Anticipated acquisition by Hitachi Rail, Ltd. of Thales SA's Ground Transportation Systems Business

ME/6971/21

SUMMARY

1. On 3 August 2021 Hitachi Rail, Ltd. (**Hitachi Rail**) agreed to acquire Thales SA's Ground Transportation Systems business (**Thales**) for €1.66 billion (the **Merger**). Hitachi Rail and Thales are together referred to as the **Parties**, and for statements referring to the future, as the **Merged Entity**.

2. The Competition and Markets Authority (**CMA**) believes that it is or may be the case that each of Hitachi Rail and Thales 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 overlap in the supply of mainline rail signalling and urban signalling systems.

4. Mainline signalling systems prevent collisions or unsafe manoeuvres on national train networks by determining the position of trains, controlling their direction, and providing authorisation to train drivers to take certain movements. These systems comprise a number of separate sub-systems, including: (i) interlockings, which are the principal safety critical component of mainline rail signalling systems; (ii) automatic train protection (**ATP**) systems, including both wayside systems (installed alongside the track) and on-board units (**OBUs**) (installed on mainline rolling stock), which ensure that trains comply with the instructions issued by the interlockings and that they travel at appropriate speeds; and (iii) operation and control systems (**OCS**), which are IT solutions designed to ensure the overall management of railway networks.

5. Urban signalling systems are railway signalling systems used for local passenger rail transit, encompassing metro and light rail and tram (**LRT**) networks. These are designed to ensure safety on urban rail networks by preventing collisions and excessive speeds, as well as improving network capacity.

Mainline signalling

6. The supply of mainline signalling in Great Britain is currently undergoing significant change.

7. A market study carried out by the Office of Rail and Road (**ORR**), which concluded in 2021, found that the introduction of digital technology is expected to drive one of the most significant modernisation programmes in the nearly 200-year history of Britain's railway infrastructure. ORR noted that the shift from legacy to digital standardised signalling systems has the potential to revolutionise the way the railway operates, delivering transformative improvements to increase capacity, lower unit costs, and reduce disruption. ORR also noted that investment in signalling systems is expected to increase significantly in the near future, with a projected five to six-fold increase in the volume of renewal works, as Network Rail, the principal customer of mainline signalling systems in the UK, looks to replace expiring legacy assets with digital alternatives.

8. At the same time, ORR found that the supply of mainline signalling in Great Britain suffered from a lack of competition. ORR noted that the market is essentially limited to only two incumbent suppliers – Siemens and Alstom – who have represented an increasing share of Network Rail's major signalling spend in recent years. ORR also identified high barriers to entry and expansion, including in the way that Network Rail has procured signalling projects in the past, make it harder for alternative suppliers, such as Hitachi Rail and Thales, to compete on equal terms.

9. ORR made a number of recommendations intended to increase competition from alternative suppliers, which Network Rail is due implement in the design of the tendering process for its next major signalling procurement, the Train Control Systems Framework (the **TCSF**).

10. The TCSF will be the procurement framework through which Network Rail procures a range of major signalling projects for a ten-year period

commencing in 2024 and will include both legacy and digital signalling projects. Network Rail intends to appoint five framework suppliers (in contrast to its prior approach of only appointing three), and to include a range of measures to help lower barriers to entry, including by providing each framework supplier with a guaranteed minimum workbank. As digital signalling is based on European standardised and interoperable technology, a wider range of competitors, including suppliers already active in digital signalling elsewhere in Europe, are expected to be competitive for the digital aspects of the framework.

11. In keeping with the CMA's established approach of assessing the commercial realities of transactions, the CMA has carried out a forward-looking assessment to the markets at issue, taking into account a range of evidence (and not just evidence of historical market performance). In this regard, the CMA's investigation has focused on considering whether the Merger would reduce competition in relation to the TCSF and the specific mainline signalling projects that will be procured through it.

12. While both Parties currently have a limited presence in UK signalling markets, the CMA found that both are established players in Europe with strong signalling capabilities, and that, absent the Merger, both would independently bid for, and be close competitors, for the TCSF. Within this context, the CMA found that both Parties would be well placed to become significant suppliers and compete closely in relation to two specific types of signalling projects that will fall under the TCSF:

    (a) the joint supply of digital interlockings and ATP wayside equipment conforming to the European Train Control Systems (**ETCS**) standard ('**ETCS ATP wayside re-signalling projects'**); and

    (b) OCS projects.

13. The CMA found that, post-Merger, the market incumbents, Siemens and Alstom, are both likely to win a place on the TCSF and compete strongly in relation to the supply of ETCS ATP wayside re-signalling projects and OCS projects. The CMA also found that a limited number of other European suppliers may be capable of competing for the TCSF. But the CMA ultimately found that these other suppliers are unlikely to be as strong competitors as either of the Parties and that the constraint they provide, both in relation to ETCS ATP wayside re-signalling projects and OCS projects, would be limited.

14. The CMA, therefore, believes that the Merger gives rise to a realistic prospect of a substantial lessening of competition (**SLC**) as a result of horizontal unilateral effects in relation to the supply of (i) ETCS ATP wayside re-signalling projects in the UK; and (ii) OCS projects in the UK.

15. The CMA also considered but ultimately found that the Merger does not give rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in the supply of a number of other mainline signalling projects, including: (i) the standalone supply of interlocking projects; (ii) the standalone supply of ETCS ATP wayside projects (**ETCS ATP wayside overlay projects**); (iii) the supply of ETCS OBU projects; and (iv) the supply of the mainline signalling products Network Rail intends to develop through the 'Optimised Train Track Operations' project (the **OTTO project**). The CMA also found that the Merger does not give rise to a realistic prospect of an SLC as a result of vertical effects in the supply of ETCS OBUs to mainline rolling stock manufacturers.

Urban signalling

16. In relation to urban signalling, the CMA's investigation focused on competition between the Parties in the supply of urban signalling projects for metros in the UK relying on communication-based train control (**CBTC**) technology (an urban signalling technology relying on continuous radio-based communication between the train and the tracks to precisely identify, at all times, the location of a train on the tracks).

17. Again, the CMA has taken a forward-looking assessment to the impact of the Merger in this market taking into account a range of evidence (and not just evidence of historical market performance).

18. The CMA found that the Parties are close competitors in relation to CBTC signalling projects for metros in the UK. Thales is the largest provider of CBTC signalling projects for Transport for London (**TfL**) services, with very few rivals. The CMA found that it is likely to continue to compete strongly in future, particularly as future UK demand is likely to be driven by demand in London. While Hitachi Rail has been a weaker competitor to date in London, the CMA found that it is an established player globally and has the capabilities to be a strong and close competitor to Thales in the UK in future as it continues to develop its experience and global portfolio of references.

19. Post-Merger, while both Siemens and Alstom are likely to remain credible competitors for CBTC signalling projects in the UK, the CMA considers it unlikely that any other competitor would constrain the Merged Entity.

20. The CMA, therefore, believes that the Merger gives rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in the supply of CBTC signalling projects for metros in the UK.

21. The CMA also considered but ultimately found that the Merger does not give rise to a realistic prospect of an SLC as a result of conglomerate effects in the bundled supply of CBTC signalling projects and urban rolling stock.

22. The CMA is therefore considering whether to accept undertakings under section 73 of the Enterprise Act 2002 (the **Act**). The Parties have until 16 December 2022 to offer an undertaking to the CMA that might be accepted by the CMA. If no such undertaking is offered, then the CMA will refer the Merger pursuant to sections 33(1) and 34ZA(2) of the Act.