and SCM Agreement and on 11 June 2003 the Commission requested the establishment of the WTO panel.

74 Report of the Panel of 22 December 2004 in WT/DS 273 Korea – Measures affecting trade in commercial vessels.

establish a *prima facie* case that the legal regime under which KEXIM operated and the APRGs and PSLs programmes offered by KEXIM constituted a subsidy *as such*[75].

(122) The Commission does not have any new elements before it at present, and the complainant has not provided any evidence, to show that these two programmes run by KEXIM have been systematically used to grant subsidised production financing. The fact that the WTO Panel concluded that some of the individual instances of the guarantees and loans contested by the Commission constituted prohibited export subsidies does not allow it to conclude that South Korea will in the future grant subsidies in this form to STX. It also cannot be assumed with sufficient likelihood and without further evidence that South Korea will in the future engage in illegal behaviour by subsidising the merged entity in breach of its WTO obligations.

Conclusion on alleged future subsidies

(123) It should therefore be concluded that there is no evidence that would allow the conclusion that South Korea is likely to grant subsidies to the merged entity in the future.

(v) Even if the merged entity was to receive subsidies in the future, their impact on the costs of the cruise ships would be limited

(124) Even if the alleged future subsidies were granted, such subsidies would not lead to a dominant position of the merged entity in the market for cruise ship for the following reasons.

STX could use the alleged subsidies only to a limited extend for building cruise ships, as they would mostly be only applicable for cruise ships built in South Korea

(125) The Commission first examined to what extent these instruments could be used for the construction of cruise ships and to what extent these instruments could be used by the merged entity.

(126) The market investigation has shown that the financing of the building of a cruise ship is typically organised in a way that the ship owner pays 15-20% of the price of the ship as an advance payment prior to the delivery of the ship and the remainder only at delivery.[76] The supplier has to provide guarantees on the reimbursement of this advanced payment in case the production fails. It appears therefore that the APRGs are only of limited relevance for the financing of cruise ship construction as they relate to only a part (15-20%) of the total value of a ship.

(127) In addition, according to the notifying party[77], APRGs granted by KEXIM (those which are claimed to contain a subsidy element resulting from the alleged difference between conditions offered by KEXIM and normal market conditions) represent only a part of APRGs currently used by STX (see Recital 116). Considering that for the period from 2005-2007, the average was [less than 50%]*%. This further reduces the impact of a potential subsidy contained in the KEXIM APRGs on the financial strength of STX.

75 *As such*, meaning that the financing instrument in itself is not a subsidy.

76 See for example the reply of Fincantieri of 28 January 2008 to Questionnaire to cruise ships competitors of 14 January 2008.

77 Reply of 7 February to the Questionnaire to STX of 30 January 2008, question 7.

(128) Finally, while, according to the evidence provided to the Commission[78], there is no restriction under the legal framework of KEXIM for extending APRGs to foreign subsidiaries of South Korean shipyards, such an extension is conditional upon the South Korean parent company providing a re-guarantee to cover the risks and the credit limit of the parent company is lowered in proportion to the guaranteed amount. KEXIM confirmed that for these reasons South Korean shipbuilders have not applied for KEXIM APRGs for their foreign subsidiaries in which they held less than 50%. This further reduces the impact of a potential subsidy contained in the KEXIM APRGs on the financial strength of STX.

(129) It follows that the decisive element for the possible strengthening of STX's financial position would be potentially subsidised PSLs extended by KEXIM. However, according to the information provided by KEXIM[79], PSLs are not available under the current legal regime for the construction of ships in foreign shipyards, including foreign subsidiaries of a South Korean shipyard. KEXIM confirmed that under the existing legal framework KEXIM was not permitted to provide individual PSLs to any foreign shipbuilders, including foreign subsidiaries of South Korean shipbuilders. It follows that STX will not be able to use KEXIM PSLs to finance shipbuilding projects outside South Korea, in particular in the European Aker Yards facilities.

(130) Regardless of any potential subsidy element inherent in KEXIM PSLs, the merged entity will not have access to such state aid for the production of cruise ships in Europe (STX does not currently produce cruise ships in South Korea either). The relative impact of potentially subsidised PSLs on the financial strength of the merged entity will clearly be reduced due to these limitations. It is unrealistic to assume that the entire cruise ship production of Aker Yards would be moved to South Korea in the foreseeable future. Indeed, it would make little commercial sense for STX to pay USD 800 million to acquire Aker Yards just to secure their know-how in the cruise ship business.

The impact of the alleged subsidies on the final production cost of a cruise ship and on the financial strength of STX would not be significant

(131) Despite these considerations, the Commission examined the evidence before it in order to assess what the impact of the use of these financing instruments would be on STX's financial situation. To this end, certain assumptions must be made.

(132) According to an estimate of the notifying party[80], which the Commission has found to be consistent with the information provided by other market participants, the cost of financing of the production of cruise ships, including the costs of borrowing the working capital and the cost of obtaining advance payment guarantees (cost of the guarantee premium), constitutes about 4 % of the total costs of producing a vessel[81].

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78 Letter of 5 February 2008 addressed by KEXIM to SXT, Annex 2 to the Reply of 5 February 2008 to the Questionnaire for STX of 30 January 2008.

79 Letter of 5 February 2008 addressed by KEXIM to SXT, Annex 2 to the Reply of 5 February 2008 to the Questionnaire for STX of 30 January 2008.

80 Reply of 15 February 2008 to the Questionnaire for STX of 13 February 2008, question 12.

81 Reply of STX of 20 February 2008 to Questionnaire to STX of 13 February 2008. STX simulates the calculation of the proportion of financial costs in relation to the price of the vessel. After deduction of a profitability margin, the Commission calculated the estimated proportion of financial costs to the total costs of production.

This figure is based on the assumption that 80% of the working capital needs is financed through external borrowing.

(133) The Commission first assessed the hypothetical situation, in which STX would be in a position to obtain the PSLs and the APRGs without any charge (interest and premium free). This would mean that STX would be able to decrease its overall production costs for vessels built in South Korea by what is normally represented by financing costs, that is by about 4%. In theory, if STX keeps the same commercial margin, it could then reflect this decrease in a reduction of the selling price that Aker Yards is currently able to offer, and which would be in any case below 4%. It is recalled that this could only apply to vessels built in the yards of the merged entity situated in South Korea.

(134) This hypothesis is based on several assumptions that make it an entirely unrealistic scenario.

(135) First, it is assumed that 80% of the working capital needs are covered by external borrowing. The market investigation has shown that shipyards finance their production in various ways: through external borrowing or through a combination of external and internal financing in various degrees[82]. This first assumption is therefore overly conservative.

(136) Second, it is assumed that the merged entity would fully translate the cost decrease into a price reduction (and not, for example, in increased margins). This is far from obvious.

(137) Third, it is assumed that STX benefits from PSLs and APRGs without any charge at all. However, it was found during the market investigation that this assumption is not correct. The notifying party has submitted that the interest rate charged on the PSLs from KEXIM corresponded in 2006 and 2007 on average to […]* per annum, compared to the average KORIBOR of 4.8%. Since no market operator was able to identify what the market benchmark for similar loans would be, the Commission assumes that it is 10% per annum which represents, however, a very conservative estimate[83]. If this was, however, the actual market rate, STX would have to bear about 50% of the costs of borrowing "normally" borne by shipyards having to borrow at market rates. This means that the reduction of costs assumed above and derived from unfair market conditions would be 50% lower and the corresponding potential price decrease could therefore only be around [0-5]*%.

(138) This potential reduction would only relate to new vessels built in South Korea and not in the yards of the merged entity in Europe. If STX were to pursue the strategy, also suggested by the complainant, of offering cruise ships at average prices of ships produced in South Korea and ships produced in Europe, the price reduction derived from the alleged subsidies would be further diluted to about [0-2]*%.

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82 Reply of 7 February 2008 to Questionnaire for STX of 30 January 2008, question 10. Reply of 6 February 2008 to Questionnaire for Fincantieri of 30 January 2008, question 5e).

83 Data available from OECD on trends in the evolution of interest rates in the EEA and South Korea between 2002-2007 indicate that short-term rates have been below or slightly above the 5% threshold and long-term rates (10 year government bonds) have been below 6% (with the exception of 2002 with around 7% for South Korea). It is therefore clear that the assumption of 10% interest rate for loans under two years, related to concrete projects and secured with collaterals is extremely conservative.

(139) To assess the importance of this potential price difference, a series of factors were taken into account.

(140) Firstly, according to the information provided to the Commission in the market investigation, the difference in the financing costs between some existing competitors is considerable showing a spread of more than 1%, depending on how each producer finances its working capital, in particular to what extent the producer has recourse to external financing. The difference in the level of financing costs does not seem to prevent these shipyards from being able to compete amongst themselves. Considering this comparison between the existing players and considering that the financing costs of the merged entity could be subsidised and thus potentially decrease from [0-5]*% of total costs to [0-5]*% of total costs, this difference would not be such as to enable the merged entity to drive Fincantieri out of the cruise ship market. It is recalled that the merged entity, on the basis of the information available to the Commission, would not be able to reduce its financing costs for its operations in Europe, which would continue having to bear financing costs corresponding to the level of its competitors with a similar structure of working capital financing.

(141) In addition, the market investigation has clearly demonstrated that customers consider a series of factors when selecting the shipyard in which to place an order[84]. Some customers have indicated that price and a successful track record in undertaking complex projects and technical capabilities of the yard were equally important parameters of competition. Several customers have clearly indicated that it was not the price, but a successful track record of undertaking complex projects that was the most important parameter of competition. Several customers have emphasised the issue of capacity constraints and the ability of a yard to deliver the ship within the time-frame desired by the customer has also been highly rated.

(142) It should be emphasised that a sudden shift of customers to new suppliers does not appear to be likely in light of the "preferential" relationships between established customers and suppliers due to, among other things, the important sister-ship effect (see Recitals 150 and 151). Considering these effects, it is likely that price will not be the decisive competition parameter.

(143) Also, it is likely that in the short-term the merged entity, if it wishes to start cruise ship production in South Korea, will have to bear some higher production costs linked to the absence of a developed sub-contractors network in South Korea (for example, the necessity to import components from Europe) and linked to the learning curve effects (for example, initially lower productivity and higher manpower consumption).

(144) It should be concluded that, on the basis of extremely conservative assumptions, the merged entity could be in a position to reduce the price of prototype ships built at the facilities in South Korea by approximately 1 to 2% thanks to the access to presumably subsidised external financing.

(145) Taking into account an average price of around EUR 450 million for a cruise ship of 100 000 gt[85], the estimated advantage would represent between EUR 4.5 and 9 million

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[84] Questionnaire to cruise ships customers of 11 January 2008, question 33.

[85] Questionnaire to cruise ship competitors of 14 January 2008. Average based on orders for the last three years.

per cruise ship, which represents between 0.1% and 0.2% of STX's turnover, taking into account this additional cruise ship. Even if this effect increased with the number of cruise ships built, it should be taken into account that the number of cruise ships ordered per year is rather limited (between 10-15 ships per year over the last three years) and therefore, even if STX were to occupy a large portion of the world orderbook, which is unlikely, the impact would still be rather limited.

(146) On the basis of the foregoing, it should be concluded that even if evidence existed that the merged entity would in the future benefit from subsidised production financing, such an advantage would not be such as to significantly increase the financial strength of the merged entity.

Even if the impact of the future alleged subsidies on the financial strength of the merged entity was significant, the features of the cruise ship market would not allow the merged entity to exert market power and to achieve a dominant position

(147) The concerns raised by Fincantieri during the market investigation suggest that the merged entity would be able to exploit its competitive advantages derived from having access to subsidies and to lower production cost to marginalise its competitors. Although the market investigation has indicated that differences in production costs between South Korea and Europe do exist (for example, with respect to the price of steel, the price difference between South Korea and Europe may represent around 5% of the final cost of a cruise ship[86]), the Commission notes that there are other important factors that strongly question the ability of the merged entity to create a dominant position on the cruise ship market as a result of its alleged enhanced financial strength.

<u>The merged entity does not currently enjoy substantial market power</u>

(148) As already mentioned, the notified transaction will not change the market structure in the cruise ships market at horizontal level, and the impact on competition derived from the vertical relationships is not significant. Aker Yard's position in the cruise shipbuilding market is around [30-35]* %[87], while Fincantieri's position is around [40-45]* % and Meyer-Werft's position is around [25-30]* %. These market shares are approximately the same regardless of whether they are considered on the basis of orders, tonnage of the ships delivered or value of sales. Other smaller players constitute the remaining [0-5]* % of the market. In addition, the market investigation has not given any indications that Aker Yards may be in a position to exert market power and in fact, it is the second player behind Fincantieri.

<u>Large and sophisticated customers will be able to mitigate any anti-competitive behaviour</u>

(149) The cruise ship market is also characterised by the presence of large customers who are likely to have, under the current market structure, some ability, in the current structure of the market, to react to possible anticompetitive behaviour from the merged entity.

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86 Commission's own calculation of the basis of the information obtained during the market investigation and reply of STX of 20 February 2008 to the Questionnaire for STX of 13 February 2008, questions 5 to 7.

87 Capacity measured in terms of capacities ordered during the period from 2004-2007.

(150) The main customers are Carnival, Royal Caribbean, MSC and STAR/NCL, four customers controlling around 80% of the cruise ships demand[88] at world-wide level. These customers have entered into long-standing preferred relationships with the main shipyards. For example, over the last seven years, one of the three main cruise ships producers (Fincantieri, Aker Yards and Meyer) has been supplying cruise ships to only one of those four main customers, representing more than 90% of its sales. One of the customers has made all its purchases from only one producer, and other two customers have purchased cruise ships only from two of the three suppliers[89].

(151) In addition, European shipyards would have the advantage over STX of being able to produce "sister" cruise ships based on prototypes designed previously and on which the producer who has designed the prototype has a clear advantage over other producers.

(152) The cost advantage was quoted by all major customers as the prevailing reason why sister ships are typically ordered from the same manufacturer that produced the prototype[90]. Established business relationships and the experience of the shipyards building the prototype also contribute to awarding the sister ship to the same shipyard that built the prototype. Indeed, it follows from the market investigation that the ship owner often co-develops the design of the prototype ship with the shipyard, oversees the production process, intervenes in the selection of subcontractors and takes part in the complex project management. Close ties are therefore created between the buyer and the shipyard already at the design stage.

(153) The market investigation has also confirmed that, despite these "preferred" relationships, customers look for quotes from various producers to keep competition and consider that at least three competitors are necessary to maintain an adequate level of competition[91]. This ability (although somewhat limited by the "sister-ship effect") follows from a continuous monitoring of the possible alternative suppliers (and their specific shipyards) either directly or via brokers. This tends to confirm the view already expressed in Case M.4104 – Aker Yards / Chantiers de l'Atlantique (see Recital 38) that with three large suppliers (Fincantieri, Aker Yards and Meyer Werft), cruise ship operators seem to have a degree of buyer power allowing them to 'play' suppliers one against the other in an efficient way.

(154) In addition, in view of the limited number of orders per year (approximately 10-15 vessels and the even more limited number of prototypes) each contract for a prototype ship (probably leading to subsequent contracts with the same cruise operator for sister ships, when not already included under the same initial contract for the prototype) represents for shipbuilders an important business opportunity to compete for. Consequently, even if fully open tenders represent a minority of cases of contracts for new cruise vessels (including sisters and prototypes), these few tenders, especially when they are likely to lead to contracts for more than one vessel, are therefore very likely to be fiercely competed for by the existing few suppliers as they represent a large part of the suppliers' turnover.

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88 In terms of gross tonnage output in the period from 2007-2012, STX's reply of 25 January to the Commission's 6.1.(c) Decision, page, 4 and footnote 5 (GP Wild report, *Cruise industry statistical review*, January 2007).

89 Questionnaire to cruise ship competitors of 14 January 2008, question 12.

90 Questionnaire to cruise ship customers of 11 January 2008, questions 28, 29 and 30.

91 Questionnaire to customers of 14 January 2008, question 26.

(155) It is therefore highly unlikely that, under the current market structure in which the three main cruise ship producers will remain in the market, that the merged entity would be able to marginalise Meyer (which in any case has not raised this concern) and Fincantieri to the extent that price increases can be subsequently imposed on customers.

Competitors are not unable to react and, in the extreme, keep re-entry as a credible threat

(156) The complainant, in its submission of 15 February 2008[92], indicated several reasons why, despite the increased prices, it could not re-enter the LNG segment in the short /medium term after most of the production has been transferred to the Far East, suggesting that this would also be the case for the cruise ship market. It is, however, considered that both markets are not comparable and that re-entry would be possible for the following reasons.

(157) A significant part of Fincantieri's turnover is generated by businesses other than the cruise ships and ferries' businesses, which means that, even if forced to adjust and rationalise its production capacity, it would still be able to continue with its other business units (repairs and conversions, naval vessels, offshore business and mega yachts)[93].

(158) More realistically, it could also find other niches to fill up its dock capacity. Examples of this alternative business may be the re-furnishing and reparations of cruise ships, either because they are getting older or due to the increased demand expected for the coming years (around 8% per annum[94]) or possibly smaller luxury cruise ships and yachts with a very high degree of sophistication. It could also expand in existing niche segments, such as offshore and specialised vessels, and Fincantieri itself states that it has done so in the past: "*…Fincantieri, in the past years, has always adapted its production capacity to the requirements of the market (for example varying the level of outsourced activities, switching productions from naval vessels to commercial vessels, such as mega yacht, fast ferries, specialized vessels, etc.), in order to limit potential lack of production workload"*[95]. There have also been examples in the market of yards moving towards other niche markets. To summarise, it cannot be assumed that all the physical facilities would be closed down following the alleged capacity rationalisation.

(159) In addition, the know-how and experience acquired for building cruise-ships would not be lost even if Fincantieri had to decrease its activity. The findings of the Commission[96] clearly indicate that the key know-how remains with the few people able to manage the complex project that a cruise ship represents. The bulk of the other needs such as the network of subcontractors, including in particular those providing turn-key projects, and even the designing capacities, also crucial and which are also partly sub-contracted to specialised engineering companies, would still be available. Moreover, even if Fincantieri lost new orders, the time lag between the production of the current ships

92 Submission of Fincantieri of 15 February 2008 *Relevance of Subsidies/State aid in EC Merger Control*, page 23, point 4 and ff.

93 Questionnaire to cruise ship competitors of 14 January 2008, question 3.

94 Questionnaires to competitors of 14 January, question 13.

95 Reply of Fincantieri of 28 January 2008 to the Questionnaire to cruise ship competitors of 14 January 2008, question 15.

96 Commission's telephone conversations with customers and competitors' answers to the Commission's request for information from competitors, question 41.

ordered and the final delivery would ensure that it would still be active for some years on the building of new cruise ships and could use this time to restructure and adjust.

(160) With respect to innovation, a gap between Fincantieri and the merged entity may take place after some years without any new orders being awarded. However, although innovation is certainly important, it should be taken into account that part of such innovation is in hands of subcontractors, and therefore available to certain extent. The clearest evidence that the crucial factor in the cruise ship market is the know-how of managing complex projects and that a certain lack of innovation can be overcome is the case of Mitsubishi, who was able to deliver in 2004 two cruise ships of very high quality without previous experience in the cruise ship market.

(161) In light of the foregoing, if market prices increased to an uncompetitive level after a monopolisation of the market, as Fincantieri alleges, and there were no alternative suppliers, there is no reason to conclude that re-entry by Fincantieri would not be possible with the support of one or more large customers.

(162) With respect to Meyer Werft, it has not raised concerns in this regard, which is an additional indication that there is little likelihood of the occurrence of the competitive scenario put forward by Fincantieri.

The LNG example

(163) The complainant also raises the issue of "monopolisation" by the South Korean shipbuilders in the LNG market[97] and that this mechanism may be replicated in the cruise ship sector. In particular, the complainant justifies its complaint by alleging the possibility of predatory pricing and the exclusion of competitors in the cruise ships and ferries segments with an illustration from the LNG sector. The complainant submits that the South Korean shipbuilders, thanks to subsidies, were able to pursue a strategy of aggressively lowering prices (in the period from 1997-2000), which allowed them to increase their market shares to a near-monopoly position and marginalise other producers. After having taken over the lead on the LNG market, the South Korean shipbuilders have been able to raise prices in the period from 2002 – 2007[98]. The complainant also indicates that this process has had a negative effect on innovation, since South Korean shipbuilders currently continue to utilise the containment system patents acquired from European shipbuilders developed in the 1970s.

(164) First, there is no evidence that the market for LNG vessels would be monopolised. Even though it is correct that the production of LNG vessels moved from Europe to Asia during the last two decades, there were at least six South Korean and Japanese players in 2004[99]. The market investigation has confirmed that these players are still active in the market today and some additional players are considered to be credible suppliers of LNG vessels (for example Hudong Zhonghua, China[100]; Mitsui, Japan[101]). Therefore, it

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97 Submission of Fincantieri of 15 February 2008 Relevance of Subsidies/State aid in EC Merger Control, page 21, section VI and page 23, point 4.

98 Submission of Fincantieri of 15 February 2008 *Relevance of Subsidies/State aid in EC Merger Control* and reply of 28 January 2008 to Questionnaire to cruise ship competitors of 14 January 2008, question 45.

99 South Korea: Heavy Daewoo, Samsung, Hyundai Heavy Industries, STX; Japan: Mitsubishi, Kawasaki Shipbuilding Corporation (public domain).

100 Reply of [customer]* of 5 December 2007 to Questionnaire to customers of 28 November 2007.

101 Reply of Fincantieri of 6 December 2007 to Questionnaire to competitors of 28 November 2007.

cannot be argued that the LNG market is a monopoly in which competition does not exists.

(165) Considering the supply structure in the LNG market, the Commission does not have any indication that the increase in prices for LNG vessels in recent years is related to anti-competitive practices resulting from monopolisation. It is observed that the price level in the shipbuilding sector has increased across all types of ships during the last six years alongside the price increment of the basic materials and components (mainly steel as a major input in the production of containers and tankers).In addition, the other factors that may have an impact on the price evolution are the continuous increase of the order books worldwide and the resulting capacity constraints.

(166) It should also be taken into account that the evolution on the exchange rate markets which shows that the weakening of the US dollar and the depreciation of other currencies (JPY, KRW and CNY) against the euro have adversely affected the competitiveness of European shipbuilders.[102]

(167) With respect to the possible impact on innovation, the only evidence provided by the complainant is that the technology used by the South Korean shipbuilders is based on patents developed in the 1970s. However, it should be noted that the described developments in the LNG sector took place at the end of the 1990s, which means that either (i) in the period 1970s-1990's such technologies were no longer developed and therefore it cannot be argued that South Korean shipbuilders have negatively affected innovation, or (ii) if innovation between 1970-1990 existed, it is clear that customers have given preference to a well established older technology if offered at competitive prices.

(168) In addition, prices in the LNG sector are currently too low for players such as Fincantieri to re-enter the market.[103]. This indicates that the LNG market remains competitive, with prices lower than what they would have been if the production would not have moved to the Far East.

(169) In any case, the LNG sector and the cruise sector are far from being comparable cases, in particular as regards the relevance of innovation and economies of scale in both sectors.

(170) Regarding innovation, it is evident that LNG, for which old technology is still used and accepted by the customers, is not comparable to cruise ships for which innovation and differentiation are key features. The complainant has not provided any evidence to conclude that the South Korean shipbuilders will reduce innovation in the cruise ship market. In addition, it should be taken into account that cruise ships' customers are large, experienced and sophisticated customers with strong buyer power and therefore it is highly unlikely that they would turn completely to alternative suppliers knowing that their innovation capabilities are not appropriate and facilitating at the same time the marginalisation of experienced cruise ship producers.

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[102] See http://www.ecb.int/stats/exchange/eurofxref/html/eurofxref-graph-usd.en.html (as seen on 4 March 2008)

[103] Fincantieri itself submitted that it would not be able to re-enter the LNG segment as it would not be able to reach the critical mass of production necessary to exploit economies of scale. Submission of Fincantieri of 15 February 2008 *Relevance of Subsidies/State aid in EC Merger Control*, page 24, point b).

(171) The complainant also indicated that the market for LNG carriers requires a mass production where economies of scales can allow significant savings. However, it should be noted that economies of scale are not as important for cruise ships as they appear to be for LNG vessels. First, the number of ships produced differs largely in both markets, amounting to around 102 cruise ships in the period from 1998-2007[104] and to 262 LNG vessels in the same period[105]. Second, and more importantly, cruise ships are highly customised products specifically designed to meet the customers requirements, leading to longer periods of negotiation, design and production (between 15-20 months for the production and up to 4 years for the entire process) and for which the advantage of economies of scale is therefore much more limited.

(172) Therefore, it may be concluded from the foregoing that it is unlikely that (i) the increase in prices since 2002 for LNG vessels occurred as a result of monopolisation and predatory pricing strategy pursued by the Southern Korean shipbuilders in the late 1990's[106], (ii) that innovation will decrease as a result of the transaction and (iii) that, even if the alleged anticompetitive effects claimed by the complainant in the LNG market were proved to exist, the same mechanism would take place in the cruise ship market given the significant differences between both markets.

(173) Hence, STX would not be able in the long term, and as a result of the alleged subsidies and the other advantages submitted by the complainant, to significantly impede effective competition in particular as a result of the creation of a dominant position on the cruise ship market.

C.1.4. CONCLUSION ON THE CRUISE SHIP MARKET

(174) On the basis of the above, it may be concluded that the proposed transaction would not significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position, on the market for the construction of cruise ships.

C.2 CONSTRUCTION OF FERRIES

(175) The in-dept market investigation also analysed the potential impact of the merger on the market for ferries. The situation is similar to the cruise ship market to a certain extent: Aker Yards is one of the major players in that business and STX is not yet present. Even though the merger will not result in horizontal overlaps between the parties, concerns have been voiced by some market participants regarding (i) the possible elimination of STX as a potential entrant into the market and (ii) the possibility of the merged entity being able to drive other competitors out of the market and monopolise it on its own, due to competitive advantages the merged entity would be enjoying and in particular due to alleged unfair subsidies. However, the situation on the market for ferries is somewhat different than the cruise ship market. In comparison to the highly

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104 Reply of STX of 25 January 2008 to the Commission's 6.1.(c) Decision, page 5.

105 Submission of Fincantieri of 15 February 2008 *Relevance of Subsidies/State aid in EC Merger Control*, page 22, table 9.

106 This conclusion is not in any way contradicting the conclusions of the European Communities in the case launched against Korea before WTO in 2002, which concerned also the LNG sector. As already mentioned in Recital 82, the relevant tests in the SCM Agreement on actionable subsidies are injury caused to the domestic industry of another Member, serious prejudice to the interests of another Member, nullification or impairment of benefits accruing to another Member under the GATT 1994 and the SCM Agreement, whereas the Community merger control operates under a different test (effects of competition test).

concentrated market for cruise ships, there are much more players present on the ferries market, which makes any possible anti-competitive effects even more unlikely.

(176) During the last five years, the market shares of the suppliers on the worldwide market for ferries were as follows:

Table 4 - market shares on the worldwide market for ferries based on orders placed in the period from 2003-2007

	Tonnage	**No. of ships**
Aker Yards	[10-15]* %	[5-10]* %
Fincantieri	[10-15]* %	[0-5]* %
Flensburger	[10-15]* %	[0-5]* %
Hyundai	[5-10]* %	[0-5]* %
Visentini	[5-10]* %	[0-5]* %
Apuania	[5-10]* %	[0-5]* %
Barreras	[0-5]* %	[0-5]* %
Austal	[0-5]* %	[5-10]* %
Jinling	[0-5]* %	[0-5]* %
Mitsubishi	[0-5]* %	[0-5]* %
Samsung	[0-5]* %	[0-5]* %
Fosen	[0-5]* %	[0-5]* %
OTHERS	25%	72%

Source: Market investigation[107]

(177) As shown in Table 4, the main players on market for ferries are Aker Yards ([10-15]* % market share on the basis of tonnage ordered), Fincantieri ([10-15]* %), Flensburger ([5-10]* %), Hyundai ([5-10]* %) and Visentini ([5-10]* %). Overall, there is a relatively large number of ferry suppliers. Customers mostly named around 20 shipbuilding companies they regard as existing competitors in the ferry market.[108] Apart from a number of smaller European players, Asian Yards have also been active in building ferries in recent years, which they also built for European customers. For example, the South Korean shipbuilder Hyundai delivered two ferries (of 43 500 gt and 55 000 gt) to the Swedish ferry operator Stena Line in 2003, another South Korean, Samsung is currently building two ferries for the same customer (the order was received in August 2007) and already delivered six ferries since 2001 (the largest of 36 000 gt); Daewoo, another major South Korean shipbuilder, has delivered six ferries including two for the Greek customer Blue Star in 2002 and two ferries for Moby Line in Italy in 2001; two Chinese competitors have also delivered ferries to Europe.[109] Mitsubishi is also building ferries but seems to concentrate on the domestic Japanese market.

107 Market reconstruction on the basis of data provided by suppliers of ferries – reply to question 10 of the *Questionnaire to ferry competitors* of 11 January 2008 – and Aker Yards' data, based on Lloyd's Register, Fairpaly WSE, Shipping Statistics, version 9,51, Database October 2007. No meaningful information about value of the ships has been gathered in order to reconstruct the value market shares. However, as is the case with cruise ships, the value shares are expected to correspond to a large extend to the shares based on tonnage ordered.

108 *Questionnaire to ferries customers* of 11 January 2008, questions 11 and 12.

109 Information provided by Meyer Werft on 21 January 2008, in reply to Questionnaire to ferry competitors of 11 January 2008, question 15.

(178) To date, STX has not built any ferries, nor has it been awarded any contract for ferries. Although some market participants see STX as a potential entrant into the ferry market, the market investigation did not point to any specific instance where STX would already be trying to secure an order with customers. As one larger customer observes, "*STX could be an entrant but has so far no experience from ferry construction. If STX decides to enter the ferry market they will likely have to do as the other Korean yards to have a test period with a ferry project and learn the specific features and differences compared with construction of freight tonnage. Without any doubt they will with normal Korean dedication and professionalism succeed, but it will be likely cost in the beginning as there are many lessons to be learnt.*"[110]

(179) In any event, even if STX was a potential entrant in the future on a stand-alone basis, its entry would not bring about any significant change in the market structure, as there is a large number of players presently active on the market. There is no reason to believe that the removal of STX as a potential entrant would lead to a significant impediment of effective competition on the ferry market.

(180) Some market participants, in particular Fincantieri (who regards the cruise ship and ferry market as one), voiced the concern that the merged entity would be able to use unfair subsidies and benefit from lower costs in building ships in South Korea and undercut the prices of ferries with the result of driving the other competitors out of the market and monopolising it on its own. The question of alleged South Korean subsidies has been analysed in depth in the previous Section concerning cruise ships, and the reasoning applies *a fortiori* for the market for ferries[111]. In addition, there are presently already three major South Korean shipbuilders active on the ferry market, and their market experience and presence in the ferry market is not insignificant (as shown in Table 4, Hyundai is the fourth largest worldwide supplier of ferries in terms of tonnes ordered during the last five years). These three large South Korean players would thus benefit from the same alleged advantages and subsidies as STX. The fact that STX as a fourth South Korean shipbuilder would get access to the know-how of building ferries via the acquisition of Aker Yards, would thus not significantly change the competitive landscape.

(181) In the light of the foregoing, it should be concluded that the notified transaction would not significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position in the ferries market.

(182) In addition, the notified transaction would not lead to a significant impediment of effective competition on the basis of a broader market definition comprising both the cruise ship and the ferries market, as there are no competition concerns on either of the narrower product market definitions namely on the cruise ships market and on the ferries market) and the reasoning used with respect to these two markets may be applied *per analogiam*.

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110 Reply of Stena RoRo of 24 January 2008 to Questionnaire to ferries customers of 11 January 2008, question 16.

111 With the exception of the argument relating to buyer power of customers, which are much more dispersed in the ferry market.

C.3. CONSTRUCTION OF PRODUCT TANKERS

(183) As referred to in Recital 17, if product tankers were to be considered to be one product market with chemical/oil tankers, the combined average market share of both companies in the period from 2004-2007 was 14.75% in terms of deliveries based on tonnage and 11% in terms of orders based on tonnage[112].

(184) Even on the basis of a narrower product market definition, that is a market for product tankers alone, the combined market shares of the parties and the increase brought about by the notified transaction would be limited. On the basis of the number of deliveries and deliveries based on tonnage [gt]* and on basis of the number of orders and orders based on tonnage, the average market share has been the following, as shown in Table 5:

Table 5 – Market shares for product tankers

2004- 2007 market shares[113]	**STX**	**Aker Yards**	**STX + Aker Yards**	**Hyundai Mipo**	**New Century**
Based on number of deliveries	13.5%	0.25%	13.75%	10.25%	6.5%
Based on tonnage of deliveries	14.75%	0.25%	15%	13.75%	9.25%
Based on number of orders	9.5%	1.25%	10.75%	15.5%	3.75%
Based on tonnage ordered	8.5%	1.5%	10%	15.5%	5.5%

Source: Notifying party

(185) The overlap between the parties on this product market during the last four years has been very limited. During that period, Aker Yards delivered product tankers only in 2006, in which year its market share in terms of deliveries [dwt]* world-wide was 1%. In the period from 2004-2005 and in 2007, the corresponding market share of Aker Yards was 0%. STX has had an average corresponding market share of 14.75%. In terms of orders [dwt]*, Aker Yards has had an average market share in the period from 2004-2007 of 1.5%, with no orders in 2004, 2006 and 2007. The corresponding average market share of STX was 8.5%. In terms of the number of ships delivered and ordered in this period, the market shares are similar.

(186) In addition, the in-depth investigation confirmed that Aker Yards is not seen as STX's closest competitor in the area of product tankers, or vice versa. According to the replies of customers, it appears that STX's closest competitors on this market are Hyundai Mipo and New Century S/Y[114], which corresponds to their relatively strong position on the market. According to the data provided by the notifying party, the market share of Hyundai Mipo in terms of deliveries [dwt]* worldwide has been on average 13.75% in the period from 2004-2007. The corresponding average market share of New Century S/Y was 9.25%. The other players have had an average market share below 10%.

112 Reply of STX of 30 November 2007 to the request of information of 26 November 2007, Annex 1.

113 The calculations are based on data submitted by the notifying party on 10 March 2008.

114 Questionnaire to customers of 28 November 2007, question 19 and Questionnaire to Product Tanker customers of 11 January 2008, question 14.

(187) The market investigation has confirmed that the market for product tankers is segmented among a high number of players, none of which is clearly a market leader. Customers have identified numerous credible suppliers of product tankers, mainly Asian yards (including STX but often not Aker Yards), one customer naming 13 companies and another stating that there would be over 20 credible suppliers of product tankers[115]. Post-merger, there will remain effective competition from a number of suppliers.

(188) The market for product tankers appears to be a bidding market that operates word-wide. Ships are typically purchased in a bidding exercise (relative to one single ship or to a series of sister vessels), primarily on the basis of price and delivery times. Transport costs do not seem to deter customers from ordering a ship from a different region; ships are typically delivered at the shipyard and used for the first commercial voyage when sailing to the region of its main operation. Apart from the existence of numerous competitors on the product tankers market, barriers to entry seem to be insignificant. Indeed, respondents to the market investigation have indicated that they observe recent market entrants in the product tanker market, such as the South Korean suppliers SPP and SLS, or new Chinese suppliers[116]. It is also evident from historical data on product tankers orders that there has been an increasing number of orders being taken from more and more newcomers in recent years.[117]

(189) On the basis of the above, it may be concluded that the notified transaction would not significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position in the product tankers market.

D. <u>ASSESSMENT – VERTICAL ASPECTS</u>

D.1 SHIP ENGINES MANUFACTURING

(190) During the market investigation some concerns were raised by certain competitors on possible negative effects as a result of the vertical relationships created by the notified transaction. Only the complainant, however, has provided more substantiated arguments in that respect.

(191) STX is currently active in ship engines manufacturing, a market in which the current cruise ships operators are absent. According to some competitors[118], the merged entity would be in a position to benefit from the upstream activities of STX, given it a significant advantage in terms of cost and time delivery. In addition, STX could concentrate the supply of its ship engines at Aker Yards, thus limiting the supply to Aker Yards competitors. It has also been argued that STX's supply of engines for cruise ships may reduce the sales of the current cruise ships engines' suppliers below the

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115 Questionnaire to customers of 28 November 2007, question 17.

116 Questionnaire to customers of 28 November 2007, question 21.

117 Data based on Clarksons Reseach Institute, provided by the notifying party. For example, SPP started to take product tankers orders on 2005 and for the year 2007 it achieved a yearly market share of 14% in terms of tonnage ordered. Another company identified as newcomer, SLS, achieved 8% market share in 2007. From the data it appears that in 2007 there were three and in 2006 four companies starting taking orders for product tankers, while these companies appear not to have previously taking orders for these types of vessels.

118 Questionnaire to cruise ship competitors of 14 January 2008, question 33.

critical mass for which investments in innovation and R&D are justified, thereby harming innovation[119].

(192) From the customers' point of view, however, vertical integration into the production of engines is not a crucial competitive element, and no concerns have been raised in this respect.

(193) The market for marine engines in general is not concentrated. In the overall marine diesel engines market, STX's market share at world-wide level in 2007 was around [15-20]*% (in terms of units delivered). Other important competitors are Wärtsilä ([15-20]*%), Yanmar ([15-20]*%), Daihatsu ([25-30]*%), Doosan ([5-10]*%) or Mitsui ([5-10]*%). In the "two-stroke" diesel engines segment, which are the ship propulsion engines mainly used for large commercial vessels in general, the market shares of the main player would be STX [15-20]*%, HHI [5-10]*%, Doosan [30-35]*30%, Mitsui [30-35]*% and Hitachi [5-10]*%. In the "four-stroke" diesel engines segment, which are the ship propulsion engines mainly used for cruise ships and ferries, for smaller commercial vessels and for electric power plants for commercial vessels, the market shares of the main player would be STX [15-20]*%, Wärtsilä [20-25]*%, Yanmar [20-25]*% and Daihatsu [30-35]*%[120].

(194) The notified transaction would lead to a vertically affected market on the basis of the market for ship engines in which STX is active and due to Aker Yard's position in the cruise ship market (more than 25%). However, STX does not produce or sell engines for cruise ships, a segment dominated by two companies, MAN B&W Diesel Group ("MAN") and Wärtsilä Corporation ("Wärtsilä")[121].

(195) According to the information provided during the market investigation[122], STX cannot produce engines suitable for use in cruise ships and/or ferries with its own technology and it has never supplied, either directly or indirectly, such engines. Instead, it uses technology licensed by MAN for the production of engines for commercial vessels. Under the licence agreement, the engines manufactured by STX (in particular via its subsidiary STX Engine) are mainly "four stroke" generator engines used for generating electrical power in commercial vessels, but not for cruise ships or ferries propulsion.

(196) STX (via its subsidiary STX Heavy Industries) also manufactures, under the licence agreement with MAN, "two stroke" propulsion engines for commercial vessels. However, STX has not produced and has never supplied, either directly or indirectly, engines which would be suitable for cruise ships or ferries. Therefore, the concerns expressed by some market participants appear to be unjustified as STX would not be in a position to supply engines for its own cruise ships.

(197) In addition, […]*.

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119 Questionnaire to cruise ship to competitors of 14 January 2008, question 33 and reply of Fincantieri of 6 February 2008 to the Questionnaire for Fincantieri of 30 January 2008, questions 13 to 18.

120 Submission of STX of 12 December 2007 and 10 March 2008.

121 Reply of Fincantieri of 6 February 2008 to Questionnaire for Fincantieri of 30 January 2008, question 18.

122 Replies of STX of 7 February 2008 and 12 February 2008 to the Questionnaire for STX of 30 January 2008, question 14.

(198) The complainant submitted[123] that any geographical limitation for engines produced under licences may be overcome by internal development of new models or by renegotiation of the licensing agreement.

(199) Regarding the possibility of developing a new model of engine for cruise ships, it is noted that STX claims that it cannot produce such engines with its own technology. In any event, it should be borne in mind that a company belonging to Fincantieri's group, Isotta Fraschini Motori, is also active in the production of marine engines and, although it also claims that it is not a position to produce such engines, there is no reason to believe that STX would be in a significant better position than Isotta Fraschini Motori to develop a new model. It should also be noted that there appears to be a contradiction between the complainant's arguments. If the hypothetical sales of engines for cruise ships by STX affected the incentives of the current producers of cruise ship engines to further innovate (since their sales would be below the critical mass justifying new investments), it would be highly likely that STX would also find unprofitable to make the necessary investments to develop a new engine for cruise ships, since also its future sales would be rather limited.

(200) With respect to the renegotiation of the current agreements […]*, MAN would still receive the economic compensation for such a licence. It is therefore difficult to conclude that MAN would have the incentive to accept the modification of the current agreement if such modification were to negatively affect its profits and its ability to continue with its research and development activities.

(201) Finally, there are examples in the industry showing that vertical integration is not a crucial factor for success. Samsung and Daewoo, for example, are not vertically integrated upstream in the production of marine engines, which has not prevented these companies from being significant suppliers of commercial vessels[124].

(202) In light of the foregoing, it may be concluded that vertical relationships created by the notified transaction with respect to ship engines manufacturing would not significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position in the various markets for commercial vessels, and in the cruise ship and ferries markets in particular.

D.2 SHIPPING SERVICES

(203) STX is also active, through its subsidiary STX Pan Ocean, in the area of shipping services, primarily in the area of dry bulk tankers (which accounted for more than 90% of STX's total portfolio of vessels used for shipping services in the last four years). There is no horizontal overlap with Aker Yards with regard to this activity.

(204) The notifying party has stated that for the shipping services related to dry bulk tankers, STX had a market share of around [0-5]* % on the world level during the period from 2004-2007. Considering that shipbuilding markets are worldwide in scope and that vessels are procured on a world-wide level, the very limited presence of STX on the downstream shipping markets does not give any reasons for concerns relating to possible

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123 Reply of Fincantieri of 6 February 2008 to Questionnaire for Fincantieri of 30 January 2008, question 13.

124 Questionnaire to cruise ship competitors of 14 January 2008, question 33.

customers' foreclosure of the merged entity's competitors on the upstream ship building market.

(205) In light of the foregoing, it may be concluded that vertical relationships created by the current transaction with respect to shipping services would not significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position in the various markets for commercial vessels, and in the cruise ship and ferries markets in particular.

VI. CONCLUSION

(206) 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 8(1) of Regulation (EC) No 139/2004.

HAS ADOPTED THIS DECISION:

Article 1

The notified concentration whereby STX Corporation acquires sole control of Aker Yards A.S.A within the meaning of Article 3(1)(b) of the Regulation (EC) No 139/2004 is hereby declared compatible with the common market and the EEA Agreement.

Article 2

This Decision is addressed to:

STX CORPORATION
STX Namsan Tower 23th Floor, 631
Namdaemunno 5-ga
100-803 Jung-gu, Seoul
Republic of Korea

Done at Brussels, 05/05/2008

For the Commission
(*signed)*
Neelie KROES
Member of the Commission