

Anticipated acquisition by Rheinmetall Defence UK Ltd of BAE Systems Global Combat Systems Ltd

Decision on relevant merger situation and substantial lessening of competition

ME/50728/19

Please note that [X] indicates figures or text which have been deleted or replaced in ranges at the request of the parties or third parties for reasons of commercial confidentiality.

SUMMARY

1. Rheinmetall Defence UK Ltd (**Rheinmetall**) has agreed to acquire a controlling interest in BAE Systems Global Combat Systems Ltd (**GCS**) (the **Merger**). Rheinmetall and GCS are together referred to as the **Parties**.
2. The Competition and Markets Authority (**CMA**) believes that it is or may be the case that each of Rheinmetall and GCS is an enterprise; that these enterprises will cease to be distinct as a result of the Merger; and that the turnover test is met. Accordingly, arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.
3. The Parties are active in the supply of new armoured fighting vehicles (**AFVs**), and the supply of upgrades and deep maintenance services to existing AFVs. Their only UK customer is the Ministry of Defence (**MoD**), which generally awards a 'prime contract' to a single contractor, which may outsource certain aspects to sub-contractors. The Parties outsource certain aspects of some of their own prime contracts with the MoD to other sub-contractors, and are also active as sub-contractors to other AFV prime contractors, although only to a very limited extent.
4. The CMA has assessed the impact of the Merger in the following frames of reference:
 - (a) the supply of prime contracting services for new AFVs on a global basis;

- (b) the supply of prime contracting services for upgrades to existing AFVs on a global basis;
 - (c) the supply of prime contracting services for deep maintenance to AFVs on a global basis; and
 - (d) the supply of sub-contracting products and services for AFVs on a global basis.
5. However, the CMA did not need to conclude on the precise product or geographic frame of reference because it identified no competition concerns on any basis.

Horizontal unilateral effects

6. In the supply of prime contracting services for new AFVs, the CMA found that the Parties are not close competitors, and third parties told the CMA that GCS imposes a weak constraint on other AFV suppliers as it has no new 'off-the-shelf' AFVs. The CMA also found that GCS had not won any tenders in recent years, the Parties face competition from other manufacturers of AFVs, and the MoD is not concerned as it also has alternative methods of procuring AFVs from other sources.
7. In the supply of prime contracting services for AFV upgrades, the CMA found that the Parties competed head-to-head for one out of the two AFV upgrade programmes tendered in recent years, and are relatively close competitors. However, the CMA believes that, after the Merger, the merged entity will continue to face sufficient competition from other suppliers of AFV upgrades.
8. In the supply of prime contracting services for AFV deep maintenance, the CMA found that the Parties are not close competitors, and there are a number of other suppliers able to constrain the merged entity.
9. In the supply of sub-contracting products and services for AFVs, the CMA found that the Merger does not raise competition concerns because the activities of the Parties as sub-contractors or sub-contractees are minimal, in particular in the UK.

Vertical effects

10. Some third parties raised concerns stating that the merged entity would be able to foreclose rivals in the supply of sub-contracting products and services for AFVs because of the IP rights owned by GCS and the capability of Rheinmetall as an AFV supplier. However, the CMA considers that due to the Parties' relatively modest shares of supply in the above frames of reference

and the MoD's ability to grant access to the necessary IP rights to other suppliers, the merged entity would lack the ability to foreclose rival sub-contractors.

11. Therefore, for the reasons stated above, the CMA believes that the Merger does not give rise to a realistic prospect of a substantial lessening of competition (**SLC**) as a result of either horizontal unilateral or vertical effects.
12. The Merger will therefore **not be referred** under section 33(1) of the Enterprise Act 2002 (the **Act**).

ASSESSMENT

Parties

13. Rheinmetall is a wholly-owned subsidiary of Rheinmetall AG, a defence group publicly listed in Germany with its head office in Düsseldorf. Rheinmetall's principal activity is to provide market, sales and shared services support for its affiliate companies and bid for, negotiate, accept and perform contracts in defence products and services. Rheinmetall's turnover in the UK in the financial year ending 31 December 2017 was £[~~XX~~].
14. GCS is a subsidiary of BAE Systems. Its principal activities are the design, manufacture, supply and in-service support of combat vehicles, howitzers and naval guns.¹ GCS's turnover in the UK in the financial year ending 31 December 2017 was £[~~XX~~].

Transaction

15. The proposed transaction (**Transaction**) consists of the acquisition by Rheinmetall of control over GCS through the acquisition of a 55% shareholding in GCS from BAE Systems Land Systems Limited (**BAES**) via a share purchase agreement. BAES will hold the remaining 45% shareholding post-Merger.
16. The Parties informed the CMA that the Merger is not the subject of review by other competition authorities.

¹ Before completion of the Transaction, the howitzer and naval guns business will be carved out of GCS and retained by BAE Systems. Therefore, this activity will not be further discussed in this decision.

Jurisdiction

17. Each of Rheinmetall and GCS is an enterprise. As a result of the Merger, these enterprises will cease to be distinct.
18. As the Parties are active in the military sector, the special turnover threshold of £1 million under s23A(1) of the Act applies. The special turnover threshold is met because the UK turnover for GCS is £[~~8~~] for the financial year ending 31 December 2017.
19. The CMA therefore believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.
20. On 15 April 2019, pursuant to section 57(1) of the Act, the CMA wrote to the Secretary of State, formally bringing the Merger to his attention, as the CMA considered that the Merger may raise public interest considerations under section 58(1) of the Act.
21. The initial period for consideration of the Merger under section 34ZA(3) of the Act started on 12 April 2019 and the statutory 40 working day deadline for a decision is therefore 13 June 2019.

Counterfactual

22. The CMA assesses a merger's impact relative to the situation that would prevail absent the merger (ie the counterfactual). For anticipated mergers the CMA generally adopts the prevailing conditions of competition as the counterfactual against which to assess the impact of the merger. However, the CMA will assess the merger against an alternative counterfactual where, based on the evidence available to it, it believes that, in the absence of the merger, the prospect of these conditions continuing is not realistic, or there is a realistic prospect of a counterfactual that is more competitive than these conditions.²
23. The Parties submitted that the appropriate counterfactual against which the impact of the Transaction should be assessed is the pre-Merger conditions. The CMA has found no evidence supporting a different counterfactual. Therefore, the CMA has assessed the Merger against the prevailing conditions of competition.

² *Merger Assessment Guidelines* (OFT1254/CC2), September 2010, from paragraph 4.3.5. The *Merger Assessment Guidelines* have been adopted by the CMA (see *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), January 2014, Annex D).

Background

24. The proposed transaction concerns AFVs. The MoD defines AFVs as tracked or wheeled armoured combat land vehicles primarily designed for offensive purposes or a specialist vehicle derived from these designs.
25. AFVs include main battle tanks, and a variety of tracked and wheeled vehicles serving a range of mission functions including infantry fighting vehicles, reconnaissance vehicles, armoured personnel carriers, ambulances and operational support vehicles.
26. AFVs and related services (such as upgrades and deep maintenance) are generally procured by the MoD through public tenders. The MoD often uses open international competitions when it does not consider there to be a need to procure from a UK based contractor for national security reasons.
27. Alternatively, the MoD can use other options to secure value for money such as through single sourcing³, foreign military sales (ie purchasing vehicles from another government), or through international collaboration arrangements.⁴
28. New AFVs tend to be procured by the MoD through infrequent large scale contracts. AFV upgrades are procured by the MoD more frequently and usually involve contracts for the provision of parts of the vehicle system (turrets, cannons and modular protection) and/or to update old technology. Lastly, deep maintenance services are typically procured by the MoD through contracts for the provision of maintenance of systems, management of spare parts, and the provision of engineering expertise to ensure safety. Deep maintenance services can be distinguished from routine maintenance as the former typically involve more complex overhauls and the latter is typically performed by the British Army.
29. The primary contractor for new AFVs, upgrades and deep maintenance may choose to sub-contract elements of a contract to other suppliers/contractors or may be required to do so by the MoD. These sub-contractors may in turn enter into contracts (ie further sub-contracts) with other suppliers to carry out the relevant work. As not all suppliers are able to manufacture a full AFV or perform and complete an upgrade, they will often partner up to combine complementary specialist skills and research, and to provide solutions for the customer at a lower financial risk for their partnerships. These partnerships can take various forms such as sub-contracting arrangements or joint venture agreements.

³ ie using the exemptions of the Single Source Contract Regulations 2014.

⁴ Such as the Organisation for Joint Armament Co-operation (**OCCAR**), from which the MoD can procure new AFVs.

30. The Original Equipment Manufacturer (**OEM**) of the AFV retains the design rights (ie IP rights) associated with the AFV, which allows the OEM the capability of providing further services to that AFV (**design authority**). In the context of the procurement of new AFVs, the MoD normally requires from the OEM access to the necessary design information for support and upgrades. This means that the MoD in most cases has the ability to procure support services and upgrades for new AFVs from suppliers other than the OEM.
31. The main recent procurement programmes relevant to AFVs are:
- (a) *Ajax*: A new AFV programme concerning the Ajax, a family of armoured fighting vehicles which is being developed by General Dynamics UK for the British Army and which was formerly known as the Scout SV (**Specialist Vehicle**). By value, it is the largest contract for the supply of new AFVs to the MoD in the last 10 years. It was awarded to General Dynamics in 2014.
 - (b) *Mechanised Infantry Vehicle (MIV)*: A new AFV programme in which the Boxer (an 8x8 wheeled vehicle) will be supplied to the MoD through OCCAR. According to internal documents, the Parties expect the contract to be awarded to the ARTEC consortium (**ARTEC**), a consortium composed of Rheinmetall and Krauss-Maffei Wegmann GmbH & Co. KG (**KMW**), [REDACTED].
 - (c) *Challenger 2 Life Extension Programme (CR2 LEP)*: An upgrade programme to the Challenger 2, the main battle tank of the British Armed Forces. Rheinmetall and GCS were awarded the current Initial Assessment Phase.⁵ The CMA understands that [REDACTED].
 - (d) *Warrior Capability Sustainment Programme (WCSP)*: An upgrade contract procured to increase the capabilities of the Warrior tracked vehicle. This tender was awarded to Lockheed Martin in 2011.
32. The Parties submitted that the Transaction takes place against a backdrop of a shrinking British Army and a commensurate decline in the UK's demand for military vehicles. In addition, the Parties stated that the AFVs which GCS today supports include many products with short remaining usable lives. For example, the Challenger 2 is an AFV originally manufactured in 1993 and is currently undergoing an upgrade (CR2 LEP) to be able to keep credible usage as a main battle tank.

⁵ In the Assessment Phase, the MoD will assess different technological or business model approaches as a means of satisfying the endorsed requirement. It is one of the phases of the CADMID cycle by which the MoD manages its procurement, in-service management and subsequent disposal of defence equipment. The CADMID cycle is composed of the following phases: Concept, Assessment, Demonstration, Manufacture, In-service and Disposal.

Frame of reference

33. Market definition provides a framework for assessing the competitive effects of a merger and involves an element of judgement. The boundaries of the market do not determine the outcome of the analysis of the competitive effects of the merger, as it is recognised that there can be constraints on merging parties from outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others. The CMA has taken these factors into account in its competitive assessment.⁶
34. The Parties overlap in the supply of prime contracting services for each of new AFVs, upgrades and deep maintenance, as well as the supply of sub-contracting products and services for AFVs.

Product scope

35. In previous decisions concerning AFVs, it was considered – but left open – that the supply of prime contracting services for AFVs constitutes a separate frame of reference from that of specific systems and weapons systems. In *BAE SYSTEMS Plc/Alvis Plc*, the predecessor of the CMA, the OFT, agreed with the parties that the relevant frames of reference should be the supply of prime contracting services for AFVs and associated systems; and the supply of associated weapons systems.⁷ The European Commission (EC) has considered the supply of AFVs in several decisions. In *BAE Systems/Alvis*, the EC found that there were separate markets for prime contracting of AFVs and the supply of specific systems.⁸ In *General Dynamics/Alvis*, the EC suggested that within the broader AFV market, the distinct functionality of AFV categories such as the infantry fighting vehicle and the associated requirements for protection and combat capabilities supported the existence of separate product markets for AFVs and related services, but the EC did not conclude on the precise definition.⁹ In *Rheinmetall/STN Atlas*, the EC considered a single market for prime contracting services for new AFVs.¹⁰

Parties' submissions

36. The Parties consider that the relevant frames of reference in this case are:

⁶ *Merger Assessment Guidelines*, paragraph 5.2.2.

⁷ OFT 2003 *BAE Systems Plc/Alvis Plc*.

⁸ EC 2004 *BAE Systems/Alvis*.

⁹ EC 2004 *General Dynamics/Alvis*.

¹⁰ EC 2003 *Rheinmetall/STN Atlas*.

- (a) The supply of prime contracting services for new AFVs and associated services (such as deep maintenance); and
 - (b) The supply of upgrades to AFVs in-life, other than on an urgent operational requirements basis.
37. The Parties submitted that this frame of reference is based on a review of relevant precedents and on recent procurement practices by the MoD. The Parties also stated that the market for AFVs has evolved since the assessments made in past decisions, and that in particular, the MoD has moved from new vehicle procurements to upgrading existing equipment.
38. In the Parties' view, there are arguments for separate frames of reference for prime contracting and sub-contracting. However, they submitted that this issue can be left open as no competition concerns arise on any basis.
39. The Parties also submitted that, even if the market were to be segmented further, eg by vehicle size (for instance, 4x4, 6x6, or 8x8) or weight (for instance, heavy, medium or light) or other factors, no competition issues would arise.¹¹

CMA assessment

40. The CMA acknowledges that demand-side substitutability is limited, as the object of AFV-related contracts is highly customized to suit the needs of the MoD. However, the CMA may aggregate products which are not demand-side substitutes in markets characterised by bidding and tendering processes where firms bid on the basis of the service they can offer to supply customers with bespoke products, if the same set of firms would have been credible bidders.¹²
41. The CMA considers that a single product frame of reference based on supply-side substitutability is appropriate in this case, due to the MoD's flexible approach in considering whether certain firms are capable of fulfilling the role of prime contractor, which itself depends on the scale and nature of the programme, and because the evidence suggests that the same set of firms generally bid for contracts involving different types of AFVs.
42. Therefore, the CMA looked at whether it should distinguish between:

¹¹ Some past decisions considered this segmentation, but they left open the question of whether these represent separate markets.

¹² [Merger Assessment Guidelines](#), paragraph 5.2.18.

- (a) Contracts for each of new AFVs, AFV upgrades and AFV deep maintenance; and/or
- (b) Prime contracting and sub-contracting.

New AFVs, upgrades and deep maintenance

43. The CMA considered the MoD's tendering practices (demand-side factors) and the competitor set for each type of prime contract (supply-side factors):

- (a) The MoD explained that the supply of new AFVs, deep maintenance of AFVs and AFV upgrades are generally tendered separately, indicating that these services/products are not considered as a 'bundle' on the demand side.
- (b) When the MoD purchases a new AFV, that AFV would be maintained (support solutions) for a limited period (first 2-3 years) by the winner of the prime contract. While the MoD told the CMA that the incumbent has some advantage in bidding for upgrades and/or deep maintenance, the MoD often provides a new, non-incumbent supplier with the necessary information to provide these services.
- (c) The CMA also notes that there are different sets of suppliers in each of the three candidate product frames of reference and tender information indicates that the incumbent AFV supplier will not necessarily be the supplier of upgrades or maintenance.

44. On this basis, the CMA has assessed the provision of prime contracting services for new AFVs, upgrades, and deep maintenance under separate frames of reference.

Prime contracting and sub-contracting

45. The CMA notes that the customer set is different for prime and sub-contracting services:

- (a) Sub-contracting can be seen as a separate upstream frame of reference from that of prime contracting (ie the services are at different levels of the supply chain). While a prime contractor faces the MoD directly, sub-contracting occurs at a business-to-business level;
- (b) Financial risks borne by the prime contractor are higher than those borne by a subcontractor;

- (c) The competitor set is different between prime contracting and sub-contracting.
46. By contrast, the scope of sub-contracts is generally around systems and sub-systems which can be applied to new AFVs, AFV upgrades and AFV deep maintenance contracts. Therefore, there is much greater demand-side substitution between sub-contracting products and services. Also, the competitor set for sub-contracting is generally similar for different projects, suggesting supply-side substitutability. Therefore, the CMA has assessed sub-contracting for all types of AFV services in a single frame of reference.

Conclusion on product scope

47. For the reasons described above, the CMA considered the impact of the Merger in the following product frames of reference:
- (a) supply of prime contracting services for new AFVs;
 - (b) supply of prime contracting services for upgrades to existing AFVs;
 - (c) supply of prime contracting services for deep maintenance to AFVs; and
 - (d) supply of sub-contracting products and services for AFVs.
48. However, it was not necessary to conclude on the exact product scope since the Merger does not raise any realistic prospect of an SLC under any frame of reference.

Geographic scope

49. In *BAE SYSTEMS Plc/Alvis Plc*, the OFT agreed with the parties that the geographic scope for AFVs and associated systems was global, given the evidence it received of successful international contracts.¹³ The EC, in *BAE Systems/Alvis*, noted that the relevant market is considered national in scope where there is a national supplier, and otherwise EEA-wide or worldwide. The same view was adopted by the EC in *General Dynamics/Alvis* and *Rheinmetall/STN Atlas*.¹⁴
50. The Parties consider that the geographic scope of the markets for prime contracting of new AFVs, upgrades and deep maintenance are all potentially

¹³ OFT 2003 *BAE Systems Plc/Alvis Plc*.

¹⁴ EC 2004 *BAE Systems/Alvis*, EC 2004 *General Dynamics/Alvis* and EC 2003 *Rheinmetall/STN Atlas*.

international. The Parties submitted that this is proved by the award of at least two UK programmes to US companies.

51. The Parties also submitted that a recent report published by the MoD on its spending with industry and commerce also shows the increasingly international nature of defence markets. For instance, five out of the top ten suppliers to the MoD in 2017/18 were foreign-owned companies.¹⁵
52. The Parties considered that evidence from the procurement processes for new AFVs, upgrades and deep maintenance shows that procurement is generally open to international competitors (in particular from Europe and the US).
53. In any event, the Parties stated that even if the geographic scope of the markets were to be considered national, there would be no competition concerns. Therefore, they said, the exact scope of geographic market can be left open.
54. The CMA notes that international competitors participated in all recent AFV-related tenders organised by the MoD and that the MoD awarded some of these tender contracts to international suppliers, such as Lockheed Martin and General Dynamics (see paragraphs 66 and 78 below).

Conclusion on geographic scope

55. On the basis of the evidence above, and in line with previous precedents, the CMA has considered the impact of the Merger in a global geographic frame of reference. However, it was not necessary to conclude on the exact geographic scope since the Merger does not raise any realistic prospect of an SLC under any frame of reference.

Conclusion on frame of reference

56. For the reasons set out above, the CMA has considered the impact of the Merger in the following frames of reference:
 - (a) supply of prime contracting services for new AFVs on a global basis;
 - (b) supply of prime contracting services for upgrades to existing AFVs on a global basis;

¹⁵ See [Finance & Economics Annual Bulletin Trade, Industry & Contracts 2018](#), page 11.

(c) supply of prime contracting services for deep maintenance to AFVs on a global basis; and

(d) supply of sub-contracting products and services for AFVs on a global basis.

57. However, the CMA did not find it necessary to conclude on the exact product or geographic frame of reference since the Merger does not raise any realistic prospect of an SLC under any frame of reference.

Competitive assessment

Horizontal unilateral effects

58. Horizontal unilateral effects may arise when one firm merges with a competitor that previously provided a competitive constraint, allowing the merged firm profitably to raise prices or to degrade quality on its own and without needing to coordinate with its rivals.¹⁶ Horizontal unilateral effects are more likely when the merging parties are close competitors. The CMA assessed whether it is or may be the case that the Merger has resulted, or may be expected to result, in an SLC in relation to horizontal unilateral effects in the supply of prime contracting services for each of new AFVs, upgrades, and deep maintenance; and the supply of sub-contracting products and services for AFVs.

Prime contracting services for new AFVs

59. The CMA assessed whether it is or may be the case that the Merger has resulted or may be expected to result in an SLC in relation to horizontal unilateral effects in the supply of new AFVs. The concern under this theory of harm is that the removal of one party as a competitor could allow the Parties to increase prices, lower quality, reduce the range of their services and/or reduce innovation.

Closeness of Competition and Competitive Constraints from other suppliers

Parties' submissions

60. The Parties submitted that the Merger raises no concerns because in the market for the supply of prime contracting services for new AFVs, there is at most very limited overlap between the Parties. Rheinmetall manufactures and

¹⁶ [Merger Assessment Guidelines](#), paragraph 5.4.1.

supplies a range of AFVs to its customers (primarily the German Government). In contrast, GCS is not currently manufacturing and/or supplying any AFVs to any customers globally.

61. The Parties submitted that, based on the tender data presented below (see Table 1), Rheinmetall's share of the market for supply of new AFVs – on the basis that the ARTEC consortium is awarded the MIV contract – in the UK in the last 10 years is [5-10%] (based on volume), or [10-20%] (based on value).¹⁷ GCS's market share is [0-5%] as it has not won any contracts in the last 10 years. The Parties estimate that the combined global market share of Rheinmetall and GCS would be [0-5%].

Internal documents

62. The CMA has considered the extent to which the Parties view each other as close competitors based on their internal documents.
63. Rheinmetall's internal documents indicate that Rheinmetall considers GCS to be a competitor for the wider category of 'tracked vehicles', but that other competitors such as General Dynamics and Patria provide a constraint at least as strong as GCS in this category. In particular:
- (a) Slide 15 of the [REDACTED] indicates that BAES (ie the parent company of GCS) provides [REDACTED] competition in tracked vehicles. Two other competitors, General Dynamics and Patria, cited in the same document have a similar competitive strength in that category;¹⁸
 - (b) Slide 18 of the 'Current Status, [REDACTED] Industrialisation Proposal' indicates that competition for the MIV project came [REDACTED] from General Dynamics and Patria.¹⁹

Tender data

64. The Parties submitted that, in the last ten years, the MoD tendered six prime contracts for the supply of new AFVs, and the Parties never competed head to head in the final stages of these competitions, but faced [REDACTED] competition from other competitors such as Oshkosh or General Dynamics.

¹⁷ A value of £[REDACTED] out of a market of £[REDACTED].

¹⁸ Annex 002-007 of the Merger Notice.

¹⁹ Annex 002-008 of the Merger Notice, page 18.

65. In addition to these six tenders, the MoD submitted that there has been a Foxhound light patrol vehicle tender which was open to competition around 2011-2013, in which neither of the Parties competed. [REDACTED].
66. Table 1 below summarises the participants at the different stages of each tender:

<i>Contracts</i>	<i>Companies to which the MOD sent the PQQ</i>	<i>Companies down-selected by the MoD for the Assessment Phase</i>	<i>Winner</i>	<i>Value</i>
MRV-P Lot 1 [REDACTED]	<ul style="list-style-type: none"> • GCS • General Dynamics • Thales • Supacat • Morgan • Oshkosh 	<ul style="list-style-type: none"> • Oshkosh 	[REDACTED]	[REDACTED]
MRV-P Lot 2 [REDACTED]	<ul style="list-style-type: none"> • GCS • General Dynamics • Thales • Supacat • Morgan 	<ul style="list-style-type: none"> • General Dynamics • Thales 	Pending	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
MIV (Anticipated to be signed in 2019/2020)	No PQQ released for this tender. The MoD instead issued a Preliminary Market Engagement. It was up to companies to respond to the invitation.	ARTEC	Pending	[REDACTED]
Ajax (open in 2009, signed in 2014)	<ul style="list-style-type: none"> • GCS • General Dynamics 	<ul style="list-style-type: none"> • General Dynamics • GCS 	<ul style="list-style-type: none"> • General Dynamics 	[REDACTED]
Foxhound	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: Merger Notice, RFI1 response and the MoD

Third party views

67. The MoD said that it does not consider GCS to be an active supplier of new AFVs. In particular, the MoD explained that:
- (a) The parent company of GCS, BAES, is a large player in the UK for other businesses, eg aerospace, naval and ammunition, but not for the design of new AFVs. GCS slimmed down its AFV production line after the manufacturing of Challenger 2 and after losing the Ajax tender against General Dynamics. Hence, GCS has no active AFV production capacity in the UK at the moment.

- (b) GCS does not have any off-the-shelf AFVs designs that would suit the needs of the MoD. Therefore, the MoD explained that GCS would be able to bid for a new AFV tender only in partnership with another supplier or as part of a consortium, the members of which might be likely to bid in their own right in any case. How the wider market supply chain forms and responds to any given tender is a matter of the market.
68. In contrast, the MoD stated that Rheinmetall is a much larger organisation in the supply of land systems both in Germany and worldwide. It is one of the largest main battle tank weapon and ordnance systems designer and manufacturers in the world, alongside KMW. For example, Rheinmetall has the rights to produce and supply the Boxer (an AFV) and other vehicles.
69. The MoD also told the CMA that different suppliers specialise in different types of AFV and that it has alternative means of purchasing AFVs through foreign military sales, ie purchasing AFVs from other governments. Other competitors named by the MoD were: KMW, Oshkosh (through a foreign military sale from the US Government), Lockheed Martin, and General Dynamics.
70. Most competitors did not raise concerns about competition for new AFVs as (in their view) the Parties are not competing closely against each other. One competitor said that GCS's business had reduced in size in recent years. Another competitor stated that there were no past substantial competition between the Parties apart from the CR2 LEP, even if other markets were to be considered.
71. Only one competitor raised concerns stating that, after the Merger, there is the 'possibility that the MoD will rely more on single sourcing given the merged entity's strong position and that the scope for competition will be reduced.' However, the CMA understands that the MoD's decision on single sourcing from a particular supplier is driven by achieving value for money and that furthermore, the MoD has other means of purchasing new AFVs (see paragraph 69 above).

Conclusion on prime contracting services for new AFVs

72. On the basis of the above evidence, the CMA believes that the Parties are not close competitors, and that the merged entity will continue to face sufficient competition from other suppliers of new AFVs post-Merger.²⁰ Therefore, the

²⁰ Given the bidding nature of the market for new AFVs and the lumpiness of demand, the CMA has put limited weight on the market share data provided by the Parties in its forward-looking assessment. Nevertheless, the CMA notes the fact that GCS has no current contracts for new AFVs is consistent with the overall finding that the CMA believes that the Merger will not give rise to a realistic prospect of an SLC in the supply of prime contracting services for new AFVs.

CMA believes that the Merger will not give rise to a realistic prospect of an SLC in the supply of prime contracting services for new AFVs

Prime contracting services for upgrades to existing AFVs

Closeness of Competition and Competitive Constraints from other suppliers

Parties' submissions

73. The Parties stated that they have competed head-to-head only in the context of the CR2 LEP, but have not competed against each other in any other upgrade contract, whether in the UK or internationally.
74. The Parties also submitted that, based on the tender data presented below (see Table 2), Rheinmetall's share of supply of prime contracting services for AFV upgrades in the UK – on the assumption it is awarded the CR2 LEP – in the last 10 years is [20-30]% based on volume, or [20-30]% based on value. GCS's market share is [0-5]% as it has [redacted] a new contract in this period. The Parties estimate that Rheinmetall and GCS's global combined market share would be [0-5]%.

Tender data

75. In the last ten years there have been two tenders for prime contracting services for upgrades to AFVs opened by the MoD. The Parties competed head-to-head for the CR2 LEP Initial Assessment Phase. Table 2 below summarises the participants in each tender. In the last ten years, GCS bid in both tenders and was not successful in the WCSP tender (Lockheed Martin was chosen).
76. In the CR2 LEP tender, the MoD published a Pre-Qualification Questionnaire and selected six potential suppliers. It assessed in detail each of the suppliers' bids and down-selected Rheinmetall and GCS. However, they did not compete further, due to a change in scope of the project.
77. The MoD explained that [redacted].
78. Table 2 below summarises the participants at the different stages of each tender:

<i>Contracts</i>	<i>Companies to which the MOD sent the PQQ</i>	<i>Companies down-selected by the MoD for the Assessment Phase</i>	<i>Winner</i>	<i>Value</i>
WCSP (2011)	<ul style="list-style-type: none"> • GCS • Oto Melara (now Leonardo) • BAE Systems • Hägglunds • BAE Systems Inc • Lockheed Martin UK 	<ul style="list-style-type: none"> • GCS • Lockheed Martin UK 	Lockheed Martin UK	£1.6 billion
CR2 LEP (2017)	<ul style="list-style-type: none"> • Rheinmetall • GCS • Lockheed Martin • KMW • CMI • RUAG • General Dynamics UK 	<ul style="list-style-type: none"> • GCS • Rheinmetall 	Pending	[REDACTED]

Source: The Parties

Internal documents

79. An internal document from Rheinmetall, dated October 2017, indicates that GCS [REDACTED] suggesting that GCS competes closely with Rheinmetall. However, the document also indicates that KMW and Nexter are seen as [REDACTED] competitors and [REDACTED].²¹ In addition, General Dynamics and Patria received [REDACTED]. Leidos and Thales received [REDACTED].
80. One internal document from GCS describes the market for the supply of prime contracting services for upgrades to AFVs as '[REDACTED]' suggesting that there are several competitors able to provide various AFV upgrades: General Dynamics, KMW, Rheinmetall, FNSS Savunma Sistemleri A.Ş., Nexter, Otokar and others.²²

Third party views

81. The MoD told the CMA that it considers GCS to be active in the supply of prime contracting services for upgrades to AFVs for which GCS is the design authority. However, the MoD said that GCS generally is not a strong competitor.
82. Competitors told the CMA that the Parties are close competitors for upgrades, in particular for the CR2 LEP (see paragraph 70 above). For example, one

²¹ Annex 002-007 of the Merger Notice, page 79-80.

²² Annex 003-048 of the Merger Notice, page 15.

competitor stated that the Merger will effectively undermine the current competition for the CR2 LEP. Another competitor said that the combination of GCS, being the design authority of a range of AFVs subject to future upgrade and deep maintenance contracts, with Rheinmetall would give the merged entity an advantage to win future tenders.

83. However, the CMA notes that the MoD generally negotiates with the OEM access to the relevant design information, so as to enable other suppliers to provide AFV-related services such as upgrades, which the MoD has done in the past. The MoD also said that on older AFVs, such as the Challenger 2, design information can be 'reverse-engineered' allowing another supplier to act (in effect) as design authority, as is the case with regard to the CR2 LEP. This is corroborated by an internal document from GCS which indicates that '[~~]'.²³ The CMA therefore believes that design authority rights do not necessarily give an incumbency advantage to the OEM when competing for AFV upgrades.~~

Conclusion on prime contracting services for upgrades to AFVs

84. On the basis of the above evidence, the CMA believes that the Parties are relatively close competitors, but that the merged entity will continue to face sufficient competition from other suppliers for upgrades to AFVs post-Merger.²⁴ Therefore, the CMA believes that the Merger will not give rise to a realistic prospect of an SLC in the supply of prime contracting services for upgrades to existing AFVs.

Prime contracting services for deep maintenance to AFVs

Closeness of Competition and Competitive Constraints from other suppliers

Parties' submissions

85. The Parties submitted that they are not close competitors in the provision of prime contracting services for deep maintenance to AFVs. GCS provides deep maintenance services for the AFVs it originally supplied to the MoD, namely CVR(T), Warrior, Challenger 2, Titan, Trojan and Terrier, while Rheinmetall does not have any support contract for AFVs.

²³ Annex 003-048 of the Merger Notice, page 21.

²⁴ As noted above (see footnote 24), given the bidding nature of the market for upgrades to existing AFVs and the lumpiness of demand, the CMA has put limited weight on the market share data provided by the Parties in its forward-looking assessment. Nevertheless, the CMA notes the fact that GCS has no current contracts for upgrades to existing AFVs is consistent with the overall finding that the CMA believes that the Merger will not give rise to a realistic prospect of an SLC in the supply of prime contracting services for upgrades to existing AFVs.

86. The Parties also submitted that, given that GCS's support (deep maintenance) contracts with the MoD for both armoured and non-armoured vehicles are only £[REDACTED] annually out of the MoD's total annual deep maintenance budget of £[REDACTED], GCS holds [0-5]% market share for deep maintenance of land systems in the UK for both armoured and non-armoured vehicles, and almost all of that [0-5]% relates to maintenance of vehicles supplied by GCS.^{25, 26}

Internal documents

87. In one of GCS's internal documents, GCS views Thales, Babcock and Leidos [REDACTED] for the deep maintenance market because of their '[REDACTED]'. In the same document, Rheinmetall is not mentioned in relation to deep maintenance.²⁷ Another internal document from GCS (setting out competitors and their contracts awarded as regards repairs and spares) indicates that there are numerous competitors active in the UK.²⁸
88. GCS also provided a global overview document of support and upgrade markets which lists the competitors active in those markets. While General Dynamics was the competitor with the most international contracts historically, and in 2017, Rheinmetall had no contracts in the same year.²⁹

Third party views

89. The MoD said that GCS and Rheinmetall are both active in the supply of prime contracting services for deep maintenance to AFVs, and that the number of alternative providers will depend on the service and on the vehicle. Accordingly, Rheinmetall's position is dependent upon the programme and [REDACTED]. The MoD also noted that the Parties had never competed head-to-head for any programme to the MoD's knowledge.
90. The MoD said that the market for maintenance services has a much wider range of alternative suppliers relative to new AFVs and AFV upgrades. Currently, there are a large number of alternative providers of deep maintenance services such as: Leidos ([REDACTED]), Babcock ([REDACTED]), Thales ([REDACTED]), Supacat ([REDACTED]), Caterpillar ([REDACTED]), and Oshkosh ([REDACTED]). The MoD said that there are also other providers which would like to enter the market.

²⁵ *ibid*, 25.

²⁶ The CMA notes that these shares of supply do not correspond directly to the product frame of reference.

²⁷ Annex 003-004 of the Merger Notice, page 11.

²⁸ See Annex 003-031 of the Merger Notice, page 6.

²⁹ Annex 003-048 of the Merger Notice, page 16.

91. As regards the MoD's methods of procurement, it explained that it may also choose to procure from particular suppliers for a variety of reasons and use collaborative procurements (which are aimed at obtaining the goods and services necessary to meet the MoD's requirements from contractors located in other nations) to achieve value for money.
92. Some competitors expressed concerns stating a potential reduction in competition for 'support' contracts as a result of the Merger.

Conclusion on prime contracting services for deep maintenance

93. On the basis of the evidence above, the CMA believe that the Parties are not close competitors in the supply of prime contracting services for deep maintenance to AFVs and that the merged entity will continue to face sufficient competition from other suppliers of deep maintenance services post-Merger. Therefore, the CMA believes that the Merger will not give rise to a realistic prospect of an SLC in the supply of prime contracting services for deep maintenance to AFVs.

Sub-contracting products and services for AFVs

Closeness of Competition and Competitive Constraints

Parties' submissions

94. The Parties submitted that, overall, both Parties do not have any significant presence in the sub-contracting market. Rheinmetall's only sub-contract represents [0-5]% of the Ajax prime contract value, whereas GCS's only sub-contract represents less than [0-5]% of the overall WCSP prime contract.

Internal documents

95. The Parties' internal documents indicate that there are a number of alternative sub-contractors active in sub-contracting.
 - (a) One GCS document mentions Thales, Raytheon and Pearson Engineering as sub-contractors involved in the MIV project.³⁰

³⁰ Annex 003-008 of the Merger Notice, pages 17-18.

- (b) For the CR2 LEP, Rheinmetall considered a number of sub-contractors, including Babcock, DSG, Thales, Selex and Pearson Engineering.³¹
- (c) Another document from GCS indicates that Lockheed Martin won [REDACTED]. Within that context, GCS sees CMI, Lockheed Martin and Nexter as its [REDACTED] competitors for turrets, but does not mention Rheinmetall.³²

Third party views

96. The MoD stated that it sees the Merger as having no impact on sub-contracting, as there are alternative choices available. The MoD said it is able to direct the prime contractor to obtain services and/or products from sub-contractors directly nominated by the MoD. The MoD also said that there is usually sufficient competition for sub-contracting services and there are alternative ways (such as single sourcing, international collaboration, etc) in which the MoD can protect value for money in this area.

Conclusion on sub-contracting products and services for AFVs

97. Based on the evidence described above, the CMA does not believe that the Merger raises any realistic prospect of an SLC in the supply of sub-contracting products and services for AFVs as the merged entity will be constrained by a number of competitors post-Merger.³³

Conclusion on horizontal unilateral effects

98. For the reasons set out above, the CMA believes that the Merger does not give rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in relation to the supply of prime contracting services for new AFVs, the supply of prime contracting services for upgrades to existing AFVs, the supply of prime contracting services for deep maintenance to AFVs, or the supply of sub-contracting services for AFVs.

Vertical effects

99. Vertical effects may arise when a merger involves firms at different levels of the supply chain, for example a merger between an upstream supplier and a

³¹ See Annex 007-002 of the Merger Notice, page 4.

³² See Annex 003-036 of the Merger Notice.

³³ Whilst the CMA has put limited weight on market share data in this context, the CMA notes that in any event the Parties have a very limited presence in sub-contracting for AFVs which is consistent with the overall finding that the CMA believes that the Merger will not give rise to a realistic prospect of an SLC in the supply of sub-contracting products and services for AFVs.

downstream customer or a downstream competitor of the supplier's customers.

100. Vertical mergers may be competitively benign or even efficiency-enhancing, but in certain circumstances can weaken rivalry, for example when they result in foreclosure of the merged firm's competitors. The CMA only regards such foreclosure to be anti-competitive where it results in an SLC in the foreclosed market(s), not merely where it disadvantages one or more competitors.³⁴ In the present case, the CMA has considered the supply of sub-contracting products and services for AFVs as one of the frames of reference in which a vertical relationship can be established.

Foreclosure of sub-contractors

101. Some competitors raised concerns that the merged entity will not have the incentive to sub-contract AFV services post-Merger.
102. The CMA's approach to assessing vertical theories of harm is to assess: (a) the ability of the merged entity to foreclose competitors; (b) the incentive of it to do so; and (c) the overall effect of such a strategy on competition.³⁵

Ability

103. The extent to which any reduction in sub-contracting activity by the merged entity would have an adverse impact on sub-contractors' ability to compete for other tenders depends in principle on the merged entity's market power in the supply of prime contracting services.
104. In its assessment of horizontal effects in relation to prime contracts (see paragraphs 59 to 93 above), the CMA has concluded that there will be sufficient competition post-Merger; and that the MoD can direct a sub-contractor to be appointed according to its requirements (see paragraph 96 above). As a result, alternative prime contractors (ie routes to the market) will remain available to sub-contractors post-Merger.
105. Rheinmetall's shares of supply in the UK are less than [20-30]% in upgrades and [10-20]% in new AFVs, assuming the MIV and CR2 LEP are to be awarded to ARTEC and Rheinmetall. Although the CMA has placed limited weight on shares of supply in its market investigation (see above), the other evidence available to the CMA also indicates that GCS, despite being the design authority of most of the UK AFV fleet, was not successful in recent

³⁴ In relation to this theory of harm 'foreclosure' means either foreclosure of a rival or to substantially competitively weaken a rival.

³⁵ [Merger Assessment Guidelines](#), paragraph 5.6.10.

tenders ([X], [X]) and that other routes to market remain (see paragraphs 69, 78-80 and 90 above).

106. On a global level, the Parties submitted that they have a market share of prime contracting services for new AFVs and AFV upgrades of less than [0-5]%, taking into account the addressable market. An internal document from GCS suggests that in the period of 2017-2026, the Parties' joint share in the supply of upgrades to AFVs and deep maintenance is around [30-40]%.³⁶ Therefore, substantial other routes to market will remain post-Merger for competing sub-contractors.
107. Some third parties argued that GCS's design rights give the merged entity an incumbency advantage. The Parties submitted that the MoD normally requires a right to exploit the IP from the original design authority for the purposes of deep maintenance and upgrades and frequently has the ability to award an upgrade contract to someone other than the OEM.
108. The CMA found that the MoD does supply other sub-contractors with the relevant information to execute sub-contracts, thereby enabling third parties to compete for and supply prime contracting services for upgrades to AFVs (see paragraphs 43(b) and 83 above). For example, in the past, the MoD has ensured that different suppliers are given access to the platform data to install new systems, eg Combat Radio Integration/Electronic Counter Measure Integration.
109. Furthermore, depending on the depth of the integration required and the age of the AFV, the MoD, by holding the above background IP rights, can also appoint a different design authority for a specific sub-component depending on risk and access to information. On older platforms such as CR2, these components can be reverse engineered, allowing another competitor to supply and implement the necessary upgrade or service.
110. Considering the evidence set out above, the CMA does not believe that that the merged entity will have the ability to foreclose competition in relation to the supply of sub-contracting products and services for AFVs and the CMA has not therefore gone on to consider incentive or effect.

³⁶ The market size underlying these estimates includes also a small range of vehicles and services not directly related to the frames of reference considered in this decision.

Conclusion on vertical effects

111. For the reasons set out above, the CMA believes that the Merger does not give rise to a realistic prospect of an SLC as a result of vertical effects in relation to the supply of sub-contracting products and services for AFVs.

Barriers to entry and expansion

112. Entry or expansion can mitigate the initial effect of a merger on competition, and in some cases may mean that there is no SLC. In assessing whether entry or expansion might prevent an SLC, the CMA considers whether such entry or expansion would be timely, likely and sufficient.³⁷

113. However, in the present case, there was no need for the CMA to conclude on barriers to entry or expansion as the Merger does not give rise to competition concerns on any basis.

Third party views

114. The CMA contacted the MoD and competitors of the Parties.

115. Third party comments have been taken into account where appropriate in the competitive assessment above.

Decision

116. For the reasons set out in this decision, the CMA does not believe that it is or may be the case that the Merger may be expected to result in an SLC within a market or markets in the United Kingdom.

117. The Merger will therefore **not be referred** under section 33(1) of the Act.

James Waugh
Director of Mergers
Competition and Markets Authority
13 June 2019

³⁷ [Merger Assessment Guidelines](#), paragraph 5.8.1.